

* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

% **Judgment reserved on: 8th August, 2016**
Judgment pronounced on: 29th August, 2016

+ **Arb. A. (Comm.) No.23/2016 & I.A. No.9551/2016**

RATTANINDIA NASIK POWER LTD Petitioner
Through Mr.Parag P. Tripathi & Mr.Rajiv
Nayar, Sr.Advs. with Mr.Rajat
Navet, Mr.Jeevesh Nagrath,
Mr.Saurabh Seth & Mr.Dalveer
Thakran, Advs.

versus

BHARAT HEAVY ELECTRICALS LTD Respondent
Through Mr.P.V.Kapur, Sr.Adv. with Mr.Punit
Tyagi, Mr.Ankit Parhar, Mr.Abhilash
Chaudhary & Mr.Ambarish Pandey,
Advs.

CORAM:
HON'BLE MR.JUSTICE MANMOHAN SINGH

MANMOHAN SINGH, J.

1. By way of this order, I propose to decide the abovementioned appeal filed by the appellant (who is the respondent in the arbitration proceedings) under Section 37(2)(b) of the Arbitration and Conciliation Act, 1996 (hereinafter referred to as the "Act") against the interim order dated 4th August, 2016 passed by the Arbitral Tribunal under Section 17 of the Act. The respondent herein is the claimant in the arbitration proceedings. The appellant has also raised a counter-claim in the arbitration proceedings which is pending adjudication.

By the impugned order, the Arbitral Tribunal has directed the release of the Advance Bank Guarantee ('ABG') as well as the

Performance Bank Guarantee ('PBG'), as the contract was terminated by the respondent.

2. The brief facts of the case as pleaded by the appellant are as under:-

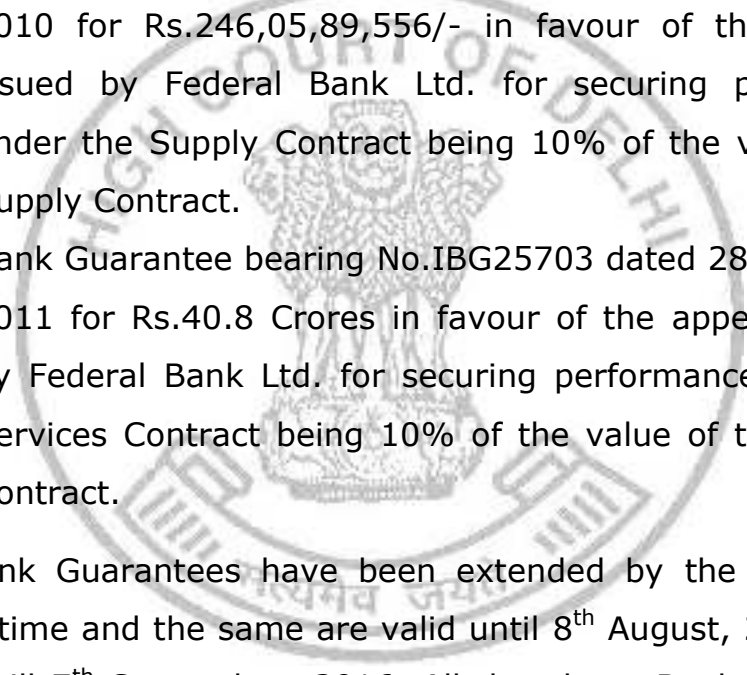
- (i) The appellant had engaged the services of the respondent for setting up of a Thermal Power Plant at Nasik, Maharashtra. The respondent was to make the supplies and was also to erect and commission the power plant. The power plant project was divided into two phases i.e. Phase-I which was for 1350 MW and Phase-II which was for 5X270 MW.
- (ii) A Letter of Award ('LOA') was issued by the appellant in favour of the respondent on 8th October, 2010, as amended on 26th April, 2011, for Design, Engineering, Manufacturing, Shop Inspection and Testing, Supply, Transportation, Erection, Commissioning and demonstration of Performance Guarantees along with comprehensive Marine cum Erection insurance of 5X270 MW Thermal Power Plant Project at Nasik, Maharashtra (Phase-II).

In terms of Clause 4.1 of the LOA, 5% of the contract price had to be paid by the appellant to the respondent as advance against security of Advance Bank Guarantee of equal amount to be provided by the respondent to the appellant. The Advance Bank Guarantee was to remain valid till recovery of advance or successful completion of commissioning, whichever was earlier.

- (iii) In addition to the Advance Bank Guarantee, the respondent was also to furnish a Contract Performance Guarantee for 10% of the contract price and which was to remain valid till the expiry of warranty period.

- (iv) The works were divided under two contracts namely, supply contract and the services contract. In furtherance of the LOA, a supply contract was executed on 26th May, 2011 (as amended on 3rd August, 2011 and on 2nd May, 2012) ('Supply Contract') and the services contract was executed on 26th May, 2011 (as amended on 2nd May, 2012) between the appellant and the respondent.
- (v) The total value of the Supply Contract was Rs.17,12,09,14,280/- ; USD 52,056,000 and Euro 8,27,24,000.
- (vi) In terms of Clause 5.1, 6 and 8.1 of the Supply Contract, the appellant paid a sum of Rs.123 Crores to the respondent towards advance payment. The receipt of this payment is admitted and cannot be disputed by the respondent.
- (vii) The appellant has also submitted that the appellant in addition to advance amount has further paid a sum of Rs.29.22 crores against supplies made by the respondent and the said amount is more than the actual sequential supplies, as required in the contract, made by the respondent.
- (viii) The total value of the Services Contract was Rs.413 Crores. In terms of Clauses 5.1, 6 and 8.1 of the Services Contract, the appellant paid a sum of Rs.17 Crores to the respondent towards advance payment. The receipt of this payment is admitted and cannot be disputed by the respondent.

3. On receipt of the advance payment from the appellant and to secure the same in terms of the Supply Contract and Services Contract, the respondent furnished the following Bank Guarantees in favour of the appellant:

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- a) Bank Guarantee bearing No.IBG23533 dated 8th November, 2010 for Rs.123,02,94,778/- in favour of the appellant issued by Federal Bank Ltd. for securing the advance under the Supply Contract.
 - b) Bank Guarantee bearing No.IBG25702 dated 28th February, 2011 for Rs. 17 Crores in favour of the appellant issued by Federal Bank Ltd. for securing the advance under the Services Contract.
 - c) Bank Guarantee bearing No.IBG23534 dated 8th November, 2010 for Rs.246,05,89,556/- in favour of the appellant issued by Federal Bank Ltd. for securing performance under the Supply Contract being 10% of the value of the Supply Contract.
 - d) Bank Guarantee bearing No.IBG25703 dated 28th February, 2011 for Rs.40.8 Crores in favour of the appellant issued by Federal Bank Ltd. for securing performance under the Services Contract being 10% of the value of the Services Contract.

4. The Bank Guarantees have been extended by the respondent from time to time and the same are valid until 8th August, 2016 with a claim period till 7th September, 2016. All the above Bank Guarantees (hereinafter collectively referred to as the "Bank Guarantees") are unconditional and are payable without any demur or protest or any recourse to the respondent and the payment under the same is liable to be made to the appellant on demand.

5. On merits, it is the case of the appellant that firstly, the work for Phase-I of the power plant was initiated and while the works for Phase-I were going on, the appellant realized that the respondent was

engaging in outright dumping of material at site, which was not even required as per the scheme of construction and establishment of a Thermal Plant, which normally spans for a duration of nearly 2 to 3 years and the supply as well as erection contract ought to be technically and sequentially executed and acted upon in such a manner that the given timelines are not violated. But in violations of such conventional and contractual obligations, the respondent in order to raise invoices and to do book building for achieving the respondent's financial targets, indulged in dumping of unwanted and untimely material supplies. Since, the scheme of contractual execution was such that the respondent was also the supplier of the material and also the service provider for erection of the plant, it could easily indulge in dumping of material sans all technical and contractual standards befitting the conventional and technical norms for establishment of a thermal plant. The modus operandi adopted by the respondent was that it used to keep supplying material at site even though the stage for erection for the same was not even foreseeable in the near future and the material that was required immediately for completion of the erection work having regard to the stage of erection had not been supplied and those supplies were being delayed because of lack of preparedness on the part of the respondent, as the respondent was dumping material at site which was of no use at the time of the supply or even in the near foreseeable future.

6. It is also the case of the appellant that the respondent did not make supplies and performed the services in terms of the contract, therefore, the appellant is, *inter alia*, entitled to refund of the advances made and the respondent is not entitled to the amount claimed by it.

On the other hand, the respondent alleges that the respondent is entitled to the amounts claimed by it as per the invoices raised by it.

In the earlier order dated 7th January, 2016, the Bank Guarantees had been directed to be kept alive by this Court in order to secure and protect the interest of the appellant. The main requirement of the bank guarantees is to secure the amount which had been advanced by the appellant and also the performance of the contract is a contractual requirement.

7. This Court by order dated 7th January, 2016 directed that OMP (I) No.205 of 2015 under Section 9 of the Act should be treated as an application under Section 17 of the Act and the status quo order dated 7th May, 2015 would continue until varied or modified by the Arbitral Tribunal.

7.1 The appellant filed its reply on 11th April, 2016 to the petition being treated by the Arbitral Tribunal as an application under Section 17 of the Act.

7.2 The respondent in April, 2016 itself had filed its statement of claim before the Arbitral Tribunal raising therein false, frivolous, baseless and misconceived claims against the appellant which are liable to be rejected.

7.3 During the pendency of the arbitration proceedings and also during the pendency of Section 9 Petition, which has been converted to Section 17 Application, the respondent filed another application on 14th April, 2016 under Section 17 of the Act praying for the release of the Bank Guarantees.

7.4 The appellant had filed a detailed statement of defence on 26th May, 2016 setting out therein the true and correct facts and had also

raised its counter claim, *inter alia*, praying return of money and for the declaration that the termination of contract was wholly illegal.

7.5 The appellant also filed a detailed reply dated 26th May, 2016 contesting and opposing the application filed by the respondent under Section 17 of the Act seeking discharge of the bank guarantees.

8. The issue before the Arbitral Tribunal is – whether the amount advanced has been adjusted or not, or the termination is valid or not, or the appellant is entitled to the prayer of performance of terms of contract once it is terminated. All these disputes *inter alia* are yet to be adjudicated on merits by the Arbitral Tribunal.

9. While the disputes were pending adjudication, the respondent gave a notice of termination to the appellant under Clause 20.3 of the Supply Contract and under Clause 49.3 of the Service Contract on 27th August, 2015. The respondent stated that if the appellant failed to remedy the alleged breaches, it would be constrained to take steps to terminate the Contracts. In response to the termination notice, on 21st October, 2015 the appellant stated that no outstanding dues are to be paid by the appellant to the respondent, in fact, the advance payment made by the appellant under the Contracts is much more than what the respondent has performed so far. It was stated that the respondent has not performed its obligation under the Contracts. The respondent on 27th November, 2015 terminated the Contracts.

10. The respondent has also made a claim against the appellant for Bank Guarantee charges to keep the Bank Guarantees alive. The claims of the respondent are being contested by the appellant which are pending adjudication.

11. In the impugned order, the Arbitral Tribunal has directed the release of Bank Guarantees in question by the impugned order by observing that the respondent is a financially sound and credit worthy Company and therefore, there would be no use in keeping the Bank Guarantees in question alive, even though, for the year ended 31st March, 2016, the respondent has posted a loss of Rs.897.00 Crores.

The impugned order is in respect of Bank Guarantees given for Phase-II of the Nasik Thermal Power Plant. Similar order has been passed by the Arbitral Tribunal for Amravati Project Phase-II as well.

12. Mr.P.V.Kapur, learned Senior Counsel appearing on behalf of the respondent argued that the contract between the parties has been terminated. The same was of determinative nature. The relief sought by the appellant for specific performance before the Arbitral Tribunal cannot be allowed under Section 14 of the Specific Relief Act. At the best, the appellant can press the relief of compensation. The respondent is the claimant who has to recover huge amount from the appellant. Therefore, the Arbitral Tribunal has taken the correct approach under those circumstances. In the present case balance has been struck between the parties. There is no need to keep the bank guarantees alive. The Arbitral Tribunal has correctly passed the order to return the bank guarantees. He has referred the following decisions:-

- (i) ***Rajasthan Breweries Ltd. v. The Stroh Brewery Company***, AIR 2000 Delhi 450
- (ii) ***Hindustan Construction Co. Ltd. v. State of Bihar & Ors.***, (1999) 8 SCC 436 (para 22)

Mr.Kapur, learned Senior counsel has also referred Section 38 of the Indian Contract Act which reads as under:-

"38. Effect of refusal to accept offer of performance.—Where a promisor has made an offer of performance to the promisee, and the offer has not been accepted, the promisor is not responsible for non-performance, nor does he thereby lose his right under the contract.

Every such offer must fulfil the following conditions:—

(1) it must be unconditional;

(2) it must be made at a proper time and place, and under such circumstances that the person to whom it is made may have a reasonable opportunity of ascertaining that the person by whom it is made is able and willing there and then to do the whole of what he is bound by his promise to do;

(3) if the offer is an offer to deliver anything to the promisee, the promisee must have a reasonable opportunity of seeing that the thing offered is the thing which the promisor is bound by his promise to deliver.

An offer to one of several joint promisees has the same legal consequences as an offer to all of them."

13. The appellant submits that the appellant were enjoined from invoking and encashing the same by order dated 7th May, 2015 in OMP (I) No.205/2015 subject to the condition that the bank guarantees are kept alive, the Arbitral Tribunal should not have directed to release/discharge the bank guarantees until the disputes are adjudicated between the parties.

14. The bank guarantees are unconditional. The law in relation to bank guarantee is well settled. There are only two exceptions in law on the basis of which the invocation and encashment of bank guarantee can be enjoined namely, (a) egregious fraud, and (b) irretrievable harm and injustice. In the impugned order, in para 10, the said two principles have been noted. However, it is argued by Mr.Rajiv Nayar,

learned Senior counsel appearing on behalf of the appellant that the financial strength of the party at whose instance the bank guarantee is given and/or the beneficiary thereof are not a factor to be even considered for the grant of injunction to interdict the invocation and encashment of a bank guarantee, let alone to make it the guiding factor for its discharge. Since, the only two known conditions have not been fulfilled and there are no reasons in the impugned order to that effect, there could not have been any injunction restraining the invocation and/or encashment of the bank guarantees. Thus, the Arbitral Tribunal could not have even injuncted the invocation and/or encashment of the bank guarantees. The least that was required to be done to balance the equities was that the respondent should have been directed to keep the bank guarantees alive as had been ordered by this Court by its orders dated 7th May, 2015 and 7th January, 2016. Instead, the Arbitral Tribunal has by the impugned order directed the release of the bank guarantees as an interim measure which is absolutely contrary to the well settled principles of law governing Bank Guarantees.

15. Mr.Rajiv Nayar, learned Senior counsel has referred the following decisions:-

- (i) ***U.P. State Sugar Corporation v. Sumac International Ltd.***, (1997) 1 SCC 568 (Paras 6, 9, 11, 12, 15, 16 & 17).
- (ii) ***Abir Infrastructure Pvt. Ltd. v. Teestavalley Power Transmission Limited & Ors.***, 214 (2014) DLT 235(Paras 31 to 35).
- (iii) ***Futecht Project (India) Pvt. Ltd. v. Abott Healthcare Pvt. Ltd. & Ors.***, 2016(155)DRJ 474 (Paras 4 to 8).
- (iv) ***Hindustan Steel Works Construction Ltd. Vs. Tarapore & Co. & Anr.***, (1996) 5 SCC 34 (Paras 5, 14 & 23).

(v) ***Dorab Cawasji Warden v. Coomi Sorab Warden & Ors.***,
1990(2) SCC 117 (Paras 15 & 16)

In reply to Mr.Kapur's arguments, Mr.Rajiv Nayar, learned Senior counsel argued that all the bank guarantees are unconditional. Pertaining to performance bank guarantees, admittedly advance payment has been received by the respondent. The appellant is agreeable not to encash the said bank guarantees if the respondent will keep the same alive. Counsel further agrees that as far as performance bank guarantees are concerned, his client is agreeable if the same be kept alive during the arbitration proceedings, in view of advance payment received by the respondent. With regard to remaining bank guarantees, let the respondent may file an affidavit by way of undertaking to secure the amount if an award is published against it.

16. In case, the decisions referred by the appellant are read in a meaningful manner, the unconditional bank guarantee is an independent contract; the underlying contract cannot be seen or looked into or be tracked as part of the bank guarantee document except for explanations. As of now, there are two different versions of the parties with regard to performance of contract. The said dispute is yet to be decided, as both the parties have raised their respective claims.

17. The reason, as mentioned in the impugned order for directing the release of the bank guarantees, is that the respondent is incurring cost in keeping the bank guarantees alive and the respondent is a Public Sector Undertaking doing substantially well and is earning profits and there is no doubt about the financial soundness and creditworthiness of the respondent. On the above premise, the Arbitral Tribunal held that

no purpose would be served to keep the bank guarantees alive, and directed the discharge/release of the bank guarantees. Without prejudice, it is submitted that the above order has been passed on the basis of a presumption that the respondent is making profit. This presumption is incorrect and contrary to the record.

18. Learned counsel for the appellant has referred certain documents to show that the respondent has suffered a pre-tax loss of Rs.1446.5 Crores and post-tax loss of Rs.897.4 Crores for the quarter/year ended 31st March, 2016 as per the audited financial result of the respondent. Counsel submits that as per his knowledge, there was also no document to show the creditworthiness and profit of the respondent. It is also argued by Mr.Nayar that the Arbitral Tribunal failed to consider that it was admitted and undisputed that advance monies have been received by the respondent from the appellant. The adjustment thereof was the subject matter of the dispute.

19. The Arbitral Tribunal has dealt with both the contracts and all the four bank guarantees together. The advance guarantees i.e. ABGs and the performance guarantees i.e. PBGs have to be considered separately. Similarly, for each of these two guarantees, the claims and counter claims are different under both the Supply Contract and Services Contract. Furthermore, under the Services Contract there is no dispute about the quantity and value of the supplies. However, the Arbitral Tribunal did not consider the same. It is also a matter of fact the Arbitral Tribunal has itself held that there are seriously arguable issues in the present case.

20. The main submission of the respondent is that since the respondent has terminated the contract albeit wrongly and illegally, and irrespective of the fact that the appellant is disputing the

termination, the respondent is entitled to release/discharge of the bank guarantees, is contrary to law because of the reason that the contract between the parties cannot now be performed in view of termination. Counsel says that the only remedy, if available with the appellant, is to press the relief of compensation and damages and the said issue is yet to be determined by the Arbitral Tribunal, thus, the impugned order does not suffer from any infirmity.

21. It is settled law that the termination of the main contract and/or a dispute in respect of termination of the underlying contract is not a ground which will affect the validity and/or enforceability of the bank guarantee. *Reliance is placed on the cases of **Hindustan Steel Works Construction Ltd.** (supra) and **U.P. State Sugar Corporation** (supra), paras 9 & 11 whereof reads as under:-*

"9. By their letter dated 6-9-1995 the State of U.P. through the Special Secretary, Government of U.P. informed the Managing Director of the appellant that it had been decided to transfer the Rohana Kalan (Muzaffarnagar unit) of the appellant to the joint sector. As a result, the expansion project of this unit should be cancelled and appropriate action in accordance with law should be taken. Thereupon the appellant cancelled the agreement by its letter dated 7-9-1995 addressed to the respondent. The appellant claimed a refund of the advance payment of Rs 3,14,78,093 as unutilised and unadjusted amount of advance payment. The appellant, by its four letters all dated 28-10-1995 addressed to the respondent invoked the three bank guarantees in respect of advance payments after giving credit to the respondent for material worth Rs 42 lakhs which had been supplied till then. The appellant also invoked the delivery guarantee for Rs 89 lakhs. The bank guarantees so invoked are: Bank Guarantee No. 9/47 dated 10-8-1989 for Rs 89 lakhs. In this bank guarantee credit for Rs 42 lakhs has been given and the invocation of the bank guarantee is only for the balance sum of Rs 47 lakhs. The second bank guarantee so invoked is No. 9/64

dated 20-11-1989 for Rs 178 lakhs. The third bank guarantee is No. 9/70 of 6-1-1990 for Rs 89 lakhs and the fourth, delivery guarantee is No. 12/88 dated 13-11-1990 for Rs 89 lakhs.

11. These bank guarantees which are irrevocable in nature, in terms, provide that they are payable by the guarantor to the appellant on demand without demur. They further provide that the appellant shall be the sole judge of whether and to what extent the amount has become recoverable from the respondent or whether the respondent has committed any breach of the terms and conditions of the agreement. The bank guarantees further provide that the right of the purchaser to recover from the guarantor any amount shall not be affected or suspended by reason of any disputes that may have been raised by the respondent with regard to its liability or on the ground that proceedings are pending before any Tribunal, Arbitrator or Court with regard to such dispute. The guarantor shall immediately pay the guaranteed amount to the appellant-purchasers on demand."

22. The respondent is relying upon the judgment of the Supreme Court in the case of **Hindustan Construction Co. Ltd.** (supra) to claim that the underlying contract must be treated as part of the guarantee. Reliance on the said judgment by the respondent is misplaced inasmuch as in the said case, the bank guarantee was conditional as has been noted in paragraph No.13 and 14 of the said judgment. In the present case, the bank guarantee is completely unconditional. Therefore, the judgment in the case of **Hindustan Construction Co. Ltd.** (supra) is not applicable.

23. The respondent has also relied upon the judgment of this Court in the case of **Rajasthan Breweries Ltd.** (supra) to allege that since the contract has been terminated, the contract being determinable in nature, the only remedy with the appellant is to seek damages/compensation and the appellant cannot seek the bank guarantee to be

kept alive, which would tantamount to specific performance of the terminated contract.

Reliance on the said judgment by the respondent is misplaced inasmuch as that as already submitted above, the bank guarantee is an independent contract separate from the underlying contract unconnected with the underlying contract. The said judgment is not in relation to bank guarantee.

24. The validity and legality of the termination itself is a subject matter of the adjudication before the Arbitral Tribunal. It is also argued by the appellant that it is not seeking specific performance of the underlying contract in the manner as canvassed by the respondent. The appellant is seeking enforcement of its legal right in relation to the bank guarantees, which are unconditional in the present case, and constitute an independent contract. The direction to the respondent to keep the same alive while injuncting the appellant from invoking and encashing the same is, in fact, a condition imposed by this Court, and not an enforcement of the contractual terms.

25. Mere presumption about the respondent making profit cannot be taken as correct as the appellant has an apprehension that if award is published in its favour, the appellant may face some difficulty in enforcing the same and it is rightly so as demonstrated by the appellant during the course of hearing. On the other hand, in the impugned order, the impression is given that financially the respondent is in sound condition and there would be no difficulty to enforce the Award, if any passed in favour of the appellant.

26. When another appeal being Arb. A. (Comm.) No.24/2016 was being argued, learned counsel for the appellant has made the

suggestion that the bank guarantees which are of securing performance may be kept alive during the pendency of the arbitration proceedings because of the reason that advance amount was received by the respondent and against the advance amount, the said bank guarantees are furnished. Counsel says that the appellant has no objection if the other bank guarantees are returned subject to the condition that either the respondent shall furnish corporate guarantees or to file an affidavit by way of undertaking that if the Award is passed against the respondent, it shall secure the amount at that point of time.

27. In view of the entire gamut of the matter and without expressing any opinion on merits of the matter, I am of the view that at least with regard to performance bank guarantees where the advance amount is received by the respondent, the bank guarantees to that extent of the amount be kept alive during the pendency of arbitration proceedings without prejudice. However, as agreed by the counsel for the appellant, the remaining amount towards the rest of the bank guarantees be released as soon as an affidavit of undertaking is filed to the effect that if the award is passed against the respondent, it shall secure the said amount. On furnishing the fresh bank guarantees of the advance amount received by the respondent, all the original bank guarantees shall be returned to the respondent forthwith. The impugned order is accordingly modified to this extent.

28. The appeal is accordingly disposed of. Pending application also stands disposed of.

29. No costs.

30. Copies of this order be given *dasti* to the learned counsel for both the parties, under the signatures of the Court Master.

(MANMOHAN SINGH)
JUDGE

AUGUST 29, 2016

