

(2015) 06 BOM CK 0007

In the Bombay High Court

Case No : Appeal (Lodging) No. 395 of 2015 in Arbitration Petition (Lodging) No. 647 of 2015

S. Satyanarayana and Co.

APPELLANT

Vs

West Quay Multiport (Private Limited) and Others

RESPONDENT

Date of Decision : 09-06-2015

Acts Referred:

Arbitration and Conciliation Act, 1996 — Section 37, 9

Citation : (2016) 2 ALLMR 280 : (2015) 4 ARBLR 531 : (2015) 4 BC 682 : (2015) 4 BomCR 274

Hon'ble Judges : M.S. Shah, C.J.;G.S. Kulkarni, J

Bench : Division Bench

Advocate : V.R. Dhond, Senior Advocate, Rashmi Khandekar, Arindam Pal and Adwitiyaa Das i/b Augustus Law Chambers, for the Appellant; S.U. Kamdar, Chirag Kamdar and Suraj Iyer instructed by Ganesh and Co., Advocates for the Respondent

Final Decision : Dismissed

Judgement

G.S. Kulkarni, J.—This Appeal under section 37 of the Arbitration and Conciliation Act, 1996 (for short the Act) is directed against an order dated 21 April 2015 passed by the learned Single Judge whereby the appellant's application filed under section 9 of the Act seeking an injunction against enforcement of two bank guarantees stand dismissed.

2. Facts: Respondent no.1 had invited bids for the works namely "Supply of materials for Construction of Compound Wall of Stack Yard for WQ-6 berth at West of M/s. Essar Pellet Plant, at Visakhapatnam Port Trust as also separate bids were invited for "labour charges" for the said work. The appellant was a successful bidder and accordingly respondent no.1 issued two letters of acceptance (LOA) both dated 27 November 2012 in favour of the appellant. One of the conditions of the letter of acceptance (LOA) was that the appellant would furnish a performance guarantee of a nationalized bank for an amount of 10 % of

the contract value. An agreement-cum-work order dated 5 December 2012 came to be executed between the parties. Schedule C of the Agreement was the agreed proforma of the performance guarantee to be executed by the appellant in favour of the respondent no.1. The appellant accordingly furnished two performance guarantees for an amount of Rs.34,00,000/- and another performance guarantee for Rs.18,50,000/-both dated 27 February 2013. These are the bank guarantees which are in question in these proceedings. These performance guarantees were required to be kept valid during the defect liability period which was eighteen months from the date of the completion of the work under the contract and for a period of six months thereafter. Some clauses under the "General Conditions of Contract" relating to the performance guarantee need to be noted. Clause 49 is the provision relating to the performance guarantee and relevant clauses therein are clauses 49.1 and 49.3 which reads thus :

49.1: "The client shall be entitled to enforce the Performance Guarantees if the Contractor fails to pay to the client any amounts due and payable by it under this Contract. The Performance Guarantee may also be enforced by the client if the contractor fails to perform any of its obligations in accordance with this contract, including to provide the contractor's documents or to perform the works or any part thereof in accordance with this contract, for the failure of the Contractor's Documents or the Works to meet the Specifications, the client's requirements or other requirements under this Contract or the concession Agreement, upon any Defects being discovered in the Works or upon the occurrence of the events specified in this Contract that enable the client may enforce the Performance Guarantees"

(Emphasis supplied)

49.2.....

49.3 " The client shall upon giving notice to the Contractor, be entitled to enforce the Performance Guarantee at the first instance without any requirement to place a demand on the Contractor for the amount as a condition precedent to the drawing of any amount covered by the Performance Guarantees. Further the client shall be entitled to enforce the Performance Guarantees or any part thereof notwithstanding any dispute pending to be determined between the Parties in respect of the default claimed by the client to have been committed by the Contractor."

3. It is not disputed that the work under contract was completed by the appellant on 22 July 2014 and the defect liability period of 18 months commenced from the said date. Clause 40 of the general conditions of contract provided for the defect liability period which reads thus :-

3. "Defects Liability Period

40.1: The Contractor shall be responsible to make good and remedying at his own expenses within such period as may be stipulated by the client any Defects,

which may develop or be noticed by the client or the client during the Defects Liability period.

40.2: The Contractor may be required to repair, replace or make good any part of the Works in order to remedy the Defect as instructed by the Client.

40.3: The Defects Liability Period shall be 18 (eighteen) Months from the Certified completion date. The Performance Guarantees shall be valid for a period of 6 (six) months beyond the end of Defects Liability period. If the Contractor fails to remedy the Defects, the client may, in lieu of the Contractor remedying and making good such Defects, remedy the Defects itself or have the Defects remedied by any third person/party and deduct from any money due to the Contractor or from its Performance Guarantees, a sum to be determined by the Engineer equivalent to the cost remedying and/or making good such Defects.

40.4: The defects liability for a part of the structure that has undergone rectification due to the defective workmanship/materials used. Construction methodology, etc which are attributable to the Contractor, in such case the defects liability for that part of the structure shall get extended further by a period of 1 (one) year from the date of completion of such rectification."

4. Another clause in the contract on which both the parties have relied is clause 39 which deals with the completion certificate. Under this clause, the manner in which the completion certificate would be issued is provided for. Clause 39 reads thus :

39. "As soon as the Works are substantially completed, the Contractor shall give a notice of such completion to the client and within 30 (thirty) days or receipt of such notice, the client shall inspect the works and shall verify the claim of Contractor and may issue notice to the Contractor indicating:

(a) The Defects to be rectified by the Contractor, i.e. the Punch List, and

(b) The completion Date

39.2: The Contractor shall within the stipulated Completion Date, from the date of receipt of the Punch List, complete all the items of work specified therein.

39.3: The Client shall issue the Completion Certificate only after the independent Engineer has intimated his approval to the Client.

39.4: The Client shall issue a final Completion Certificate on successful completion of the Defects Liability Period."

(Emphasis supplied)

5. It is not in dispute that the defect liability period has commenced from 22 July 2014 and would expire in March 2016. During this defect liability period a document titled as "experience certificate" dated 18 August 2014 came to be issued by the respondent no.1 in favour of the appellant which certifies that the appellant has completed the work under the contract and that the same is

satisfactory. In the note appearing in the said Certificate it is stated that this Experience Certificate is issued at the written request of the contractor (appellant) to be submitted for tender and registration purposes only and is not valid for any other purpose. The appellant had substantially relied on this certificate to contend that the work under contract was completed satisfactorily and that the respondent no.1 therefore, cannot have any grievance in respect of the work under the contract as undertaken by the appellant.

6. It appears that the respondent no.1 noticed defects in the works executed by the appellant under the contract. Respondent no.1 therefore by two separate letters dated 6 April 2015 addressed to the respondent no.2-bank, invoked the bank guarantees in question. These letters are similarly worded except for the amounts. The relevant portion of one of the letter reads thus :

" We refer to the subject Guarantee issued by you ("Guarantor") and herewith submit our first written demand to pay us the amount of Rs.34,00,000/- (Rupees Thirty Four Lakhs only) (the "Guaranteed Amount"). This amount claimed is due by way of loss or damage caused to or would be caused to or suffered by us by reason of breach by the Contractor (M/s. S.Satyanarayana and Co) of the terms and conditions contained in the LOA.

Kindly remit the said amount of Rs.34,00,000/-(Rupees Thirty Four Lakhs only) to our bank account by Real Time Gross Settlement (RTGS) as per details mentioned below."

7. After invoking the bank guarantee respondent no.1 thereafter addressed a letter dated 7 April 2015 to the appellant recording of the breach of the conditions of LOA. Respondent no.1 stated as under :

" It is to inform you that you are in breach of the terms and conditions contained in the LOA inter alia on account of delays and defects. By reason of such breach, loss or damage is caused to us and would be caused to us and suffered by us."

8. It is the case of respondent no.1 that the respondent no.2-bank entered into an unwarranted correspondence with the appellant and intentionally delayed remitting the payments under the bank guarantees. As the parties in terms of clause 55.2 of the contract had agreed to refer the disputes arising under the contract for an arbitration, the appellant moved the learned single Judge by filing an application under section 9 of the Act seeking an injunction against enforcement of the bank guarantees by respondent no.1. Respondent no.1 appeared before the learned Single Judge and filed its reply affidavit. By the impugned order the learned single Judge rejected the said application filed by the appellant.

9. Learned counsel for the appellant in assailing the impugned order has made the following submissions :

(i) The appellant was entitled for an injunction against enforcement of the bank guarantee as this is a case where the respondent no.1 has played a fraud.

(ii) Respondent no.1 was invoking bank guarantee for malafide and collateral purposes dehors the original contract;

(iii) The invocation of the bank guarantee is in fact a counter-blast as the Appellant has undertaken legal proceedings in respect of another contract of dredging awarded to the appellant by respondent no.1;

(iv) The general conditions of contract were required to be considered by the learned single Judge. These conditions were required to be read into clauses 1 and 2 of the bank guarantee. The submission is that the terms and conditions of the original contract stand incorporated in conditions of the bank guarantee. It is submitted that such reading of the clauses of the bank guarantee would show that the respondent no.1 had no authority to invoke the bank guarantee in as much as the work under the contract was satisfactorily completed and a certificate namely Experience Certificate dated 18 August 2014 was issued in favour of the Appellant. Once such a certificate is issued grievance about any defect in the contract could not have been raised by the respondent no.1.

(v) The facts of the case demonstrate that this is a case falling within the exceptions which would warrant an injunction to restrain the respondent no.1 from enforcing the bank guarantees.

In support of these submissions, learned counsel for the appellant has relied on the decision of the Supreme Court in case of Hindustan Construction Co. Ltd. Vs. State of Bihar and Others, AIR 1999 SC 3710 : (2000) 99 CompCas 297 : (1999) 3 CTC 618 : (1999) 8 JT 142 : (1999) 6 SCALE 486 : (1999) 8 SCC 436 : (1999) 3 SCR 554 Supp : (2000) 1 UJ 336 : (1999) AIRSCW 3747 : (1999) 9 Supreme 1 and the decision of the learned Single Judge of this Court in case of Western Coalfields Ltd. and Another Vs. Rajesh and Another, (2012) 1 BC 395 : (2012) 1 MhLj 394 .

10. On the other hand, in supporting the impugned order learned counsel for respondent no.1 submits that the contentions as raised on behalf of the appellant is misconceived in as much as the bank guarantee is irrevocable and unconditional which entitle the respondent no.1 to invoke the bank guarantee on account of the defects in work as discovered by the respondent no.1 during the defect liability period. It is submitted that the appellant is in fact calling upon the Court to adjudicate on the issue as to whether any defects have arisen, which according to respondent no.1 can never be the scope of proceedings under section 9 of the Act, as also it would be ex-facie contrary to the terms and conditions of the bank guarantee. It is submitted that respondent no.1 is the sole judge to take a decision to invoke and enforce the bank guarantees. In support his submissions learned counsel for respondent no.1 has placed reliance on the decision of the Supreme Court in the case of BSES Ltd. (Now Reliance Energy Ltd.) Vs. Fenner India Ltd. and Another, AIR 2006 SC 1148 : (2006) 1 ARBLR 388 : (2006) 2 BC 20 : (2006) 130 CompCas 8 : (2006) 2 CompLJ 430 : (2006) 2 CTC 137 : (2006) 1 CTLJ 228 : (2006) 2 JT 192 : (2006) 143 PLR 227 : (2006)

2 SCALE 186 : (2006) 2 SCC 728 : (2006) AIRSCW 721 : (2006) 2 Supreme 106 and the decision of the learned Single Judge of this Court in M/s. ANCL and Co. (India) Pvt.Ltd vs. Corporation Bank dated 17 January 2013 in Arbitration Petition (Lodging) No. 67 of 2013.

11. It is well-settled that a bank guarantee is an independent contract between the bank and the beneficiary and thus the bank guarantee is required to be honoured in accordance with its terms. If the bank guarantee is unconditional and irrevocable the exceptions in the bank not honouring its obligations under the bank guarantee are firstly a fraud of which the bank has a clear notice. Such a fraud must be of an egregious nature so as to vitiate in its entirety the underlying transaction. The nature of the fraud should be such that the beneficiary of the bank guarantee is seeking to be benefited from such fraud. The second exception are the "special equities" such as an irretrievable injury or irretrievable injustice which would be caused to the party at whose instance the bank guarantee is issued and if an injunction at the relevant time is not granted the party can never be compensated for such an injury. U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd., (1987) 2 ARBLR 279 : (1988) 1 CompLJ 39 : (1987) 4 JT 406 : (1987) 2 SCALE 1149 : (1988) 1 SCC 174 : (1988) 1 SCR 1124 and BSES Ltd. vs Fenner Ltd. (supra)} Adverting to these settled principles of law we consider facts of the present case.

12. Under the bank guarantee in question the respondent no.2-bank has agreed to irrevocably and unconditionally pay to the respondent no.1 the amounts under the bank guarantees, against any loss or damage caused or suffered, or would be caused or suffered by the respondent no.1 by reason of any breach by the contractor (appellant), of any of the terms contained in the LOA. These payments have been undertaken to be made by respondent no.2-Bank without proof or condition or without demur or reservation, contest, recourse, protest and without any inquiry from the respondent no.1 or the appellant and merely on a demand from the respondent no.1 stating that the amount claimed is due by loss or damage caused or would be caused or suffered by the respondent no.1 by reason of any breach by the appellant of any of the terms of the conditions contained in the LOA. These conditions are contained at clauses 1 and 2 (page 315) which reads thus :

1. " The Guarantor at the request of the Contractor hereby irrevocably and unconditionally undertakes and covenants to pay to the Client an amount not exceeding Rs.34,00,000/-(Rupees Thirty Four Lakhs only) against any loss or damage caused to or suffered or would be caused to or suffered by the Client by reason of any breach by the Contractor of any of the terms and conditions contained in the "LOA"

2. The Guarantor does hereby undertake to pay the amounts due and payable under this guarantee without further proof or conditions and without demur, reservation, contest, recourse or protest and without any enquiry of the Client or the Contractor, merely on a demand from the Client stating that the amount

claimed is due by way of loss or damage caused to or would be caused to or suffered by the Client by reason of any breach by the Contractor of any of the terms and conditions contained in the LOA. Any such demand made on the Bank shall be conclusive as regards the amount due and payable by the Bank under this Guarantee. However, the Guarantor's liability under this Guarantee shall be restricted to an amount not exceeding Rs.34,00,000/-(Rupees Thirty Four Lakhs only) (the "Guaranteed Amount").

(Emphasis supplied)

It is thus, clear that the nature of the bank guarantees is irrevocable and unconditional and there is an obligation on respondent no.1 to honour the same without any reservation, contest or protest and any inquiry to that effect with the appellant.

13. The contention as urged on behalf of the appellant that there is a fraud on the part of respondent no.1 in invoking the bank guarantee is misconceived and without any basis. There is no material whatsoever placed on record even to remotely suggest that there is any fraud which is to the knowledge of the respondent no.2-bank of which respondent no.2-bank is seeking to take benefit in invoking the bank guarantees in question. It is therefore, rather surprising as to how such a submission is being advanced.

14. The next submission as urged on behalf of the appellant is that the action of invoking the bank guarantee on the part of respondent no.1 is a counter-blast in view of the fact that the appellant had raised a dispute against the respondent no.1 in respect of another contract for which the appellant had approached this Court by filing proceedings under section 9 of the Arbitration and Conciliation Act being Arbitration Petition (Lodging) No. 505 of 2014. Having examined this plea, we do not think that there is any merit in this contention. There is no material to show that invoking of the bank guarantees in question has anything to do with the dispute in respect of the other contract.

15. Learned counsel for the appellant has vehemently contended that the "experience certificate" dated 18 August 2014 issued by the respondent no.1 would show that the work executed by the appellant under the contract had been completed to the satisfaction of respondent no.1. It is contended that respondent no.1 could not have invoked the bank guarantee during the defect liability period as in any event, under the general terms of contract it is the liability of the appellant to remove the defects that would be noticed by respondent no.1. It is submitted that the other conditions of contract were therefore, required to be seen and since the defects would be remedied by the appellant during the defect liability period invocation of the bank guarantee at the hands of respondent no.1 was totally unwarranted and therefore it ought to be held that invocation of the bank guarantee is malafide and for collateral purposes and a fraud. In support of this contention, learned counsel for the appellant has drawn our attention to various clauses of the conditions of the contract which we have noted above.

16. On examining the general conditions of contract and the document of the bank guarantee's in question, we find that there is no merit in this submission as urged on behalf of the respondents. The contention of the appellant if accepted, would amount to re-writing the terms and conditions by the bank guarantee. The terms of the conditions of bank guarantee are explicit. The respondent no.1 is the sole judge in regard to the invocation and enforcement of the bank guarantee. The wide amplitude of clauses 1 and 2 of the bank guarantee (supra) makes it clear that the contracting parties to the bank guarantee have left it to the absolute discretion of respondent no.1 in regard to its invocation when defects are discovered by respondent no.1. The appellant is not in a position to absolutely demonstrate that the parties agree that there is no defect and/or requirement of further repairs during the defect liability period. On the contrary, it is the case of the appellant that if such defects are noticed or have occurred the same would be remedied by the appellant as the defect liability period as in operation. This being the position, and admittedly a dispute having arisen between the parties on the issue of the defects, the invocation of the bank guarantees at the hands of the respondent no.1 in the facts of the case certainly is outside the exceptions warranting an injunction. The terms of the bank guarantee are required to be honoured by the bank. Such submissions which go contrary to the terms of the bank guarantee cannot be countenanced.

17. Learned counsel for the appellant relying on the experience certificate submits that once the experience certificate dated 18 August 2014 was issued by respondent no.1 a stand contrary to the same cannot be taken by respondent no.1 and invoke the bank guarantee. This submission cannot be accepted for two reasons firstly, the experience certificate dated 18 August 2014 is not a completion certificate issued by respondent no.1 as per the terms and conditions of the contract. This certificate appears to have been issued at the request of the appellant to enable the appellant to submit the same for a tender and for registration purposes which is clear from the note recorded below the certificate which reads thus :

"Note: 1. This certificate is issued on the written request of the Contractors to submit for tendering and registration purpose only and is not valid for any other purpose.

2. The Defects liability period starts from the date completion (22.07.2014) as per the Contract Agreement."

A reference to the work being satisfactory as contained in this experience certificate therefore, would be of no consequence qua the bank guarantees and for the appellant to contend that the appellant ceases to have any liability in respect of the work under the contract in question. The appellant's contention that the defects which were pointed out by respondent no.1 after the date of completion were rectified to the satisfaction of respondent no.1 is also of no consequence as it is not the case of the appellant that the defect liability period has come to an end and that invocation of the bank guarantee is after the expiry

of the defect liability period.

18. On behalf of the appellant reliance is placed on the decision of the Supreme Court in the case of Hindusthan Construction Co.Ltd vs State of Bihar (supra). In this decision the Supreme Court was dealing with a case where the bank had issued a bank guarantee relating to mobilisation advance which was in terms of clause 9 of the principal contract. The case of the Hindusthan Construction Company Ltd. (HCCL) was that the bank guarantee could be invoked only if the amount lent to HCCL as "mobilisation advance" had become payable in terms of clause (9) of the principal contract which was specifically referred in the bank guarantee and that the conditions contemplated by clause 9 did not exist and hence invocation was bad. It is in this context the Supreme Court in paragraph 13 observed that a condition in the original contract having been incorporated in the bank guarantee the bank guarantee could not be said to be unconditional or unequivocal conferring an unfettered right to invoke the same by a beneficiary. However, facts of the present case are quite different. It is not in dispute that the defects are noticed by the respondent no.1 and that the bank guarantee postulates its invocation if such defects are noticed by the respondent no.1. There is a dispute between the parties in regard to the nature of the defects or whether at all they have arisen which would be an issue to be gone into in the arbitration proceedings. However, the same cannot be a ground to injunct the respondents against enforcement of the bank guarantee. In the light of these facts, reliance of the appellant on the decision in the case of Hindusthan Construction Company Ltd. is totally misplaced.

19. Another decision as relied on behalf of the appellant is in the case of Western Coalfields vs Rajesh S/o Nandlal Biyani (supra) rendered by the learned single Judge of this Court. The facts which fell for consideration of the learned Single Judge in the said decision are totally uncomparable. This was a case where invocation of the bank guarantee was not for the purpose or reasons stated in the bank guarantee but, for some extraneous reasons in as much as the appellant Western Coalfields had invoked the bank guarantee for the reason that initially a fake bank guarantee was submitted by the respondents which later on came to be replaced along with penal interest for the period during which fake bank guarantee remained with the said appellant. The learned single Judge held that invocation thus was not for breach of the terms of the contract but for extraneous reasons and thus held that injunction which was granted by the trial Court was justified. The learned single Judge also held that in fact the invocation was contrary to the terms of the bank guarantee which permitted invocation for failure/negligence in the performance of terms and conditions of the contract. Having considered the facts of the said decision, we are certain that this decision is of no avail to the appellant.

20. In the present case, the demand as raised by the respondent no.1 is in terms of the bank guarantee. The respondent no.1 has shown prima facie material that loss or damage is caused to the respondent no.1 which would be an acceptable

reason under the bank guarantee for respondent no.1 to invoke the same. Thus, the demand for enforcement of the bank guarantee as raised by respondent no.1 is in accordance with the terms of the bank guarantee and cannot be faulted. We therefore find no force in the submission as made on behalf of the appellant that invocation of the bank guarantee by the respondent no.1 is not in consonance with the terms and conditions of the bank guarantee.

21. In the light of the aforesaid deliberation, we find no merit in the present appeal. Appeal is accordingly dismissed. No order as to costs.