
(1992) 11 AHC CK 0058

In the Allahabad High Court

Case No : Writ Petition No. 3273 of 1991 (M/B)

U.P.State Bridge Corporation Ltd., Lucknow

APPELLANT

Vs

National Building Construction Company Limited & Another

RESPONDENT

Date of Decision : 04-11-1992

Acts Referred:

Civil Procedure Code, 1908 (CPC) — Order 39 Rule 1, Order 39 Rule 2
Constitution of India, 1950 — Article 226
Contract Act, 1872 — Section 126

Citation : (1992) 11 AHC CK 0058

Hon'ble Judges : S.Saghir Ahmad, J and S.Dikshit, J

Final Decision : Dismissed

Judgement

S. Saghir Ahmad), J.—This petition was disposed of by us by a short order dated 4th November, 1992. We now proceed to give our reasons.

2. M/s U.P. State Bridge Corporation Ltd. (Petitioner) which is a Government company within the meaning of Section 617 of Indian Companies Act and carries on the work of construction of bridges is pitched, in this petition, against a Government of India undertaking, namely, M/s National Building Construction Company Ltd. which is wholly owned by the Central Government.

3. Respondent No. 1 was awarded a contract by the State of Gujarat for construction of a bridge over river Mahi on the AhmedabadVadodara expressway. It was for this contract that the petitioner had agreed to work as subcontractor of respondent no. 1 under the agreement dated 2881989 (Annexure1) under which responsibility of designing of bridge was entrusted to the petitioner. Clause16 of the aforesaid agreement provided that in case contract of respondent no. 1 with the State of Gujarat was terminated, the agreement between the petitioner and respondent no. 1 regarding subcontract would also stand automatically terminated.

4. In pursuance of the aforesaid agreement, respondent no. 1 had to advance a huge amount of money to the petitioner who was required to furnish two bank

guarantees, namely, (i) Mobilisation Advance Guarantee and (ii) Performance Guarantee which the petitioner furnished on his account with the UCO Bank, NakaHindola Branch, Lucknow for a total amount of Rupees two crores and forty six lacs. Copies of both the bankguarantees have been annexed as Annexures IA and IB to the petition.

5. The contract between the respondent no. 1 and State of Gujarat stood suddenly terminated and consequently the agreement between the petitioner and respondent DO. 1, regarding subcontract also stood terminated. It was at this stage that the opposite party no. 1 invoked the bank guarantees and required the UCO Bank (respondent no. 2) to pay the amount covered by the bank guarantees to respondent no. 1. It is the invocation of the aforesaid bank guarantees which has given rise to the present writ petition in which the principal plea raised on behalf of opposite party no. 1 is that the aforesaid two bank guarantees represent two independent contracts between respondent no. 1 and the UCO Bank and since UCO Bank had unconditionally undertaken to pay to respondent no. 1 the amount of Rs. two crores and forty six lacs, the invocation of the Bank guarantees cannot be objected to by the petitioner as the bankguarantee was given for his benefit and at his instance. It is also pleaded that the present writ petition which relates to contractual obligation between respondent no 1 and respondent no. 2 is not maintainable at the instance of the petitioner.

6. The first contention raised by Sri P.N. Mathur appearing on behalf of the petitioner is that under section 126 of the Contract Act a "Contract of Guarantee" is a contract to perform the promise or discharge the liability, of a third person in case of his default and since in the instant case petitioner had not committed any default in the performance of his promise or discharge of his liabilities, respondent no. 1 was not justified in invoking the bank guarantees.

7. Sections 126 and 127 of the Contract Act which contain relevant statutory provisions are reproduced below:

Section 126. Contract of guarantee, surety, principal debtor and creditor: A Contract of guarantee is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the surety the person in respect of whose default the guarantee is given is called the principal debtor and the person to whom the guarantee is given is called the creditor. A guarantee may be either oral or written.

Section 127. Consideration for guarantee; Anything done, of any promise made, for the benefit of the Principal debtor, may be a sufficient consideration to the surety for giving the guarantee.

8. Contract of guarantee as defined under section 126 of the Act is essentially an agreement which contemplates three persons, namely, the surety who gives the guarantee; the Creditor to whom guarantee is given and the Principal debtor for

whose default guarantee is given, But a simultaneous tripartite contract between surety, creditor and principal debtor is not necessary (See: Prasanjit Mahtha v. The United Commercial Bank Ltd. AIR 1979 Pat. 151 and Punjab National Bank Ltd. v. Sri Bikram Cotton Mills Ltd and Anr. AIR 1970 SC 1973). An implied request to surety by principal debtor is sufficient for the contract of guarantee. Such a request to the surety to undertake obligation need not be an express request.(Raja Jagannath Bakhsh Singh v. Chandra Bhukhan Singh & another AIR 1937 Oudh 19). It is not necessary that the Principal debtor should, as a matter of law, be an express party to the contract of guarantee. It is sufficient that the principal debtor is a party by implication to the contract.

9. Bank guarantee is a contract of guarantee. It is an important instrument in international trading of a country and is also an accepted mode of international trade. The obligation under Bank guarantee may be an unqualified obligation depending upon the terms on which the agreement is set out by the parties. It is essentially a contract between the bank and the beneficiary of the guarantee. In seeking to enforce the guarantee, the beneficiary, in effect, seeks to realise the surety furnished by the third party. It is for this reason that the court have always been very slow to interfere with its operation not merely on the ground of their importance in international trade but also on the ground that the beneficiary is assured of the payment by the bank irrespective of the noncompliance of the contract into which he had entered with the third party.

10. The Bank guarantee is different from an irrevocable letter of credit but the two, namely, bank guarantee and letter of credit have a common especially, namely, that both have great importance in international trade and the courts have generally refused to Interfere with the autonomy of an irrevocable letter of credit or bank guarantee.

11. In *M/s Tarapore & Co. Madras v. M/s V/O Tractors Export, Moscow* and Anr. 1969(2) SCR 920, it was held by the Supreme Court;

“that an irrevocable letter of credit has a definite implication. It is independent of and unqualified by the contract of sale of other underlying transactions. It is a mechanism of great importance in international trade and any interference with that mechanism is bound to have serious repercussions on the international trade of this country. The autonomy of an irrevocable letter of credit is entitled to protection and except in very exceptional circumstances court should not interfere with that autonomy.”

12. In this case some dispute had arisen between *M/s Tarapore & Co.* with the Russian firm in whose favour an irrevocable letter of credit Was issued. Russian firm wanted to realise the money from the Bank on the strength of letter of credit but *M/s Tarapore & Co.* filed a suit in Madras High Court on the original side and obtained a temporary order of injunction restraining the bank from making payment to the firm. The order of temporary injunction was, however, vacated on an appeal, by the Division Bench of the High Court and it was

thereafter that the matter reached to Supreme Court. The Supreme Court laid down that letter of credit is independent of or unqualified by the contract of sale or under lying transactions and that the autonomy of an irrevocable letter of credit is entitled to protection. The Court further held that as a rule courts refrain from interfering with that autonomy.

13. In *Punjab National Sank v. Sri Vikram Cotton Mills Ltd. & Anr.* AIR 1970 SC 1973, the Supreme Court noticed the distinction between the 'contract of Indemnity and 'contract of guarantee' and observed as under;

'A contract of guarantee requires concurrence of three persons the principal debtor, the surety and the creditor the surety undertaking an obligation at the request express or implied of the principal debtor. The obligation of the surety depends substantially on the principal debtor's default under a contract of indemnity liability arises from loss caused to the promisee by the conduct of the promisor himself or by the conduct of another person.

14. In paragraph 11 of the report, the Supreme Court scrutinised the terms of bond and noticed that the bond was expressly called an 'agreement of guarantee' wherein it was recited that Ranjit Singh guaranteed to the Bank, payment on demand, of all monies which may at any time be due to the bank from the Company, The bond was held to be a contract of guarantee and extent of liability of Ranjit Singh was found to be determined upon the terms of the bond which was held to be enforceable at law.

15. In *United Commercial Bank v. Bank of India and others* AIR 1981 SC 1426, the Supreme Court observed as under;

'In the light of these principles, 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.'

The Supreme Court in the above case also observed as under:

'A letter of credit sometimes resembles and is analogous to a contract of guarantee. In *Elia v. Matsas* (1962) 2 LI LR 485, Lord Denning, M.R. while refusing to grant an injunction stated:a bank guarantee is very much like a letter of credit The Courts will do their utmost to enforce it according to its terms. They will not, in the ordinary course of things, interfere by way of injunction to prevent its due implementation. Thus they refused in *Malax v. British Imex Industries Ltd.* But that is not an absolute rule. Circumstances may arise such as to warrant interference by injunction.

A bank which gives a performance guarantee must honour that guarantee according to its terms. In *R.D. Harbottle (Mercantile) Ltd v. National Westminster Bank Ltd.* (1977) 3 WLR 752, Kerr, J. considered the position in principle. We

would like to adopt a passage from his judgment at p. 761: It is only in exceptional cases that the courts will interfere with the machinery of irrevocable obligations assumed by banks. They are the lifeblood of international commerce. Such obligations are regarded as collateral to the underlying rights and obligations between the merchants at either end of the banking chain. Except possibly in clear cases of fraud of which the banks have notice, the courts will leave the merchants to settle their disputes under the contracts by litigation or arbitration as available to them or stipulated in the contracts. The courts are not concerned with their difficulties to enforce such claims: these are risks which the merchants take. In this case the plaintiffs took the risk of the unconditional wording of the guarantees. The machinery and commitments of banks are on a different level. They must be allowed to be honoured, free from interference by the courts. Otherwise trust in international commerce could be irreparably damaged. (Emphasis supplied)

16. After having held that a letter of credit is a contract of guarantee, the Supreme Court on the question of temporary injunction laid down in the above judgment as under:

It is somewhat unfortunate that the High Court should have granted a temporary injunction, as it has done in this case, to restrain the appellant from making a recall of the amount of Rs. 85,84,456 from the Bank of India in terms of the letter of guarantee or indemnity executed by it. 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 injunctions 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 under 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.

17. In *Maharashtra State Electricity Board, Bombay v. Official Liquidator*, High Court, Ernakulam and anr. AIR 1982 SC 1497, the Supreme Court held that where under a letter of guarantee, the Bank undertakes to pay certain amount to the Electricity Board during fortyeight hours of the demand and the payment of the amount guaranteed by the Bank is not made dependent upon the proof of any default, the Bank has to pay the amount due under the letter of guarantee given by it to the Board. In paragraph 6 of the report, the Supreme Court observed as under:

the document under which the Company in liquidation had given a fixed deposit receipt and certain quantity of zinc ingots as security to the Bank for executing the letter of guarantee in favour of the Electricity Board are independent of each other in so far as their legal incidents are concerned,

The Supreme Court further proceeded to say that under the bank guarantee the Bank had undertaken to pay to Electricity Board any sum up to Rupees 50, 000

and in order to realise it, all that the Board had to do was to make a demand. Once a demand is made the Bank has to pay the amount to the Board which was not under any obligation to prove any default on the part of principal debtor as the liability of the Bank was absolute and unconditional. The decision of the Supreme Court in Punjab National Bank Limited v. Sri Bikram Cotton Mills (Supra) was relied upon.

18. The other important question which Was decided by the Supreme Court in this case was that it was not open to the High Court to make an order prohibiting tire Board from realising the amount guaranteed by the Bank.

19. In Centax (India) Ltd. v. Vinma Impex Inc. and others, AIR 1986 SC 1924, the Supreme Court has laid down that an order of temporary injunction cannot be made restraining the bank from enforcing the bankguarantee. The Supreme Court considered the English decision in Hamzeh Malas v. British Imex Industries Ltd. (1958) 2 QB 127, in which it was held that an injunction cannot be granted in respect of letter of credit and that in the matter of bankguarantee, the same consideration would apply as applied to a letter of credit and laid down that an order of injunction cannot be granted to prohibit the enforcement of Bankers" letter of indemnity.

20. The above decisions of the Supreme Court were considered by that court itself in U.P. Cooperative Federation Ltd. v. Singh Consultants & Engineers (P) Ltd. JT 1987 (4) SC 306, and it was laid down 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 case of fraud or in case of irretrievable injustice be done, the Court should interfere.?

21. We may refer to another decision of the Supreme Court in General Electric Technical Services Company Inc. v. M/s Punj Sons (P) Ltd. and another, JT 1991(3) SC 360 in which it was laid down as under:

?The law as to the contractual obligations under the bank guarantee has been well settled in a catena of cases. Almost all such case have been considered in a recent judgment of this Court in U.P. Cooperative Federation Ltd., v. Singh Consultants and Engineers (P) Ltd 1988 (1) SCC 174: wherein Sabyasachi Mukharji, J., as he then was, observed (at 189) "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.?

22. In view of the above decision of the Supreme Court, it is clear that all the principles which are applied to an irrevocable letter of credit also apply to a bank guarantee and just as letter of credit is to be given effect to, the transactions evidenced by the Bank guarantee would not be interfered with by issuing any order of injunction. If the bank guarantee is in unequivocal terms and is not

made conditional on the default of the person for whose behalf guarantee is given, it is to be enforced without requiring the party to prove default on the part of principal debtor. Except in the case of fraud or where irretrievable injustice would result, the court will not interfere with the banking transactions evidenced by letter of guarantee by issuing any prohibitory order.

23. It is in the light of the above Supreme Court decisions that we have to examine the transaction evidenced by documents contained in Annexures 1A & 1B to the petition.

24. In the instant case, respondent no. 1, who had appointed the petitioner as its subcontractor under the agreement (Annexure1) wanted to give a sum of Rs. two Crore and fortysix lacs to the petitioner for execution of the work undertaken, namely, construction of bridge in state of Gujarat but before placing the money in the hands of the petitioner, it required the latter, namely, the petitioner to furnish bank guarantees and the bank (respondent No. 2) provided the bank guarantee evidenced by Annexures 1A and 1B containing an unconditional and unequivocal promise of respondent no.2 to furnish, on demand, a sum of Rs. 2 Crore and 46 lacs to the respondent no. 1.

25. Annexure 1A is headed as 'Bank Guarantee For Mobilization Advance'. We may reproduce paragraphs 1 to 5 and 10 of this document which read as under:

1. M/s. U.P. State Bridge Corporation Ltd., 16 Madan Mohan Malviya Marg, Lucknow (hereinafter called associate) has entered into an agreement dated 28.9.89 with you for execution of work specified in the said agreement as per terms and conditions stipulated in the said Agreement.

2. Total value of contract of the said work is Rs. 12.30 Crores (Rs. Twelve Crores & Thirty Lakhs only) and you have agreed to release/released mobilization advance of Rs.1.23 Crores on furnishing of a Bank guarantee for its refund for equal amount of Rs. 1.23 Crore (Rs. One Crore twenty three lakhs only) to you AND

3. M/s U.P. State Bridge Corporation Ltd., have approached us for the issuance of the said Bank Guarantee in your favour in the amount of Rs. 1.23 Crore (Rupees One Crore, twenty three lakhs only). We, therefore, issue this Bank Guarantee to you.

4. We do hereby unconditionally and irrevocably undertake to pay you immediately on the day and time of DEMAND AND without any DEMUR such amount or amounts as may be demanded by you from us under this guarantee not exceeding a sum of Rs. 1.23 Crore (Rs. One Crore twenty three lakhs only) in aggregate without any further question or reference to Uttar Pradesh State Bridge Corporation Ltd.

5. It is hereby clarified that we shall make & be liable to make to you immediately on demand & without demur payment(s) mentioned in para 4 above, upon a mere notice in writing given by you to us notwithstanding any

difference between you and us and or you and M/s U.P. State Bridge Corporation Ltd. under or in respect of the payability of the said sum by M/s. U.P. State Bridge Corporation Ltd. or by us to you and your such demand shall be final and binding on us, and shall not be open to challenge by us and we undertake to make the payment forthwith, without any delay or questions.

10. That you shall be the sole judge of the genuineness or otherwise of the demand and the default of U.P. State Bridge Corporation and your decision and demand in this regards for the purposes of Bank Guarantee shall be final and binding on us.?

26. The recital in paragraphs 4 and 5 reproduced above would show that the Bank had given an unconditional and irrevocable undertaking to pay immediately on demand an amount not exceeding a sum of Rupees One Crore and 23 lacs without any question or reference to the U.P. State Bridge Corporation. The Bank guarantee further proceeded to say that notwithstanding the difference which might have arisen between the parties including M/s U.P. State Bridge Corporation, the amount in question would be paid on demand without any demur.

27. Annexure 1B is headed as 'Bank Guarantee Against performance Bond'. It recites as under:

'We hereby unconditionally and irrevocably undertake to pay you immediately on the day and time of demand without any demur such amount or amounts as may be demanded by you from us under this guarantee not exceeding a sum of Rs. 1,23,00,000/(One Crore twenty three lakhs only) in aggregate without any further question or reference to U.P. State Bridge Corporation Ltd. and your demand shall be final and conclusive.'

28. The portion extracted above would indicate that Bankguarantee contained in Annexure 1B is also an unconditional and irrevocable undertaking made by the Bank to pay opposite party no. 1, namely, National Buildings Construction Corporation Ltd., a sum of Rupees One Crore and Twenty Three lacs without any question or reference to U.P. State Bridge Corporation Ltd.

29. In view of the language in which the above two documents are written, it is clear that the Bank (Opposite Party No.2) gave an unconditional, categorical and irrevocable undertaking to Opposite Party No. 1 to pay to it the sum specified in two documents referred to above on the mere demand of opposite party no. 1 without any reference to the petitioner or to his default, Whether or not default was committed by the petitioner in performance of the contract was immaterial. The undertaking to pay was not dependent upon the default of the petitioner. It was, as pointed out above, absolute, unconditional and irrevocable. In view of the unconditional undertaking of the Bank to pay to Opposite Party No. 1 the amount indicated in Annexures 1A & 1B on the mere demand of opposite party no. 1, it is not open to the petitioner to contend that the bankguarantees given on its behalf by UCO Bank (Opposite Party No2) were not enforceable unless it

was shown that it had committed default in performance of its contract.

30. In a situation of this nature as is evidenced by Annexures 1A & 1B, the contract of bankguarantee is to be held to be an independent contract between opposite party no. 1 and opposite party no. 2 and was not dependent upon the default of the petitioner. This contract can be enforced as between the opposite party no. 1 and 2 by mere demand of opposite party no.1. On a demand so made, the opposite party no.2 has no option but to pay.

31. The two principal relief's claimed in the writ petitions are:

?(1) That the writ, direction or order in the nature of Mandamus be issued commanding the respondent no. 1 not to invoke the Bank Guarantees give by the petitioner to it for a sum of Rs. Two Crores forty six lakhs only contained in Annexures 1A and IB to this writ petition.

(ii) That a writ in the nature of prohibition be issued restraining the opposite party no. 2 from encashing the Bank Guarantee in favour of respondent no. 1.?

32. In view of above discussions and in view of the settled legal position evidenced by pronouncements of the Supreme Court, relief's claimed in this petition cannot be granted and no mandamus can be issued to command the opposite party no. 1 not to invoke the bank guarantee and/or to command the opposite party no. 2 not to pay the amount covered by the two bank guarantees to opposite party no. 1 particularly as the petitioner has not pleaded nor has he made out any case of fraud or any irretrievable injustice likely to be caused to him or irreparable loss being done to him.

33. Learned Counsel for the respondent no. 1 has contended that the present petition was not maintainable as the enforcement of bank guarantees by respondent no. 1 is strictly in terms of the contractual obligation as between the parties, namely, opposite party no. 1 and 2 as evidenced by the documents contained in Annexures 1A & 1B of the writ petition. It is contended that the bank guarantees are non statutory contracts and, therefore, the writ petition in respect of the aforesaid contracts would not lie.

34. In *Radha Krishna Agarwal v. State of Bihar*, AIR 1977 SC 1496, it has been held that the writ petition in respect of nonstatutory contracts is not maintainable. The decision in the case of *M/s. Radhakrishna Agarwal (Supra)* has been approved and followed by the Supreme Court in subsequent decision in the case of *Premji Bhai Pannar and others v. Delhi Development Authority and others* (AIR 1980 SC 738) in which it was observed as under:

? But after the State or its agents have entered into the field of ordinary contract, the relations are no longer governed by the Constitutional provisions but by the legally valid contract which determines right and obligations of the parties interse. No question arises of violation of Article 14 or of any other constitutional provision when the State or its agents purporting to act within this field, perform any act. In this sphere, they can only claim rights conferred upon

them and are bound by the terms of the contract only, unless some statute steps in and confers some special statutory power or obligation on the State in the contractual field which is apart from contract? (See: Radhakrishna Agarwal v. State of Bihar (1977) SCR 249 at p. 255.)?

35. This position was reiterated by the Supreme Court in Life Insurance Corporation of India v. Escorts Ltd. and others, AIR 1986 SC 1370 and in Bareilly Development Authority and another v. Ajay Pal Singh and others, AIR 1989 SC 1076.

36. We are, therefore of the opinion that the present writ petition for a Mandamus to Opposite Party No. 1 not to enforce the bankguarantees or a Mandamus to opposite party No.2 not to pay the amount covered by the bankguarantees to Opposite Party No. 1 is not maintainable as both the bankguarantees constitute nonstatutory contracts.

37. Even if the present petition was maintainable regarding which we are of the positive opinion that it is not, a Mandamus restraining the parties from enforcing the bank guarantees could not be issued in view of the authoritative pronouncements of the Supreme Court already discussed above.

38. For the reasons stated above, the petition is dismissed. There will be no orders as to costs.

(Petition dismissed.)