(2008) 04 DEL CK 0106

In the Delhi High Court

Case No : CS (OS) 1347 of 2007

Smart Chip Ltd. APPELLANT

Vs

Central Bureau of Narcotics and Another RESPONDENT

Date of Decision : 09-04-2008

Acts Referred:

Arbitration and Conciliation Act, 1996 — Section 8, 8(1), 9

Citation : (2008) 04 DEL CK 0106

Hon'ble Judges : S. Ravindra Bhat, J

Bench : Single Bench

Advocate : S.K. Mehra and Anupama Khatrin, for the Appellant; Rajeeve Mehra and Sumesh Bajaj for Defendant No. 1/Union of India, for the Respondent

Judgement

S. Ravindra Bhat, J.

IA 1195/2008 (Under Section 8 of Arb. Act)

1. This is an application u/s 8 of the Arbitration and Conciliation Act, 1996 (hereafter referred as the Act) seeking reference of the disputes which are the subject matter of the present suit, to arbitration.

2. The brief and undisputed facts emerging on a reading of the plaint averments and application are narrated as follows:

3. The plaintiff and the defendants entered into an agreement on 7.12.2001 by which the plaintiff was nominated as a ''Project Implementer''. The work specifications, terms and conditions of the contract were outlined in various clauses of the Agreement. Originally, as per Clause 16, the plaintiff would submit one surety in place of bank guarantee, spelt out in the tender as a trade off for 20% advance payment and that a solvent surety certified by any scheduled Bank could be sufficient.

4. The Agreement also incorporated the following conditions relating to termination and dispute resolution through arbitration:

37. Termination

37.1. No breach of performance by the Program Implementer shall be treated as giving rise to termination of the contract by the Department unless the CBN had given a notice of forty five days to enable the supplier to carry out such corrections, updates and take such other necessary action to bring Hardware, Software and performance as per the satisfactory performance level.

37.2. Continued failure by the Project Implementer to rectify legitimate deficiency identified by the department or increasing the efficiency at par, CBN shall have a right to terminate the contract by giving 90 (ninety) days notice to the Project Implementer for winding up of operations. However, in order to find out reasons of failure and efforts made by the Project Implementer to improve the efficiency, CBN may constitute a committee consisting of representative of CBN and Project Implementer to review the efforts made by the Project Implementer and expectation of the department. This committee will submit its recommendations within the period allowed by the Narcotics Commissioner or otherwise agreed by any designated authority.

37.3. Notwithstanding anything contained in this agreement the Government shall have power either to revoke or cancel the contract at any time on the expiry of notice of 90 days to the Project Implementer without assigning any reason.

37.4. In the event of termination of this contract, based on the recommendations of the committee or otherwise, department will have to acquire all Hardware, Software, cards and consumables on as is where is basis installed at all the Centres of the department at the price to be determined by government approved valuer/experts. The department shall be free to complete the project at the risk and cost of the Project Implementer.

37.5 In the event the Project Implementer has to suspend services being placed in a position of not being able to discharge the responsibility under the contract for reasons solely beyond the control of the Project Implementer and such suspension continues for more than a period of 90 days, the contract shall be deemed to be terminated.

38. Arbitration

38.1. CBN and Project Implementer shall make every effort to resolve amicably by direct negotiation in case of disagreement or dispute arising between them under or in connection with this contract.

38.2. To decide whether there is a dispute within the meaning of the contract about the contractual obligation of the entire parties, reference shall be made to the terms and conditions of the tender documents, bid submitted by the supplier and any other correspondence made on the subject or relevant to the subject between the parties.

38.3. If after 90 days after the commencement of direct negotiation, CBN and Project Implementer are unable to resolve any dispute amicably under this contract, either party may resort to arbitration.

38.4. If a dispute arising out of and/or in connection with and/or in relation to this agreement or breach or termination here of exists between the parties and the same cannot be settled within thirty (30) days by mutual discussions. Such disputes or differences shall be referred to Arbitration under the provisions of the Arbitration and Conciliation Act, 1996.

5. According to the plaintiff, a fact not denied by the defendant, parties agreed to amend the conditions subsequently on 7.8.2003. The condition relating to Bank Guarantee was substituted in the following terms:

Clause 16:

The Project Implementer as per the discussions with the Department has submitted a Bank Guarantee by Indian Overseas Bank of Rs.14,31,075/- as a Performance Guarantee. The said Bank Guarantee shall be renewed by the Project Implementer from time to time till the completion of the project.

6. The conditions relating to termination and arbitration was substituted. The amended contract stipulated, in that regard as follows:

37. Termination

37.1. Delays in the Project Implementer''s performance: Project Implementer shall perform in accordance with the time schedule specified by the Government as indicated in the Implementation Schedule. Any delay by the Project Implementer in the performance of its contract obligations shall render the Project Implementer liable to, at the option of the Government, any or all of the following:

(i)Forfeiture of its Bank Guarantee; and/or

(ii) Termination of the contract for default.

However, this clause is subject to the fulfillment of the provisions as per Clauses 37.2, 37.3, 37.4 and 37.5.

37.2. No breach of performance by the Program Implementer shall be treated as giving rise to termination of the contract by the Department unless the CBN had given a notice of forty-five days to enable the supplier to carry out such corrections, updates and take such other necessary action to bring Hardware, Software and performance as per the satisfactory performance level.

37.3. Continued failure by the Project Implementer to rectify legitimate deficiency identified by the department or increasing the efficiency at par, CBN shall have a right to terminate the contract by giving 90 (ninety) days notice to the Project Implementer for winding up of operations. However, in order to find out reasons of failure and efforts made by the Project Implementer to improve the efficiency, CBN may constitute a committee consisting of 1) a representative of CBN 2) a representative nominated by the Ministry of Finance (Department of Revenue 3) an expert in the area of hardware and software as recommended by the Ministry of Finance (Department of Revenue) and 4) a representative of Project Implementer to review the efforts made by the Project Implementer and expectations of the department. This committee will submit its recommendations within the period allowed by the Narcotics Commissioner or otherwise agreed by any authority designated by the Ministry of Finance (Department of Revenue).

37.4. Notwithstanding anything contained in this agreement the Government shall have power either to revoke or cancel the contract at any time on the expiry of notice 90 days to the Project Implementer without assigning any reason.

37.5. In the event of termination of this contract, based on the recommendations of the committee or otherwise, department will acquire all Hardward, Software, cards and consumables supplied by the Project Implementer for the project on as is where is basis installed at all the Centres of the department, in respect of which payment as indicated in the Implementation Schedule has already been made by CBN to the Project Implementer, at no extra cost, and all other material at the price to be determined by the Government approved valuer/expert. The department shall be free to complete the project at the risk and cost of the Project Implementer.

37.6. In the event the Project Implementer has to suspend services being placed in a position of not being able to discharge the responsibility under the contract for reasons solely beyond the control of the Project Implementer and such suspension continues for more than a period of 45 days, the contract shall be deemed to be terminated.

37.7. Termination for Insolvency: The Government may at any time terminate the contract by giving a written notice of 30 days to the Project Implementer without compensation to the Project Implementer, if the Project Implementer becomes bankrupt or otherwise insolvent, provided that such termination will not prejudice or effect any right of action or remedy which has accrued thereafter to the Government.

38. Arbitration

38.1. CBN and Project Implementer shall make every effort to resolve amicably by direct negotiation in case of disagreement or dispute arising between them under or in connection with this contract.

38.2. To decide whether there is a dispute within the meaning of the contract about the contractual obligation of the entire parties, reference shall be made to the terms and conditions of the tender documents, bid submitted by the supplier and any other correspondence made on the subject or relevant to the subject between the parties.

38.3. If CBN and Project Implementer are unable to resolve the dispute within a period of 30 days, the matter will be referred to arbitration as indicated in 38.4 below.

38.4. Arbitration: All disputes, differences, claims and demands arising under or pursuant to or touching the contract shall be referred to the sole arbitrator to be appointed by the Secretary, Department of Revenue, Ministry of Finance, Govt. of India. The award of the sole arbitrator shall be final and binding on both the parties under or in accordance with the provisions of the Arbitration and Conciliation Act, 1996 or any statutory modification or re-enactment thereof for the time being in force. Such arbitration proceedings shall be held at Gwalior, Madhya Pradesh.

7. The plaintiff furnished a bank guarantee, issued by the second defendant bank? i.e. Canara Bank, which was valid up to 30.7.2007. It was earlier issued on 26.7.2005. Initially, it was for a period of one year and subsequently re-validated up to 30.7.2007.

8. The plaintiff alleges that the defendant sought to illegally impose a condition that it had to extend the bank guarantee for at least one year by its letter dated 9.7.2007. The letter was marked to the Canara Bank with a request to ensure that the guarantee was renewed by the plaintiff and in case the plaintiff did not renew it by 29.7.2007, the letter was to be treated as a claim thus seeking encashment of the bank guarantee. The present suit was triggered by this communication.

9. The plaintiff alleges that it never had any intention of evading from its lawful obligations and in fact wanted to fulfill its terms fully. It further alleges that the defendant has withheld large amounts of money and is seeking to pressurize it unfairly and illegally while trying for encashment of bank guarantee. In these circumstances, it approached the Court seeking permanent and mandatory injunction against the first defendant from encashing the bank guarantee, issued by the second defendant.

10. The applicant - defendant has relied upon the Clause 38 and contended that the disputes raised are squarely covered in its terms and that since the efforts to settle too have been of no avail, this Court should exercise its powers u/s 8 and refer the disputes to arbitration. The plaintiff had adverted to the conditions of the contract and also that the parties are bound by Clause 38 which clearly stipulates that all disputes, differences, claims and demands arising under or pursuant to or touching the contract shall be referred to the sole Arbitrator to be appointed by the Secretary, Department of Revenue, Ministry of Finance, Govt. of India, in terms of Clause 38(4).

11. The applicant - defendant also states that the bank guarantee was to be kept alive by the plaintiff till completion of the project. The same was an integral part of the amended contract and bound both the parties. Learned Counsel for the applicant has relied upon the condition in the bank guarantee, i.e. Clause 8, which reads as follows:

...The dispute relating to this guarantee shall be resolved as per the terms and conditions of the said Agreement and it''s Addendum. The Bank Guarantee shall be operative only on completion of all responsibilities as per the agreement including zero date of implementation as provided by Smart Chip Limited.

12. The plaintiff, in its reply, has denied that the disputes of the present Bank can be subject to arbitration. Reliance is placed upon Clause 37 to say that in terms of Clause 37.2, the defendant was under an obligation first to issue notice to show deficiencies within a period of 45 days and subsequent to such event, if the plaintiff failed to carry out proper rectification, the defendant was empowered to terminate the contract by giving 90 days notice. The defendant also relies upon Clause 38 itself and contends that various steps or sequence of events contemplated do not visualize that disputes can be straightway referred to the Arbitrator. It was contended by learned Counsel for the plaintiff that the defendant did not ever seek recourse to either Clause 37 or even Clauses 38.1, 38.2 and 38.3. It is submitted that if the defendant - applicant is contending today that the disputes are arbitrable, an obligation was cast upon it to first call upon the plaintiff and try to resolve them through mutual negotiations and later submit it to the Committee contemplated under Clause 37.3. In the absence of these steps, it was contended that this Court cannot invoke its powers under Clause 39.

13. It was also contended that the plaintiff''s suit for injunction restraining the defendant from encashing the bank guarantee, cannot per se arbitrable.

14. From the above narrative, it is evident that the parties to the contract dated 7.12.2001 had initially agreed that the advance amount given to the plaintiff could be secured through a surety, in accordance with the original Clause 16. However, for reasons known to both the parties, this condition was substituted on 7.8.2003 whereby the requirement of surety was substituted with the condition of the plaintiff having furnished to a bank guarantee. It is not in dispute that the plaintiff complied with this condition and did furnish a bank guarantee which was renewed from time to time. The bank guarantee issued by defendant No. 2 at the behest of the plaintiff was valid till 30.7.2005.

15. Apparently, the defendant No. 1 formed the opinion that the plaintiff was reluctant to extend the bank guarantee and that was construed as a cause for its invocation. It, Therefore, wrote to the second defendant - bank on 9.7.2005 stating that in case the guarantee were not extended the proceeds were deemed to have been encahsed on 27.1.2005. The question is whether this cause of action is covered by Clause 38 or whether the failure of the defendant to seek recourse to the sequential procedure outlined in Clause 37 precludes maintainability of the present application u/s 8.

16. Section 8 of the Act is cast in imperative terms; it reads as follows:

8. Power to refer parties to arbitration where there is an arbitration agreement-
(1) A judicial authority before which an action is brought in a matter which is the

subject of an arbitration agreement shall, if a party so applies not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration.

(2) The application referred to in Sub-section (1) shall not be entertained unless it is accompanied by the original arbitration agreement or a duly certified copy thereof.

(3) Notwithstanding that an application has been made under Sub-section (1) and that the issue is pending before the judicial authority, an arbitration may be commenced or continued and an arbitral award made.

17. The object of the above provision is to ensure that where the parties have contracted for a mutually dispute resolution through arbitration, the Court should respect that regardless of the plaintiff''s espousing his cause of action in respect of the normal civil process. The mandatory form is to be gleaned from the use of the expression "judicial authority" and "shall". In such circumstances, the Court is expected to ensure that the intention of the parties to have the disputes resolved through arbitration is given effect to.

18. The objections raised by the plaintiff to the reference u/s 8 are two fold. One is premised on an application of Clause 37 which envisages that the defendant - applicant should follow certain steps before it can seek forfeiture of bank guarantee or terminate the contract for any default. Clause 37.1 enables the defendant employer to seek recourse to such sanctions. However, they are subject to Clauses 37.2 and 37.3. These too in turn require the defendant employer to give notice, asking the programme implementor to cure deficiencies in a time bound manner and in case such deficiencies have not been cured to terminate the contract after issuing 90 days notice. Clause 37.4, however, gives overriding power to either revoke or cancel the contract at any time by expiry of 90 days to the Project Implementer without assigning any reason.

19. Clause 38 follows Clause 37. It obliges both parties to resolve their disputes amicably by negotiations. Clause 38.2 states that to decide whether there is a dispute about the meaning of contract between the parties reference shall be made to the terms and conditions and finally Clause 38.3 states that if the defendant and Project Implementor are unable to resolve the disputes within 30 days, the matter can be referred to arbitration.

20. The main submission of the plaintiff was that none of the moves contemplated in Clause 37.3 or 38.2 were resorted to and that the defendant has unilaterally sought to invoke the bank guarantee.

21. A conjoint reading of both the conditions, i.e. Clause 37 and 38 with Clause 8 of the bank guarantee would show that the later was conceived as an independent instrument and that any disputes relating to it too would be resolved in terms of the conditions of the Agreement. Thus whether the obligation to keep the bank guarantee alive or whether the failure of the plaintiff

to comply with such terms or other terms amounted to breach of contract, could not have been the subject matter of Clause 8 of the bank guarantee. Even, if it were assumed (as contended by the plaintiff) that Clauses 37.2 and 37.3 and the conditions of Clause 38 have not been followed, the fact remains that according to the plaintiff itself there are disputes arising out of the contract between the parties. This dispute pertains to the alleged unlawful and unjustified invocation of the bank guarantee. Whatever be the merits of such a dispute, there can be no gainsaying that it would be squarely covered under Clause 38.4, in that it is a dispute arising out of the contract and relating to interpretation of its terms.

22. During the course of the hearing, the applicant - defendant had relied upon a communcation dated 8.8.2007 addressed by the plaintiff itself which after narrating several facts and events, stated as follows:

21. Thus under the above said Clauses, there are many disputes which needs to be resolved and no effort are being made by the department to sort the disputes and by this letter we wish to resolve all the disputes and recover our legitimate dues, within 30 days from receiving this letter by your office. If the disputes are not resolved within 30 days then we request you to refer this matter to Arbitration by appointing an impartial and neutral arbitrator under Clause 38.4 of the amended agreement.

23. In view of the above reasons, this Court is of the opinion that the disputes sought to be agitated in these proceedings are arbitrable. As far as the argument relating incapability or lack of jurisdiction to the Arbitrator to issue injunction is concerned, apart from the fact that the plaintiff adduced the authority in that regard, there exists no impediment in law preventing an Arbitrator, from issuing an injunction. An injunction or even a declaration are reliefs that can be granted by the Court. All that happens when parties enter into an arbitration agreement is that in stead of the Court, they substitute the forum, by an agreed adjudicator in the shape of the Arbitrator.

24. As a matter of fact in reply to the present application itself in paragraph 17, the plaintiff states that it has a right u/s 9 of the Arbitration and Conciliation Act to approach the Court for protection.

25. In view of the above, the application has to succeed. It is accordingly allowed.

IA 1195/2008 is accordingly disposed of.

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26. During pendency of the present suit, the Court had initially issued an order restraining the defendant from encashing the bank guarantee. That order has been kept alive and on 29.1.2008, the plaintiff was directed to secure extension of validity of the bank guarantee till December 2008. The said direction shall bind the plaintiff. In case, the arbitration proceedings do not end before 31.12.2008, the bank guarantee shall be renewed for a further period of one year or till the completion of the arbitration proceedings whichever is later.

27. In view of the orders in is No. 1195/2008, the dispute raised by the plaintiff is hereby referred to arbitration in terms of Clause 38.4 of the amended agreement entered into between the parties on 7.8.2005. The suit has to, Therefore, be accordingly dispose of.

28. The suit, CS(OS) 1347/2007, is disposed of in the above terms.

