

Akai Impex Ltd. Vs. General Steel Export and Others

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Court : Mumbai

Decided On : Aug-19-1997

Reported in : 1998(2)ALLMR170; 1998(2)BomCR199

Judge : S.S. Nijjar, J.

Acts : [Code of Civil Procedure \(CPC\), 1908](#) - Order 38, Rules 1 and 2; [Indian Contract Act, 1872](#) - Sections 126

Appeal No. : Notice of Motion No. 2059 of 1995 in Suit No. 1587 of 1995

Appellant : Akai Impex Ltd.

Respondent : General Steel Export and Others

Advocate for Def. : H.J. Thakkar, Adv., i/b Harihar Bhawe

Advocate for Pet/Ap. : Ms. Rajani Iyer and V.K. Ramabhadran, Advs.

Judgement :
ORDER

S.S. Nijjar, J.

1. This suit has been filed by the plaintiffs for a declaration that the first defendants are not entitled to claim, demand or receive an amount to the extent of U.S. \$ 2,16,819.55 under the Letter of Credit, hereinafter referred to as the 'L/C', dated

30th August, 1994. Prayer is also made for a permanent injunction restraining the first defendant from claiming or receiving the said amount. The Notice of Motion has been taken out for an injunction in similar terms. An affidavit in support of the Notice of Motion has been filed. Affidavit in reply has been filed by the defendant No.

2. No replies have been filed by defendant Nos. 1, 3 and 4 although the service is stated to have been effected upon them.2. Briefly stated the facts are that the first defendant by an offer (offer/Performa) dated 17th August, 1994 agreed to sell cold rolled sheets of various sizes and gauges on certain terms and conditions. The payment was by way of an irrevocable L/C payable 180 days after shipment i.e. B/L. The value of the L/C in terms of the offer/offer/Performa dated 17th August, 1994 which was opened by the second defendants in favour of the third defendant was U.S.\$ 10,44,000. Subsequently on 5th October, 1994 by an amendment the value of the L/C was reduced to U.S.\$ 8,57,500 and the quantity of HR coils was reduced from 3000 M.T. to 2500 M.T On 7th November, 1994 the plaintiffs obtained from the second defendant a copy of the B/L dated 3rd November, 1994, a copy of the invoice, a copy of the packing list, a copy of the lest certificate, a copy of the certificate of origin and a copy of the certificate of weight. The cargo loaded on the vessel 'AMER VED' arrived in Bombay on 7th December, 1994. The plaintiffs took delivery of the said cargo and the same was transported by trucks to different warehouses. Prior to the transport of the cargo the trucks in which it was loaded were weighed on the weighbridge outside the Port and the plaintiffs found that though the number of bundles stated by the first defendant was correct as 424 but the actual weight of the cargo was 2204.000 M.T. against the declared weight of 2589.560 M.T. The plaintiffs, therefore, by a fax dated 19th December, 1994 informed the fourth defendant accordingly. They were informed that the cargo would be kept in the same condition in which it was received. They were invited for a personal inspection in order to compensate the plaintiffs for the loss due to shortloading. Defendant No. 4 is the agent of defendant No. 1. In view of this defendant No. 4 inspected the said cargo and found that what had been stated by the plaintiff is correct. By a letter dated 20-1-95 the plaintiffs pointed out to the first defendant that according to the survey carried out by SGS India Ltd. in all the 146 bundles the net shortage worked out to 121.715 M.T. There was a shortage of

about 14 per cent. Thus the claim was lodged by the plaintiff with the first defendant for a sum of U.S. \$ 2,16,819.53. This claim included the cost of material, amount of duty paid to Customs, expenses incurred for weighment, trucking charges, weighbridge charges, the amounts paid to SGS India Ltd. for inspection, warehousing charges etc. The fourth defendant also called upon the first defendants to settle the claim of the plaintiffs as contained in their letter dated 20th Jan. 1995. By a fax dated 16th Feb. 1995, fourth defendant confirmed to the plaintiffs that the first defendants have in fact confirmed/accepted the findings of the SGS India Ltd., report and admitted the shortage of 218 M.T and had also agreed to settle the claim without delay. In the fax message it is stated that it was proposed by the first defendant that as a first gesture to help the plaintiffs the credit period for this L/C would be extended by about 3 months free of cost to the plaintiffs. The claim for the shortage of about 218 M.T from the bundles which are actually inspected by SGS and certified in their report will be settled without delay. In view of the intended settlement, representative of the plaintiffs actually went to Switzerland and met the representative of the first defendants on 7th April, 1995. The first defendants refused to settle the claim even to the extent of 218 M.T. The first defendant was ready and willing to compensate the plaintiffs only to the extent they receive from their supplier. The first defendants were further willing to give price reduction in future business. The first defendants despite admitting shortage in weight were not ready and willing to make any payment in respect of the said shortage to the plaintiff. The aforesaid offer of the first defendant is reflected in a fax dated 7th April, 1995 addressed by the first defendant to the fourth defendants. The plaintiffs, however, refused to sign this settlement as the first defendants were not willing to make any payment unless and until they receive the same from their suppliers. It is thereafter stated by the plaintiffs that the first defendants had contracted to supply to the plaintiffs 2509.560 M.T. of cold rolled sheets. The first defendants have accordingly furnished the aforesaid documents, evidencing shipment of the said cargo, packing list, bill of lading, invoice and certificate of weight representing that 424 bundles weighed 2509.560 M.T. The shortage was discovered only after the plaintiffs had taken delivery. The plaintiffs submit that the certificate of weight, bill of lading, invoice, packing list which are part of the various documents to be furnished by the first defendants are patently fraudulent. The first

defendants have issued the same with an intent to defraud the plaintiffs and obtain payment through L/S opened by the second defendants in favour of the third defendants. The first defendants are bound and liable to pay the plaintiffs the amount claimed in the suit being the value of the cargo short shipped by the first defendants, the duty paid thereon and various other expenses incurred by the plaintiffs. As per the L/C the second defendants had to pay to the third defendants on expiry of 180 days from shipment the price of the cargo. The second defendants had to pay U.S. \$ 857,500 on or about 1st May, 1995. At the time of the filing of the suit it was apprehended that the second defendants are liable to remit the suit amount after the expiry of 180 days to the third defendants on or about 1st May, 1995. If the said amount is remitted, irreparable harm and injury resulting in irretrievable injustice would be caused to the plaintiffs. The plaintiffs will not be in a position to recover their claim from the first defendants who are a foreign party. In the aforesaid circumstances it is prayed that the reliefs as prayed for ought to be granted to the plaintiffs.

3. An affidavit in support of the Notice of Motion has been filed wherein the aforesaid averments have been reiterated. No affidavits in reply have been filed by the defendant Nos. 1, 3 and 4. Defendant No. 2 has, however, filed an affidavit in reply. This affidavit has been filed after the ad-interim injunction came to be granted on 27th April, 1995. A perusal of the order dated 27th April, 1995 shows that ad-interim injunction in terms of prayer clauses (a) and (b) operative till 15th June, 1995 only was granted. Liberty to apply for grant of ad-interim reliefs and extension of the order was also granted after notice to the defendants. The plaintiffs gave notice to the defendants and the matter came up for hearing on 13th June, 1995. Again none was present on behalf of the defendants. Consequently the ad-interim order dated 27th April, 1995 came to be confirmed. Thereafter an application was made by defendant No. 2 for vacating the ad-interim order. This application was dismissed. Liberty was granted to defendant No. 2 to apply for an expeditious hearing of the Notice of Motion. Thus the Notice of Motion has come up for hearing.

4. An affidavit in reply has been filed by defendant No. 2 on 23rd February, 1996. In this affidavit it is stated that the Notice of Motion taken out by the plaintiffs is an

abuse of the process of Court. The injunction order dated 27th April, 1995 has been obtained by suppressing the material facts from this Court. The suit does not disclose any cause of action. It is further stated that the plaintiffs in fact have acted fraudulently in approaching this Court. The opening of L/C on the request of the plaintiffs is admitted. Defendant No. 3 was requested by defendant No. 2 to add their confirmation to the L/C as requested by the plaintiffs on 18th April, 1994. The dates of the shipment were changed from time to time. Documents for encashing of the L/C were received from defendant No. 3. They were presented to the defendant No. 2 who accepted the same on 1st December, 1994 for payment on 1st May, 1995. This date was informed by defendant No. 2 to defendant No. 3. Accordingly beneficiaries of the L/C effected shipment on 3rd November, 1994. The documents relating to shipment confirming to the L/C terms were received at the branch which when presented to the drawees i.e. the plaintiffs were duly accepted by them on 1st December, 1994 for payment on 1st May, 1995. This acceptance was conveyed to the negotiating Bank. As per terms of the L/C, the negotiating Bank was to claim reimbursement from the Down Town Service Branch, New York of the plaintiffs. It is stated that the Banks deal with documents only. In Article 4 of UCP 500 it is stated 'In credit operations all parties concerned deal with documents, and not with goods, services and/or other performances to which the document may relate. 'It is further stated that if there are any problem with regard to quality/quantity the same have to be sorted out between the plaintiffs and the beneficiaries. The Bank cannot interfere in such cases as the Bank has to honour its undertaking and fulfil their documents of credit. Reference is made to 1993 Revision ICC Publication 500 which reads as follows :

'Credits, by their nature, are separate transactions from the sales or other contract (s) on which they may be based and Banks are in no way concerned with or bound by such contracts (s), even if any reference whatsoever to such contract (s) is included in the credit. Consequently the undertaking of a Bank, to pay, accept and pay draft (s) or negotiate and/or to fulfil any other obligation under the credit, is no subject to claims or defences by the applicant resulting from his relationships with the issuing Bank or the beneficiary.'

The L/C has been confirmed by defendant No. 3 Bank. Defendant No. 2 authorised defendant No. 3 to reimburse defendant No. 3 with the New York Branch for the full amount of documents. Defendant No. 2 also authorised their New York Branch to cover the plaintiff on due date for the full amount of documents. Now the defendant No. 3 has issued a notice to defendant No. 2 claiming interest at the rate of 10 per cent per annum from the due date i.e. 1st May, 1995. In these circumstances it is stated that the plaintiffs have accepted the bills for payment to defendant No. 2 which were drawn by the beneficiaries under the L/C opened by Industrial Finance Branch, Bombay on behalf of the plaintiffs. If there is any dispute between the company and the beneficiary regarding goods the Bank is not concerned with the same. It is further stated that in the international business and economic affairs, non-payment would mean not honouring the responsibility which State Bank of India, defendant No. 2, is bound to honour and would adversely affect the credibility/acceptability of the commitment/instruments issued by S.B.I. in the International market. After receiving the notice from United Overseas Bank, Geneva, defendant No. 3, it is all the more urgent and necessary to make the payment. This affidavit has been filed for the purpose of seeking the vacation of the ad-interim order.

5. On these pleadings, Ms. Iyer learned Counsel appearing for the plaintiffs, has submitted that the beneficiary, defendant No. 1 has clearly played a fraud. They induced the plaintiffs to open a L/C in their favour when they had no intention whatsoever of sending the goods as agreed upon in the contract. They were to ship to the plaintiffs the quantity of 2509.560 M.T. of the cold rolled steel. They in fact sent only 2204 M. T. but in the documents it was stated that the goods had been despatched in accordance with the contract. The documents were presented to the negotiating Bank, defendant No. 3 who in turn had forwarded the same to defendant No. 2. In the documents the weight of the steel supplied was mentioned as correct. In fact it was to the knowledge of the defendant No. 1 that there have been a shortsupply. Having committed a fraud upon the plaintiff, defendant No. 1 cannot be permitted to take advantage of the same on the ground that they are entitled to receive the money under the L/C. Counsel has referred to a number of authorities to support her submissions. Counsel first relies on judgement of the Supreme Court in the case of Svenska Handelsbanken v. M/s. Indian Charge

Chrome and others, : AIR 1994 SC626 . Pointed reference has been made to paragraph 67 of the said judgement. In that paragraph the observations of the Supreme Court in an earlier judgement given at pages 1145, 1146 and 1148 are restated which reads as under.

'67. The modern documentary credit had its origin from letters of credit. The letter of credit has developed over hundreds of years of international trade. It was intended to facilitate the transfer of goods between distant and unfamiliar buyer and seller. It was found difficult for a buyer to pay for goods prior to their delivery. The Bank's letter of credit came to bridge this gap. In such transactions, the seller (beneficiary) receives payment from the issuing Bank when he presents a demand as per the terms of the documents. The Bank must pay if the documents are in order and the terms of credit are satisfied. The Bank, however, was not allowed to determine whether the seller had actually shipped the goods or whether the goods conformed to the requirements of the contract. Any dispute between the seller and the buyer must be settled between themselves. The courts, however, in carving out an exception to this rule of absolute independence held that if there has been a 'fraud in the transaction' the Bank could dishonour beneficiary's demand for payment. The courts have generally permitted dishonour only on the fraud of the beneficiary not the fraud of somebody else.'

In view of the observations contained in this paragraph, Ms. Iyer has submitted that the beneficiary has disentitled themselves from receiving any benefit under the L/C with regard to the short supply. It is submitted that the claim put forward by the plaintiff is genuine and thus it is only restricted to the compensation with regard to the short supply of the steel. In the present case since the beneficiary and the seller are one and the same, therefore, the fraud is obviously committed by the beneficiary. Counsel has then relied upon 1978 (1) All E.R. 976, *Edward Owen Engineering Ltd. v. Barclays Bank International Ltd.* Pointed reference has been made to the observations made on pages 981 and 982 which read as under :

'To this general principle there is an exception in the case of what is called established or obvious fraud to the knowledge of the Bank. The most illuminating case is of *Sztejn v. J. Henry Schroder Banking Corpn.* which was heard in the New

York Supreme Court in 1941. After citing many cases Shientag, J., said this :

'It is well established that a letter of credit is independent of the primary contract of sale between the buyer and the seller. The issuing Bank agrees to pay upon presentation of documents, not goods. This rule is necessary to preserve the efficiency of the letter of credit as an instrument for the financing trade.'

He said that in that particular case it was different because --

'.....on the present motion, it must be assumed that the seller has intentionally failed to ship any goods ordered by the buyer. In such a situation, where the seller's fraud has been called to the Bank's attention before the drafts and documents have been presented for payment, the principle of the independence of the bank's obligation under the letter of credit should not be extended to protect the unscrupulous seller.'

'That case shows that there is this exception to the strict rule; the Bank ought not to pay under the credit if it knows that the documents are forged or that the request for payment is made fraudulently in circumstances when there is no right to payment. I would in this regard quote the words of Browns, L.J., in an unreported case when he was sitting at first instance. It is Bank Russo Iran v. Gendon Woodroffe & Co. Ltd., He said.

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

But as Kerr, J., said in this present case..... in cases of obvious fraud to the knowledge of the Banks, the courts may preclude Banks from fulfilling their obligation to third parties.'

In view of the above it is submitted by Ms. Iyer that by filing the suit the fraud has been brought to the notice of the Bank. The fraud is obvious. There is no need of any further evidence. The certificate has been issued by the agent of the defendant No. 1 themselves to the effect that there is a short supply. In view of the

above it is submitted by the Counsel that they are entitled to the confirmation of the ad-interim order granted by this Court on 27th April, 1995. In the event the said order is not confirmed the plaintiff will suffer irreparable loss and injury because they will not be able to recover the moneys from the defendant No. 1 who happens to be a foreign party.

6. In reply to the aforesaid submissions, Mr. Thakkar, Counsel for defendant No. 2 has submitted that so far as the Banks are concerned they are governed by time tested and well regulated norms. The Bank has to be governed by the Uniform Customs and Practice for documentary credit Rules of International Chamber of Commerce revised from time to time. The latest rules are contained in the UCP 500 which became effective from 1st January, 1994 known as 'Uniform Customs and Practice for Documentary Credits, 1993 Revision' replacing UCP 400, 1983. Counsel has relied on Article 4 of the instructions called 'UCP 500' which is as under.

'Article 4.

Documents v. Goods/Services/Performances In credit operations all parties concerned deal with documents, and not with goods, services and/or other performances to which the documents may relate.'

In view of this it is submitted by the Counsel that all that the defendant No. 2 and defendant No. 3 Banks are required to do before making payment under the L/C is to see that the documents are in order. They are not at all concerned with the goods, services or other performances to which the documents may relate. Thus so long as the documents stated the required quantity and they were not fraudulent on the face of it the payments have to be made. It was not possible for the Bank to know that there has been a short supply of goods nor was it any of their business to inspect the goods before making the payment. Counsel has further submitted that the law has by now been well settled by a catena of judgements of the Supreme Court and a Division Bench of this Court. Counsel has relied upon (i) 1978 (1) All E.R. 976, (ii) U.P. Coop. Federation Ltd. v. Singh Consultants and Engineers (P) Ltd., : [1988]1SCR1124 , (iii) : AIR 1994 SC626 , (iv) and (v) : AIR 1997 SC1644 . It is submitted that in all these cases it has been

categorically held that when in the course of commercial dealings, unconditional Bank guarantee is given or accepted, the beneficiary is entitled to realise such a Bank guarantee in terms thereof irrespective of any pending disputes

7. I have given anxious consideration to the submissions made by Counsel. In my view, the Bank giving a Guarantee is bound to honour it as per its terms irrespective of any dispute raised by its customer. The very purpose of giving such a Bank guarantee would otherwise be defeated. The courts should, therefore, be slow in granting an injunction to restrain the realisation of such a Bank guarantee. The existence of any dispute between the parties to the contract is not a ground for issuing an injunction to restrain the enforcement of Bank Guarantee. The courts have carved out only two exceptions. A fraud in connection with such a Bank Guarantee which would vitiate the very foundation of such a Bank Guarantee. Hence, if there is such a fraud of which the beneficiary seeks to take advantage, he can be restrained from doing so. The second exception relates to cases where allowing the encashment of an unconditional Bank guarantee would result in irretrievable harm or injustice to one of the parties concerned. But the harm or injustice contemplated under this head must be of such an exceptional and irretrievable nature as would override the terms of the guarantee and the adverse effect of such an injunction on commercial dealings in the country. The two grounds are not necessarily connected, though both may coexist in some cases. After noticing all the judgements of the Supreme Court, a Division Bench of this Court has culled out certain principles applicable to the Bank Guarantees and letters of credit. The Division Bench in *Kisan Sahakari Chini Mills Ltd. v. Richardson and Cruddas Ltd. and anr.*, has held as under.

'17. The principles that emerge from the above decisions of the Supreme Court can be summed up thus :

(i) That a Bank guarantee is ordinary a contract quite distinct and independent of the underlying contract, the performance of which it seeks to secure and the Bank is required to honour the guarantee according to its terms. 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 under a

performance guarantee is created by the document of guarantee itself. Once that document is in order, the Bank giving the guarantee must honour the same and to make payment.

(ii) The commitments of the Banks under a Bank guarantee must be honoured free from interference by the courts. Otherwise trust in commerce, internal and international, would be irreparably damaged.

(iii) It is only in exceptional cases, that is to say in case of irretrievable injustice or fraud that the Court should interfere.

(iv) The nature of fraud is fraud of an egregious nature as to vitiate the entire underlying transaction. It is fraud of the beneficiary, not the fraud of somebody else. There must be a specific plea of fraud. The party alleging fraud must necessarily plead and produce all necessary evidence in proof of the fraud in execution of the contract of guarantee. Moreover, fraud like any other charge of a criminal proceeding must be established beyond reasonable doubt. A finding as to fraud cannot be based on suspicion and conjecture. The material and evidence have to show it. (v) Irretrievable injustice should be of kind arising in irretrievable situation. The irreparable harm should not be speculative. It should be genuine and immediate as well as irreversible. It should be a case where the party seeking restraint on invocation of Bank guarantee has no adequate remedy of law at all and the harm to him would be irreparable. The subsequent dispute in the performance of the contract does not give rise to cause nor the Court would be justified on that basis to issue an injunction from enforcing a Bank guarantee, because the party is not left without remedy in such a case. He is entitled to damages and other consequential reliefs.

(vi) The same principle will apply to cases where injunction is sought against a party seeking to invoke the Bank guarantee because the net effect of such an injunction is to restrain the Bank from performing the Bank guarantee. That is so, because one cannot do indirectly what one is not free to do directly.'

A perusal of the said principles show that the Bank guarantee is ordinarily a contract quite distinct and independent of the underlying contract. The

commitments of the Banks under a Bank Guarantee must be honoured free from interference by the courts. It is only in exceptional cases, that is to say, in cases of irretrievable damage or fraud that the Court should interfere. The nature of fraud is fraud of an egregious nature as to vitiate the entire underlying transaction. It is fraud of the beneficiary, not the fraud of somebody else. There must be a specific plea of fraud. The party alleging fraud must necessarily plead and produce all necessary evidence in proof of the fraud. Fraud like any other charge of a criminal proceeding must be established beyond reasonable doubt. A finding as to fraud cannot be based on suspicion and conjecture. In this case, a perusal of the plaint itself would show that the parties in Fact have been trying to settle with each other. It has been categorically stated in the plaint that the representative of the plaintiffs personally went to Switzerland and met the representative of defendant No. 1. During the meeting to the shock and surprise of the plaintiff, the first defendant refused to settle the claim of the plaintiffs even to the extent of 218 M.T. The first defendants admitted the shortage in weight to the extent of 218 M.T. However, they were ready and willing to compensate the plaintiffs only to the extent of the amount they received from their suppliers. The first defendants (the beneficiary) were even willing to give price reduction in future business. Despite admitting shortage in weight they were, however, not ready and willing to make any payment in respect of the said shortage to the plaintiff. In view of such averments it cannot be held at this stage that such a fraud has been committed by the beneficiary which would go to the root of the transaction of issuing L/C. Judgement after judgement have cautioned that in matters where letters of credit or Bank guarantees had been issued, the courts should use extreme caution in granting injunctions at the interim stage. The injunction can be granted if the fraud is obvious on the fact of it. The Bank had notice of it before payment. Non-grant of injunction would cause irretrievable injustice. The Division Bench has categorically stated in proposition No. 6 that the same principles will apply to cases where injunction is sought against a party seeking to invoke the Bank guarantee because the net effect of such an injunction is to restrain the Bank from performing the Bank Guarantee. That is so because one cannot do indirectly what one is not free to do directly. Keeping the aforesaid observations in view I am of the opinion that it would not be possible to grant interim relief to the plaintiff. This is so because the

efficacy and confidence in making payment by L/C has to be protected. This is necessary for trade, both National and International. The Supreme Court in *Sevenska* case *supra* has clearly explained the origin and development of documentary credit. It was intended to facilitate the transfer of goods between distant and unfamiliar buyer and seller. The Bank must pay on presentation of complete documentation in terms of the L/C. The Bank is not to determine whether the seller had actually shipped the goods or whether the goods conformed to the requirement of the contract. Any dispute between the seller and the buyer must be settled between themselves. In the present case, the plaintiff is only claiming that the defendant No. 1 has not shipped the full quantity of contract. This act of short supply would not itself lead to the presumption that a fraud has been committed. No circumstances have been pointed out which would lead to the conclusion that irretrievable injustice would be done to the plaintiff if the injunction is not granted. Only plea raised is that the defendants being a foreign party, it would be difficult to recover the money. Thus, grant of injunction would be against the well settled principles of law. The Supreme Court in the case reported in : AIR 1994 SC626 (*supra*), has clearly held that mere difficulties in execution of the decree cannot be equated with irretrievable loss. The Supreme Court in the case of *U.P. State Sugar Corporation v. Sumac International Ltd.*, : AIR 1997 SC1644 held that the performance guarantee constitute independent and separate contracts between the guarantor Bank and the beneficiary, and these independent rights, liabilities and obligations cannot be treated as technical pleas. It is settled time and again that the opening of the letter of credit is a totally separate contract from the contract which has been entered into by the parties which is popularly known as 'underlying transaction'. The importance of this has been discussed in the judgement reported in 1978 (1) All E.R. 976. The judgement of Lord Denning is noticed in paragraph 19 which is as under.

'Applying these principles there can hardly be any doubt that injunction can only be granted in the case of established fraud. That can only be done at the stage when the parties are led evidence and all the documents have been perused.'

8. The Supreme Court in the case of *U.P. State Sugar Corporation* (*supra*) has considered all the aspects of the law relating to a situation like the present one.

Therein in paragraphs 12 and 14 it is observed as under:

'12. The law relating to invocation of such Bank guarantees is by now well settled. When in the 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 guarantee is bound to honour it as per its terms irrespective of any dispute raised by its customer. The very purpose of giving such a Bank guarantee would otherwise be defeated. The courts should, therefore, be slow in granting an injunction to restrain the realization of such a Bank guarantee. The courts have carved out only two exceptions. A fraud in connection with such a Bank guarantee would vitiate the very foundation of such a Bank guarantee. Hence, if there is such a fraud of which the beneficiary seeks to take advantage, he can be restrained from doing so. The second exception relates to cases where allowing the encashment of an unconditional Bank guarantee would result in irretrievable harm or injustice to one of the parties concerned. Since 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, the harm or injustice contemplated under this head must be of such an exceptional and irretrievable nature as would override the terms of the guarantee and the adverse effect of such an injunction on commercial dealings in the country. The two grounds are not necessarily connected, though both may coexist in some cases. In the case of U.P. Co-op. Federation Ltd. v. Singh Consultants and Engineers (P) Ltd., 1988 B.J. 154 which was the case of a works contract where the performance guarantee given under the contract was sought to be invoked, this Court, after referring extensively to English and Indian cases on the subject, said that the guarantee must be honoured in accordance with its terms. The Bank which gives the guarantee is not concerned in the least with the relations between the supplier and the customer; nor with the question whether the supplier has performed his contractual obligation or not, nor with the question whether the supplier is in default or not. The Bank must pay according to the tenor of its guarantee on demand without proof or condition. There are only two exceptions to this rule. The first exception is a case when there is a clear fraud of which the Bank has notice. The fraud must be of an egregious nature such as to vitiate the entire underlying

transaction. Explaining the kind of fraud that may absolve a Bank from honouring its guarantee, this Court in the above case quoted with approval the observations of Sir John Donaldson, M.R. in *Bolivinter Oil SA v. Chase Manhattan Bank*, All ER at p. 352): (at S.C.C. p. 197)

'The wholly exceptional case where an injunction may be granted is where it is proved that the Bank knows that any demand for payment already made or which may thereafter be made will clearly be fraudulent. But the evidence must be clear both as to the fact of fraud and as to the Bank's knowledge. It would certainly not normally be sufficient that this rests on the uncorroborated statement of the customer, for irreparable damage can be done to a Bank's credit in the relatively brief time which must elapse between the granting of such an injunction and an application by the Bank to have it charged.'

This Court set aside an injunction granted by the High Court to restrain therealisation of the Bank guarantee.'

'14. On the question of irretrievable injury which is the second exception to the rule against granting of injunctions when unconditional Bank guarantees are sought to be realised the Court said in the above case that the irretrievable injury must be of the kind which was the subject-matter of the decision in the *Itek Corpn.* case. In that case an exporter in USA entered into an agreement with the Imperial Government of Iran and sought an order terminating its liability on stand by letters of credit issued by an American Bank in favour of an Iranian Bank as part of the contract. The relief was sought on account of the situation created after the Iranian revolution when the American Government cancelled the export licences in relation to Iran and the Iranian Government had forcibly taken 52 American citizens as hostages. The US Government had blocked all Iranian assets under the jurisdiction of United States and had cancelled the export contract. The Court upheld the contention of the exporter that any claim for damages against the purchaser if decreed by the American Courts would not be executable in Iran under these circumstances andrealisation of the Bank guarantee/ letters of credit would cause irreparable harm to the plaintiff. This contention was upheld. To avail of this exception, therefore, exceptional circumstances which make it impossible

for the guarantor to reimburse himself if he ultimately succeeds, will have to be decisively established. Clearly, a mere apprehension that the other party will not be able to pay, is not enough. In Itek case there was a certainly on this issue. Secondly, there was good reason, in that case for the Court to be prima facie satisfied that the guarantors i.e. the Bank and its customer would be found entitled to receive the amount paid under the guarantee.'

9. Counsel for the plaintiff has also relied on the Division Bench judgment of this Court reported in Swiss Bank Corporation v. Jai Hind Oil Mills Co. and another, 1994 (1) B.C.R. 371. In that case, it was held that the Bank is not obliged to make the payment if the documents are found to be forged or the beneficiary has committed fraud. It is further held that the Bank is not obliged actively to ascertain whether the alleged fraud can be proved. In cases where fraud exception is pleaded, it is necessary to establish the fraud clearly and unambiguously. In my view, the reliance upon the said judgment of the Division Bench is misplaced by the Counsel for the plaintiff. The judgement rather says that the relief cannot be granted unless and until the fraud is established clearly and unambiguously. At this interim stage, it cannot possibly be held that the fraud has been established clearly and unambiguously. The attitude of the parties rather seems to have been for conciliation. It is only when the efforts of settlement have failed that the plaintiffs thought it fit and proper to file the present suit. It is obvious that on the basis of the admissions made by the defendant No. 1 it would be relatively easy for the plaintiff to obtain a decree against defendant No. 1. Defendant No. 1 has clearly admitted breach of contract but those admissions cannot be raised to such a level of importance to say that it amounts to admission of fraud. The decree having been granted it would not be all that difficult to execute the same against defendant No. 1. Thus in view of the law laid down by the Supreme Court and this Court the plaintiffs to avail of the exception of irreparable injustice would have to show exceptional circumstances which make it virtually impossible for them to execute the decree if it ultimately succeeds. A mere apprehension that the other party will not be able to pay is not enough. In my view, therefore, no irretrievable damage or loss would be caused to the plaintiff if no interim relief is granted. In view of what has been stated above I find no merit in the Notice of Motion. The same is hereby dismissed with no order as to costs.

10. In view of the fact that interim injunction has been continued since 27th April, 1995 the operation of this order is stayed for a period of one month to enable the plaintiff to carry the matter in appeal.

11. Notice of Motion dismissed.

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