



2024 : DHC : 3262



* IN THE HIGH COURT OF DELHI AT NEW DELHI

Reserved on: 14th December, 2023

%

Pronounced on: 22th April, 2024

+ O.M.P. (COMM) 447/2018, I.A. 14687/2018 (Condonation of delay)

SRIRAM CABLES PVT LTD

..... Petitioner

Through: Mr. Ankit S. Mr. Arnav Kumar and
Mr. Gurdas Khurana, Advocates.

versus

UNION OF INDIA

..... Respondent

Through: Mr. Ashok Singh, Advocate.

CORAM:

HON'BLE MS. JUSTICE NEENA BANSAL KRISHNA

J U D G M E N T

NEENA BANSAL KRISHNA, J.

1. The Petition under Section 34 of the Arbitration and Conciliation Act, 1996 (*hereinafter "Act, 1996"*), has been filed by the petitioner, to challenge the Arbitral Award dated 23.04.2018, whereby the Claim of the Petitioner, for a refund of Rs. 2,05,40,091/- on account of wrongful encashment of the Warranty Bank Guarantees by the respondent, was rejected by the learned Sole Arbitrator.

2. *Briefly stated*, the Bid submitted by the petitioner in furtherance of the Tender floated by the Respondent in July 2015, was accepted for supply of 660 MT of Copper Wire. On 29.09.2015. A Running Contract (*RgC No: CORE/S/1101/5248/20334*) was executed between the parties, for supply of



total 660MT of Copper Wire, at the Basic Rate of Rs. 5,02,479.68/-, per MT. The Basic Rate was subject to *Price Variation Clause* contained in the contract document. The Running Contract was valid for a period of one year i.e. till 28.09.2016. Under the Running Contract, the respondent was required to place Supply Orders in the name of the Consignees, indicating the consignee wise quantities and delivery period, in each Supply Order.

3. Pursuant to the Supply Order dated 29.10.2015, the petitioner delivered 650.865 MT of Goods in total twenty (20) consignments within the schedule delivery period. The Supply Order was issued on Severable Contract basis i.e. each consignment amounted to a separate contract with separate delivery period *inter se* the parties and a separate Bill was raised against each consignment.

4. The procedure agreed was that on verification of the Bills and supporting documents and after due satisfaction, the Paying Authority of the respondent (i.e. the Financial Advisor and Chief Accounts Officer, CORE Allahabad) paid 90% of the billed amount to the petitioner. The Goods before being dispatched were also inspected by the third party Agency (*Rites Pvt. Ltd.*) and were found to be in conformity with the contract specifications and quality standards. The goods received against the 20 bills were duly acknowledged and accepted by the ultimate Consignee nominated by the respondent. There was no dispute in regard to the quality and the quantity of the Goods delivered by the petitioner and all the obligations were discharged by the petitioner satisfactorily, according to the obligations under the Contract. Thereafter, the respondent also released the balance 10% of the payment due under the aforesaid twenty Bills upon furnishing of corresponding twenty Warranty Bank Guarantees by the petitioner,



according to **Clause 27 and 28 of the Running Contract** read with **Clause 8 of the General Conditions of Contract**. Each Warranty Bank Guarantee was equivalent to 10% of the bill amount.

5. The Warranty Bank Guarantees were issued to guarantee that the goods delivered by the petitioner, were free from all defects and faults and were in conformity with the contract specifications and drawings and that the goods operated properly during the warranty period. The Warranty Bank Guarantees were valid for a period of 33 months, from the date of delivery of Goods. However, almost after one year from the date of release of payment to the petitioner, the respondent issued a letter on 14.02.2017, alleging over-payments in respect of 17 consignments and threatened to initiate recovery proceedings against the petitioner. The letter was responded to by the petitioner and was followed by subsequent exchange of communications.

6. Eventually, the respondent *vide* its letter dated 28.04.2017, invoked Warranty Bank Guarantees and sought encashment of total amount of Rs.2,05,40,091/-, for which no reason was stated in the letter.

7. The petitioner was thus, compelled to invoke **Arbitration Clause contained in Clause 9 of GCC**. The arbitration proceedings were initiated, in which the petitioner submitted its Claim and the same was contested by the respondent.

8. Eventually, the learned Arbitrator passed the **impugned Award dated 23.04.2018** *inter alia* arriving at the conclusions as under:-

“(a) The Petitioner has wrongly applied the Price Variation formulae contained in the contract document, as a result of which over-payments have been made by the Respondent to the Petitioner.



(b) As per Clause 2400 of IRS Conditions of Contract, the Respondent was contractually and legally entitled to encash the Warranty Bank Guarantee on account of alleged over-payments being made to the Petitioner under the Bills."

9. The Award has been challenged by the petitioner, on the **grounds** that it is *perverse, unreasonable, patently illegal, against the Public Policy of India* and liable to be set-aside under Section 34 (2) (a)(iv), Section 34(2)(a)(v), Section 34(2)(b) and Section 34(2A) of the Act, 1996.

10. The **first ground** of challenge is that the learned Arbitrator was ***unilaterally appointed by the respondent***, without any consultation with the petitioner. He was an ex-employee of the respondent and had been regularly advising the respondent. The learned Arbitrator was disqualified under Seventh Schedule and also lacked inherent jurisdiction to proceed with the matter and was therefore, ineligible to act as an Arbitrator. Moreover, the learned Arbitrator failed to file any Declaration, in terms of the Form specified in the Sixth Schedule of the Act, which is mandatory as it addresses the independence and impartiality of the learned Arbitrator; the Award is liable to be set-aside on this ground itself.

11. The **second ground** of challenge is that the learned Arbitrator failed to appreciate that the Bank Guarantee could be invoked only for the purpose for which they were furnished, in terms of the ***Clause 27 and 28*** of the Contract. The Bank Guarantees were to guarantee that the Goods delivered by the petitioner to the respondent, were free from all defects and faults and were in conformity with the Contract specifications during the warranty period. However, the alleged reason for encashing the Bank Guarantees, was



on account of alleged over-payment, which was not a justifiable reason under the law or the Contract.

12. The petitioner has further asserted that each consignment for which a separate Warrantee Bank Guarantee (equivalent to 10% of the billed amount) was furnished, was issued to cover goods delivered under one particular bill or one particular consignment and amounted to separate twenty Contracts. Even if the contention of the respondent about alleged over payment is accepted, the bank Guarantees could have been invoked only for that corresponding bill in regard to which over-payment had been alleged to have been made by the respondent. The respondent, however, has illegally encashed three Warrantee Bank Guarantees, namely, (i) BG No. 7132IBGSI60025 corresponding to the bill/Invoice No. 575-576 dated 18.01.2016 (ii) BG No. 7132IBGSI60026 corresponding to the bill/ Invoice No. 577-578-578 dated 18.01.2016 and (iii) BG No. 7132IBGSI60027 corresponding to the bill/ Invoice No. 580-581-582 dated 19.01.2016, even though no over-payment was alleged by the respondent in regard to these Invoices. The Warrantee Bank Guarantee was operational only for that particular Bill and could not have been invoked on account of alleged over-payment under other Bills. *It is thus, contended that the encashment of Warrantee Bank Guarantees was patently illegal, arbitrary and irrational,* which the learned Arbitrator has overlooked and failed to appreciate in accordance with the terms of the Contract.

13. The petitioner has contended that by encashing Warrantee Bank Guarantees, the respondent has indirectly ended up 'recovering' the money even before the adjudication of its claim, which is not permissible on the plain reading of the Clauses of the Contract. The invocation of Bank



Guarantees in law was bad, illegal and *non-est*.

14. Learned Arbitrator wrongly noted that the *Price Variation Formulae* was wrongly applied by the claimant. Furthermore, since the 100% payment of the bills was made on behalf of the respondent, they are now estopped from claiming that the petitioner's application of *Price Variation Formulae*, was not correct. The conduct of the respondent amounts to waiver and acquiescence and they cannot be permitted to reagitate the wrong application of the *Price Variation Formulae* by the petitioner entitling them to realize the differential amount by invoking the Bank Guarantees. It is an afterthought having been raised after more than one year of releasing the entire payments.

15. Furthermore, even though there is no evidence led by the respondent, the Arbitrator has arrived at a conclusion that the petitioner received over payment because of manipulation of raw-material Invoices and was guilty of deficiency of services while performing its contractual obligations. These findings of the learned Arbitrator are not supported by any evidence.

16. It is, therefore, submitted that the impugned award suffers from the patent illegality and is based on no evidence and the findings are in contraventions of the terms of the Contract. Therefore, the impugned award is liable to be set aside.

17. **The respondent in its Reply has submitted** that this Court has no territorial jurisdiction to entertain the present petition as the seat of arbitration does not give the jurisdiction to this Court. The office and works of the petitioner is at Alwar, Rajasthan. Moreover, neither the material was supplied in Delhi nor was the office of the respondent in Delhi. The present petition is, therefore, liable to be rejected on the ground of *lack of territorial*



jurisdiction.

18. The respondent has asserted that the issue in the present petition, was of the overpayment to the claimant and the recovery of the same by encashing the Bank Guarantees which had been rightly invoked as has also been endorsed by the Ld. Arbitrator. The procedure of payment was that the bills of the purchase of raw material from its supplier, were required to be submitted by the petitioner. Then the inspection which included quality and quantity of the raw material as per the bills of the petitioner, was required to be done by the RITES. The price of the Copper as stated in the Purchase Bill was of vital importance as the same became the basis of rates at which the payment was to be made to the petitioner. The rate of raw material is the determining factor for the price payable to the petitioner under PVC.

19. It is submitted that there is a *Price Variation Clause* and the final price payable to the claimant is calculated on the basis of the formula which reads as under: -

$$P1 = P + (CD2 * L2 - CD1 * L1)$$

P1 = Final price payable per Metric Tone (MT) in Indian Rupees

P = Price per MT as quoted in contract in Indian Rupees

CD2 = Custom Duty at time of import

CD1 = Custom Duty at time rate quoted."

20. Since, the petitioner had not imported the Copper and had purchased the Copper from within India both CD2 and CD1 became one as there is variation in custom duty and loses relevance in calculations of final price payable. The above-mentioned formula thus gets simplified to: -

$$P1 = P + (L2 - L1)$$

L1 = Price of copper as in the Purchase order



L2= Price arrived at stated below.

For the calculation of L2 three prices of the Copper are relevant.”

21. Average monthly LME cash settlement rate per MT for the month, 3 months prior to date of offering for inspection for lot. LME stands for London Metal Exchange rate.

- a) LME cash settlement (Mid Day) rate on the date of invoice.
- b) Invoice rate in Invoice of Actual purchase.
- c) L2 is the minimum of price, A, B and C.

22. It is the price B which was very relevant as the same is generally less than the price A and C. This price B varied with the date. Price B is the LME price on the date of invoice. It is the price of London Metallic Exchange as on the date of invoice and the date of the invoice is very vital for arriving at price B which keeps on varying daily.

23. The petitioner is claimed to have committed fraud in respect of price B which is the LME price on the date of Invoice. It is asserted that the raw material Invoices produced by the petitioner at the time of inspection were different from those that were submitted by the petitioner for claiming payments. The rates of Copper were shown to be higher by the petitioner intentionally in order to extract more money from the respondent. The Accounts Department at Allahabad was not aware and relying on the bills along with the attached raw material invoices, made the calculation and the over-payments got made to the petitioner at the time of final payment. It is asserted that the petitioner had indulged in unethical business practices and had manipulated the Final Bill and is not entitled to any relief.

24. It is further submitted that the ground of challenge under Section 34 of the Arbitration and Conciliation Act, 1996 is limited and the petitioner



has failed to show any valid ground for challenging the impugned Award and the present petition is liable to be dismissed. Reliance has been place on the decision in ONGC vs. Saw Pipes (2002) 1 SCC 594.

25. Moreover, the Petition under Section 34 is not equivalent to an Appeal as has been held in the cases of The President, Union of India & Another vs. Kalinga Construction Co. (P) Ltd., AIR 1971 SC 1646, Hindustan Tea Co. vs. K. Shashikant & Co., AIR 1987 SC 81, R.K. Khanna & Others vs. International Airport Authority of India & Others, 1995 (1) Arbitration Law Reporter 148, State of Madhya Pradesh vs. Babu Lal Pathak, AIR 1974 Madhya Pradesh 179, Comibatore District Podu Thozillar Samgam vs. Bala Subramania Foundry & Others, AIR 1987 SC 2045.

26. **On merits**, it is submitted that the Arbitrator has been appointed as per the terms of Contract. It is denied that he was regularly advising the respondent or was ineligible to act as the Arbitrator according to Schedules 5 and 7 of the Arbitration and Conciliation Act, 1996. It is also denied that the Arbitrator did not file the requisite Declaration under the Act or he lacked inherent jurisdiction to act as an Arbitrator.

27. It is denied that the Bank Guarantee could be encashed only in case of breach of obligation under the Bank Guarantee and not for the breach of the terms of the Contract. It is claimed that the petitioner was guilty of filing wrong Invoices and also the PVC calculations; the law of estoppels is not attracted in cases where the petitioner itself is guilty of concealment, fraud and presenting wrong documents. The petitioner itself has averred that the respondent had waived its right of overpayment, which implies that the petitioner also admits that there were overpayments made to the petitioner.



Furthermore, the Arbitrator had rightly held that the overpayments had been made to the petitioner because of wrong application of *Price Variation Formula* and the Award calls for no interference.

28. The respondent has further denied that the Ld. Arbitrator has incorrectly upheld the decision of the respondent to encash the Bank Guarantees or that such finding of the Ld. Arbitrator suffers from non-application of mind or is contrary to the terms of the Contract.

29. It is, therefore, submitted that the present petition is without merit and is liable to be dismissed.

30. In the **Rejoinder to the Reply of the Respondent**, the Petitioner has reiterated its assertions and has submitted that the stand of the respondents is merely evasive and vague and they have not been able to address any of the objections raised in the present Petition with respect to the unilateral appointment of the Ld. Sole Arbitrator (ex-employee of the Petitioners) as well as non-filing of the Declaration as mandated under the Act, 1996, which gives rise to justifiable doubts as to his independence and impartial. It has also been reiterated that the Warranty Bank Guarantees were specific in nature and could have been encashed only in case of breach of its warranty obligations and admittedly, the Respondent, till date, has not raised single dispute regarding the quality or quantity of the goods supplied. Thus, there is error apparent on the face of award as the Ld. Sole Arbitrator has failed to understand the import of the Running Contract and the Terms of the GCC as well as the Bank Guarantees, calling for setting aside of the Impugned Award.

31. To buttress the above arguments, the learned Counsel for Petitioner has placed reliance on the decisions in *Perkins Eastman Architects DPC vs. HSCC (India) Ltd.*, (2020) 20 SCC 760, *Bharat Broadband Network Ltd. vs. United*



Telecoms Ltd., (2019) 5 SCC 755, Ram Kumar and Anr. vs. Shriram Transport Finance Co. Ltd. 2022/DHC/005313, Govind Singh vs. M/s Satya Group Pvt. Ltd., 2023/DHC/000081, Ruia Exports & Anr. vs. Moneywise Financial Services Pvt. Ltd., O.M.P. (COMM.) 16/2020 decided by the Co-ordinate Bench of this Court on 18.01.2023, Kotak Mahindra Bank vs. Narendra Kumar Prajapat 2023:DHC:3705-DB, Man Industries (India) Ltd. vs. Indian Oil Corporation Ltd., 2023:DHC:3875, Hanuman Motors Pvt. Ltd. & Anr. vs. M/s Tata Motors Finance Ltd. Arbitration Petition 241/2022, Bombay High Court and Cholamandalam Investment and Finance Company Ltd. vs. Amrapali Enterprise and Anr. EC 122/2022, Calcutta High Court.

32. Submissions heard and judgments perused.

33. The respondent, at the outset in its Reply to the present petition, has taken a preliminary objection in regard to the maintainability of the present petition by claiming that in terms of the **Clause 9 of GCC**, the territorial jurisdiction does not lie with this Court and therefore, the present petition is liable to be rejected on this ground itself.

34. **Clause 9 of GCC** provides for Arbitration. Sub-clause (g) of Clause 9 of GCC reads as under: -

“Clause 9(g): The venue of arbitration shall be the place from which the acceptance note (supply order) has been issued or such other place as the Arbitrator at his discretion determine.”

35. **Clause 12 of the GCC** deals with the jurisdiction of the Courts which reads as under: -

“Clause 12: - The courts at Allahabad (U.P.) shall alone have the jurisdiction to decide any dispute arising out of or in respect of the Contract. No deviation in this regard will be acceptable.”

36. In the present case, the learned Arbitrator got appointed in Delhi and



the arbitration proceedings were also conducted in Delhi, thereby implying that he decided the "venue" of arbitration as Delhi, in accordance with **Clause 9(g)** of the GCC. Additionally, the petitioner has its registered office of works in New Delhi and the cause of action arose in Delhi as the bills along with the invoices were dispatched from Delhi, the payments were received by the Petitioner at Delhi and the Warranty Bank Guarantees were encashed by the Respondent at Delhi. Though, **Clause 12** of the Agreement provides for jurisdiction of the Courts but in **Clause 9 (g)**, which specifically deals with arbitration, it is nowhere provided that the seat of arbitration shall be at Allahabad.

37. The controversy about the "seat" and "venue" has been arising frequently since the Act 1996 does not specifically use either word viz., "seat" or "venue" but uses the word "place". In the case of Bharat Aluminium Co. vs. Kaiser Aluminium Technival; Service, Inc., (2012) 9 SCC 552, the Constitution Bench of the Supreme Court observed that Section 2 (1)(e) of the Act 1996 only defines the Court, the Act 1996 has to be construed keeping in mind Section 20 of the Act 1996, which gives recognition to party-autonomy. The legislature has intentionally vested jurisdiction with two courts, i.e., the court which would have the jurisdiction where the *cause of action arose*, and the courts where the *arbitration takes place*. This was necessary as on many occasions, most of the Agreements provide for a seat of arbitration at a place which would be mutual to both the Parties. Therefore, the Courts, where the arbitration takes place, would be required to exercise supervisory control over the arbitration proceedings.

38. In the BSG SGS Soma JV. v. NHPC Ltd. (2020) 4 SCC 234, following the Roger Shashoua v. Mukesh Sharama (2009) EWHC 957, the



Apex Court laid down the test for determination of the seat which reads as under –

“ It will thus be seen that wherever there is an express designation of a “venue” and no designation of any alternative place as the “seat”, combined with a supranational body of rules governing the arbitration and no other significant contrary indicia, the inexorable conclusion is that the stated venue is actually the juridical seat of the arbitral proceedings.”

39. The above judgment of BGS Soma (Supra) forms the *locus classicus* on the issue. While dealing with the issue of maintainability of petitions preferred under Section 34 of the Act 1996, which had been instituted before the Faridabad courts, the core issue arose as to whether the seat of arbitration was liable to be construed as New Delhi or Faridabad . Akin to the factual matrix of the present case, the proceedings of the Arbitral Tribunal had taken place and a unanimous award was pronounced at New Delhi but the objections under Section 34 were filed before the District and Sessions Judge, Faridabad in the State of Haryana. It was held that the challenge before the Faridabad courts had been wrongly instituted, competent court was that of New Delhi, being the seat of arbitration.

40. The Co-ordinate Bench of this Court in Reliance Infrastructure Ltd. v. Madhyanchal Vidyut Vitran Nigam Ltd., 2023 SCC OnLine Del 4894 observed that a generic jurisdiction clause in an Agreement would not supersede or override the supervisory jurisdiction of the Courts, and held as under:-

“ 32. On a conspectus of the aforesaid judgments, the position of law that emerges is that when the contract contains an arbitration clause that specifies a “venue”, thereby anchoring



the arbitral proceedings thereto, then the said “venue” is really the “seat” of arbitration. In such a situation the courts having supervisory jurisdiction over the said “seat” shall exercise supervisory jurisdiction over the arbitral process, notwithstanding that the contract contains a clause seeking to confer “exclusive jurisdiction” on a different court.”

41. From a perusal of the above judgments, it becomes evident that where ever is the ‘seat’ or ‘place’ of arbitration as determined by the Learned Arbitral Tribunal, that Court would have jurisdiction to entertain the application under Section 34 of the Act, 1996.

42. In the present case as well, in **Clause 9(g)**, it was specifically provided that the venue of arbitration shall be the place from which the *Acceptance Note* is issued or such other place as the Arbitrator at his discretion may determine. The Supply Orders have been issued from Allahabad, Uttar Pradesh to the petitioner at Delhi, therefore, it can easily be held that the *Acceptance Note* was issued from Delhi.

43. Furthermore, the Learned Arbitrator has conducted the entire proceedings in Delhi, to which no objection at any point of time has been taken on behalf of the respondent. Pertinently, even in the Reply filed by the respondent in the present proceedings, the respondent has stated that the seat of the arbitration does not impart the jurisdiction to this Court thereby implying that the respondent has also not denied that the seat of arbitration was in Delhi.

44. It can easily be inferred that the arbitration proceedings having been conducted in Delhi, the seat and venue both were in Delhi, the objection taken on behalf of the respondent in regard to the territorial jurisdiction of this Court to entertain the present Petition under Section 34 of the Act, 1996



is untenable. The present petition has been rightly filed before this Court, which has the jurisdiction to entertain the same.

45. Essentially, there are two challenges which have been raised by the petitioner under Section 34 of the Act 1996 i.e. (i) *Arbitrator was a disqualified under Fifth and Seventh Schedule of the Act, 1996*, and (ii) *encashment of Warranty Bank Guarantees against its terms*.

(i) Disqualification of the Ld. Arbitrator under Fifth and Seventh of the Arbitration and Conciliation Act, 1996: -

46. An objection has been taken on behalf of the petitioner that the Arbitrator, who was unilaterally appointed by the respondent without consulting the petitioner, was an ex-employee of the respondent. He had been regularly advising the respondent and no Declaration in terms of the Form specified in the Sixth Schedule of the Arbitration and Conciliation Act, 1996 has been filed by the Arbitrator.

47. While the Act, 1996 recognises the autonomy of the parties to choose their own Arbitrator in terms of their Agreement, it also countenances that fairness, transparency and impartiality are the virtues which are equally important incidents for consideration in the appointment of the Arbitrator. The autonomy conferred on the parties is not unbridled and any appointment of the Arbitrator has to meet the prerequisite of his neutrality and impartiality which are the bedrock on which the foundation of arbitration rests.

48. In the case of Voestalpine Schienen GMPH vs. Delhi Metro Rail Corporation Limited (2017) 4 SCC 665, it was held that under Section 12(5) of the Act, 1996, notwithstanding any prior agreement to the contrary, any person whose relationship, with the parties or counsel or the subject-matter



of the dispute, falls under any of the categories specified in the Seventh Schedule, shall be ineligible to be appointed as an arbitrator. It was further observed that the validity of an appointment procedure which clearly contemplates appointment of an arbitrator by only one party without any counterbalancing of that power by giving the other contracting party any say in the choice of arbitrator to be appointed, would also fall foul of Section 12 (5) read with Seventh Schedule of the Act, 1996. It would be apposite to highlight that the Apex Court disapproved of a Panel of Arbitrators from which the other party may select an arbitrator as it “*created room for suspicion*”.

49. Further, while analysing the impact of appointment procedures wherein one contracting party is in a comparatively more dominating position, this Court in Margo Networks (P) Ltd. Vs. Railtel Corpn. of India Ltd 2023 SCC OnLine Del 3906 and CMM Infraprojects Ltd. Vs. IRCON International Ltd 2021:DHC:2578 and Pankaj Mittal Vs. Union of India Order dated 16.12.2021 passed by this Court in ARB.P. 607/2021, has observed that the arbitration appointment procedure under which “*the scales are tipped in favour of the respondent*” would inherently be in contravention with the object of Section 12 (5) read with Seventh Schedule of the Act, 1996.

50. Thus, applying the above crystallized principles of law in the present case, it becomes imperative to analyse the validity of the procedure of the appointment of the arbitrator and whether the same was clearly in contravention of the Scheme of the Act, 1996.

51. **Clause 9 of the GCC** envisaged Arbitration procedure, which is reproduced hereunder :-



"9. Arbitration

a) In the event of any question, dispute or difference arising under these conditions or any special conditions of contract, or in connection with this contract (except as to any matters the decision of which is specially provided for by these or the special conditions) the same shall be referred to the sole arbitration of a Gazetted Railway Officer appointed to be the arbitrator, by the General Manager in the case of contracts entered into by the Zonal Railways and Production Units; by any Member of the Railway Board, in the case of contracts entered into by the Railway Board and by the Head of the Organisation in respect of contracts entered into by the other Organisations under the Ministry of Railways. The Gazetted Railway Officer to be appointed as arbitrator however will not be one of those who had an opportunity to deal with the matters to which the contract relates or who in the course of their duties as railway servant have expressed views on all or any of the matters under dispute or difference. The award of the arbitrator shall be final and binding on the parties to this contract.

b) In the event of the arbitrator dying, neglecting or refusing to act or resigning or being unable to act for any reason, or his award being set aside by the court for any reason, it shall be lawful for the authority appointing the arbitrator to appoint another arbitrator in place of the outgoing arbitrator in the manner aforesaid.

c) It is further a term of this contract that no person other than the person appointed by the authority as aforesaid should act as arbitrator and that if for any reason that is not possible, the matter is not to be referred to arbitration at all.

d) *****

e) *****

f) *****

g) *****

h) ***"**

52. **Arbitration Clause 9(a) of the GCC** provides that the arbitrator



would be a *Gazetted Railway Officer*, who would be appointed by the General Manager in the case of contracts entered into by the Railway Board and production units; by any Member of the Railway Board in case of contracts entered into by the Railway Board ; by the Head of Organization in case of contracts entered into by the other Organizations under the Ministry of Railways. Hence, the appointing Authority is clearly the Respondent, which indicates without an iota of doubt, that the scales evidently tipped in the favour of the Respondent leading to reasonable concerns about the arbitrator's impartiality. Further, **Clause 9(b)** provides that in case the Arbitrator so appointed by the Respondent, is incapable or unable to act and discharge his duties, the power to freshly appoint another Arbitrator would also vest with the Respondents solely. Additionally, **Clause 9(c)** provided that no person other than the person so appointed by the respondents, would act as an Arbitrator and in such a case the dispute would not be referred to arbitration at all.

53. A cumulative appraisal of the above clauses clearly demonstrates that the procedure for appointment was only a "one -way" procedure and the power to single handedly decide who would be the Arbitrator, only vested with the Respondents. There never existed even a shred of counterbalancing of this unilateral power as the Petitioners had no role to play in this procedure, whether it was initial appointment or substitution in case the Arbitrator became disabled to act as any arbitrator at any subsequent stage. The absolute power of appointment was assumed by the respondent is further evident from Clause 9(c) which contained an "My way or High Way" attitude as it provided that there would be no arbitration in case the respondent does not appoint the arbitrator. *Such unilateral appointment*



arbitrators have been judicially proscribed, irrespective of whether the arbitrator appointed is not biased and or not prejudiced. The procedure for appointment of arbitrator was Unilateral with no participation by the petitioner, is hit by Section 12(5) read with Seventh Schedule of the Act, 1996.

54. Principles of natural justice play a critical role in avoiding any potential risk of miscarriage of justice as arbitration requires adjudication on rights of the parties involved. The first principle of natural justice is '*nemo judex in causa sua*', which means 'no man can be a judge in his own cause' which is the basis of any '*reasonable apprehension of bias*' that may arise during any judicial process.

55. In the case of Voestalpine (supra), it was observed that in such an eventuality, i.e., when the Arbitration Clause finds foul with the amended provisions, the appointment of an arbitrator would be illegal, empowering the court to appoint such arbitrator(s) as may be permissible. While emphasising on the independence and impartiality as the hallmark of any arbitration proceedings, it was observed that if the Arbitrator appointed is found to be non-independent or non-impartial, his appointment shall be rendered ineligible in terms of the Arbitration and Conciliation Act, 1996. The rationale behind this rule is that the Arbitrator has an adjudicatory role to perform and therefore, must be independent of the parties as well as be impartial.

56. The Apex Court in the case of Perkins Eastman Architects DPC & Anr. vs. HSCC (India) Ltd. AIR 2020 SC 59, recognised the importance of ensuring that the Arbitrator having an interest in the outcome of the matter is not appointed so as to obviate any doubt as to the impartiality or



independence of the Arbitral Tribunal.

57. The test for determination of competence of the Arbitrator proposed to be appointed, was laid down by the Apex Court in the case of *TRF Ltd. vs. Energo Engineering Projects Ltd.* (2017) 8 SCC 377, “whether he would have an interest in the outcome of the dispute”. The element of eligibility was relatable to the interest that he may have in the decision.

58. Section 12 read with Schedules V and Schedule VII of the Act, 1996 read with S.12(1)(b) specify the categories of persons who can or cannot be appointed as arbitrators. the grounds on which the eligibility of the arbitrator can be challenged, are primarily governed by Section 12 read with the Vth, VIth and the VIIth Schedule.

59. The Fifth Schedule (read with Section 12(1)(a) of the Act, 1996 lists the various instances and circumstances that create justifiable doubts in the mind with respect to the independence and impartiality of the sole arbitrator or the panel of arbitrators appointed. It broadly discusses the conditions when the arbitrator is doubted for its impartiality or being biased towards one of the parties or the relationships of the arbitrator with the other parties.

60. The Fifth Schedule read with Section 12(2) of the Act, 1996 provides specifically that the Arbitrator at the time of his appointment and throughout the arbitral proceedings shall, without delay, disclose to the parties in writing any circumstances referred to in Sub-Section (1) unless they have been informed of them by him.

61. The Sixth Schedule of the Act, 1996 provides the format in which the said Declaration is to be given. It provides that the past or present relationship or interest in any of the parties or any relationship to the subject matter in dispute has to be disclosed. It is also required to state if it had any



financial business or professional association of any kind which was likely to give rise to justifiable doubts as to their independence. Thus, to ensure the sanctity of an arbitral proceeding, Section 12 of the Act, 1996 read with Schedule VI underlines the importance of disclosure to maintain the independence and impartiality of an Arbitrator.

62. Unlike the Fifth Schedule, the *Seventh Schedule (read with Section 12(5) of the Act 1996)* relates to instances which directly result in the “ineligibility” of a person from being appointed as an arbitrator and *de jure* disqualify him from being appointed as an arbitrator unless the parties had expressly waived the applicability of the provision in writing after the agreement was entered into.

63. In the case of HRD Corporation (Marcus Oil and Chemical Division) vs. GAIL (India) Limited (Formerly Gas Authority of India Limited) (2018) 12 SCC 471, the Apex Court had explained the scope of Schedules V and VII in the context that Section 12 of the Arbitration and Conciliation Act, 1996. It has been observed that if a person falls in any of the categories as specified in the Seventh Schedule, he becomes ineligible to act as Arbitrator and the ineligibility goes to the root of the appointment, making such Arbitrator *de jure* ineligible to be an Arbitrator. It was further observed that Items 1 to 19 of the Fifth Schedule are identical with the aforesaid items in the Seventh Schedule. The only reason that these items also appear in the Fifth Schedule is for purposes of disclosure by the arbitrator, as unless the proposed arbitrator discloses in writing his involvement in terms of Items 1 to 34 of the Fifth Schedule, such disclosure would be lacking in material particulars, in which case the parties would be put at a disadvantage as such information is often within the personal knowledge of the arbitrator alone. It



is for this reason that it appears that Items 1 to 19 also appear in the Fifth Schedule.

64. In the present case, *firstly*, the respondent in its Reply to this objection, neither has given any explanation nor is it asserted that the Declaration under Section 12 of the Act, 1996. Apart from a vague denial, no averment has been made that the mandatory Declaration under Section 12 of the Act, 1996 as per the prescribed form in the Sixth Schedule, was ever made by the Arbitrator. The records of the Arbitrator have been stated to be unavailable by the Arbitrator *vide* his Affidavit dated 09.06.2023. The vague denial without there being any explanation from the respondent, can only lead to one inference that no requisite Declaration had been filed by the Ld. Arbitrator. Pertinently, the Petitioner at no stage, had waived the applicability of Section 12(5) of the Act, 1996. Merely because the petitioner had not raised any objections to the unilateral appointment in the arbitral proceedings, would not make the appointment valid. Since this disqualification goes to the root of the proceedings, such plea has to be addressed in the present Petition under S.34 of the Act.

65. Further it has been held in the case of Hindustan Zinc LTD. v. Ajmer Vidyut Vitran Nigam Ltd. (2019) 17 SCC 82 that an objection to the unilateral appointment can be taken for the first time at any stage or in the collateral proceedings, including an Appeal under Section 37 of the Act, 1996.

66. *Secondly*, it is not disputed that the Learned Arbitrator was an ex-employee of the respondent. There is specific averment made by the petitioner that the Arbitrator was regularly rendering the respondent's advisory work which again has only been vaguely denied without any



further explanation. Thus, the inevitable conclusion is that this is a clear case where the procedure of appointment itself provided for *unilateral appointment* and also that the Arbitrator was an ex-employee of the respondent, which is against the express mandate of Section 12 read with Seventh Schedule of the Arbitration and Conciliation Act, 1996. Such unilaterally appointed Arbitrator inherently lacked jurisdiction to adjudicate and it vitiates the entire arbitral proceedings making the Award *non-est*.

67. The Arbitral Award dated 23.04.2018 is, therefore, liable to be set aside on this ground of ineligibility of the Arbitrator, being a unilateral appointment.

(ii) The Warranty Bank Guarantee encashment has been done against the terms of the Warranty Bank Guarantees: -

68. The *second ground* agitated on behalf of the petitioner is that each Bank Guarantee was an Independent Contract for independent Invoices and consignments and the same could have been encashed only in accordance with its terms. The respondent, however, has encashed it not for any of the reasons as stipulated in the Bank Guarantee, but for recovery of the alleged overpayments made to the petitioner by the respondent, under the Contract. Thus, the learned Arbitrator erred in upholding the invocation of Bank Guarantee which is against the Fundamental Law of the Land and the findings are *perverse* which are in conflict with the Law and also the facts of the case. In fact, the findings in respect of the Bank Guarantees are not supported by any evidence and the Bank Guarantees have been interpreted in contravention of its terms.

69. The *respondent on the other hand*, has justified the invocation of Bank Guarantee by saying that it has been done in terms of the Contract, to



realise the amounts that were found outstanding against the petitioner. It is claimed that there is no perversity in the findings of the learned Arbitrator and this objection taken by the petitioner, is not tenable.

70. *To comprehend the challenge to the Bank Guarantee, it would be first pertinent to understand the nature of the Bank Guarantee.*

71. The commercial transactions of the nature involved in the present Petition, were riddled with several complexities including high commercial gains and losses and run the risk of losses on account of non-performance or delay in performance of contractual obligations, amongst other challenges. In the commercial transactions, the interest of the parties in securing the payments under the Commercial Contract, is paramount. The *Contract of Bank Guarantee* is one such mechanism to mitigate the chances of losses and recovery of the due amounts because of non-performance or default in performance of contractual obligations.

72. Generally, in a Bank Guarantee there exist three parties i.e. the Creditor, the Debtor and the Bank. The Bank Guarantee is an independent Agreement wherein the obligation of the Bank is absolute and distinct from the underlying Contract in respect of which any dispute may arise between the parties.

73. The independent nature of the Bank Guarantees was highlighted in the case of *Dwarikesh Sugar Industries Ltd. vs. Prem Heavy Engineering Works (P) Ltd.*, (1997) 6 SCC 450, wherein it was observed that when in a course of commercial dealings, an unconditional Bank Guarantee is given or accepted, the beneficiary is entitled to realize such a Bank Guarantee in terms thereof irrespective of any pending disputes. The Bank giving such a Bank Guarantee is bound to honour it, as per its terms as the very purpose of



giving such a Bank Guarantee would otherwise be defeated.

74. Similarly, in the case of Svcnska Handelsbanken vs. Indian Charge Chrome Ltd., (1994) 1 SCC 502, the Apex Court observed that what is important is that the Bank Guarantee should be in unequivocal terms, unconditional and recite that the amount would be paid without demur or objection and irrespective of any dispute that might have cropped up or might have been pending between the beneficiary under the Bank Guarantee or the person on whose behalf the Guarantee was furnished. The terms of the Bank Guarantee are, therefore, extremely material. It represents an independent contract between the Bank and the beneficiary, both being bound by the terms thereof. The invocation, therefore, will have to be in accordance with the terms of Bank Guarantee, or else, the invocation itself would be bad.

75. The only exceptions recognised for injuncting the invocation of bank guarantee were explained in the case of Hindustan Steelworks Construction Ltd. vs. G.S. Atzval & Co. (Engineers) (P) Ltd., (1996) 5 SCC 34, wherein the Supreme Court while reiterating that in case of an unconditional Bank Guarantee, the obligation of the Bank is to pay the amount, on its invocation, further explained that the only exceptions recognised for injuncting the invocation of bank guarantee is *fraud* or the *special equities*. Determination of the disputes *inter se* the parties in terms of the Contract, is not a consideration for the Bank to deny or refuse to pay the amount, on invocation of bank guarantee by the Creditor.

76. Another ground where the Courts may interfere and restrain encashment of Bank Guarantee was specified in the case of Ansal Engineering Projects Ltd. vs. Tehri Hydro Development Corporation Ltd.,



(1996) 5 SCC 450, wherein the Apex Court further added the principle of *irreparable injury* to the already recognised two categories of *fraud* and *special equity*.

77. After referring the various Judgments, the Apex Court pithily summed up the position of Bank Guarantee in the case of Larsen Toubro Ltd. vs. Maharashtra SEB (1995) 6 SCC 68, by observing:

“the Rule is well established that a bank issuing a guarantee is not concerned with the underlying Contract between the parties to the contract. The duty of the bank is created by the documents itself. Once the documents are in order the bank giving the guarantee must honour the same and make payment ordinarily. The Courts shall also not interfere directly or indirectly to withhold payment or else the trust in commerce internal and international would be irreparably damaged. In case of breach of terms of contract, the parties are at liberty to get their disputes resolved through litigation or Arbitration. The remedy arising ex-Contractu too is not barred and the cause of action for the same is independent of enforcement of the bank guarantee.”

78. In the case of Continental Construction Ltd. and Anr. Vs. Satluj Jal Vidyut Nigam Ltd. (2006) SCC OnLine Del 56, the Coordinate Bench of this Court concluded that a Bank Guarantee must be strictly invoked in its terms by a person empowered to so invoke it under the terms of the Guarantee.

79. In the case of Biba-Chem Private Ltd. vs. Hi-tech Carbon & Anr., 1995 (34) DRJ 520, this Court had observed that the Court is only to consider the terms of the Deed of Bank Guarantee and no other document to decide whether it has been invoked in consonance with the terms contained therein. Once, it has been invoked in accordance with its terms, other questions would become wholly irrelevant. Issues of Bank Guarantee, therefore, have to be decided only on the basis of the terms of the Guarantee



itself making it completely separate from the main Contract. It would not be appropriate to go through the terms of the main Contract to find out as to whether there was any breach of Contract or that the plaintiff has suffered any loss in the performance of its obligations by the plaintiff and therefore, was justified in compensating itself for its losses by invoking a Bank Guarantee. It is, therefore, evident that the Bank Guarantee is an independent Contract and is governed by the terms contained therein. The Reference to the terms of the underlying Contract, cannot be made in order to consider whether the Bank Guarantee had been invoked justifiably.

80. In the light of the aforesaid principles, the facts of the present Case may be now considered. **Clause 8 of General Conditions of Contract** (GCC) which provided for Warranty/Guarantee, reads as under:-

“8. Warranty/Guarantee:

(a) *The contractor/Seller hereby covenants that it is a Condition of the Contract that all goods/stores/articles furnished to the Purchaser under this contract shall be of the highest grade, free of all defects and faults and of the best materials, quality, manufacture and workmanship throughout and consistent with the established and generally accepted standards for materials of the type ordered and in full conformity with the contract specification, drawing or sample, if any and shall, if operable, operate properly.*

(b) *The contractor also guarantees that the said goods/stores/articles would continue to conform to the description and quality as aforesaid, for a period of 30 months after their delivery or 24 months from the date of placement in service whichever shall be sooner, and this warranty shall survive notwithstanding the fact that the goods/stores/articles may have been inspected, accepted and payment therefore made by the Purchaser.*



(c) *If during the aforesaid period, the said goods/stores/articles be discovered not to conform to the description and quality aforesaid or have deteriorated, otherwise that by war and tear, the decision of the Purchaser in that behalf being final and conclusive and that the Purchaser will be entitled to reject the said goods/stores/articles or such portions thereof as may be discovered not to conform to the said description and quality. On such rejection, the goods/stores/articles will be at the Seller's risk. If the Contractor/Seller so desires, the rejected goods may be taken over by him or his agents for disposal in such manner as he may deem fit within a period of 3 months from the date of such rejection. At the expiry of the period, no claim whatsoever shall lie against the Purchaser in respect of the said goods/stores/articles, which may be disposed of the foregoing, all the provisions in the Indian Railways Standard Conditions of Contract relating to the rejection of stores and failure and termination and clause 3100-02 above shall apply.*

(d) *The contractor/Seller shall, if required, replace the goods or such portion thereof as have been rejected by the purchaser, free of cost, at the ultimate destination, or at the option of the Purchaser, the Contractor/Seller shall pay to the Purchaser, the value thereof at the contract price and such other expenditure and damage as may arise by reason of the breach of the conditions herein being specified. Nothing herein contained shall prejudice any other right of the Purchaser in that behalf under this contract or otherwise."*

81. Twenty Performance Bank Guarantees had been admittedly furnished independently by the petitioner according to **Clause 8 of GCC read with Clause 27 and 28 of the Running Contract**, in respect of 20 Invoices for 20 Consignments, pursuant to the Running Contract dated 29.09.2015, under which the Supplier was required to furnish Bank Guarantee for warranty plus three months additional time (33 months in all) to the extent of 10% of



value of the Contract in Railways Standard Acceptable Form. These bank guarantees were to guarantee that the said goods/stores/articles would continue to conform to the description and quality as aforesaid, for a period of 30 months after their delivery or 24 months from the date of placement in service whichever shall be sooner, and this warranty shall survive notwithstanding the fact that the goods/stores/articles may have been inspected, accepted and payment therefore made by the Purchaser. Therefore, these BGs were for the specific purpose to ensure that quality and quantity of goods supplied conformed to the specifications and could be invoked only if the goods were found to be non-conforming during the warranty period of 33 months. It was absolutely independent of the payments under the Running Contract.

82. The terms of the Warranty Bank Guarantee were unequivocal and categorically provided in its **Clause 4 of the Warranty Bank Gurantee**, No.7132IBGIS160025 dated 17.02.2016, (which is similar in all Bank Guarantee), reproduced as under:-

“2. AND WHEREAS according to the terms of the said Contract, it has been stipulated that payment of balance 10% of the value of the stores would be made, provided that the seller furnishes to the purchaser Bank Guarantee from a recognized schedule Bank, acceptable to the purchaser for 10% of the value of the said contract, valid for a period covering I full the guarantee period as per the warranty clause of the said conditions of the contract, being the condition attached to and forming part of the contract.

4. That in consideration of the promise and at the request of the said sellers, we hereby irrevocably undertake and guarantee to pay to the Government of India at such other place as may be determined by you



forth with on demand and without any demur merely on demand from the Government stating that the amount claimed is due by way of loss or damage caused to or would be caused to or suffered by the Government by reason of breach by the said contractor(s) of any of terms or conditions contained in to perform the said agreement, or by reason of the contractor(s) failure to perform the said agreement any sum up to a maximum amount of Rs.25,30,059/- (Rupees Twenty Five Lacs Thirty Thousand Fifty Nine Only) representing 10% of the value of the stores dispatched under the said contract in case the sellers make default in paying the said sum or make any default in performance, observance or discharge of the guarantee contained in the said contract.”

83. Each Bank Guarantee had a reference to its payment Bill as is evident from all the Bank Guarantees and **Clause 8 of the Bank Guarantee No.7132IBGIS160025** dated 17.02.2016, for reference, is reproduced as under:-

“8. This Bank Guarantee comes into force when the balance 10% (Ten percent) of the value of the stores shipped, as per G.R.No.1903-1904 Dated 18.01.2016 and date of receipt of material is on 22.01.2016 under the said contract, has been paid and will remain in full force and effect upto 22.10.2018 i.e. for 33 months counted from the date of receipt of material.

11. That no claim under this Guarantee shall be entertained by us unless the same has been preferred by the Government within the said date.”

84. From the terms of the Warranty Bank Guarantee, it is evident that these Bank Guarantee had been furnished against the independent Invoices as a Guarantee of the conditions attached therein. The Warranty Bank



Guarantee, therefore, was to ensure that the goods furnished under the Contract were of highest grade, free of all defects and faults and consistent with the established and generally accepted standards for material, at the time they were ordered. Each of the Bank Guarantee was to be kept alive for 33 months from the date of delivery of goods to ensure that they are free from any defects. *The Performance Guarantee, therefore, was only as a Guarantee for the quality of the goods during the Warranty period of 33 months.* By the very nature of a Bank Guarantee it could have been invoked only if after the supply of goods, there was any defect found during the Warranty period of 33 months.

85. Significantly, in the present case, it has been categorically admitted by the Respondents that there were no defects found in the goods entitling the respondent to encash the Bank Guarantee. There is no dispute with respect to the quality and the quantity of the goods, as per the terms of the Contract.

86. The Bills of the material along with the bill of purchase of raw-material(Copper) in support thereof, were duly submitted by the petitioner. These bills and the corresponding raw-material invoices, were duly considered by the Accounts Department of the respondent and the payments were made to the petitioner. Admittedly, all the payments against the bills including of the Final Bill that were raised, had been cleared by the respondent.

87. According to the respondent, subsequently at the time of inspection by the RITES, it was found that *over payment* had been made against the respective 20 Bills on account wrong application of the *Price Variation Formula* based on manipulated rates of Copper/raw-material and that the petitioner had submitted different Invoices for claiming payments. It was



thus, realised that there was an over payment against the various bills, as detailed hereunder:-

S.No.	WBG No.	WBG Amount	Bill No.	Alleged overpayment	Status of WBG
1.	7132IBGIS160002	34,48,955/-	500-501-502	6,23,983/-	Encashed
2.	7132IBGIS160050	16,35,496/-	653	21,27,695/-	-
3.	7132IBGIS160031	11,98,149/-	551	11,14,213/-	-
4.	7132IBGIS160051	11,90,086/-	652	15,34,567/-	-
5.	7132IBGIS160028	12,03,229/-	549-550	11,14,500/-	Encashed
6.	7132IBGIS160047	11,20,177/-	642	13,15,320/-	-
7.	7132IBGIS160030	6,01,989/-	548	5,57,418/-	Encashed
8.	7132IBGIS160027	17,84,453/-	580-581-582	*	Encashed
9.	7132IBGIS160045	14,95,323/-	647-649	19,45,480/-	-
10.	6004IBGIS160091	14,17,763/-	699-701	5,22,487/-	Encashed
11.	7132IBGIS160026	17,85,979/-	577-578-579	*	Encashed
12.	6004IBGIS160114	18,38,762/-	744-745	1,33,499/-	Encashed
13.	7132IBGIS160001	9,05,035/-	518-519	1,57,958/-	-
14.	7132IBGIS160029	18,07,065/-	545-546-547	16,72,254/-	Encashed
15.	7132IBGIS160025	25,30,059/-	575-576	*	Encashed
16.	7132IBGIS160052	5,98,135/-	655	7,73,707/-	-
17.	7132IBGIS160048	26,72,817/-	646-650	16,84,432/-	-
18.	7132IBGIS160046	18,72,188/-	639-644-645	14,59,233/-	-
19.	6004IBGIS160199	14,30,627/-	1 & 2	1,02,500/-	Encashed
20.	6004IBGIS160049	26,91,210/-	640-643-648651	36,08,071/-	Encashed
	Total	3,32,27,497/-		2,05,40,091/-	

88. The respondent thus, invoked 11 Warranty Bank Guarantees in order



to adjust the alleged over-payments of Rs.2,05,40,091/- which has been made by the respondent against the bills that were raised by the petitioner.

89. What emerges from the Chart mentioned above, is that even though over-pricing was allegedly done in respect of certain bills, the Warranty Bank Guarantees invoked are not of the corresponding Invoices, but had been invoked randomly against any Invoice, even if there was no over payment in regard to it, in order to realise the entire alleged amount which according to respondent, had been paid wrongly. For example, there was no overpayment in regard to Invoices at serial no. 8, 11 and 15 despite which the BGs have been encashed. Likewise, though there is alleged overpayment in respect of Invoices at Serial No. 2, 3, 4, 6, 9, 13, 16, 17 and 18 but the corresponding BGs have not been encashed.

90. As has been already discussed above in detail, the Bank Guarantees being specific independent Contracts governed by the terms contained therein, could have been unconditionally invoked in case the quality of the goods after the delivery was found to be defective during the Warranty period of 33 months from the date of supply of goods. It is quite evident that the Bank Guarantees have been invoked by the respondent in contravention of the Fundamental Law relating to encashment of Bank Guarantees in violation of the terms of the Performance Bank Guarantees and the GCC and the Running Contract between the parties. The remedy with the respondent in case it felt that their invoices were over billed or that the over payment had been made, was to raise its claim for recovery of the overpaid amount but it could not have invoked the Bank Guarantees in contravention of its terms. In fact, Legal Notice dated 14.02.2017 had also been sent seeking clarification on alleged over-payment in Bills of Supply and initiating



recovery action of alleged over-payment.

91. The learned Arbitrator has referred to **Clause 2400 under Indian Railway Standard Conditions of Contract (IRS-CC)** to hold that the respondent was entitled to retain the amount or part thereof, wherever any claim for payment arises out of or under the Contract against the Contractor. Since the excess payment was detected on post auditing, the respondent was entitled to encash the Bank Guarantees and retain the money.

92. **Clause 2400** under Indian Railway Standard Conditions of Contract (IRS-CC) relied by the learned Arbitrator, is reproduced as under:-

“2400. Withholding and lien in respect of sums claimed.

*Whenever any claim or claims for payment of a sum of money arises out of or under the contract against the Contractor, the Purchaser shall be entitled to **withhold** and also have a lien to **retain** such sum or sums in whole or in part from the security, if any, deposited by the Contractor and for the purpose aforesaid, the purchaser shall be **entitled to withhold the said cash security deposit or the security, if any, furnished** as the case may be and also have a lien over the same pending finalization or adjudication of any such claim. In the event of the security being insufficient to cover the claimed amount or amounts or if no security has been taken from the Contractor, the Purchaser shall be entitled to withhold and have lien to retain to the extent of the such claimed amount or amounts referred to supra, **from any sum or sums found payable or which at any time-thereafter may become payable** to the Contractor under the same contract or any other contract with the Purchaser or the Government **pending finalization or adjudication of any such claim.***

It is an agreed term of the contract that the sum of money or moneys so withheld or retained under the lien referred to above, by the Purchaser will be kept withheld or



retained as such by the Purchaser till the claim arising out of or under the contract is determined by the Arbitrator (if the contract is governed by the arbitration clause) or by the competent court as prescribed under clause 2703 hereinafter provided, as the case may be, and that the Contractor will have no claim for interest or damages whatsoever on any account in respect of such withholding or retention under the lien referred to supra and duly notified as such in the Contractor.”

93. From the bare perusal of the above Clause, it is evident that this Clause would get invoked only for “withholding” and for “lien to retain” in respect of claims raised by the Purchaser, only when there exists a whole or in part, a security amount which has been furnished by the Contractor. The said security amount, in part or whole, would be withheld or retained, if furnished, pending finalization or adjudication of any of such claims raised by the Purchaser against the Contractor. In case the security amount furnished is insufficient to cover the entire claim or no security has been taken by the Contractor, the Purchaser shall be entitled to withhold and have lien of such claim amount or amounts referred to from any sum or sums found payable under the same Contract, pending finalization of the adjudication of the disputes.

94. In the present case, it is pertinent to refer to the **Running Contract** dated 29.09.2015 that was entered into between the parties. *Vide Clause 29* the parties agreed to waive off “Security Deposit” as the firm was an RDSO approved source for tendered items and the tendered items were *non-safety items*. Therefore, under the Running Contract, the deposition of security amount, as provided under **Clause 2400**, had been expressly waived off. Once, there was no security amount available with the respondent, the



Clause 2400 could not have been possibly invoked it, in the first place.

95. It is also pertinent to observe that the lien could have been exercised on entire or part of the security amount, only if it was found that there was something which was payable or there was a dispute in regard to the amount to be paid by or to the respondent.

96. In the present case admittedly, the Final Payment under the Running Contract had been made after due verification of the Bills. It is only subsequently, that the respondents allegedly on post audit found over-payment against certain bills. As already observed above, in case any over payment had been made, then the respondent should have raised a dispute for adjudication rather than being a judge of its own cause and use its dominant position to encash the Bank Guarantees in contravention of the specific conditions stated therein.

97. The other aspect which is evident is that as per **Clause 27** and **28** of the Running Contract, the supplier was required to furnish BG for warranty period plus three month's additional time to the extent of 10% of value of Contract in Railways Standard Acceptable Form. It is quite apparent that the Bank Guarantees required to be furnished under **Clause 28** were independent of the security deposits. Moreover, as already discussed above, each Bank Guarantee was an independent Contract governed by its own terms. The clause applicable to security deposits could not have been made applicable to the Bank Guarantees, as has been done by the learned Arbitrator. This interpretation as given by the learned Arbitrator is absolutely contrary to the terms of the Contract itself and suffers from a patent illegality. The learned Arbitrator fell in error of law in equating security with Bank Guarantee and treating them as interchangeable.



98. Similar situation was considered by a Co-ordinate Bench of this Court in Bharat Sanchar Nigam Ltd. vs. Teracom Ltd. OMP (COMM) 431/2019, wherein it was observed that there is no principle in law whereby the respondent cannot be permitted to retain the Performance Guarantee as security after the performance of the Contract has been acknowledged.

99. In the present case as well, the Bank Guarantees have been encashed because the respondent after post auditing, concluded that there was over payment on account of manipulation of invoices. The encashment was not in terms of BG on account of quality or quantity of the goods being found not in accordance with the terms of the Contract during the Warranty period of 33 months, but on account of alleged over payment under the Contract as admittedly the payments had been already made against the Final Bill. From the submissions of the respondent itself, it is evident that the Bank Guarantee had not been invoked in accordance with the terms contained therein.

100. The scope of a challenge under Section 34 of the Arbitration and Conciliation Act, 1996 is limited to the grounds stipulated in Section 34 as held in MMTC Limited v. Vedanta Ltd., (2019) 4 SCC 163. Comprehensive judicial literature on the scope of interference on the ground of Public Policy under Section 34 was postulated in Associate Builders vs. DDA, (2015) 3 SCC 49. The Apex Court placed reliance on the judgment of ONGC v. Saw Pipes, 2003 (5) SCC 705 to determine the contours of Public Policy wherein an award can be set aside if it is violative of 'The fundamental policy of Indian law', 'The interest of India', 'Justice or morality' or leads to a 'Patent Illegality'.

101. For an Award to be in line with the 'The fundamental policy of Indian



law', the Tribunal should have adopted a judicial approach which implies that the Award must be fair reasonable and objective and in accordance with the law of the land. The ground of '*patent illegality*' is applied when there is a contravention of the substantive law of India, the Act 1996 or the rules applicable to the substance of the dispute.

102. In Hindustan Zinc Limited vs Friends Coal Carbonisation, (2006) 4 SCC 445, the Apex Court referred to the principles laid down in *Saw Pipes* (supra) and clarified that it is open to the court to consider whether an Award is against the specific terms of contract, and if so, interfere with it on the ground that it is *patently illegal* and *opposed to the public policy of India*.

103. The Apex Court in the case of Ssangyong Engineering & Construction Co. Ltd. Vs. National Highways Authority of India AIR 2019 SC 5041 has exhaustively dealt with the expression "*patent illegality*" and which acts of the Arbitral Tribunal would come within the purview of patent illegality. The only correct interpretation of a contract would be if no reasonable person could have arrived at a different conclusion while interpreting the relevant clauses of the contract and that any other interpretation would be irrational and in defiance of all logic, however, the findings would suffer from the vice of irrationality and perversity if the Arbitrator arrived at his findings by taking irrelevant factors into account and by ignoring vital clauses of the contract. Hence, the Apex Court held that the court could intervene and review the merits of an award if it is found to be on wrong interpretation of the Contract and thus, '*patently illegal*'.

104. Though construction of the terms of a contract is primarily for an Arbitrator to decide, but if the arbitrator construes the contract in such a way



that it could be said to be something that no fair-minded or reasonable person would do, the Award would suffer from patent illegality, making it liable to be set- aside under Section 34 of the Act 1996.

105. In the present case, the findings of the learned Arbitrator, allowing the encashment of the Bank Guarantees by relying upon **Clause 2400 of IRS-CC** is completely not only against the express provisions of the Contract which did not authorise the respondent to encash the Bank Guarantee merely on the allegations of over payment to the petitioner, but is clearly against the Fundamental Law and suffers from patent illegality in being absolutely contrary to the terms of Contract and the law on encashment of BGs. Therefore, the Award is liable to be set-aside on this ground as well.

Conclusion:

106. The Petition under Section 34 of the Arbitration and Conciliation Act, 1996 is therefore, allowed and the Arbitral Award dated 23.04.2018 is hereby set-aside. The parties are at liberty to seek appropriate remedy under the Law for redressal of their dispute.

(NEENA BANSAL KRISHNA)
JUDGE

APRIL 22, 2024/RS