M/s. Tarapore & Co., Madras

Vs

M/s. V. O. Tractors Export, Moscow and Another

And

M/s. V. O. Tractors Export, Moscow

Vs

M/s. Tarapore & Co., Madras

Civil Appeals Nos. 2251, 2252, 2305 and 2306 of 1968

(S. M. Sikri, K. S. Hegde JJ)

26.11.1968

JUDGMENT

HEDGE, J. –

1. These are connected appeals. They arise from Civil Suit No. 118 of 1967, on the original side of the High Court of Judicature at Madras. Herein the essential facts are few and simple though the question of law that arises for decision is of considerable importance.

2. The suit has been brought by M/s. Tarapore & Co., Madras (hereinafter referred to as the "Indian Firm"). That firm had taken up on contract the work of excavation of a canal as a part of the Farakka Barrage Project. In that connection they entered into a contract with M/s. V.O. Tractors Export, Moscow (which will hereinafter referred to as the "Russian Firm") for the supply of construction machinery such as Scrapers and Bulldozers. In pursuance of that contract, the Indian Firm opened a confirmed, irrevocable and divisible letter of credit with the Bank of India, Limited for the entire value of the equipment i.e. Rs. 66,09,372/- in favour of the Russian Firm negotiable through the Bank for Foreign Trade of the U.S.S.R., Moscow. Under the said letter of credit the Bank of India was required to pay to the Russian firm on production of the documents particularised in the letter of credit along with the drafts. One of the conditions of the letter of credit was that 25 per cent. of the amount should be paid on the presentation of the specified documents and the balance of 75 per cent. to be paid one year from the date of the first payment. The agreement entered into between the Bank of India and the Russian firm under the letter of credit was "subject to the Uniform Customs and Practice for Documentary Credits (1962 Revision), International Chamber of Commerce Brochure No. 222". Article 3 of the Brochure says that :

> "An irrevocable credit is a definite undertaking on the part of an issuing bank and constitutes the engagement of that bank to the beneficiary or, as the case may be, to the beneficiary and bona fide holders of drafts drawn and/or documents presented thereunder, that the provisions for payment, acceptance or negotiation contained in the credit will be duly fulfilled, provided that all the terms and conditions of the

credit are complied with.

> An irrevocable credit may be advised to a beneficiary through another bank without engagement on the part of that other bank (the advising bank), but when an issuing bank authorises another bank to confirm its irrevocable credit and the latter does so, such confirmation constitutes a definite undertaking on the part of the confirming bank either that the provisions for payment or acceptance will be duly fulfilled or, in the case of a credit available by negotiation of drafts, that the confirming bank will negotiate drafts without recourse to drawer.
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> Such undertakings can neither be modified nor cancelled without the agreement of all concerned."

3. Article 8 of the Brochure says :

> "In documentary credit operations all parties concerned deal in documents and not in goods.
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> Payment, acceptance or negotiation against documents which appear on their face to be in accordance with the terms and conditions of a credit by a bank authorised to do so, binds the party giving the authorisation to take up the documents and reimburse the bank which has effected the payment, acceptance or negotiation ...."

4. The only other article in that Brochure which is relevant for our present purpose is Article 9 which reads :

> "Banks assume no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any documents, or for the general and/or particular conditions stipulated in the documents or superimposed thereon; nor do they assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods represented thereby, or for the good faith or acts and/or omissions, solvency, performance or standing of the consigner, the carriers or the insurers of the goods or any other person whomsoever."

5. On the strength of the aforementioned contract, the Russian Firm supplied all the machinery it undertook to supply by about the end of December, 1965, which were duly taken possession of by the Indian Firm and put to work at Farakka Barrage Project. They are still in the possession of the Indian Firm. After the machinery was used for some time, the Indian Firm complained to the Russian Firm that the performance of the machinery supplied by it was not as efficient as represented at the time of entering into the contract and consequently it had incurred and continues to incur considerable loss. In that connection there was some correspondence between the Indian Firm and the Russian Firm. Thereafter the Indian Firm instituted a suit on the original side of the High Court of Madras seeking an injunction restraining the Russian Firm from realizing the amount payable under the letter of credit. During the pendency of that suit the parties arrived at an agreement on August 14, 1966 at Delhi (which shall be hereinafter referred to as the Delhi Agreement). The portion of that agreement which is relevant for our present purpose reads as follows :

> "Tarapore & Co., Madras, agree to withdraw immediately the court-case filed by

them against "Tractors export" Moscow, in the Madras High Court.

2. Immediately on Tarapore withdrawing the case V.O. "Tractors export" agree to instruct the Bank for Foreign Trade of the U.S.S.R. in Moscow, not to demand any further payment against L.C. established by Tarapore & Co., Madras, for a period of six months from the due dates in the first instance. During this period both the parties shall do their best to reach an amicable settlement.

3. In case the settlement between the two parties is not completed within this period of six months, V.O. Tractors export shall further extend the period of payment by further period of six months for the settlement to be completed.

4. Tarapore and Co., shall authorise their Bank to keep the unpaid portions L.C. valid for the extended period as stated above."

6. At this stage it may mentioned that the Russian Firm had received from the Bank of India 25 per cent. of the money payable under the letter of credit very soon after it supplied to the Indian Firm the machinery mentioned earlier. In pursuance of the aforementioned agreement the Indian Firm withdrew the suit. Thereafter there were attempts to settle the dispute. In the meantime the Indian Rupee was devalued. The contract between the Indian Firm and the Russian Firm contains the following term :

"Payment for the delivered goods shall be made by the buyers in Indian Rupee, in accordance with the Trade Agreement between the USSR and India, dated 10th June, 1963. All the prices are stated in Indian Rupees. One Indian Rupee is equal to 0.186621 grammes of pure gold. If the above gold content of Indian Rupee is changed, the prices and the amount of this Contract in Indian Rupee shall be revalued accordingly on the date of changing the gold parity of the Indian Rupee."

7. This clause will be hereinafter referred to as the "Gold Clause". In view of that clause, the price fixed for machinery supplied stood revised. Consequently under the contract, the Indian Firm had to pay to the Russian Firm an additional sum of about rupees twenty-six lakhs. Accordingly the bankers of the Russian Firm called upon the Indian Firm to open an additional letter of credit for payment of the extra price payable under the contract. They also intimated the Indian Firm that the extension of time for the payment of the price of the machinery supplied, agreed to at Delhi will be given effect to only after the Indian Firm arranges for the additional letter of credit asked for. The Indian Firm objected to this demand as per its letter of 20th September, 1966. The relevant portion of that letter reads :

"We are rather surprised to see this, because by our arrangement, dated the 14th August, 1966 at New Delhi, you had agreed to give further time for the payments on the withdrawal of the Madras High Court case. That was the only condition that was talked about and incorporated in our written agreement. If you will be good enough to refer to the agreement, dated the 14th August, 1966, you will find that we were obliged to withdraw the Madras Suit pending talks of settlement and immediately on our withdrawing this suit, you agreed to instruct your Bankers not to demand any further payment under the letter of credit. There is absolutely no reference in that agreement to our having to open any additional letter of credit in view of the devaluation of the Indian Rupee .... We would therefore request you to

> immediately instruct your Bankers in Moscow to advise our Bankers regarding the extension of time for payment under the letter of credit without any reference to any additional letters of credit in view of devaluation .... Moreover, when the entire question is open for amicable settlement between us, it is not possible to determine what exactly will be the amount payable and unless that amount is known, it is not possible to open additional letters of credit to give effect to the gold clause ...."

8. On November 1, 1966, the Russian Firm sent to the Indian Firm, addendum No. 1 modifying the original contract in accordance with the gold clause. The last clause of that addendum recited that "all other terms and conditions are as stated in the abovementioned contract" (original contract). The Indian Firm objected to that addendum as well as to the demand for opening an additional letter of credit. In that connection the Russian Firm wrote a letter to the Indian Firm on November 29, 1966. As considerable arguments were advanced on the basis of that letter, we shall quote the relevant portion of that letter :

> "............ We confirm that you have signed with us the addendum No. 1 to our Contract No. 61/Tarapore-220/65, dated the 2nd February, 1965, at our request for the sole and specific purpose of satisfying our bankers. We confirm further that this addendum will not in any manner prejudice the arrangement we have come to in Delhi on the 14th August, 1966, and is without prejudice to your claims and points of controversy regarding which we shall have further discussions with a view to reach an amicable settlement.
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> Under this addendum, the company will extend the letter of credit for one year and accept the drafts for the difference in value of 57.5 per cent. due to devaluation. The final amount payable will be in accordance with the settlement."

9. Thereafter the Russian Firm appears to have drawn drafts on the Indian Firm for the excess amount payable under the gold clause. For one reason or the other, no settlement as contemplated by the Delhi Agreement was reached. The Indian Firm complained that the Russian Firm never made any serious attempt to resolve the dispute, whereas the Russain Firm alleged that it found no substance in the complaint made by the Indian Firm as regards the machinery supplied. In the suit as brought, as well as in these appeals that controversy is not open for examination. Suffice it to say that the parties did not amicably settle the dispute in question. When the extended time granted under the Delhi Agreement was about to come to a close, the Indian Firm instituted the suit from which these appeals have arisen. In that suit the only substantive relief asked for is that the Bank of India as well as the Russian Firm should be restrained from taking any further steps in pursuance of the letter of credit opened by the Indian Firm in favour of the Russian Firm. Therein temporary injunctions were prayed for in the very terms in which the permanent injunctions were prayed for. At a subsequent stage a further injunction restraining the Russian Firm from enforcing its right under the gold clause was also prayed for. The Russian Firm opposed those applications but the trial Judge granted the temporary injunctions asked for. The Russian Firm took up the matter in appeal to the Appellate Bench of that High Court which reversed the order of the trial judge by its order, dated October 9, 1968, but it certified that they are fit cases for appeal to this court. When the applications in the appeals seeking interim orders came up for consideration by this court the Russian Firm entered its caveat. It not only opposed the interim reliefs prayed for, it further challenged the validity of the certificates granted by the High Court on the ground that the orders appealed against are not final orders within the meaning of Article 133 of the Constitution.

Evidently as a matter of abundant caution, the Indian Firm had filed two separate applications seeking special leave to appeal against the orders of the Appellate Bench of the Madras High Court. After hearing the parties this court revoked the certificate granted holding that the orders appealed against are not final orders but at the same time granted special leave to the Indian Firm to appeal against the orders of the Madras High Court. Civil Appeals Nos. 2051 and 2052 of 1968 are appeals filed by the Indian Firm.

10. Before the Appellate Bench of the High Court of Madras, the Indian Firm had objected to the maintainability of the appeals filed by the Russian Firm on the ground that orders appealed against are not judgments within the meaning of Clause 15 of the Letters Patent of the Madras High Court, but that objection had been overruled by the Appellate Bench following the earlier decisions of that High Court. That contention was again raised in the appeals filed by the Indian Firm in this court. To obviate any difficulty the Russian Firm applied to this court for special leave to appeal against the interim orders passed by the trial judge. We allowed those application and consequently Civil Appeals Nos. 2305 and 2306 of 1968 came to be filed.

11. In view of the appeals filed by the Russian Firm in this court against the interim orders made by the trial judge it is not necessary to decide whether the appeals filed by the Russian Firm before the Appellate Bench of the Madras High Court were maintainable ? On that question, judicial opinion is sharply divided as could be seen from the decision of this Court in Asrumati Debi v. Kumar Rupendra Deb Rajkot and others. ((1953) SCR 1159) Hence we shall confine our attention to the question whether the temporary injunctions issued by the trial judge are sustainable ?

12. The scope of an irrevocable letter of credit is explained thus in Halsbury's Laws of England (Vol. 34), Paragraph 319 at p. 185 :

> "It is often made a condition of a mercantile contract that the buyer shall pay for the goods by means of a confirmed credit, and it is then the duty of the buyer to procure his bank, known as the issuing or originating bank, to issue an irrevocable credit in favour of the seller by which the bank undertakes to the seller, either directly or through another bank in the seller's country known as the correspondent or negotiating bank, to accept drafts drawn upon it for the price of the goods, against tender by the seller of the shipping documents. The contractual relationship between the issuing bank and the buyer is defined by the terms of the agreement between them under which the letter opening the credit is issued; and as between the seller and the bank, the issue of the credit duly notified to the seller creates a new contractual nexus and renders the bank directly liable to the seller to pay the purchase price or to accept the bills of exchange upon tender of the documents. The contract thus created between the seller and the bank is separate from, although ancillary to, the original contract between the buyer and the seller, by reason of the bank's undertaking to the seller, which is absolute. Thus the bank is not entitled to rely upon terms of the contract between the buyer and the seller which might permit the buyer to reject the goods and to refuse payment therefor; and, conversely the buyer is not entitled to an injunction restraining the seller from dealing with the letter of credit if the goods are defective."

13. Chalmers on "Bills of Exchange" explains the legal position in these words :

> "The modern commercial credit serves to interpose between a buyer and seller a third

> person of unquestioned solvency, almost invariably a banker of international repute; the banker on the instructions of the buyer issues the letter of credit and thereby undertakes to act as paymaster upon the seller performing the conditions set out in it. A letter of credit may be in any one of a number of specified forms and contains the undertaking of the banker to honour all bills of exchange drawn thereunder. It can hardly be overemphasized that the banker is not bound or entitled to honour such bills of exchange unless they, and such accompanying documents as may be required thereunder, are in exact compliance with the terms of the credit. Such documents must be scrutinised with meticulus care, the maxim de minimis non curat lex cannot be invoked where payment is made by letter of credit. If the seller has complied with the terms of the letter of credit, however, there is an absolute obligation upon the banker to pay irrespective of any disputes there may be between the buyer and the seller as to whether the goods are up to contract or not."

14. Similar are the views expressed in "Practice and Law of Banking" by H. B. Sheldon; "the law of Banker's Commercial Credits" by H. C. Gutteridge; "the Law relating to Commercial Letters of Credit" by A. G. Davis; "the Law relating to Banker's Letter of Credit" by B. C. Mitra and in several other text-books read to us by Mr. Mohan Kumaramanglam, learned counsel for the Russian Firm. The legal possession as set out above was not controverted by Mr. M. C. Setalvad, learned Counsel for the Indian Firm. So far as the Bank of India is concerned, it admitted its liability to honour the letter of credit and expressed its willingness to abide by its terms. It took the same position before the High Court.

15. The main grievance of the Indian Firm is that if the Russian Firm is allowed to take away the money secured to it by the letter of credit, it cannot effectively enforce its claim arising from the breach of the contract it complains of. It was urged on its behalf that the Russian Firm has no assets in this country and therefore any decree that it may be able to obtain cannot be executed. Therefore, it was contended that the trial court was justified in issuing the impugned orders. The allegation that Russian Firm has no assets in this country was not made in the pleadings. That apart in the circumstances of this case that allegation has no relevance. An irrevocable letter of credit has a definite implication. It is a mechanism of great importance in international trade. Any interference with that mechanism is bound to have serious repercussions on the international trade of this country. Except under very exceptional circumstances, the Court should not interfere with that mechanism.

16. For our present purpose we shall assume without deciding that the allegations made by the Indian Firm are true. We shall further assume that the suit as brought is maintainable though Mr. Kumaramangalam seriously challenged its maintainability. But yet, in our judgment, the learned trial Judge was not justified in law in granting the temporary injunctions appealed against. Ordinarily this court does not interfere with interim orders. But herein legal principles of great importance affecting international trade are involved. If the orders impugned are allowed to stand they are bound to have their repercussion on our international trade.

17. We have earlier referred to several well known treatises on the subject. Now we shall proceed to consider the decided cases bearing on the question under consideration.

18. A case somewhat similar to the one before us came up for consideration before the Queens Bench Division in England in Hamzeh Malas and Sons v. British Imex Industries Ltd. ((1958) 2 QB 127) Therein the plaintiffs, a Jordanian firm contracted to purchase from the defendants, a British

firm, a large quantity of reinforced steel rods, to be delivered in two instalments. Payment was to be effected by opening in favour of the defendants of two confirmed letters of credit with the Midland Bank Ltd. in London, one in respect of each instalment. The letters of credit were duly opened and the first was realized by the defendants on the delivery of the first instalment. The plaintiffs complained that that instalment was defective and sought an injunction to bar the defendants from realising the second letter of credit. Donovan, J., the trial judge refused the application. In appeal Jenkins, Sellers and Pearce, L. JJ. confirmed the decision of the trial judge. In the course of his judgment Jenkins L.J. who spoke for the Court observed thus :

> "We have been referred to a number of authorities, and it seems to be plain enough that the opening of a confirmed letter of credit constitutes a bargain between the banker and the vendor of the goods, which imposes upon the banker an absolute obligation to pay, irrespective of any dispute there may be between the parties as to whether the goods are up to contract or not. An elaborate commercial system has been built up on the footing that bankers' confirmed credits are of that character, and, in my judgment, it would be wrong for this court in the present case to interfere with that established practice.
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> There is this to be remembered, too. A vendor of goods selling against a confirmed letter of credit is selling under the assurance that nothing will prevent him from receiving the price. That is of no mean advantage when goods manufactured in one country are being sold in another. It is, further, to be observed that vendors are often reselling goods brought from third parties. When they are doing that, and when they are being paid by a confirmed letter of credit, their practice is - and I think it was followed by the defendants in this case - to finance the payments necessary to be made to their suppliers against the letter of credit. That system of financing these operations, as I see it, would break down completely if a dispute as between the vendor and the purchaser was to have the effect of "freezing", if I may use that expression, the sum in respect of which the letter of credit was opened".

19. In Urquhart Lindsey and Co. Ltd. v. Eastern Bank Ltd., ((1922) 1 KB 318) the King's Bench held that the refusal of the defendants bank to take and pay for the particular bills on presentation of the proper documents constituted a repudiation of the contract as a whole and that the plaintiffs were entitled to damages arising from such a breach. It may be noted that in that case the price quoted in the invoices was objected to by the buyer and he had notified his objection to the bank. But under the terms of the letter of credit the bank was required to make payments on the basis of the invoices tendered by the seller. The court held that if the buyers had an enforceable claim, that adjustment must be made by way of refund by the seller and not by way of retention by the buyer.

20. Similar opinions have been expressed by the American Courts. The leading American case on the subject is Dulien Steel Products Inc., of Washington v. Bankers Trust Co. (Federal Reporter, 2nd Series 298, P. 836) The facts of that case are as follows :

> "The plaintiffs, Dulien Steel Products Inc., of Washington, contracted to sell steel scrap to the European Iron and Steel Community. The transaction was put through M/s. Marco Polo Group Project Ltd., who were entitled to commission for arranging the transaction. For the payment of the commission to Marco Polo, plaintiffs procured an irrevocable letter of credit from Seattle First National Bank. As desired by Marco Polo this letter of credit was opened in favour of one Sica. The defendant

> bankers confirmed that letter of credit. The credit stipulated for payment against (1) a receipt of Sica for the amount of the credit, and (2) a notification of Seattle Bank to the defendants that the plaintiffs had negotiated documents evidencing the shipment of the goods. Sica tendered the stipulated receipt and Seattle Bank informed the defendants that the Dulien had negotiated documentary drafts. Meanwhile after further negotiations between the plaintiffs and the vendees the price of the goods sold was reduced and consequently the commission payable to Marco Polo stood reduced but the defendants were not informed of this fact. Only after notifying the defendants about the negotiation of the drafts drawn under the contract of sale, the Seattle Bank informed the defendants about the changes underlying the transaction and asked them not to pay Sica the full amount of the credit. The defendants were also informed that Sica was merely a nominee of Marco Polo and has no rights of his own to the sum of the credit. Sica, however, claimed payment of the full amount of the credit. The defendants asked further instructions from Seattle Bank but despite Seattle Bank's instructions decided to comply with Sica's request. After informing Seattle Bank of their intention, they paid Sica the full amount of the credit. Plaintiffs thereupon brought an action in the District Court of New York for the recovery of the moneys paid to Sica. The action was dismissed by the trial court and that decision was affirmed by the Court of Appeals. That decision establishes the well known principle that the letter of credit is independent of and unqualified by the contract of sale or underlying transaction. The autonomy of an irrevocable letter of credit is entitled to protection. As a rule, courts refrain from interfering with that autonomy."

21. A half-hearted attempt was made on behalf of the Indian Firm to persuade us not to apply the principles noticed above as in these appeals we are dealing with a complaint of fraud. The facts pleading in the plaint do not amount to a plea of fraud despite the assertions of the Indian Firm that Russian Firm was guilty of fraud.

22. Evidently with a view to steer clear of the well established legal position, Mr. Setalvad, learned Counsel for the Indian Firm, urged that the letter of credit was no more enforceable as the original contract stood modified as a result of the Delhi Agreement and the subsequent correspondence between the parties. It was urged that according to the modified contract, the Indian Firm is only liable to pay the price that may be settled between the buyer and the seller. This contention has not been taken either in the plaint or in the arguments before the trial judge or before the Appellate Bench. It is taken for the first time in this court. This is not purely a legal contention. The contention in question bears on the intention of the parties who entered into the agreement. No one could have known the intention better than the plaintiff who was a party to the contract. If there was such an intention, the plaintiff would have certainly pleaded the same. That apart, we are unable to accept the contention that either the Delhi Agreement or the subsequent correspondence between the parties modified the original contract. The Delhi Agreement merely provided that the parties will try and settle the dispute out of court, if possible. Much was made of the letter written by the Russian Firm to the Indian Firm on 29-11-1966 wherein as seen earlier it was stated :

> "that the final amount payable will be in accordance with the settlement."

23. This letter has to be read along with the other letters that passed between the parties. If so read, it is clear that the statement that the final payment will be made in accordance with the settlement is subject to the condition that the parties are able to arrive at a settlement. Otherwise the parties continue to be bound by the original contract subject to the extension of the time granted under the

Delhi Agreement for the payment of the price. As regards the additional payment demanded by the Russian Firm, there is no occasion for issuing any temporary injunction. If the Indian Firm does not comply with that demand the law will take its course. It is for that Firm to choose its course of action.

24. In the result we allow Civil Appeals Nos. 2305 and 2306 of 1968 with costs of the appellant therein and set aside the temporary injunctions granted by the trial judge. The other appeals are dismissed with no order as to costs. The costs to be paid by the Indian Company.

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