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IN THE HIGH COURT OF DELHI AT NEW DELHI

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CS(OS) 1252/2000

20th November, 2012

EMCO LIMITED

.....Plaintiff

Through: Mr. Jay Savla, Advocate.

VERSUS

MALVIKA STEEL LIMITED & ORS.

..... Defendants

Through: Mr. P.S. Bindra, Advocate with Mr. Ketan
Madan, Advocate for defendant No.2.

CORAM:

HON'BLE MR. JUSTICE VALMIKI J.MEHTA

To be referred to the Reporter or not?

VALMIKI J. MEHTA, J (ORAL)

1. The subject suit has been filed by the plaintiff-company M/s. EMCO Limited for declaration and permanent injunction. Though there are three defendants in the suit, the relief of injunction is claimed against the defendant No.2 for preventing it from encashing the bank guarantee issued by the defendant No.3- Dena Bank. The bank guarantee was issued on the request of the defendant No.1 by the defendant No.3 and of which the defendant No. 2 is the beneficiary.

2. The facts of the case are that the defendant No.1 placed a purchase order upon the plaintiff for supply of various transformers. The purchase order is dated 31.10.1996 and the same was for design, engineering, manufacture, supply, supervision of erection, testing and commissioning nine Nos.12.5/15 MVA, 33/6.9 KV transformers alongwith mandatory spares. The transformers were to be supplied originally under three lots on or before April, 1997, May, 1997 and June, 1997. The disputes in the present case pertain to the supply of two transformers with the mandatory spares under the second lot. There were various amendments to the purchase order with respect to extension of time for supply of transformers and for the purpose of present judgment it is not required to refer to all such amendments except the amendment dated 18.11.1998 by which the supply of second lot was to be completed by 31.7.1998 and thereafter which period was extended upto 31.3.1999. In order to secure the performance of the contract, the plaintiff had to and therefore it got issued a performance bank guarantee from the defendant No.3 in favour of the defendant No.2. Actually the beneficiary would have been defendant No. 1 who placed the purchase order, however, on the agreement between the defendant Nos. 1 & 2, the defendant No. 2 became the beneficiary. The bank guarantee in question is the bank guarantee dated 8.10.1998 for a sum of ₹ 8.5 lacs. The validity period of this bank guarantee was upto

31.5.2000. This bank guarantee was invoked by the defendant No.2 by its letter dated 26.5.2000 and which has been challenged in the present suit on the ground that the said invocation is fraudulent. The invocation is said to be fraudulent inasmuch as the plaintiff claims to have duly supplied the two transformers and the mandatory spares which pertained to second lot of two numbers of transformers to be supplied under the purchase order dated 31.10.1996.

3. The subject suit has thus been filed claiming the reliefs of declaration and injunction and the main relief in which is that the subject bank guarantee dated 8.10.1998 is void on account of fraudulent conduct of the defendant No. 1 and hence no payment under the said bank guarantee should be made by the defendant No.3 to the defendant No.2.

4. Defendant No.2 has appeared and filed its written statement. No one however has appeared for the defendant No.1 which has been set exparte. Defendant No.3 was the bank which issued the bank guarantee and it is only a proforma party.

5. The defence of the defendant No.2 is that the bank guarantee has been invoked in terms of the requirement of the bank guarantee inasmuch as the defendant No.1 is guilty of breach of contract and that the plaintiff by means of the letter dated 22.12.1999 had been informed by the defendant No. 1 that the plaintiff

had committed a breach of contract by failing to supply the spares/lose items as stated in the said letter. It is therefore claimed by the defendant No.2 that on account of breach of contract by the plaintiff, the defendant No.2 was entitled to invoke and seek encashment of the bank guarantee as per such term of the bank guarantee which so provided for encashment on account of breach.

6. The following issues were framed in this suit on 2.8.2005:-

- “1. Whether this Court has territorial jurisdiction to try and entertain the present suit?
2. Whether the plaint is duly signed and verified by duly authorized person on behalf of the Plaintiff?
3. Whether the plaint has been valued correctly for the purposes of Court fee and jurisdiction?
4. Whether Defendant Nos.1 and 2 have committed fraud and the demand by Defendant is fraudulent and invocation of Bank guarantee is made with a view to counter blast the action taken by the Plaintiff as averred in para 4(w) of the plaint?
5. Whether the Plaintiff is entitled to an order of permanent injunction in terms of prayer (c)(i) and (ii)?
6. Whether invocation by Defendants of the Bank guarantee dated 8.10.1998 is void, unenforceable and of no legal effect?
7. Relief.”

Issue Nos.1 to 3

7. These issues are not pressed on behalf of defendants.

Issue Nos.4 to 6

8. These issues are really the crux of the matter. The bank guarantee in question in this case has been proved and exhibited as Ex.PW1/7. The invocation

letter dated 26.5.2000 has been proved and exhibited as Ex.PW1/17. The defendant No.2 has proved and exhibited the letter of the defendant No.1 dated 26.5.2000 to it with respect to default committed by the plaintiff in supply of the mandatory spares as Ex.DW2/3. I may note that the bank guarantee has also been exhibited by the defendant No.2 as Ex.DW2/1.

9. The law with respect to encashment of bank guarantee is well settled. Courts do not interdict encashment of bank guarantees unless the demand is not made in accordance with the bank guarantee or there is an egregious fraud. Issues with respect to breach of contract between the purchaser and seller are not in realm of invocation/encashment of the bank guarantee. Once the bank guarantee is invoked as per its terms, the fact that there may be disputes between the parties to the contract is not a ground for staying the encashment of the bank guarantee.

10. Let us therefore see the terms of the bank guarantee in this case and the relevant letter of invocation to find out as to whether the invocation letter is valid or not. The bank guarantee is as under:-

“The Industrial Finance Corporation of India Ltd.,
Delhi Regional Office
4th Floor, Core No.5,
P.B. No.3043
Scope Complex
7 Lodhi Road
New Delhi-110 003

1) Whereas M/s. The Industrial Finance Corporation of India Ltd., company incorporated under Indian Company Act, 1956 having its registered office at Bank of Baroda Building, 16, Sansad Marg, New Delhi-01 (hereinafter called the "Purchaser") have placed a purchase order No.DRO/MSL/ELS/100/98-2401 dated 30/03/1998 for supply of 6 Nos.12.5/15 MVA, 33/6.9 KV Transformer for Malvika Steel Ltd.'s Integrated Steel Project Jagdishpur with M/s. Emco Transformers Limited, Plot No.F-5, Road No.28, Wagle Industrial Estate, Thane-400 604 (hereinafter called as "Supplier") who have accepted the above said order vide letter dated 30/03/1998.

2) And Whereas, the purchaser have, in lieu of retention money towards supply of 2 Nos. 12.5/15 MVA, 33/6.9 KV Transformers and guarantee from Dena Bank, Industrial Finance Branch, Maker Tower E, Cuffe Parade, Mumbai-400 005, the Banker's of the Supplier.

3) And Whereas, the Purchaser have, called upto the Supplier to furnish a Bank Guarantee for a sum of ₹ 8,50,000/- (Rupees Eight Lacs Fifty Thousand only) towards supply of 2 Nos.12.5/15 MVA Transformers for successful commissioning and performance of the 2 Nos.12.5/15 MVA Transformers (3rd & 4th Unit) as per the aforesaid order of the Purchasers.

4) We, the Banker of the Supplier hereby irrevocable and unconditionally guarantee payment to the purchaser upto and not exceeding altogether a sum of ₹ 8,50,000/- (Rupees Eight Lacs Fifty Thousand only) in case of any breach on the part of the supplier in the execution and performance of the 2 Nos.12.5/15 MVA Transformers covered in the aforesaid Purchase Order supplied by the Supplier and the decision of the Purchaser will be final and binding on us regarding such breach. The payment will be final and binding on us regarding such breach. The payment will be released by us on demand and without reference to the supplier.

(underlining is mine)

5) We, Dena Bank, Industrial Finance Branch, Maker Town E, Cuffe Parade, Mumbai-400 005 shall pay the amount demanded by the Purchaser without any demur and delay even, if any Civil Suit or Court Case is pending regarding the performance of the 2 Nos.12.5/15 MVA Transformers or otherwise.

6)Notwithstanding anything to contrary contained hereinabove, liability under guarantee is restricted to ₹ 850,000/- (Rupees Eight Lacs Fifty Thousand only). Our guarantee shall remain in force until “12” (Twelve) months from the date of successful commissioning of the 2 Nos.12.5/15 MVA Transformers or 18(eighteen) months from the date of receipt of last consignment against the above order of the purchaser i.e upto 31/05/2000.

7)The decision regarding successful commissioning and installation of the 2 Nos.12.5/15 MVA Transformers confirmed by the purchaser will be final and binding on us.

8)All your right under the guarantee shall be forfeited and we shall be relieved and discharged from all liability thereunder unless a claim under the guarantee is made in writing on or before the stipulated time as given above.

Notwithstanding anything contained herein:

1)Our liability under this Bank Guarantee shall not exceed ₹ 850,000/- (Rupees Eight Lacs Fifty Thousand only)

2)This Bank Guarantee shall be valid only upto 31/05/2000.

3)We are liable to pay the guaranteed amount or any part thereof under this Guarantee only and only if you serve upon us a claim or demand on or before 31/05/2000.

Dated at Mumbai this 8th day of October, 1998.”

11. The letters of invocation dated 26.05.2000 reads as under:-

“DRO/PR.H/781/2000

The Branch Manager,

Dena Bank,

Industrial Finance Branch,

Maker Tower E, Cuffe Parade,

Mumbai-400005.

Re: Encashment of Bank Guarantee No.12762/98 dated 8.10.1998 for ₹ 8,50,000.00-a/c M/s Emco Transforms Limited.

On behalf of M/s Emco Transformers Limited, Plot No.F-5, Road No.28, Wagle Industrial Estate, Thane-400 604 (Maharashtra) you have executed an irrevocable & unconditional Bank Guarantee being No.12762/98 dated 8.10.1998 favouring ourselves for an amount of ₹ 8,50,000.00.

As the said M/s Emco Transformers Limited committed breach in execution and performance of two numbers 12.5/15 MVA Transformers covered in the contract, we hereby invoke the said Bank Guarantee and call upon you to pay ₹ 8,50,000.00 to us forthwith at New Delhi on receipt of this letter failing which we shall be constrained to take appropriate action against you as may be deemed fit for recovery of the said amount together with interest and costs.

(underlining is mine)

Yours sincerely,

(Prasenjit Kar)
Deputy General Manager (Law)”

12. The letter of the defendant No.1 to the defendant No.2 stating the breach has been committed by the plaintiff in failing to supply the mandatory spares is Ex.DW2/3 dated 26.5.2000 and the same reads as under:-

“May 26, 2000

IFCI Ltd
Delhi Regional Office
IFCI Tower, Nehru Place
New Delhi-110 019

Reg: Equipment Leasing Assistance of ₹ 100 crore-Purchase Order No.DRO/MSL/ELS/10/98-2401 to M/s Emco Transformers.

Dear Sir,

Please refer to our letter dated May 19, 2000 whereby we have mentioned that the supplier has not complied with the terms of purchase order and had requested to encash their Performance Bank Guarantee.

The terms not complied are as follows:

1. Short supply of items as transformer oil, nuts, bolts & fittings,
2. Non supply of spares and accessories
3. Non availability of technical persons at the time of inspection & installation at the site.

You are requested to take further necessary action.

Thanking you,

Yours faithfully,
For Malvika Steel Ltd.

N.N. Saxena
DGM Finance.”

13. A reading of the bank guarantee alongwith the invocation letter as also the letter Ex.DW2/3 of the defendant No.1 to the defendant No.2 shows that the bank guarantee in question specifically entitles encashment of the same once the beneficiary informs the defendant No.3-bank that there is a breach on the part of the supplier/plaintiff in execution and performance of the contract qua the two numbers of transformers. The relevant clause is clause 4 of the bank guarantee and which has been reproduced in its entirety above. When we see the invocation letter Ex.PW1/17 it is clear that the said letter specifically states that the invocation is done because of the breach committed by the plaintiff in the execution and

performance of the contract qua two numbers of transformers. This language of the invocation letter is exactly the same as contained in and as required by para 4 of the bank guarantee. The demand therefore made under the letter Ex.PW1/17 is in accordance with the terms of the bank guarantee. Since the bank guarantee was valid upto 31.5.2000, the same has thus been invoked within the validity period.

14. In my opinion, this Court cannot grant the relief of declaration and injunction as prayed for by the plaintiff inasmuch as the demand/invocation of the bank guarantee in the present case is in terms of the bank guarantee and the demand is within the validity period of the bank guarantee. Once there are disputes between the supplier and buyer with respect to contract i.e non-supply of spares as stated in the invocation letter, then, in such a case the beneficiary being the defendant No.2 is entitled to invoke and encash the bank guarantee because the requirement of encashment of the bank guarantee is fulfilled that there is breach in execution and performance of the contract for supply of two numbers of transformers as per the invocation letter. Whether in reality there is or is not any breach of the contract i.e. the aspect on merits is not one which the issuing bank of the bank guarantee has to consider for making payment under the bank guarantee. It is in fact for this reason that para 5 of the bank guarantee specifically states that the amount demanded will be paid without any demur or delay, and, even if a

Court case is pending with regard to performance of the contract qua the two numbers of transformers.

15. Counsel for the plaintiff sought to place reliance upon the judgment of a learned Single Judge of the Bombay High Court in the case of ***Crest Communications Ltd. Vs. State Bank of India and Anr. 2000 (2) Bom. L.R. 193*** of R.M. Lodha, J. (as his Lordship then was) to canvass the proposition that once no performance is required to be further done as per the contract, the performance bank guarantee cannot be enforced. Of course, there is no dispute to the proposition that if a performance guarantee is given on the basis of same being valid for the performance period and the performance itself admittedly has been done or on the performance period has come to an end, there would be no requirement of making payment under the bank guarantee. The judgment in the case of ***Crest Communications (supra)*** in this regard relies upon the earlier judgment of the Supreme Court in the case of ***Larsen and Toubro Limited Vs. Maharashtra State Electricity Board, AIR 1996 SC 334.***

16. In the facts of the present case defendant Nos.1 and 2 are disputing/denying that the entire performance under the bank guarantee is complete. It is being alleged by the defendant Nos.1 and 2 that the plaintiff has committed breach of contract in not supplying of the mandatory spares and so duly

stated in the letter dated Ex.DW2/3. Once there are allegations of breach of contract, as already stated above, the issuing bank cannot stop the payment of bank guarantee inasmuch as issues of performance or breach of contract are not issues for stopping encashment of the bank guarantee. The facts in the case of ***Crest Communications (supra)*** were thus different from the facts of the present case inasmuch as the judgment in that case proceeded on the basis that the performance which was required to be done under the contract in the case was complete. As already stated, in the present case, admittedly there are allegations made by the defendant Nos.1 and 2 that performance under the contract is not complete as the mandatory spares are not supplied. Once, therefore, there is breach of contract by non-supply of mandatory spares, it cannot be thus said that performance under the contract is complete and hence the judgment in the case of ***Crest Communications (supra)*** which is based upon the judgment of the Supreme Court in the case of ***Larsen and Toubro Limited (supra)*** cannot apply to the facts of the present case.

17. Issue Nos.4 to 6 are accordingly decided against the plaintiff and in favour of defendant No.2 and it is held that the invocation letter being in accordance with the terms of the bank guarantee, there is no ground to stop payment of the bank guarantee on account of alleged fraud.

Relief

18. In view of the above, plaintiff is not entitled to the reliefs as claimed for in the suit. The suit is accordingly dismissed, leaving the parties to bear their own costs.

NOVEMBER 20, 2012
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VALMIKI J. MEHTA, J.