

(1998) 04 DEL CK 0077
In the Delhi High Court
Case No : F.A.O. (OS) 244 OF 1993

U.P. Jal Nigam and Another		APPELLANT
	Vs	
M/s Bhasin and Associates Ltd. and Another		RESPONDENT

Date of Decision : 16-04-1998

Acts Referred:

Citation : (1998) 3 AD 334 : (1998) 73 DLT 26

Hon'ble Judges : Y.K. Sabharwal, J;C.K. Mahajan, J

Bench : Division Bench

Advocate : Ms. Sandhya Goswami, for the Appellant; Ms. Geeta Mittal, Ms. Arti Bansal and Ms. Puja Jain, for the Respondent

Judgement

C.K. Mahajan, J.—The present appeal is directed against the judgment and order dated September 30, 1992 disposing of an application under Order 39 Rules 1 and 2 CPC restraining the appellants from encashing the bank guarantee No. 24/90006/89 dt. 11.1.1989 and 24/90032/89 dt. 11.2.1989 on the basis of the letter of demand dated 11-7-1991.

2. The appellants invited tenders for an I.D.A. Credit Project on 1st June, 1987 for construction and commissioning of raw water intake and water treatment plant of 100 m.l.d. capacity including supply, delivery, erection of all civil, mechanical and electrical equipments, machinery etc. The contract was awarded to the respondent No.1/plaintiff for the value of Rs. 574.416 lakhs. The work was to be completed within 45 months from the date of commencement of the contract. The value of the contract was revised to Rs. 542.416 lakhs. Formal contract was signed and in terms of the said contract, two bank guarantees were furnished by the plaintiff/respondent No.1 given as security for performance of the obligations towards the appellants and the bank, in terms of the bank guarantees, undertook to indemnify the appellants against any loss or damage caused to or suffered by it by reason of any breach by the contractor of the terms and conditions of the contract.

3. According to the appellants respondent No.1/plaintiff defaulted in the execution of the contract and the action of the respondent No.1/plaintiff resulted in delay and stoppage of execution of the work resulting in loss and injury to the appellants. In the course of execution of the contract, controversies arose between the appellants and the respondent No.1/plaintiff with regard to execution of the contract. The appellants sought to invoke the two bank guarantees furnished by respondent No.1/plaintiff in favor of the appellants. The respondent NO.1/plaintiff to stop the encashment of the bank guarantees filed a suit for permanent injunction. An application was also filed for an interim injunction and relief of injunction was sought on the ground that (a) invocation of the bank guarantees was not in accordance with the terms of the bank guarantees and (b) special equities justified the grant of injunction. It may also be pointed out that there is an arbitration clause in the agreement providing for reference of the disputes to arbitration. The respondent No.1/plaintiff did not resort to the arbitration clause but moved the court and obtained an injunction restraining the appellants from encashing the bank guarantees.

4. The appellants contended that the bank guarantees were invoked in accordance with law and they were entitled to encash them. On the plea of special equities it was contended that the respondent No.1/plaintiff was at fault and on that account the appellants suffered heavily. Thus, they were entitled to invoke the bank guarantees. A plea of territorial jurisdiction was also taken up and it was contended that the contract ousts the jurisdiction of the Delhi Court.

5. The learned Single Judge allowed the application and granted injunction by holding that the bank guarantee had not been invoked in terms of the bank guarantees in as much as no loss or damage is alleged to have been suffered in the said letter of invocation and the order of the Superintending Engineer, referred to in the letter of the Executive Engineer of the same date and relied upon as a part of the invocation letter, was not on record and could not be relied upon. The learned Single Judge did not go into the plea of special equities and confined his findings on the question of invocation of bank guarantee. The preliminary objection with regard to jurisdiction raised by the appellants was rejected as being without merit.

6. The relevant portions of two bank guarantees are reproduced hereunder:

"We Punjab & Sind bank, IBD, 6, Scindia House, New Delhi (hereinafter referred to as the Bank) do hereby undertake to pay to the Nigam an amount not exceeding Rs. 57, 44,160/- against any loss or damage caused to or would be suffered by the Nigam by reason of any breach by the said contractor of any of the terms and conditions contained in the said tender.

We Punjab & Sind Bank, IBD, 6 Scindia House, New Delhi do hereby undertake to pay the amount due and payable under this guarantee and without any demur merely on a demand from the U.P. Jal Nigam stating that the amount claimed is due by way of loss or damage caused to or would be caused to or suffered by the

U.P. Jal Nigam by reasons of any breach by the said contractor of any of the terms or conditions contained in the said tender or by reason of the contractor's failure to perform the said agreement. Any such demand made on the bank shall be conclusive as regards the amount due and payable by the Bank."

"We Punjab & Sind Bank, IBD, 6, Scindia House, New Delhi guarantors do hereby undertake to indemnify and keep indemnified the Jal Nigam to the extent of Rs. 28, 72,080/-(Rupees Twenty Eight Lakhs Seventy Two Thousand and Eighty only) due to loss or damage caused to or suffered by the Jal Nigam of any breach of the said Tenderors of any breach by them of their terms and conditions contained in the said tender and authorise the said Executive Engineers to recover the same directly from the Guarantors".

"Whereas the guarantors further agree that the amounts due or the amount of damage or loss caused to or suffered by the Jal Nigam are binding on us and we undertake to pay the amount guaranteed hereunder or part thereof as required, without demur within one week of the same being merely demanded by the Executive Engineer".

7. We have heard the counsel for the parties at length and perused the record. We have also examined the letter of the Superintending Engineer.

8. The first guarantee made it clear that the bank had undertaken to pay to the appellants an amount not exceeding Rs.57,44,160/- against loss or damage caused to or would be suffered by the appellants by reasons of breach by the respondent No.1/plaintiff and it undertook to pay the amount due and payable without any demur merely on demand from the appellants.

9. It is contended by the counsel for the appellants that the learned Single Judge ignored the most relevant and vital document while granting the interim injunction restraining the appellants from encashing the bank guarantee. The letter of the Superintending Engineer dated 11th July, 1991 contains a statement of losses caused to the appellants due to lapses, latches, non-performance and breach of the contract on the part of the respondent No.1/plaintiff. The letter was filed with the written statement. The original bears the receipt endorsement of respondent No.1/plaintiff. It is not in dispute that copy of letter of the Superintending Engineer was on record of the suit. It was enclosed to the letter of Executive Engineer which was sent to the Bank invoking the Bank guarantees. The bank guarantee was thus invoked in strict accordance of the terms of the guarantee and as per well settled principles laid down by the courts in this regard.

10. The counsel for the respondent No.1/plaintiff also conceded that the said letter of the Superintending Engineer was filed in Court by the appellants and also admitted receipt of the said letter.

11. The law relating to contractual obligations under the bank guarantee has been well settled by the Supreme Court and the High Courts. The general trend of decisions of the Supreme Court and the various High Courts relating to

guarantees and letters of credit is that such documents are to be honoured as per the terms of the documents and interference is to be resorted to only in exceptional circumstances. Such documents are to be enforced strictly in accordance with the terms of the contents of the instrument. The intention of the parties as gathered from a reasonable construction of the language of a particular contract must govern the decision of the Court as to the assessment of a particular liability thereunder. The liability of the bank to pay the amount of the bank guarantee becomes absolute only after the terms of the bank guarantee are fulfilled.

12. It has been observed by the Supreme Court in *U.P. Cooperative Federation Limited Vs. Singh Consultants and Engineers*, 1988 (1) S 174 that in order to restrain the operation either of irrevocable letter of credit or of confirmed letter of credit or of bank guarantee, there should be serious dispute and there should be 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 negated and the fabric of trading operations will get jeopardised. It was also observed that the bank must honour the bank guarantee free from interference by the Courts otherwise trust in commerce, internal and international, would be irreparably damaged. It is only in exceptional cases, for instance fraud or in case of irretrievable injustice that the Courts should interfere. It was also observed that whether it is a traditional bond or performance guarantee, the obligation of the bank appears to be the same.

13. In a recent judgment of the Supreme Court in *Dwarikesh Sugar Industries Ltd Vs. Prem Heavy Engineering Works (P) Ltd. and another*, 1997 (6) S 450, the aforesaid decision of *U.P. Cooperation Federation Limited* (supra) was relied upon and followed and the Supreme Court observed:

"The law relating to invocation of such bank guarantee is by now well settled. When in the course of commercial dealings an unconditional bank guarantee is given or accepted, the beneficiary is entitled to realise such a bank guarantee in terms thereof irrespective of any pending disputes. The bank giving such a guarantee is bound to honour it as per its terms irrespective of any dispute raised by the customer. The very purpose of giving such a bank guarantee would otherwise be defeated. The courts should, Therefore, be slow in granting an injunction to restrain the realisation of such a bank guarantee. The courts have carved out only two exceptions. A fraud in connection with such a bank guarantee would vitiate the very foundation of such a bank guarantee. Hence if there is such a fraud which the beneficiary seeks to take the advantage, he can be restrained from doing so. The second exception relates to cases where allowing the encashment of an unconditional bank guarantee would result in irretrievable harm or injustice to one of the parties concerned. In most of the cases payment of money under such a bank guarantee would adversely affect the bank and its customer at whose instance the guarantee is given, the harm or

injustice contemplated under this head must be of such an exceptional nature as would override the terms of the guarantee and the adverse effect of such an injunction on commercial dealings in this country.

The second exception to the rule of granting injunction i.e., the resulting of irretrievable injury has to be such a circumstance which would make it impossible for the guarantor to reimburse himself, if he ultimately succeeds. This will have to be decisively established and it must be proved to the satisfaction of the court that there would be no possibility whatsoever of the recovery of the amount from the beneficiary, by way of restitution."

14. In the case of U.P. State Sugar Corporation Vs. Sumac International Limited, 1997 (1) S 568 the Supreme Court has summarised the principles which the courts must apply while considering the question whether to grant an injunction which has the effect of restraining the encashment of bank guarantee.

15. In the present case the invocation issued by the appellants was in accordance with the terms of the bank guarantee and the bank was, Therefore, under an obligation to honour its undertaking and to make the payment. The guarantee was issued to ensure timely performance of the agreement by respondent No.1/plaintiff. The guarantee made it clear that the bank undertook to pay against any loss or damage caused or would be suffered by reason of breach of any of the terms and conditions, and pay without demur, merely on demand, stating that the amount is due by way of loss or damage suffered by reason of breach and lastly demand on bank shall be conclusive. The learned single Judge ought not to have issued an injunction which had the effect of restraining the bank from fulfilling its contractual obligation in terms of the bank guarantee. The injunction of the court ought not to be an instrument nullifying the terms of the contract, agreement or undertaking which is lawfully enforceable. In the second guarantee the bank undertook to indemnify the appellants, due to loss or damage caused to or suffered by the appellant on account of breach of the terms and conditions of the tender and authorised Executive Engineer to recover them from the guarantors. Further the guarantors agreed that amount payable due to damage or loss caused was binding on the bank and the bank undertook to pay without demur on demand by the Executive Engineer. The learned single Judge erred in not considering the letter of the Superintending Engineer. The said letter was not considered though it was on the suit file and had been filed along with the written statement. The said letter was also acknowledged by the respondent No.1/plaintiff. The learned Single Judge examined the terms of the bank guarantee in light of the letter of invocation to the bank dated 11th July, 1991 and did not examine the enclosed letter of the Superintending Engineer detailing the losses and injury and computation thereby showing that the terms of the bank guarantee had been complied with. The learned Single Judge observed in the judgment "I have already noticed that the plaintiff says that the order of the Superintending Engineer mentioned in the above letter was not received by it. The defendant has not placed the same on

record." The learned single Judge lost sight of the fact that the said document was filed by the appellants in the suit and a copy of the same was served on the respondent no.1/plaintiff and acknowledged by them by way of an endorsement. A demand having been made on the bank by the appellants, respondent No.1/plaintiff could not have sought a restraint in the absence of fraud or special equities, and the requirements of the bank guarantee having been met which is evident from a reading of the letter of the Superintending Engineer along with the letter of invocation.

16. We may now examine the crucial conditions in the bank guarantees creating liability of the bank to make payment. The bank undertook to pay against loss or damage caused or would be suffered by the appellants; pay without demur; merely on demand of the appellants stating that the amount is due by way of loss or damage caused by reason of breach by the respondent No.1/plaintiff of the terms and conditions contained in the tender; demand on the bank shall be conclusive as regards the amount due and payable by the bank; undertake to pay amount not exceeding Rs.57,44,160/-.

17. Written notice was given to the bank and to the respondent No.1/plaintiff. The letter of invocation along with the order of the Superintending Engineer was filed in the Court along with the written statement. The guarantees were invoked in strict accordance of its terms as well as settled principles with regard to restraining of encashment of bank guarantees. The learned single Judge did not have the benefit of examining the letter of the Superintending Engineer enclosed with the letter of invocation. The facts showing that all the conditions of the bank guarantee have been fulfilled were disclosed in the demand notice. The liability of the bank to pay the amount of the bank guarantees became absolute. The appellants categorically exercised its judgment that respondent No.1/plaintiff failed to carry out the obligations imposed on it by the agreement. The appellants have shown that they became entitled to recover the amount under the bank guarantee because the respondent No.1/plaintiff failed to perform its obligations under the contract.

18. Learned counsel for the appellants placed reliance on General Electric Technical Services Company Inc. Vs. Punj Sons (P) Ltd. and another, (1991) 4 S 230. In the said case, the respondent executed bank guarantees undertaking to pay the appellants the amount guaranteed without any demur merely on demands stating that the amount is due by way of loss or damage caused to or would be caused to or suffered by the appellants by reason of any breach committed by the respondent No.1/plaintiff of any one of the terms and conditions contained in the agreement or by reason of respondent No.1/plaintiff's failure to perform the agreement and also stating that any such demand by the appellants would be conclusive as regards the amount due and payable by the bank under the guarantee. The respondent No.1/plaintiff having failed to perform the contract within the stipulated time, the appellants terminated the respondent No.1/plaintiff's right to continue the project and

sought encashment of the bank guarantee from the bank on ground of such failure. The respondent No.1/plaintiff filed a suit for injunction against the appellants in the High Court and obtained from the Court stay of encashment of bank guarantee. The question arose as to whether the court was justified in doing so at the instance of the respondent No.1/plaintiff. The Supreme Court allowed the appeal and held that the High Court had misconstrued the terms of the bank guarantee and in terms thereof the restraint order ought not to have been passed and accordingly the order was set aside. Reliance was also placed in *Hindustan Steel Works Construction Ltd. Vs. Tarapore & Co. & Anr.*, 1996 (5) SCA 187. The facts of that case were somewhat similar to the facts of the present case and the decision supports the case of the appellants. The Supreme Court held as under :

"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 bank guarantee is allowed to be encashed, the court should interfere. In this case fraud had not been pleaded and the relief for injunction was sought by the contractor/Respondent No.1 on the ground that special equities or the special circumstances of the case required it. The special circumstances and/or special equities which have been pleaded in this case are that there is a serious dispute on the question as to who has committed breach of the contract, that the contractor has a counter claim against the appellant, that the disputes between the parties have been referred to the arbitrators and that no amount can be said to be due and payable by the contractor to the appellant till the arbitrators declare their award. In our opinion, these factors are not sufficient to make this case an exceptional case justifying interference by restraining the appellant from enforcing the bank guarantees. The High Court was, Therefore, not right in restraining the appellant from enforcing the bank guarantees.

19. Reliance was also placed on a decision of the Supreme Court in *The State Trading Corporation of India Limited Vs . Jainsons Clothing Corporation and Another*, 1994 (4) SCA 332 and *Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another*, in support of the contentions.

20. On a careful consideration of the respective contentions made by the learned counsel for the appellants and respondent No.1/plaintiff, we are of the view that there should be no restraint order against the appellants from invoking/encasing the bank guarantees. The commitments of the bank must be honoured free from interference by the courts unless there are exceptional circumstances, that is to say, a case of fraud or a case where irretrievable injustice would result if the bank guarantee was allowed to be encashed. Fraud is not a ground for obtaining restraint order in the present case. It is, Therefore, to be seen whether irretrievable injustice would be done if the bank guarantee is allowed to be encashed.

21. From a perusal of the facts of the present case we do not find that the case of respondent No.1/plaintiff is covered in the category of "irretrievable injustice" so as to invite an order of restraint. The appellants were not required to prove its case before any arbitrator or any other forum in respect of the loss and damage suffered by it by reason of breach of the contract as a condition for encashment of bank guarantee. If the appellants/beneficiaries of the bank guarantee encashes the same wrongly and without having any cause, the person at whose instance the bank guarantee was given, has a remedy to go to arbitration if there be an agreement for arbitration, or by way of a civil suit. Thus the respondent No.1/plaintiff was not without any legal remedy. When respondent No.1/plaintiff sought an injunction from encashment of bank guarantees, the said respondent knew that the appellant under the bank guarantee would be entitled to encash the same and the bank would honour the same without any demur.

22. So far as the bank guarantee is concerned it is a contract between the bank and the appellants. The respondent No.1/plaintiff, at whose instance the bank guarantee is given, is not a party to the bank guarantee. Therefore, fraud must be shown to have been committed or irretrievable injustice done or caused, only then the respondent No.1/plaintiff would be allowed to injunct the appellant from encashing the same. In the present case if the bank guarantee is allowed to be encashed, we do not see that any irretrievable injustice would be done to the respondent No.1/plaintiff.

23. Even the mobilisation bank guarantee cannot be restrained because this guarantee is a security deposit guarantee also. The letter of invocation, sent by the appellants to respondent No.2-bank, conforms to the terms of the bank guarantee and this is a matter entirely between the appellant and the bank which has given the bank guarantee in question. The parties to the bank guarantee are the bank and the appellants. We are thus of the view that the contentions raised by respondent No.1/plaintiff are without force.

24. For the aforesaid reasons, the impugned judgment cannot be sustained. In the result, the appeal is allowed. The Judgment and order passed by the learned single Judge is set aside. The parties are left to bear their own costs.