

THE HONOURABLE SRI JUSTICE SANJAY KUMAR
AND
THE HONOURABLE SRI JUSTICE P.KESHA RAO

COMCA NOs.40 AND 43 OF 2019

COMMON ORDER

(Per Sri Justice Sanjay Kumar)

1. These two appeals arise out of the order dated 15.07.2019 passed by the learned Judge, Commercial Court-cum-XXIV Additional Chief Judge, City Civil Court, Hyderabad (*for brevity*, 'the Commercial Court'), in C.O.P.No.31 of 2019, a petition filed under Section 9 of the Arbitration and Conciliation Act, 1996. They are therefore amenable to final disposal at the stage of admission by way of this common order.
2. The core issue that arises before us presently is whether the Commercial Court was justified in refusing to grant an injunction as prayed for by Everest Industries Limited, NOIDA, Uttar Pradesh, the petitioner in C.O.P.No.31 of 2019, restraining MW High Tech Projects India Private Limited, Hyderabad, the first respondent therein, from invoking the unconditional bank guarantee issued by Kotak Mahindra Bank Limited, the second respondent therein. In consequence, the issue also arises as to whether the Commercial Court was right in thereafter directing MW High Tech Projects India Private Limited, the first respondent, to furnish third party security, despite refusal of an injunction, and to pay proportionate costs.
3. Parties shall hereinafter be referred to as arrayed in C.O.P.No.31 of 2019 on the file of the Commercial Court.
4. Facts, to the extent admitted and relevant, are as follows: The first respondent was awarded the work of designing, fabricating, supplying and erecting a pre-engineered building for the manufacturing facility of Jaguar & Company Private Limited at RIICO Industrial Area, Bhiwadi, Rajasthan.

In turn, the first respondent awarded a subcontract of this work to the petitioner under letter dated 05.10.2016. A composite agreement for supply and erection of the pre-engineered building was entered into by and between them under Purchase/Frame Order dated 25.11.2016. In terms thereof, the petitioner was to complete the project by 15.03.2017. The defect liability period agreed upon was one year from the date of handing over of the completed project. In the event of failure to complete the project as per schedule, liquidated damages were payable @ 0.5% of the total contract value per week delayed, subject to a maximum of 5% of the total contract value. The Purchase/Frame Order provided for settlement of disputes through arbitration at Hyderabad in accordance with the Arbitration and Conciliation Act, 1996 (*hereinafter*, 'the Act of 1996'). The petitioner was also required to furnish an unconditional and irrevocable performance bank guarantee for 5% of the contract price, which was to be kept valid till the end of the defect liability period. In terms of this requirement, the petitioner furnished a bank guarantee for Rs.1,44,08,036/- from the second respondent bank. Thereunder, the bank unconditionally and irrevocably guaranteed to pay the first respondent Rs.1,44,08,036/- immediately upon receipt of a written demand advising it that the petitioner had not fulfilled its obligations under the subcontract.

5. Admittedly, the petitioner completed the project and handed over the project site to the first respondent only on 31.08.2018. Correspondence ensued thereafter with regard to certain defects in the execution of the project and according to the petitioner, the same were satisfactorily attended to. While so, the petitioner claimed that it received e-mail dated 08.04.2019 from the second respondent bank stating that it had received a request from the first respondent, *vide* letter dated 04.04.2019, seeking to invoke the bank guarantee. Under letter dated

06.04.2019, the second respondent bank however informed the first respondent of its inability to honour the request, pointing out that the invocation did not contain a declaration that the petitioner had not fulfilled its obligations under the subcontract, as required by the bank guarantee.

6. It was at this stage that the petitioner approached the Commercial Court, by way of C.O.P.No.31 of 2019 filed under Section 9(1)(ii) of the Act of 1996, seeking the following interim measures of protection against the first and second respondents:

- i) Restrain Respondent No.1 by way of injunction from invoking the Schedule Bank Guarantee issued by the Respondent No.2 on behalf of the Petitioner.
- ii) Restrain Respondent No.2 from honouring/releasing/transferring/encashment of the Schedule Bank Guarantee issued by the Respondent No.2 to the Respondent No.1 on behalf of the Petitioner either at the request of the Respondent No.1 or otherwise.
- iii) Direct the Respondent No.1 to forthwith deposit an amount of Rs.1,44,08,036/- (Rupees One Crore Forty Four Lakhs Eight Thousand Thirty Six only) or furnish an equivalent security for the said amount.
- iv) Pass such other further order/orders as this Hon'ble Court may deem fit and proper in the facts and circumstances of the case.'

7. By the order under appeal, the Commercial Court allowed the petition in part, directing the first respondent to furnish third party security for Rs.1,44,08,036/- on or before 01.08.2019 but denying an injunction as prayed for. The petitioner was however held entitled to proportionate costs.

8. Aggrieved by the denial of an injunction, the petitioner filed COMCA No.40 of 2019. Aggrieved by the direction to furnish third party security and to pay proportionate costs, the first respondent filed COMCA No.43 of 2019. Both these appeals were filed before this Court under Section 13 (1A) of the Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts Act, 2015.

9. Heard Sri K.V.Rusheek Reddy, learned counsel for the petitioner, and Sri D.Prakash Reddy, learned senior counsel representing Sri Avinash Desai, learned counsel for the first respondent.

10. We may note, at the outset, that the law relating to injunctions restraining invocation of unconditional bank guarantees is well settled. In the course of commercial dealings, when an unconditional bank guarantee is given, the beneficiary is entitled to realise such a bank guarantee in terms thereof and the bank is bound to honour it as per its terms, irrespective of any dispute raised by its customer. The objective behind a bank unconditionally and irrevocably promising to pay, on demand, the amount of liability undertaken in the guarantee, without any demur or dispute, is to inculcate respect for free flow of commerce & trade and to increase faith in commercial banking transactions, unhedged by pending disputes between the rival parties. A bank guarantee is an independent contract between the bank and the beneficiary thereof. Irrespective of any dispute between the beneficiary and the party at whose instance the bank has given the guarantee, the bank is obliged to honour its guarantee, if it is unconditional and irrevocable. The bank is neither concerned with the relations between the beneficiary and its customer nor is it concerned with the question whether either of them had failed in their contractual obligations. The bank must pay according to the tenor of its guarantee, on demand, without proof or condition.

We may also note the recognised exceptions to the aforestated general rule against restraint on invocation of bank guarantees – (A) Where there is established fraud of an egregious nature which would vitiate the entire underlying transaction and (B) Where allowing the encashment of the unconditional bank guarantee would result in irretrievable injury, harm or injustice to the other party. 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. Therefore, the injury, harm or injustice contemplated under this head must be of an exceptional and irretrievable nature. It has to be such a circumstance which would make it impossible for the guarantor to reimburse himself, if he ultimately succeeds. This would have to be decisively established and it must be proved to the satisfaction of the Court that there would be no possibility whatsoever of recovery of the amount from the beneficiary by way of restitution. Mere apprehension that the other party would not be able to pay is not enough.

(See ANSAL ENGINEERING PROJECTS LTD. V/ s. TEHRI HYDRO DEVELOPMENT CORPORATION LTD.¹, U.P.STATE SUGAR CORPORATION V/ s. SUMAC INTERNATIONAL LTD.², DWARI KESH SUGAR INDUSTRIES LTD. V/ s. PREM HEAVY ENGINEERING WORKS (P) LTD³, BSES LTD. (NOW RELIANCE ENERGY LTD.) V/ s. FENNER INDIA LTD.⁴, MAHATMA GANDHI SAHAKRA SAKKARE KARKHANE V/ s. NATIONAL HEAVY ENGG. COOP. LTD.⁵, HIMADRI CHEMICALS INDUSTRIES LTD. V/ s. COAL TAR REFINING CO.⁶ and ADANI AGRI FRESH LTD. V/ s. MAHABOOB SHARIF⁷)

11. Of late, Courts have also coined 'special equities' as a ground for restraining invocation of bank guarantees of this nature, but we find that the exact contours of this phrase have not been delineated in clear terms. In fact, in some of the decisions cited *supra*, the Supreme Court interpreted this phrase as inclusive of 'irretrievable injury or injustice'.

¹ (1996) 5 SCC 450

² (1997) 1 SCC 568

³ (1997) 6 SCC 450

⁴ (2006) 2 SCC 728

⁵ (2007) 6 SCC 470

⁶ (2007) 8 SCC 110

⁷ (2016) 14 SCC 517

12. We may now note certain crucial factual aspects in the case on hand. The initial invocation of the bank guarantee by the first respondent came to naught as the bank refused to honour the same as there was no declaration that the petitioner had failed to fulfil its obligations under the subcontract. However, without awaiting invocation of the bank guarantee afresh by the first respondent, the petitioner rushed to the Commercial Court by way of the subject petition. We are informed that the first respondent again invoked the bank guarantee but the said letter of invocation is not part of the record and for good reason. That being so, the reason for invocation of the bank guarantee by the first respondent is not disclosed as yet. In such a situation, the petitioner can only surmise and speculate as to what could be the grounds for such invocation. This, in essence, was its endeavour before the Commercial Court, as is clear from the order dated 15.07.2019. On the one hand, it contended that as the project site was handed over by it in August, 2018, invocation of the bank guarantee several months later was not justified. On the other hand, it alleged on the strength of newspaper reports that the first respondent was in a financial crisis and that the bank guarantee had been invoked to overcome financial difficulties. Further, it claimed that delay in the completion of the project could not be solely attributed to it and even if any damages were to be claimed from it, the same would not justify such invocation. According to it, Jaguar & Company Private Limited had expressed satisfaction with its work and there was thus no call for the first respondent to invoke the bank guarantee.

13. The first respondent contested the claim of the petitioner before the Commercial Court contending that no grounds were made out for injuncting it from invoking the bank guarantee in terms of the settled legal position. It denied the allegation that it was in financial trouble and

asserted that it was part of a large German multinational conglomerate having business in more than 20 countries.

14. Thereupon, the Commercial Court framed the following points for consideration:

- '1. Whether the petitioner could establish the circumstances, in which, an injunction order can be granted against respondent No.1 from invoking bank guarantee?
2. Whether the Court can direct the 1st respondent to furnish security to an amount of Rs.1,44,08,036/- (Rupees One Crore Forty four lakhs eight thousand and thirty six only)?

15. Having considered case law on the subject, the Commercial Court found that the proof required to establish special equities was of a higher degree but the same was not established by the petitioner. The Commercial Court further opined that even if the first respondent was facing any financial trouble, it could not be said that it was about to become insolvent and would be incapable of paying monies if the petitioner succeeded in the arbitration proceedings. Observing that the bank guarantee in question was an unconditional and irrecoverable one, the Commercial Court held that the petitioner failed to establish entitlement to the relief of injunction against encashment thereof.

16. As regards the second point, the Commercial Court opined that as the default liability period was almost over and Jaguar & Company Private Limited had not raised any objection as to the quality of the work, a case was made out for grant of relief under Order 38 Rule 5 CPC. This observation was made despite the finding that there was no material to conclude that the first respondent was in a financial crisis. The Commercial Court further reasoned that refusal of an injunction would entitle the first respondent to encash the bank guarantee and if the petitioner succeeded in the arbitration proceedings, it would have to recover the amount from the first respondent. It is on this basis that it

directed the first respondent to furnish third party security within a time frame and pay proportionate costs.

17. In this factual matrix, Sri K.V.Rusheek Reddy, learned counsel, would argue that the first respondent has no inviolable right to invoke the bank guarantee as per its whims. He would assert that when there is no justification on facts for invocation of a bank guarantee, the case would come within the ambit of 'special equities', a recognized exception to the general rule of non-intervention in matters pertaining to invocation of bank guarantees.

18. *Per contra*, Sri D.Prakash Reddy, learned senior counsel, would contend that that it is not open to the Commercial Court to go beyond the noted exceptions to the general rule and look into the merits of the matter. He would assert that the satisfaction certificate relied on by the petitioner itself indicated that the quality of performance was below par in relation to most of the parameters, clearly demonstrating that there was a lot left to be desired in the petitioner's performance.

19. Having given our earnest consideration to the pertinent facts in the backdrop of the settled legal position, we are not persuaded to agree with Sri K.V.Rusheek Reddy, learned counsel. When a bank guarantee is unconditional, the bank is bound to pay according to the dictates of such guarantee on demand, without further proof or conditions. Therefore, the question of seeking justification for invocation of an unconditional bank guarantee *per se* does not arise. Be it noted that all that was required for invocation of the bank guarantee was a declaration by the first respondent that the petitioner had not fulfilled its obligations under the subcontract. Once such a statement was made, encashment of the bank guarantee necessarily had to follow. In any event, the contentions of Sri K.V.Rusheek Reddy, learned counsel, are just shots in the dark, as it cannot be said at

this stage with any certainty as to why the first respondent chose to invoke the bank guarantee. A number of obligations are set out in the subcontract and the speculative arguments urged before us, to the effect that none of the obligations were breached, require us to initiate a roving enquiry which, on the face of it, would be wholly beyond jurisdiction. As already pointed out *supra*, justification for invoking an unconditional bank guarantee would not be within the domain of review by the Court dealing with a plea to restrain such invocation.

20. We may also note that 'equity', as generally understood, means fairness or the application of general principles of justice to correct or supplement the law. In terms of this definition, we are of the considered opinion that the ambit of 'special equities' cannot be stretched to the extent of including an enquiry into the justification for invoking an unconditional bank guarantee. Precedential wisdom also does not support such construction. We therefore hold that it would not be open to the Court, while dealing with an application for restraining invocation of an unconditional bank guarantee, to go into the merits of the matter in the guise of 'special equities' and decide as to whether such invocation was justified on facts or not. To that extent, the Commercial Court erred in recording *prima facie* findings on these aspects. Such findings shall therefore have no binding value in the arbitral proceedings or in a later judicial proceeding.

21. We find that the decision in GANGOTRI ENTERPRISES LIMITED V/ s. UNION OF INDIA⁸, relied upon by Sri K.V.Rusheek Reddy, learned counsel, turned on its own individual facts. The bank guarantee in that case was not furnished in relation to the contract for which it was invoked but for performance of another contract. This

⁸ (2016) 11 SCC 720

circumstance along with the fact that the sum claimed by the party invoking the bank guarantee was not a sum due *in praesenti*, being in the nature of damages, weighed in favour of the said party and resulted in grant of an injunction. Further, the Supreme Court categorically observed therein that every case would have to be decided with reference to the facts involved therein. Thus, this decision is of no avail to the petitioner.

22. Similarly, in *HINDUSTAN CONSTRUCTION CO. LTD. V/ s. STATE OF BIHAR*⁹, the bank guarantee itself contained a condition referring to Clause 9 of the principal agreement and it was only if the circumstances referred to in the said clause were made out that the bank guarantee could be invoked. It was in these circumstances that the Supreme Court held that invocation of the bank guarantee would necessarily have to be in accordance with the terms of the bank guarantee or such invocation itself would be bad.

23. On the facts presently obtaining, we find that the bank guarantee in the case on hand was an unconditional one requiring only a declaration by the first respondent that the petitioner had failed to fulfill its obligations under the subcontract and nothing further. Once such a declaration is made by the first respondent, no attempt can be made, be it by the petitioner, the second respondent bank or even by the Court, to examine the validity of such an assertion so as to injunct invocation of the bank guarantee. The endeavour of the petitioner is to initiate an enquiry into the justification for such invocation which is beyond the jurisdiction of the Court while dealing with a plea to restrain such invocation. We therefore deem it wholly unnecessary to go into the merits of the matter, be it in connection with the delay in completion of the project or the alleged

⁹ (1999) 8 SCC 436

satisfaction of Jaguar & Company Private Limited with the work executed by the petitioner.

24. We accordingly hold that no error was committed by the Commercial Court in refusing an injunction to the petitioner restraining the first respondent from invoking the subject bank guarantee and the second respondent bank from honouring it.

25. Coming to the second issue, given its own finding that there could be no inference that the first respondent had become insolvent and would not be in a position to pay, we are perplexed as to why the Commercial Court thought it fit to direct the first respondent to furnish third party security. As per the settled legal norm, more than a mere apprehension is required in this regard and allusion by the petitioner to some news reports in support of its contention that the first respondent was facing financial difficulties was wholly insufficient to sustain such a direction. The reasoning that if the first respondent encashed the bank guarantee and if the petitioner thereafter succeeded in the arbitration proceedings it would have to recover the amount, to justify imposition of this condition, is without logic or basis as a similar situation would arise in every case of encashment of a bank guarantee. When the Commercial Court found no evidence of the first respondent facing any financial crisis, there was no cause made out to impose such a condition. Further, as imposition of proportionate costs upon the first respondent was only due to imposition of this condition by the Commercial Court, the same was also equally unjustified. The first respondent could not be mulcted with such costs when it was the petitioner who came up with a petition for an injunction restraining invocation of an unconditional and irrevocable bank guarantee.

26. On the above analysis, we find no grounds whatsoever to interfere with the refusal by the Commercial Court to grant an injunction to the

petitioner restraining the first respondent from invoking the unconditional bank guarantee issued by the second respondent bank. We further find that the direction by the Commercial Court to the first respondent to furnish third party security was wholly unjustified on facts and in law. In consequence, imposition of proportionate costs upon the first respondent was equally unjustified on facts and in law.

In the result, COMCA No.40 of 2019 is dismissed and COMCA No.43 of 2019 is allowed. Given the circumstances of the case, we make no order as to costs.

SANJAY KUMAR, J

P.KESHAVA RAO, J

29th JULY, 2019

PGS

