Supreme Court of India
Dwarikesh Sugar Industries Ltd vs Prem Heavy Engineeing Work on 7 May, 1997
Author: Kirpal.
Bench: K.S. Paripoornan, K. Venkataswami, B.N. Kirpal

PETITIONER:
DWARIKESH SUGAR INDUSTRIES LTD.

Vs.

RESPONDENT:
PREM HEAVY ENGINEEING WORK

DATE OF JUDGMENT: 07/05/1997

BENCH:
K.S. PARIPOORNAN, K. VENKATASWAMI, B.N. KIRPAL

ACT:

HEADNOTE:

JUDGMENT:

J U D G M E N T THE 7TH DAY OF MAY, 1997 Present:

Hon'ble Mr.Justice K.S.Paripoornan Hon'ble Mr Justice K.Venkataswami Hon'ble Mr Justice B.N.Kirpal Harish N.Salve, Sr.Adv., Krishan Mahajan, P.H.Parekh, Ms. Indu Varma, Advs. with him for the appellant Sudhir Chandra, Sr.Adv., Manmohan, Sanjay Raghuvanshi, R.

Sasiprabhu, Advs. with him for the Respondents.

J U D G M E N T The following Judgment of the Court was delivered: KIRPAL. J.

Special leave granted.

Having been thrawted by orders of the court below in it attempt to get encashment of the bank guarantees, issued by the State Bank of India, Meerut Cantt. Branch (respondent no.2) respondent no.l has led to the filing of this appeal by aggrieved beneficiaries.

The appellant and respondent no.1 had entered into an agreement on 27th July, 1994 whereby

respondent no.1 was to supply boiling house equipment the cost of which was Rs. 5.23 crores. The supply of equipment and material was to start from 15 September, 1994 and the same was to be completed by 10th August, 1995, as per the schedule of the supply agreed to by the parties.

According to one of the clauses of the aforesaid agreement respondent no.l had agreed to furnish bank guarantees in favour of the appellant. Out of the above six, only four bank guarantees were furnished including bank guarantee no. 40/51 dated 1st December, 1994 for a sum of Rs.26,15,000/- and bank guarantee no.40/47 dated 24th November, 1994 for a sum of Rs.35 lacs. These are the bank guarantees with which we are concerned in the present case. Bank guarantee no.40/51 was issued to ensure timely delivery of equipment and supply by respondent no. 1. The relevant clauses of the said bank guarantee no.40/51 are as follows:

> "In consideration of the premises the Guarantor hereby unconditionally and irrevocably undertake to pay to the Purchaser on their first written demand and without demur such a sum not exceeding Rs.26,15,000/- (Twenty six lacs fifteen thousand only) as the purchasers may demand representing 5% (five per cent) of the contract price, and if the guarantor fails to pay the sum on demand the guarantor shall also pay on the sum demanded interest at the bank lending rates then prevailing reckoned from the date of demand till the date of payment.

2.The guarantor shall pay to the purchaser on demand the sum under clause 1 above without demur and requiring the purchasers to invoke any legal remedy that may be available to them, it being understood and agreed firstly that the purchasers shall be the sole judge of and as to whether the sellers have committed breach(es) of any of the terms and conditions of the said agreement and secondly that the right of the purchasers to recover from the guarantor any amount due to the purchasers shall not be affected or suspended by reasons of the fact that any dispute or disputes have been raised by the sellers with regard to their Lability or that proceedings are pending before any Tribunal arbitrator(s) or Court with regard to or in connection therewith, and thirdly that the guarantor shall immediately pay the aforesaid guaranteed amount on demand and it shall not be open to the guarantor to know the reasons of or to investigate or to go into the merit of the demand or to question or to challenge the demand or to know any fact affecting the demand, and lastly that it shall not be open to the guarantor to require the proof of the liability of the seller to pay the amount before paying the aforesaid guaranteed amount to the purchasers The other bank guarantee no.40/47 was originally issued for a sum of Rs.51,70,000/- for securing advance payment. The agreement contemplated the liability being gradually reduced and on 28th August, 1995 this bank guarantee was reduced for a diminished amount of Rs.33 lacs. The relevant clause of this bank guarantee is as follows:

> "In consideration of the premises the guarantor hereby unconditionally and irrevocably undertakes to pay to the purchaser on their first written demand and without demur such a sum not exceeding Rs.51,70,000/- (Rupees fifty one lacs seventy thousand only) as the purchasers may demand representing 10% (Ten per cent) of the contract price, and if the guarantor fails to pay the sum on demand the guarantor shall also pay on the sum demanded interest at the bank lending rates then

prevailing reckoned from the date of demand till the date of payment. Provided that liability of the guarantor hereunder shall reduce to the extent of the advance adjusted under clause 13 of the said agreement.

The guarantor shall pay to the purchaser on demand the sum under clause 1 above without demur and requiring the purchasers to invoke any legal remedy that may be available to the them, it being understood and agreed firstly that the purchaser shall be the sole judge of and as to whether the sellers have committed any breach(es) of any of the terms and conditions of the said agreement and secondly that the right of the purchasers to recover from the guarantor any amount due to the purchasers shall not be affected or suspended by reasons of the fact that any dispute or disputes have been raised by the seller with regard to their Liability or that proceedings are pending before any Tribunal, arbitrator(s) or court with regard thereto or in connection therewith, and thirdly that the guarantor shall immediately pay the aforesaid guaranteed amount on demand and it shall not be open to the guarantor to know the reasons of or to the investigate or to go into the merits of the demand or to question or to challenge the demand or to know any facts affecting the demand, and lastly that it shall not be open to the guarantor to require the proof of the liability of the seller to pay the amount before paying the aforesaid guaranteed amount to the purchasers".

According to the appellant respondent no.l did not supply the equipment at site, within the time allowed, nor replaced any of the defective items which, according to the appellant, had resulted in the ate commencement of the trial crushing in the mill. It is further the case of the appellant that it had to make direct purchases of many parts from other sources as the respondent no.1 had failed to supply the equipment Ultimately by letter dated 21st November, 1995 written to respondent no.2, the appellant invoked the bank guarantee. The material portion of this letter was as follows:

"We wish to inform you that M/S Prem Heavy Engineering Works (P) Ltd. Ram Mill, Delhi Road, Meerut have failed to fulfill the condition of our agreement dated 27.7.1994 in so far as timely supply of the machinery and equipment under order with them . "As per clause 14 of the supply agreement M/s Prem - Heavy Engineering Works (P) Ltd., Meerut has failed to deliver the equipments and its commissioning within the scheduled time frame. Now we hereby invoke the aforesaid guarantee for Rs.26,l5,000/-(Rupees twenty six lacs fifteen thousand only) 5% of the contract value and enclose here with the original guarantee for your record. Kindly hand over the Demand Draft in our favour payable at Najibabad, Distt. Bijnor, Uttar Pradesh towards the invocation amount."

As on 28th November 1995 respondent no.1 had already obtained and ex parte injunction restraining the encashment of bank guaranteee, no payment was made to the appellant by the bank.

Respondent no.1 then filed another injunction application dated 12th January, 1996 with regard to the second bank guarantee dated 24th November, 1994 which was for a sum of Rs.33 lacs. It obtained an Ex parte injunction in respect thereto on the same day. Being ignorant of this the

appellant wrote a letter dated 16th January, 1996 to the respondent bank invokeing the said bank guarantee no. 40/47. In the said letter it was stated that respondent no.1 had failed to deliver the equipment as per the terms of the agreement and that the appellant had bought equipment from various markets due to which the advance amount which had been paid to respondent no.1 in respect of which this bank guarantee had been issued, remained unadjusted. The bank was accordingly required to pay the said amount of Rs.33 lacs.

According to the appellant it is only after 16th January, 1996 that it became aware of the filing of the aforesaid suit and the injunction application and it entered appearance in Court on 18th January, 1996 even though no notice had been served on it. As per the appellant, there was delay in the disposal of the injunction application, consequently it approached the High Court for appropriate directions and the Allahabad High Court vide order dated 10th may, 1996 directed the civil Judge, Meerut Cantt, to dispose of the suit within the time fixed by it .

By a detailed order dated 20th August 1996, the Second Civil Judge (Sr. Division) Meerut vacated the ex parte injunctions which had been granted and dismissed the injunction applications. In arriving at this conclusion it observed that respondent no.1 had not stated that the work had been completed and nor was there any allegation of cheating or fraud contained in the plaint which had been filed. The trial court referred to a number of decisions of this Court and came to the conclusion that there was no basis, in law, for the grant of any interim prohibitory order.

The appellant on 22th August, 1996 again approached the respondent bank for the encashment of the bank guarantees, but without success.

Respondent no.1 then filed revision petition on. 257 of 1996 on 10th September. 1996 before the Allahabad High Court challenging the order dated 20th August, 1996 of the trial court. single judge of the Allahabad High Court took up the revision petition and disposed it of on the same day and after setting aside the order dated 20th August, 1996 it remanded the matter back to the trial court for a fresh decision but, at the same time, directed that till the disposal of injunction application the bank guarantees in question shall not be invoked or encashed. The trial court was directed to hear the parties within fifteen days of the receipt of the order and to dispose of the injunction application within fifteen days thereafter. Needless to date, due to dilatory tactics adopted by respondent no1 which is evident from the documents available on the record of this "As per clause 14 of the supply agreement M/s Prem - Heavy Engineering Works (P) Ltd., Meerut has failed to deliver the equipments and its commissioning within the scheduledtime frame.

Now we hereby invoke the aforesaid guarantee for Rs.26,l5,000/-(Rupees twenty six lacs fifteen thousand only) 5% of the contract value and enclose here with the original guarantee for your record. Kindly hand over the Demand Draft in our favour payable at Najibabad, Distt.

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While allowing the civil revision the single judge in his judgment did not think it necessary to refer to the judicial diecisions which were cited before him. The court observed that reference to the same was not becessary because the trial court, who had observed that the plaint did no contain any allegation with regard to fraud, had not noticed that allegation of fraud was cantained in the injuction application. The learned judge noticed that the liability of bank under the guarantee was

absolute and that it was not supposed to question the authority of the benificiary to encash the bank guarantee but observed that the same " could not be the guideline for allowing the defendant to encash the bank guarantee unless there was a finding that the defendant was having undue enrichment thereby".

The aforesaid decision of the High Court has been assailed by Sh. Harish N. Salve, learned senior counsel for the appellant, who has contended that the High Court fell in serious error in ignoring and not in even feferrin g to the decisions of this Court where the principles regarding the grant of injunction in matters relating to encashment of bank guarantees have been clearly spell out. Had this been done, the learned counsel submits, the High Court could not, in law, have continued with the temporary injunction.

Numerous decisions this Court rendered over a span of nearly two decades have laid down and reiterated the principles which the Courts must apply which considering the question whether to grant an injunction which has the effect of restraining the encashment of a bank guarantee. We do not think iot necessary to burden this judgment by referring to all of them. Some of the more recent pronouncements on this point where the earlier decisions have been considered and reiterated are Svenska Handelsbanken Vs. Toubro Ltd. Vs. Maharashtra State Electricty Board and ors. [(1995) 6 SCC 68], Hindustan Steel Works Construction Ltd. Vs. G.S. Atwal & co. (Engineers) Pvt. Ltd. [(1995) 6SCC 76] and U.P. State Sugar Corporation Vs. Sumac International Ltd. [(1997)1 SCC 568]. The gemeral principle which has been laid down by this court has been summarised in the case of U.P. state sugar Corporation's case as follows:

> "The law relating to invocation of such bank guarantees in by now well ssettled. When in the course of commercial dealings an unconditional bank guarantee is given or accepted, the beneficial is entitled to realize suchj a bank guarantee in terms thereof ireespective of any pending disputes. The bank giving such a guarantee is bound to honlur, ir as per its terms irrespective of any dispute raised by its costomer. The very purpose of giving such a bank a bank guarantee would othrwise be defeated. The courts should, therefore, be slow in granting an injunction to restrian the realization of such a bank guarantee. The courts have carvede out only two exceptions. A fraud in connection with such a bank guarantee would vitiate the very foundation with such a bank guarantee would vitiate the very foundation of such a bank guarantee. Hence if thre is such a fraud of which the beneficiary seeks to take the advantage, he can be restrained from doing so.
>
> The second exception relates to case where allowing the encashment of an unconditional bank guarantee would result in irretrievable harm or injustice to one of the parties concerned. Since in most 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 contemplanted under this head must be of such an exceptional and irretrievable nature as would override the terms of the guarantee and the adverse effect of such an injunction of the guarantee and the adverse effect of such an injunction on commercial dealings in the country."

Dealing with the queation of franud it has been held that fraud has to be an established fraud. The following observation of sir John Donaldson, M.R. in Bolivinter oil SA V. Chase Manhattan Bank (1984) 1 All ER 351, are apposite:

> "The wholly exceptional case where an injunction may be granted is where it is proved that the bank knows that any demand for payment already made or which may threafter be made will clearly be fraudulent. But the evidence must be clear both as to the fact of fraud and as to the bank's knowledge .It would certainly not normally be wufficient that rests on the ujncorroborated statement of the customer, for irreparable damage can be done to a bank's credit in the relatively brief time which must clapse between the granting of such an injunction and an application by the bank to have it charged."

(emphasis supplied) The aforesaid passage was approved and followed by this court in U.P. coooperative Federation Ltd. Vs. Singh consultants and Engineers (P) Ltd. [(1988) 1 SCC 174].

The secondly 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 due Court that there would be no possbility whatsoever of the recoverv of the amount from the beneficiaIy. by way of restitution.

In the instant case, as has been already noticed there were two types of bank guarantees which were issued. Bank Guarantee No. 40/51 for Rs.26,15,000/- was issued to issues timely y performance of the agreement by respondent No. 1. the relevant terms of this guarantee firstly makes it clear that the that has unconditional and irrevocably undertaken to pay to pay to the appellant, on written demand and without demand, the amount demanded it. Secondly, Clause II of the said guarantee clarifies that the payment shall be made without demand and on the undertaking that the appellant is to be sole judge whether the seller has committed any breach. Consequently the right of the appellant to recover the guaranteed amount is not to be effected or suspended by reason of any dispute which can be raised or pending before the courts tribunals or arbitrator Thirdly the guarantor had no right to know the reasons of or to investigate the merits of the demand or to question or to challenge the demand or to know any fact affecting the demand and lastly it was not open to the bank to require the proof of the liability of respondent No.1 to pay the amount before paying the aforesaid guaranteed amount to the appellant.

The letter of invocation issued by the appellant demanding the payment ot Rs.26,15000/- was in accordance with the terms of bank guarantee No. 40/51 and the bank was, threfore, under an obligation to honour its undertaking and to make the payment . It, however, chose not to fulfil its obligation. If the bank could not in law avoid the payment, as the demand had bneen made in terms of the banjk guarantee, as has been done in the present case, then the court 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. An injunction of the court ought not to be an instrument which is used in nullifying the terms of a contrant, agreement or undertaking which is used in nullifying the terms

of contract, agreement or undertaking which is lawfully enforceable. In its aforesaid letter dated 24th November, 1995 respondent no.1 had clearly admitted that entire supply had not been made. In view of this also the High court was not justified in granting an injunction.

Bank guarantee No.40/97 dated 24th November, 1994, which had been issued to secure the advance of Rs. 129.24 lacs which had been given by the appellant, was also similar in terms to the earlier bank guarantee No. 40/51. The main contract between the parties contemplated that the amount of bank guarantee shall stand reduced on adjustment being made. It is contended by Shri Sudhier Chandra, learned counsel for the respondents that the full amount was ginen adjusted and no amount remained outstanting and, therefore, the bank guarantee No.40/47 could no longer be regarded as alive . In support of this contention, the learned counsel relied on the observations of this Court in Larson & Turbo Ltd. Vs. Maharashtrata state Electricity Board and ors. (1995) 6 SCC 68 where an injunction was granted wheree the bank guarantee which was issued was to be kept alive till the successful completion of trial operations. our opinion, this decision can be of no assistance to respondent no. 1 because in Larson & Turbo~s case (supra) this Court found that the guarantee which had been given by the bank was to ensure only till the successful completion of the trail operations and the taking over of the plant. The documents revealed that the contractual terms in this regard has been complied with and after successful completion of the trial operation, the plant had admittedly been taken over. In view of this Court that the terms of the bank gurantee did not permit its invocation once the trial operation have been successfully completed.

In the present case clause 3 of bank guarantee No. 40/47 relating to adjustment of the advance stipulated as follows:

> "The guarantee shall come into force from the date thereof and shall remain valid till the full advance amount is adjusted under Clause 13 of the said agreement which according to the terms and conditions of the said Agreement is stipulated to be adjusted proportionately from each bill of the Sells against actual deliveries of the machinery and equipment at site but if the deliveries as aforesaid have not been completed by the Sellers within the said period for any reason what soever the Guarantor hereby undertakes that the Sellers shall furnish a fresh or renewed guarantee on the Purchaser's proforma for such further period as the purchaser's may intirmate failing which the guarantor hall pay to the purchaser's a sum not exeeeding Rs. 51,70,000/-(Rupees Fifty one lacs seventy thousand only) or the residual amount of balance unadjusted advance left after proprotionae adjustment in acccordance with clause 1 above as the purchaser may demand."

No plea was taken before the courts below and no document has bcen shown to us by the respondents, which can prima ficie indicate that the full amount to us by the respondents, which can prima facie indicate that the full amount of advance had been adjusted under Clause 13 of the main contrant between the appellant and the defendant no.1 According to the appellants, the original guarantee was for Rs. 51,70,000/- but the same, after adjustment of the advance, in terms of clause 13 of the main agreement, stood reduced to Rs.33,00,000/- This amount was still outstanding and, therefore, the bank guarantee had not come to an end and was rightly invoked.

Coming to the allegation of fraud, it is an admitted fact that in the plant itself, there was no such allegation was initially only in the first application for the grant of injunction that in a paragraph it has been mentioned that the appellant therein had invoked the bank guarantee arbitrarity. this application contains no facts or particulars in support of the allegation of fraud. A similar bald averment alleging fraud is also contained in the second application for injunction relating to bank guarantee No. 40/47. This is not a case where defendant no. 1 had at any time alleged fraud prior to the filing of injunction application. The main contract, pursuant to which the bank guarantees were issued, was not sought to be avoided by alleged fraud, nor was it at any point of time alleged that the bank guarantee was issued because any fraud had been played by the appellant. We have no manner of doubt that the bald assertion of fraud had been made solely with a view to obtain an order of injunction . In the absencce of established fraud and not a mere allegation of fraud and that also having been made only in the injunction application , the court could not, in the present case have granted an injunction relating to the encashment of the bank guarantees.

It is unfortunate that the High Court did not consider it necessaly to rrfer to various judicial pronouncements of this Court in which the principles which have to be fullowed while examining an application for grant of interim relief have been clearly laid down. The observation of the High Court that reference to judicial decisions will not be of much importance was cleart a me1hod adopted by it in avoiding to fo11ow and apply the law as laid down by this Court. Yet another scrious for which was carmnitted by the High Court, in the present case, was not to examine the tenns of the bank guarantee and consider the letters of invocation which had been written by the appellant. If the High Court had trail the trouble of examining the documents on record, which had been referred to bv the trial court, in its order refilsing to grant injunction, the court would not have granted the interim injunction. We also do not find any justification for the High Court in invoking the alleged principle of adjust enrichment to the facts of the present case and then deny the appettant the Iight to cncash the bank guarantee. 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 guaranmtee the applicability of the principle of undue enrichment has no application.

We are constrained to make these observation with regard to the manner in which the High Court had dealt with this case because this is not an isolated cade where the courts, while disobeying or not complying with the law laid down by this Court , have at time been liberal in granting injunctgion restraining encalhment of bank guarantees.

It is unfortunate, that notwithstanding the authoritative the pronouncements of this Court, the High Courts and the courts subordinate thereto, still seem intent on affording to this Court innumerable opportunities for dealing with this area of law, thought by this Court to be well settled.

When a position, in law, is well settled as a result of judicial pronouncement of this Court, it would amount to judicial impropriety to say the least, for the subordinate courts including the High Courts to ignore the settled decisions and then to pass a judicial ordor which is clearly contrary to the setded legal position. Such judicial adventurism cannot be permitted and we strongly deprecate the tendency of the subordinate courts in not applying the settled principles and in passing whimsical orders which necessarily has the effect of granting wronful and unwarranted relief to one of the

parties. It is time that this tendency stops.

Before concluding we think it appropriate to mention about the conduct of the respondent - bank which has chosen not to be in this case. From the facts stated hereinabove it appears to us that the respondent bank has not shown professional efficiaency, to say the least, and has acted in a partisan manner with a view to help and assist respondent no. 1. At the time when there was no restraint order from any Court, the bank was under a legal and moral obligation to honour its commitments. It, however, failed to do so. It appears that the bank deliberately draged its feet so as to enable respondent no.1 to secure favourable order of injunctgion from the Court. Such conduct of a bank is difficult to appreciate We do not wish to say anything more but it may feel that it will be prejudicial in the event of the appellant taking action against it.

For the aforesaid reasons this appeal is allowed. The judgment and order of the Allahabad High Court dated 10th September, 1996 in revision petition no.257 of l996 is set aside and the order of the trial court datded 20th Auguat, 1996 dismissing the injunction application is restored. The appellant would be entitled to cost which are quantified at Rs.20,000/-.