
(2001) 12 DEL CK 0045
In the Delhi High Court
Case No : OMP No. 313 of 2001

Vindhya Telelinks Ltd.

APPELLANT

Vs

Mahanagar Telephones Nigam Limited and Another

RESPONDENT

Date of Decision : 12-12-2001

Acts Referred:

Arbitration and Conciliation Act, 1996 — Section 9
Constitution of India, 1950 — Article 226

Citation : (2001) 12 DEL CK 0045

Hon'ble Judges : B.N. Chaturvedi, J

Bench : Single Bench

Advocate : Rajiv Nayar and Sitesh Mukherji, for the Appellant; K.N. Bhat Ashok Mathur and Vivek Tyagi, for the Respondent

Final Decision : Partly Allowed

Judgement

B.N. Chaturvedi, J.—Faced with invocation of performance bank guarantee dated 4.10.1999, in pursuance of letter No. MTNL/BG/1047 dated 4.10.2001 of Mahanagar Telephone Nigam Limited (respondent No. 1) to the State Bank of India, Main Branch, Rewa (MP), (respondent No. 2.) the petitioner, M/s. Vindhya Telelinks Limited, approaches this Court for intervention by seeking to invoke its power u/s 9 of the Arbitration and Conciliation Act, 1996.

2. Facts unfolded by pleadings indicate that for procurement of PIJF Telecom Cables of different sizes, the respondent No. 1 floated a tender dated 14.5.1999 leading to submission of its bid by the petitioner in response thereto. The petitioner turned out to be a successful bidder. Accordingly, a Letter of Intent dated 29.09.1999 was issued to the petitioner. On completion of certain formalities, including furnishing of a performance bank guarantee, for a sum of Rs. 37,10,529/-, the respondent No. 1 issued a purchase order dated 12.10.1999 for supply of PIJF Cables of thirteen different sizes, as specified in Annexure- "A" thereto. The supplies were to be made in a phased manner by the scheduled dates of delivery, as indicated in Annexure - "B" to the purchase order. Out of a

total quantity of 1,49,520 CKM of PIJF Cables of all the thirteen sizes required to be delivered by 15th of February, 2000, the petitioner supplied 62,200.6 CKM to the respondent No. 1 by the second week of January, 2000. For rest of the supplies, the petitioner, by its letter dated 12.01.2000, requested the respondent No. 1 for extension of time till 31st of March, 2000. By a memorandum dated 28.2.2000, the respondent No. 1, however, extended the delivery period for seven sizes of PIJF Cables only, and request for extension of delivery time for the remaining six sizes was, thus, not acceded to by the respondent No. 1. In view of persistent requests for extension of delivery period in respect of remaining six sizes, the respondent No. 1, eventually, relented and extended the delivery period up to 31st of March, 2000 for another four sizes vide its memorandum dated 16.5.2000. In spite of repeated requests, no extension of delivery period for the remaining two sizes of PIJF Cables being 2000/0.4(A) and 2000/0.4(UA), was, however, granted.

3. On or about 26th of June, 2001m the petitioner received a letter dated 26.06.2001 from the respondent No. 1 terminating the contract by short closure of outstanding supplies and the petitioner was asked to deposit a sum of Rs. 7,43,907/- on account of liquidated damages at the earliest.

4. The petitioner filed a CWP. No. 4143/01 under Article 226 of the Constitution of India for issuance of appropriate writ "to record, withdraw and/or cancel the impugned letter dated 26.06.2001 forthwith in accordance with law". The same was, however, dismissed, vide order dated 3.9.2001, as not maintainable on the ground that it was not open to the petitioner to invoke the writ jurisdiction of the Court in the given case.

5. Short closure of outstanding supplies of the said two sizes and imposition of liquidated damages is pleaded to be arbitrary and unjustified being contrary to the terms and conditions of the contract, as contained in Clause 18 of the tender document. Clause 18 reads thus:

"18. TERMINATION FOR DEFAULT:

18.1. The Purchaser may, without prejudice to any other remedy for breach of contract, by written notice of default, sent to the Supplier, terminate this contract in whole or in part,

a) if the supplier fails to deliver any or all of the goods within the time period(s) specified in the Contract, or any extension thereof granted by the Purchaser pursuant to Clause 15.

b) if the supplier fails to perform any other obligation(s) under the Contract; and

c) if the Supplier, in either of the above circumstances, does not remedy his failure within a period of 30 days (or such longer period as the Purchaser may authorise in writing) after receipt of the default notice from the Purchaser.

18.2 In the event the Purchaser terminates the contract in whole or in part,

pursuant to para 18.1 the Purchaser may procure, upon such terms and in such manner as it deems appropriate, goods similar to those undelivered and the supplier shall be liable to the Purchaser for any excess cost for such similar goods. However, the supplier shall continue performance of the contract to the extent not terminated. The purchaser may, without prejudice, on the happening of any of circumstances, it its other rights under law or the contract provided elsewhere, purchase the balance quantity ty of the goods at the risk and cost of the supplier and look to him for the payments thereof and can also claim a set off of any dues payable under the contract to the supplier against his any dues under the contract of any previous contract."

6. It is asserted that in terms of Clause 18.1.(c), the respondent No. 1 was obliged to give a notice of default of at least 30 days to the petitioner before terminating the contract on part thereof. Issuance of such a notice, according to the petitioner, constituted a condition precedent to the termination of the contract and in the absence of such a notice the letter dated 26.6.2001 terminating the contract is pleaded to be void and imposition of damages to the tune of Rs. 7,43,907/-, without affording the petitioner an opportunity of making outstanding supplies, as contrary to the contractual stipulation.

7. Restraint against invocation of bank guarantee is being sought primarily on the grounds; firstly, that the termination of contract was illegal and bad in law for the reasons set out hereinabove, secondly, that the contract does not permit the respondent No. 1 to invoke the bank guarantee to satisfy the alleged claim of liquidated damages without any adjudication as to the actual injury and/or quantum of damages; thirdly, the respondent No. 1 by seeking to effect recovery of the amount of liquidated damages can not be allowed unjust enrichment, and, lastly, that the special equities are in favor of the petitioner and the invocation of the bank guarantee is contrary to the terms of guarantee.

8. The petitioner claims to be taking steps to invoke the arbitration clause for adjudication of disputes arising out of alleged illegal action of termination of contract and recovery of liquidated damages of Rs. 7,43,907/-, by an arbitral tribunal.

9. Clause 20 of the contract incorporates an arbitration clause, which reads thus:

"20. ARBITRATION:

If a dispute arises out of or in connection with this contract, or in respect of any defined legal relationship associated therewith or derived legal relationship associated therewith or derived there from, the parties agree to submit that dispute to arbitration under the ICADR Arbitration Rules, 1996.

The authority to appoint the Arbitrator(s) shall be the International Centre for Alternative Dispute Resolution."

10. The respondent No. 1 opted against filing any reply to the petition. Invocation of bank guarantee was sought to be justified on the plea that failure

of petitioner to ensure delivery of the cables in question by the stipulated dates rendered it liable to pay the liquidated damages. It was argued that the bank guarantee being an independent and distinct contract between the Bank and the beneficiary, the petitioner cannot meddle with invocation of the same on the ground that short closure of outstanding supplies was resorted to in breach of terms embodied in Clause 18.1.(c).

11. I have heard arguments on both the sides.

12. The controversy awaiting adjudication is a limited one. It a series of decisions of the Apex Court, including " General Electric Technical Services Company Inc. Vs. M/s. Punj Sons (P) Ltd. and another, ; " Ansal Engineering Projects Ltd. Vs. Tehri Hydro Development Corporation Ltd. and Another, " Dwarikesh Sugar Industries Ltd. Vs. Prem Heavy Engineering Works (P) Ltd., and another, ; " I.T.C. Limited Vs. Debts Recovery Appellate Tribunal and Others, ; & " Federal Bank Ltd. Vs. V.M. Jog Engineering Ltd. and Others, , relied upon by the learned counsel for the respondent No. 1, and also, " Hindustan Construction Co. Ltd. Vs. State of Bihar and Others, , referred to by the learned counsel for the petitioner, provide a clear answer to the question relating to invocation of bank guarantee.

13. The bank guarantee represents an independent contract between the bank and the beneficiary and the terms thereof bind both the parties. The terms of the bank guarantee are, thus, extremely material. The invocation must, Therefore, be in accordance with the terms of the bank guarantee and any deviation there from would render the very invocation bad in law. Except in the case of fraud, which could be as established fraud, or where irretrievable injury was likely to be caused to the guarantor, the courts would be reluctant to grant injunction against the invocation of bank guarantee. This is the dictate of law laid down by the Apex Court in Hindustan Construction company Limited (supra).

14. In " U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd., , the Supreme Court held:

".....an unconditional bank guarantee could be invoked in terms thereof by the person in whose favor the bank guarantee was given and the courts would not grant any injunction restraining invocation, except in the case of fraud or irretrievable injury."

Reiteration of the same principle may be noticed in " Svenska Handelsbanken Vs. M/s. Indian Charge Chrome and others, ; Larsen and Toubro Limited Vs. Maharashtra State Electricity Board and others, " Hindustan Steel Workers Construction Ltd. Vs. G.S. Atwal and Co. (Engineers) Pvt. Ltd., " National Thermal Power Corporation Ltd. Vs. M/s. Flowmore Private Ltd. and another, " State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another, " Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another, as also in " AIR 1997 1644 (SC)

15. It is important to bear in mind that for application of aforesaid principle, the

bank guarantee should be in unequivocal terms, unconditional and recite that the amount would be paid without demur or objection and irrespective of any dispute that might have cropped up or might have been pending between the beneficiary under the bank guarantee and the person on whose behalf the guarantee was furnished. Bank has only to verify whether the amount claimed was within the terms of the bank guarantee. Unless fraud or special equity is, *prima facie*, made out as triable issue by specific pleading and strong evidence so as to prevent irretrievable injustice to the party concerned, beneficiary cannot be restrained from encashing the bank guarantee till decision of the arbitrator/court on amount due and payable to the beneficiary. (See *Ansal engineering Projects Limited (supra)*).

16. Adverting to the case on hand, in the context of contention questioning legality of termination of contract and entitlement of the respondent No. 1 to proceed to recover the amount of liquidated damages without adjudication as to the actual injury and/or quantum of damages as well as the plea regarding unjust enrichment, suffices to say that invocation of the bank guarantee cannot be interfered with on any of these grounds.

17. In *Ansal Engineering Projects Limited (supra)*, where one of the contentions was that the bank guarantee could not be invoked until the amount due and payable was determined in the suit, negating the plea so raised, the Supreme Court held:

"It is settled law that bank guarantee is an independent and distinct contract between the bank and the beneficiary and is not qualified by the underlying transaction and the validity of the primary contract between the person at whose instance the bank guarantee was given and the beneficiary. Unless fraud or special equity exists, is pleaded and *prima facie* established by strong evidence as triable issue, the beneficiary cannot be restrained from encashing the bank guarantee even if dispute between the beneficiary and the person at whose instance the bank guarantee was given by the bank, had arisen in performance of the contract or execution of the works undertaken in furtherance thereof....."

18. In para 6 of the same judgment, it was laid down:-

".....The liability of the bank is absolute and unequivocal; it would thereby be clear that the bank is not concerned with the ultimate decision of a court and a tribunal in its finding after adjudication as to the amount due and payable by the petitioner to the first respondent. What would be material is the quantification of the liability in the letter of invocation....."

19. In *Dwarkesh Sugar Industries Limited (supra)* dealing with the question of applicability of the principle of "unjust enrichment", the Supreme Court, observed:

".....If the High Court had taken the trouble to see the law on the point, it would have been clear that in encashment of bank guarantee the applicability of the

principle of undue enrichment has no application."

20. Next, in connection with the contention that the invocation of the bank guarantee is contrary to the terms of the guarantee, Section (iii) of the tender document incorporating general conditions of contract may be noticed. Clause 4.1 thereof stipulates furnishing of performance security (PBG) and clause 4.2 provides:

21. Annexure-"B" to the purchase order dated 12.10.1999 vide Annexure-"D" specifies the scheduled dates of delivery of respective sizes of PIJF Cables. Admittedly, the petitioner failed to make supply of the two sizes of cables by the stipulated date and requested for extension of delivery period, which was, however, not granted. Thus, supply of cables in question by the scheduled dated of delivery was one of the contractual obligations on the part of the petitioner. Apart from this, the petitioner was also required to render certain services, as specified in Clause 8 and 9 of General Conditions of Contract, which are reproduced as under:-

"8. INCIDENTAL SERVICES (WHERE REQUIRED)

8.1 The supplier may be required to provide any or all of the following services:-

- a) Performance of supervision of on-site assembly and/or start-up of the supplied goods;
- b) Furnishing of tools required for assembly and/or maintenance of supplied goods;
- c) Performance of supervision or maintenance and/or repair of the supplied goods, for a period of time agreed by the parties provided that this service shall not relieve the supplier of any warranty obligations under this contract; and

8.2. Financial implications of these services shall be clearly indicated in the offer."

9.0. SPARES:

9.1. The supplier shall be required to provide a list of the following materials and notifications pertaining to spare parts manufactured or distributed by the supplier of spares including cost and quantity ty considered for arriving at prices of spares in Clause 9 Section A.

- a) Such spare parts as the purchaser may elect to purchase from the supplier provided that such purchase shall not relieve the supplier of any warranty obligations under the contract; and
- b) In the event of termination of production of the spare parts:
 - i) Advance notification to the purchaser of the pending termination (not less than 2 years) in sufficient time to permit the purchaser to procure needed requirement; and

ii) following such advance intimation of termination, furnishing at no cost to the purchaser, the blue prints, drawings and specifications of spare parts, if any when requested.

9.2. Over a period of 3 years starting from the date of final acceptance, the supplier shall supply, at his own cost, all necessary spares which have not been included in the offer as part of the requirement. These spares should be supplied within a maximum period of 30 days from the notification by the purchaser of his need. Delivery schedule shall be the essence of the contract."

22. The General Conditions of Contract also contains a Warranty Clause to the following effect:

"10. WARRANTY

10.1. The contractor shall warrant that stores to be supplied shall be new and free from all defects and faults in material, workmanship and manufacture and shall be of the highest grade and consistent with the established and generally accepted standards for materials of the type ordered and shall perform in full conformity with the specifications and drawings. The contractor shall be responsible for any defects that may develop under the conditions provided by the contractor and under proper use, arising from faulty materials, design or workmanship such as corrosion of the equipment, inadequate quantity ty of material to meet equipment requirements, inadequate contact protection, deficiencies in circuit design and or otherwise and shall remedy such defects at his own cost when called upon to do so by the purchaser who shall state in writing in what respect stores in faulty. This warranty shall survive inspection or payment for, and acceptance of goods, but shall expire except in respect of complaints notified prior to such date, twelve months after the stores have been taken over under Clause 5.5.

10.2. If it becomes necessary for the contractor to replace or renew any defective portion/portions of the equipment under this clause, the provisions of the clause shall apply to the portion/portions of equipment so replaced or renewed or until the end of the above mentioned warranty period. If any effect is not remedied within a reasonable time, the purchaser may proceed to do the work at the contractor's risk and expenses, but without prejudice to any other rights which the purchaser may have against the contractor in respect of such defects.

10.3. Replacement under warranty clause shall be made by the contractor free of all charges at site including freight, insurance and other incidental charges."

23. The respondent No. 1 invoked the bank guarantee vide letter dated 4.10.2001 for recovery of liquidated damages to the tune of Rs. 7,43,907/-. A verbatim reproduction of the letter of invocation makes it read:

Speed Post

No. MTNL/BG/1047

Date 4.10.2001

To,

The Chief Manager,

State Bank of India,

Main Branch,

Rewa-486006(MP)

Sub:- Invocation of Bank Guarantee No. 0468/99-2000/97 dated 4.10.99 for Rs. 37,10,529/- issued on behalf of Vindhya Telelinks Ltd.

Please refer to above said guarantee, we invoke the said bank guarantee for Rs. 7,43,907/- (Rupees Seven Lakhs Forty Three Thousand Nine Hundred & Seven only). Hence, we call upon you to send the amount immediately. The amount may be sent by pay order. The pay order may be drawn in favor of Mahanagar Telephone Nigam Limited, New Delhi.

Thanking you

(D.A. PRASANNA KUMAR)

CHIEF ACCOUNTS OFFICER (BKF)

Copy to:-

DF(MM-III). Corporate Office, New Delhi.

24. Evidently, the letter of invocation simply required the respondent No. 2 to remit Rs. 7,43,907/- by way of a pay order without even specifying the kind of breach on account of which the bank guarantee was invoked so as to enable the respondent No. 2 to find that the invocation was in accordance with the terms of the guarantee. To ascertain if the invocation of the bank guarantee was in accordance with the terms thereof, it is worthwhile to take note of the relevant part of the bank guarantee running to the following effect:-

"The Bank hereby irrevocably and unconditionally guarantees to the Mahanagar Telephone Nigam Limited that the Seller shall render all necessary and efficient services which may be required to be rendered by the Seller in connection with and/or for the performance of the said Letter of Intent and further guarantees that the goods which shall be supplied by the Seller under the said Letter of Intent shall be actually performing the WORK required of it to the satisfaction of the MTNL and shall be free from the defects arising from faulty materials, designs and workmanship, such as corrosion of the equipment, inadequate quantity ty of materials, inadequate contract protection, deficiencies in Circuit Design and/or otherwise, whatsoever and in the event of the Seller's falling of neglecting to render necessary services as aforesaid and/or in the event of the

goods failing to give satisfactory performance or proving not free from deficiencies or defects as herein before mentioned and in the said Purchase Order and particularly warranty clause mentioned therein, the Bank shall indemnify and keep the MTNL indemnified to the extent of Rs. 37,10,529/- (Rupees Thirty Seven Lac Ten Thousand Five Hundred and Twenty Nine Only) against any loss or damage that may be caused to or suffered by the MTNL by reason of any breach by the Seller of any of the aforesaid terms and conditions the Bank further undertake to pay to the MTNL, such sum not exceeding Rs. 37,10,529/- (Rupees Thirty Seven Lac Ten Thousand Five Hundred and Twenty Nine Only) on demand and without DEMUR in the event of Seller's failure to perform and discharge the aforesaid several duties and obligations on his part to be observed and performed under the Letter of Intent and/or deficiencies and defects in the satisfactory performance of the goods and equipment.

The decision of the MTNL as to whether the Seller has failed to or neglected to perform or discharge his duties and obligation as aforesaid and/or whether the goods are free from deficiencies and defect and are capable of performing the work required and as to the amount payable to the MTNL by the Bank herein shall be final and binding on the Bank."

25. Notably, though in terms of Clause 4.2, reproduced earlier, the performance bank guarantee could be invoked in any eventuality where the petitioner failed to perform any of its obligations under the contract, the terms set out in the bank guarantee, for breach whereof, the respondent No. 1 could invoke the same, do not include the incidence of failure to make supplies by the scheduled date/s. Here, it is significant to note that the respondent No. 1 invokes the bank guarantee for petitioner's failure to supply two sizes of cables in question by the stipulated date. Clearly, thus, the invocation of the bank guarantee, in the given case, was not in accordance with the terms of the bank guarantee and Therefore bad in law. Invocation of the bank guarantee itself being bad in law, the respondent No. 1 cannot enforce the payment of the amount of liquidated damages in pursuance of its letter dated 4.10.2001.

26. Apart from seeking an interim injunction against invocation of the bank guarantee in terms of prayer (a) & (b), the petitioner has further prayed for passing of an interim order restraining the respondent No. 1 "from giving any effect to or further effect to their letter dated 26.6.2001". By the letter dated 26.6.2001, the respondent No. 1 conveyed the decision of short closure of outstanding supplies and imposition of liquidated damages. Legality or otherwise of short closure of outstanding supplies and justifiability of the demand for liquidated damages are matters left open for adjudication by the arbitral tribunal on a reference being made in terms of the arbitration agreement between the parties and finding of this Court on these counts in uncalled for.

27. The petition is, thus, partly allowed. The respondent No. 1 is restrained from invoking the bank guarantee dated 4.10.1999 and the respondent No. 2 is enjoined from making payment to the respondent No. 1 under the said bank

guarantee, in pursuance of their letter dated 4.10.2001. The relief under prayer Clause (c) is declined and the petition stands dismissal to the extent.

28. There shall be no order as to costs.