Supreme Court of India
I.T.C. Limited vs The Debts Recovery Appellate ... on 19 December, 1997
Author: M. Jagannadha Rao.
Bench: Suhas C. Sen, M. Jagannadha Rao.

PETITIONER:
I.T.C. LIMITED

Vs.

RESPONDENT:
THE DEBTS RECOVERY APPELLATE TRIBUNAL & ORS.

DATE OF JUDGMENT: 19/12/1997

BENCH:
SUHAS C. SEN, M. JAGANNADHA RAO.

ACT:

HEADNOTE:

JUDGMENT:

THE 19TH DAY OF DECEMBER, 1997 Present:

Hon'ble Mr. Justice Sushas C.Sen Hon'ble Mr. Justice M.Jagannadha Rao Soli J. Sorabjee, Sr. Adv., S.Ganesh, Ravinder Narain, Ms. Punitta, Ms. Juhi, Advs. for M/s. J.B.D. & Co., Advs. with him for the appellant M.J. Rupal, U.A. Rana, Sudhanshu Tripathi, Advs. for M/s. Fox Mandal & Co., and S.N. Bhat, Advs. for the Respondents J U D G M E N T The following Judgment of the Court was delivered: M. JAGANNADHA RAO., J Leave granted.

The appellant has preferred this appeal against the judgment of the High Court of Karnataka dated 14.8.1997 in Writ Appeal No. 2876 of 1997. The Writ Appeal was filed against the judgment of the learned Single Judge dated 9.4.1997 dismissing the Writ Petition filed by the appellant against the orders of the Debt Recovered Tribunal and Appellate Tribunal rejecting the application of the appellant filed under Order 7 Rule 11 of the Code of Civil Procedure.

The appellant was the 5th defendant in the suit filed by the 3rd respondent, namely, the Corporation - Bank which has its zonal office at Bangalore. The suit was filed in the year 1985 by the said Bank against at Guntur in Andhra Pradesh and against the appellant I.T.C. Limited. The relief claimed in the suit was for a sum of Rs. 52,59,639.66. The defendants 1 to 4 above mentioned are respondents

4 to 7 in this appeal. The first respondent is the Debt Recovery Appellate Tribunal and the 2nd respondent is the Debt Recovery Tribunal. After the suit was filed in the Civil Court it was transferred to the Debt Recovery Tribunal on 9.10.1995. Before the said Tribunal the appellant filed an application under order 7 Rule 11 of the Civil Procedure Code for rejecting the plaint so far as the appellant was concerned on the ground that no valid cause of action had been shown against the appellant. The said application was rejected by the Tribunal on 12.12.1996 holding as follows:-

> "Objections filed. Heard. Cause of action is a mixed question of fact and law. Hence I.A. 3 cannot be entertained at this stage. Post for evidence".

Against the said order, the appellant filed an appeal before the Appellate Tribunal which was dismissed by the said Tribunal on 3.3.1997 holding that in view of the averments in the plaint and particularly para 12, the question about the liability of the appellant was to be determined at the trial on merits. It stated that the appellant had admittedly received Rs. 32 lacs under the Bills of Exchange or Letters of Credit and the question whether the appellant was justified in receiving the said amount or not and whether plaintiff-Bank was entitled to recover the said amount from the appellant - were to be determined only at the trial. Accordingly the appeal was dismissed in limine.

The appellant filed Writ Petition 9564/1997 in the Karnataka High Court which was again dismissed by an order dated 9.4.1997 holding that the question has to be decided at the trial and that it could not be stated that there was no cause of action at all disclosed in the plaint against the appellant. Against the said judgment the appellant filed Writ Appeal 2876/1997 which was dismissed on 14.8.1997 holding that at the stage of an application under Order 7 Rule 11 C.P.C. in order to find out whether the plaint did not disclose a cause of action, the Court should not look into anything else except the plaint. Further, after the issues were framed and the case was posted for evidence, it was not desirable to consider the application filed under Order 7 Rule 11, C.P.C.

Was shall refer to the facts of the case as set out in the plaint. The first defendant belonging to Tadikonda family (hereinafter called the buyers) approached the plaintiff Bank in December 1979 for the issue of a Letter of credit in favour of the appellant-Company for an amount of Rs. 32 lacs for the purpose of securing the payment towards supply of Cigarettes manufactured by the appellant and for certain other facilities. The plaintiff-Bank sanctioned L.C. facility for the said sum and agreed to open the L.C. and issued a "revolving Letter" of Credit No. 1/1980 dated 12.11980 in favour of the appellant for Rs. 32 lacs available against demand bills of the appellant at sight, "without recourse" to the full invoice value of the goods purporting to be supply of Cigarettes by the appellant. At the request of the buyers the Letter of Credit was renewed from time to time and the last one was on 20.1.1983 till 20.1.1984. Thereafter the buyer again approached the plaintiff - Bank for additional Letter of Credit in favour of the appellant - Company and this was in August 1983 and the plaintiff Bank agreed to open an additional Letter of Credit in favour of the appellant and did so in April 1983 and issued a "revolving Letter" of Credit 1/883 in favour of the appellant for Rs. 18 lacs against demand bills of the appellant on the buyers at sight "without recourse" for the full invoice value of the goods purporting to the supply of Cigarettes manufactured by the appellant. In respect of the above Letters of Credit the buyers executed necessary loan documents in favour of the Bank for issue of confirmed irrevocable Letter of Credit, Letter of General Lien relating to immovable

properties, etc. Demand Promissory Notes were also executed by the buyers.

The plaint then states that the appellant availed the benefits of drawing various sums on several dates purporting to be for despatch of goods (Cigarettes) by the appellant to the buyers (defendants 1 to 4) and that was hose the appellant appropriated the amounts drawn as against goods purportedly despatched by the appellant to the buyers. It stated in para 6 of the plaint, that "the 5th defendant misrepresented to the plaintiff that the goods were despatched while presenting the relevant demand bills for negotiation under L.C. and fraudulently obtained payments." After referring to the refusal of the buyers to make good the payment made by the Bank to the appellant to the extent of the money already paid by the bank to the appellant under the L.Cs, the plaint proceeded to state that the plaintiff demanded reimbursement of the said amounts by the buyers and that the buyers informed the plaintiff that in fact, there was no movement of the goods by the appellant and that unless there was such a movement, the appellant was not entitled to draw any amount under the L.C. facility from the plaintiff - Bank. It was stated in para 8 of the plaint that the buyers by letter dated 23.1.1984 stated that the appellant had drawn the bills for an amount of 18 lacs without support of actual movement of stock of Cigarettes on 1.9.1983. It was stated in para 8 that the Bank has now realised that the appellant had drawn monies from the Bank without movement of goods to the buyer and had therefore acted fraudulently. The plaint than proceeds to state in para 9, that the appellant had committed breach of faith and acted contrary to the terms of the Letters of Credit and that the plaintiff issued registered notices to all the parties. The appellant stated in its reply dated 18.4.1984 that the payments had been received by it only for the supplies made and towards monies definitely due thereby. This according to the Bank implied that the goods were not despatched under the terms of the Letters of Credit. Plaintiff them stated that appellant had appropriated the monies from the Bank under the guise of L.C. facilities to adjust some other liabilities incurred by the buyers towards the appellant under different transactions than envisaged in the L.C. facilities. The plaint referred to in para 10 to a reply dated 13.4.1984 of the buyers to the effect that the bills were drawn by the appellant and money appropriated towards the trading balance dues of the buyers. The plaint then stated that both the appellants as well as buyers acted contrary to the terms of the Letters of Credit and monies were drawn wrongly by the appellant misrepresenting the fact as to despatch of goods and the amount was appropriated towards other liabilities of the buyer towards the appellant. Both the buyers as well as the appellant had the benefit of these illegal drawings and therefore both were liable to reimburse the plaintiff with interest. In para 12 of the plaint it was then stated as follows:

> "The 5th defendant has drawn the amounts contrary to the terms of Letters of Credit. The payments by the plaintiff to the 5th defendant was due to the mistaken assumption that the 5th defendant had despatched the cigarettes which entitled the 5th defendant to the payments under the Letter of credit. The plaintiff discovered the mistake when it received the letter of the first defendant dated 23.1.1984 as also the reply of the defendants 1 and 5 dated 13.4.1984 and 18.4.1984 respectively. The payments to the 5th defendant being under/due to the mistake, as aforesaid, the plaintiff will entitled to be repaid of the said amounts by the 5th defendant. The 5th defendant has unjustly enriched itself by the several payments."

In para 14 of the plaint again there is an allegation that the appellant was guilty of false representation that goods in question had been despatched when in fact the 5th defendant received the payments towards other claims against the buyers.

As already stated, the Tribunal and the High Court, on the above averments in the plaint, refused to reject the plaint.

Learned counsel for the appellant - Company Shri Soli J. Sorabjee contended that the Court was entitled to reject the plaint under Order 7 Rule 11 C.P.C. at any stage of the suit even if the issues were framed and even if the matter was posted for evidence. Learned counsel also contended that it is well settled that in regard to payment under Bank Guarantees or irrevocable Letters of Credit, the contract between the sellers (appellant) and the Bank was independent of the contract between the buyers and sellers in respect of the goods and that the Bank had no authority to refuse payment on the ground of any alleged breach of contract by the sellers in their contract with the buyers. The only exceptions which have been recognised by the Courts were cases of fraud or irretrievable injury. In the case of those exceptions, the buyers could seek and injunction against the Bank before the Bank paid money to the sellers. No such injunction was sought by the buyers. Further, the exceptions relating to forgery or fraud and misrepresentation recognised by the Courts relate to the forgery or fraudulent presentation of the documents tendered to the Bank. The case on hand did not come within the said exceptions and, therefore, there was no cause of action against the appellant. Learned counsel also contended, that merely because the word fraud or misrepresentation were used in the plaint, the Bank could not claim that the said allegations have to be accepted as true for purposes of Order 7 Rule 11 C.P.C.

On the other hand, learned counsel for the respondent - Bank submitted that in view of the averments in the plaint relating to misrepresentation and fraud by the appellant, the said allegations have to be taken to be true when the appellant's application under Order 7 Rule 11 was taken up for consideration and it was not permissible for the court to refer to any other material for the purpose of deciding whether thee was any cause of action against the appellant.

The first point here is whether the power to reject the plaint under Order 7 Rule 11 C.P.C. can be exercised even after the framing of issues, and when the matter is posted for evidence. This point has arisen because the Division Bench of the High Court has referred to this aspect while dismissing the appeal.

We may stated that in the context of Order 7 Rule 11 C.P.C., a contention that once issues have been framed, the matter has necessarily to go to trial has been clearly rejected by this Court in Azhar Hussain vs. Rajiv Gandhi [1986 (Supp.) SCC 315] (p.324] as follows:

> "In substance, the argument is that the Court must proceed with the trial, record the evidence, and only after the trial....is concluded that the powers under the Code of Civil Procedure for dealing with a defective petition which does not disclose cause of action should be exercised. With respect to the learned counsel, it is an argument which it is difficult to comprehend. The whole purpose of conferment of such powers

> is to ensure that a litigation which is meaningless and bound to prove abortive should not be permitted to occupy the time of the Court"

The above said judgment which related to an election petition is clearly applicable to suits also and was followed in Samar Sing vs. Kedar Nath [1987 (Supp.) SCC 663]. We therefore hold that the fact that issues have been framed in the suit cannot come in the way of consideration of this application filed by the appellant under Order 7 Rule 11 C.P.C.

We shall next deal with the question whether the allegations in the plaint prove a cause of action against the appellant for recovery by the bank, of the amounts already paid under the irrevocable letter of Credit.

The principles regarding the payment of amount covered by bank guarantees or Irrevocable Letters of Credit are fairly well settled. They have been discussed in detail in several cases and there is an exhaustive discussion of the principles in U.P Cooperative Federation Ltd. vs. Singh Consultants & Engineers [1988 (1) SCC 174]. Reference was also made by the learned counsel before us to the judgment of the Calcutta High Court in United Commercial bank cs. Human Synthetics Ltd. [AIR 1985 Cal. 961] (to which one of us, Suhas C. Sen, J. was a party). It will be noticed that the above cases do say that the bank has to honour the Bank guarantee or Letter of Credit subject of course to the case of two exceptions where there was fraud or irretrievable injury. In the present case, the contention for the Bank is based on fraud or misrepresentation by the appellant. That is stated to be the cause of action in the plaint.

Question is whether a real cause of action has been set out in the plaint or something purely illusory has been stated with a view to get out of Order 7 Rule 11 C.P.C. Clever drafting creating illusions of cause of action are not permitted in law and a clear right to sue should be shown in the plaint. (See T. Arivandandam vs. T.V. Satyapal & Another [1977 (4) SCC 467]).

It is now well settled that the question whether goods were supplied by the appellant or not is not for the Bank. This point has already been decided by the decision of this Court in U.P. Cooperative Federation case referred to above. In that case it was stated (at p. 193) by Jagannatha Shetty, J. as follows:

> "The bank must pay if the documents are in order and the terms of credit are satisfied. The Bank, however, was not allowed to determine whether the seller had actually shipped the goods or whether the goods conformed to the requirements of the contract. Any dispute between the buyer and the seller must be settled between themselves. The courts, however, carved out an exception to this rule of absolute independence. The courts held that if there has been "Fraud in the transaction" the bank could dishonour beneficiary's demand for payment. The courts have generally permitted dishonour only on the fraud of the beneficiary, not the fraud of somebody else."

It will be noticed from the underlined portion in the above passage that there will be no cause of action in favour of the Bank in cases where the seller has not shipped the goods or where the goods have not conformed to the requirements of the contract. the Bank, in the present case before us, could not, by merely stating that there was non- supply of goods by the appellant, use the words "fraud or misrepresentation" for purposes of coming under the exception. The dispute as to non-supply of goods was matter between the seller and buyer and did not, as stated in the above decision, provide any cause of action for the Bank against the seller.

Learned counsel for the respondent then relied upon Bank Russo-Iran vs. Gordon Woodroffe & Co. Ltd. [1972 The Times, 4th Oct] (Reported in (1972) 116 Sol Jo 921) where Browne, LJ stated as follows:

> "In my judgment, if the documents are presented by the beneficiary himself, and are forged or fraudulent, the bank is entitled to refuse payment if the bank finds out before payment, and is entitled to recover the money as paid under a mistake of fact if it finds out after payment"

The above passage was quoted with approval by Lord Denning M.R. in Edward Owen vs. Barclays Bank International [1978 (1) All ER 976 (CA) (at 982)].

It is to be noted that the above passage from the judgment of Browne, LJ speaks of 'forged' or 'fraudulent' documents. If the documents presented by the seller before the Bank were forged or were fraudulent to the knowledge of the seller, surely the Bank would have an independent cause of action against the seller for it was an act of the seller which was responsible for inducing the Bank to release the funds. But here, in the case before us, there is no question of the appellant having presented any presented any forged documents or fraudulent documents.

We may, illustrate this aspect - relating to fraudulent documents' - by referring to the well- known case of UCM (Investments) vs. Royal Bank of Canada [1982 (2) All ER 720 (HL) decided by the House of Lords which has been referred to by this Court in the U.P.Cooperative Federation case (supra). In that case the date 15th December, 1976 was falsely and fraudulently entered on the Bill of Loading as the date on which the goods were shipped even though the goos were actually shipped on 16th December, 1976 and the Bank which came to know about this fact refused to pay. The House of Lords held that the bank could have justifiably refused to pay because the Bill of Loading, which was one of the documents to be presented before the Bank, was there a fraudulent document. Having laid down the principle as stated above, the House of Lords however held on facts that the said false statement on the bill of loading was not made by the seller but was made by the shipping agent and inasmuch as the sellers were not responsible, the Bank could not refuse payment. We are referring to this case only to illustrate what could be a 'fraudulent document' presented before the Bank by the sellers. We shall also refer a little later to another case in Sztejn vs. H.Henry Schroder Banking Corporation [(1941) 31 NYS (2d) 631] which is also a case of presentation of 'fraudulent documents'.

Likewise in the 'Cement scandal Case' in Establissement Esefka International Anstalt vs. Central Bank of Nigeria [1979 (1) LLoyds Law Reports 445 (CA)], Lord Denning pointed out that the

shipping documents, the bills of loading, certificates etc. were there forged and were all "moonshine" and there wee no such shipping vessels at all. That case is an example of forged documents.

What is necessary for the Bank to refuse payment is a case of clear "fraud" and the Banks knowledge as to such fraud (Bolivinter Oil S.A. vs. Chase Manhattan Bank N.A.) [1984 (1) (1) LLR 392]. As pointed by Lord Denning and Lord Lane in Edward Owen the Bank cannot refuse payment merely because according to it the claim was "dishonest" or "suspicious" or it appeared to be a sharp practice but it must be established as 'fraud'. Lord Ackner in United Trading Corporation S.A. & Murray Clayton Ltd. vs. Allied Arab Bank Ltd. & Others [1985 (2) LLR 554 (CA)] held that the Bank could object to pay not because the demand was not "honestly" made but was made fraudulently. Waller, J. in Turkiye vs. Bank of China [1996 (2) LLR 611 (617-618)] said that the question was whether the demand for payment was "fraudulent". Mere allegations and counter allegations between the parties as to breach of contract, non-payment of advances or non-supply of machinery did not amount to fraud.

In the result we hold that an allegation of non-supply of goods by the sellers to the buyers did not by itself amount, in law, to a plea of 'fraud' as understood in this branch of the law and hence by merely characterising alleged non-movement of goods as 'fraud', the Bank cannot claim that there was a cause of action based on fraud or misrepresentation. Nor is the case before us one where thee is an allegation of presentation of forged or fraudulent documents.

Learned counsel for the respondent then relied upon the judgment in Discount Records Ltd. vs. Barclay's bank Ltd. [1975 (1) All ER 1071]. In that case, Megarry, J. referred to the American case in Sztejn vs. J. Henry Schroder Banking Corporation [(1941) 31 NYS (2d) 631] decided by the New York Court of Appeals. In that case Shientag, J. distinguished cases of breaches of warranty as to quality from cases of deliberate failure to supply goods and said:

> "In such a situation, where the seller's fraud has been called to the bank's attention before the drafts and documents have been presented for payment, the principle of the independence of the bank's obligation under the letter of credit should not be extended to protect the unscrupulous seller"

Megarry,J. then distinguished the American Case on the ground that "It was important to notice that in the Sztejn case, the proceedings consisted of a motion to dismiss the formal complaint on the ground that it disclosed no cause of action. That being so, the Court had to assume that the facts stated in the complaint were true".

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Learned counsel for the respondent Bank contended that the case before us which is concerned with an application under Order 7 Rule 11(a) CPC for rejecting a plaint on the basis of "absence of cause of action from a reading of the plaint" was identical with the Sztejn case and hence what Megarry, J. stated Discount Records Ltd. directly applies.

It is true, we are also dealing with a question whether the plaint disclosed a cause of action. But here the allegation in the plaint is only one relating to absence of movement of goods by the seller. As pointed in the decided cases and in particular in the U.P. Cooperative Federation Case and other cases decided by this Court and also Courts elsewhere, mere absence of movement has never been, in this branch of law, treated as amounting to fraud, Such non- movement, event if the allegation is to be treated as true, could be for goods reasons or for reasons which were not good. But that is not 'fraud'. In Sztejn (See law relating to commercial credit by A.G. Davis (2nd Ed, 1954) (p160-61 for facts of this case) the position was different. There the complaint was that the sellers who were to ship complaint was that the sellers who were to ship 'bristles' deliberately placed 50 cases of material on board a steamship, procured a bill of loading from a steamship company and obtained customary invoices. The documents described the goods as bristles as per the letter of credit. In fact, the Indian sellers had filled the 50 crates with 'Cowhair' and other worthless material and rubbish with intent to simulate genuine merchandise and so 'defraud' the plaintiff, the buyers - who has instructed the defendants to issue the letter of credit. The sellers then drew a draft under the letter of credit to the order of the Chartered bank of India, Australia and China and delivered the draft and the 'fraudulent documents' to the chartered Bank at Cawnpore for collection on account of the sellers. The buyer brought the action which succeeded, to restrain the defendants from paying the draft. The Learned Judge said (p.634):

> "It must be assumed that the seller has intentionally failed to ship any gods ordered by the buyer. In such a situation, where the seller's fraud has been called to the bank's attention before the draft and documents have been presented for payment, the principle of the independence of the bank's obligation under the letter of credit should not be extended to protect the unscrupulous seller. It is true that even though the documents are forged or fraudulent, if the issuing bank has already paid the draft

> before receiving notice of the seller's fraud, it will be protected if it exercised reasonable diligence before making such payment. However, in the instant action Schroder had received notice of Transea's active fraud before it accepted or paid the draft. The Chartered Bank, which stands in no better position than Transea, should not be heard to complain because Schroder is not forced to pay the draft accompanied by documents covering a transaction which it has reasons to believe is fraudulent"

It will be noticed that Sztejn was a case where 'fraudulent documents' were presented which simulated shipping of goods which were not only not shipped but on the other hand the seller shipped some rubbish deliberately. Therefore the allegations in the complaint filed by the buyers in that case were based upon the above facts - which as per the legal position in this branch of law - i.e. presentation of 'fraudulent document's where goods were deliberately not shipped and an attempt was made to pass off 'rubbish' as the goods ordered for - amounted to 'fraud'.

As stated above non-movement of goods by the seller could be due to a variety of tenable or untenable reasons, the seller may be in breach of the contract but that by itself does not permit a plaintiff to use the word "fraud" in the plaint and get over any objections that may be raised by way of filing an application under Order 7 Rule 11 CPC. As pointed out by Krishna Iyer,J. in T.Arivandandam's case, the ritual of repeating a word or creation of an illusion in the plaint can certainly be unravelled and exposed by the Court while dealing with an application under Order 7 Rule 11(a). Inasmuch as the mere allegation of drawal of monies without movement of goods does not amount to a cause of action based on 'fraud', the Bank cannot take shelter under the words 'fraud' or 'misrepresentation' used in the plaint.

Learned counsel for the appellant also contended that this was a case where a letter of credit was without recourse to the invoice value.

For the aforesaid reasons, we hold that there is no cause of action even from the plaint allegations, against the appellant. Appeal allowed and the plaint is rejected under Order 7 Rule 11(a) as against the appellant-5th defendant. Appeal is allowed accordingly to the extent. Thee will be no order as to costs.