

# **SUPREME COURT OF INDIA**

UBS AG

Vs

State Bank of Patiala

Appeal (Civil) 2578 of 2006 (Arising Out of Slp) No.5639 of 2006); Civil Appeal No. .2579./2006 (Arising Out of Slp ) No.6134 of 2006); Civil Appeal No. .2580../2006 (Arising Out of Slp ) No.6141 of 2006)

(B. P. Singh and Altamas Kabir, JJ)

10.05.2006

## **JUDGMENT**

### **ALTAMAS KABIR, J.**

The Petitioner-Bank, namely, United Bank of Switzerland, Lausanne, Switzerland (hereinafter referred to as 'USB AG') filed three separate Summary Suits, being Nos. 8907 of 2000, 1515 of 2000 and 6089 of 1999, against the State Bank of Patiala, Federal Bank Limited and United Western Bank, respectively. The Petitioner-Bank took out Summons for Judgment No.783 of 2003 in Summary Suit No.897 of 2000 against the State Bank of Patiala. Two similar Summons for Judgment Nos. 784 of 2003 and 786 of 2003 were also taken out by the Petitioner-Bank in connection with Summary Suit Nos. 1515 of 2000 and 6089 of 1999. Inasmuch as, the said three suits were filed in respect of various Letters of Credit, where the terms and conditions were identical and the defence taken were also identical, the said three Summons for Judgment were taken up for hearing and disposal analogously and were dismissed by a common order dated 28th October, 2005. The Learned Single Judge of the High Court of Judicature at Bombay also granted unconditional leave to the Respondent-Banks to defend their respective suits.

Three separate Special Leave Petitions, being Special Leave Petition ) Nos. 5639 of 2006, 6141 of 2006 and 6134 of 2006, have been filed against the common judgment disposing of the said three suits and since they involve common questions of law and fact, they have been taken up for

admission together.

Since the facts in the three matters are more or less similar, we will first deal with the facts relating to the Special Leave Petition in respect of the State Bank of Patiala (SLP) No. 5639 of 2006).

On 27th March, 1998, on the request of its client, M/s Hamco Mining & Smelting Ltd, the State Bank of Patiala issued an Irrevocable Letter of Credit for a sum of U.S. Dollars 1,320,900 to the Petitioner-Bank. The beneficiary of the Letter of Credit was M/s. Frobevia S.A. The said Letter of Credit appears to have been issued for the import of 255.00 MT of Tin Ingots by M/s. Hamco Mining & Smelting Ltd. On 30th March 1998, the Petitioner-Bank confirmed the said Letter of Credit, which was to be valid till 23rd September, 1998. On 6th April, 1998, upon production of relevant documents by the beneficiary, the Petitioner-Bank made payment under the said Letter of Credit to the said beneficiary, namely, Frobevia S.A. Despite having made payment of the entire amount covered by the Letter of Credit to the beneficiary, the Petitioner-Bank agreed to the extension of the maturity date of the Letter of Credit from 23rd September, 1998 till 21st March, 1999. On 3rd February, 1999, the advocate for the Respondent-Bank wrote to the Petitioner-Bank that the Respondent Bank had received information that M/s. Hamco Mining & Smelting Ltd, M/s. Frobevia and one Solo Industries Ltd., having its offices at London and Sharjah, in connivance with other group companies of Hamco had been perpetrating huge frauds on several banks in India. It was also mentioned that from the enquiry undertaken, it was clear that M/s. Frobevia did not ship any goods on the vessel in question and the Bill of Lading negotiated by M/s. Frobevia was fraudulent. By the said letter, the Petitioner-Bank was informed further that the Respondent-Bank had been advised not to make any payment under the above mentioned Letter of Credit dated 27th March, 1998 and the Petitioner-Bank was put 'on caution' and was advised not to negotiate the export bills presented by M/s. Frobevia and further not to make any payment to M/s. Frobevia in respect of the said Letter of Credit.

Notwithstanding the aforesaid letter dated 3rd February, 1999, the Petitioner-Bank demanded remittance of the entire amount covered by the Letter of Credit, which was due for payment on 21st March, 1999. On receipt of two such demands made on 17th March 1999 and 23rd March, 1999, the Respondent-Bank replied drawing the attention of the Petitioner-Bank to the letter written by its learned advocate on 3rd February, 1999, informing the Petitioner-Bank that it had been advised not to make any payment under the aforesaid Letter of Credit dated 27th March, 1998, favouring M/s. Frobevia S.A.

On receipt of the said communication, the Petitioner- Bank wrote to the Respondent-Bank on 7th April, 1999 indicating that documents presented by the beneficiary had been negotiated and payments had already been made on 6th April, 1998 long prior to the allegations of fraud indicated by the learned advocate of the Respondent-Bank. It was pointed out that irrespective of the said fact, under the Uniform Custom and Practice for Documentary Credit 500 (hereinafter referred to as 'UCP 500') the Respondent-Bank was under an obligation to reimburse on the due date of the Letter of Credit, the amount already paid by the Petitioner-Bank to the beneficiary. There was no evidence that the beneficiary had acted fraudulently. The Respondent-Bank was once again requested to remit the actual outstanding amount, together with interest at the rate of 5.7%, from the date of maturity

upto the date of payment to the account of the Petitioner- Bank, that is, UBS AG, Stamford Branch, C.T., U.S.A. Inasmuch as, despite the repeated demands, the Respondent-Bank did not reimburse the Petitioner-Bank in respect of the amount paid to the beneficiary under the Letter of Credit before receipt of the letter dated 3rd February, 1999, written by the advocate of the Respondent-Bank, the Petitioner-Bank sent a legal notice dated 30th June, 1999 informing the Respondent-Bank that on account of their failure to honour their commitments under 'UCP 500', the Petitioner-Bank would be constrained to file a suit for recovery of their dues.

Pursuant thereto, the Petitioner-Bank instituted Summary Suit No. 897 of 2000 in the Ordinary Original Civil Jurisdiction of the High Court of Judicature at Bombay under Order XXXVII of the Code of Civil Procedure, 1908. As indicated, hereinbefore, two similar suits on similar causes of action, were filed by the Petitioner-Bank against the Federal Bank Limited and United Western Bank, being Summary Suit Nos. 1515 of 2000 and 6089 of 2000, respectively. Inasmuch as, the three Special Leave Petitions against the said three suits have been taken up for consideration together, leave is granted in all the three Special Leave Petitions.

The short point for decision in these appeals is whether unconditional leave could have been granted to the Respondent-Banks to defend the suits filed against them by the Appellant- Bank for their refusal to reimburse the Appellant-Bank in respect of the amounts disbursed to the beneficiary of the Letters of Credit before being informed of the fraud allegedly perpetrated by the beneficiary and the constituent of the Respondent-Banks.

The Letter of Credit issued by the Respondent-Bank requests the Appellant-Bank to advise the beneficiary that the Respondent-Bank was establishing an Irrevocable Letter of Credit for 1,320,900 U.S. Dollars only. The Letter of Credit further indicates the 20th of June, 1998 as the expiry date for shipment and 10th of July, 1998, for negotiation in Switzerland. It was further stipulated that the documents for negotiation were to be presented within 21 days from the date of the shipping documents and were to be accompanied by the documents evidencing shipment of 255 metric tonnes of tin ingots. In paragraph 12 of the Letter of Credit it was particularly indicated that the credit was subject to Uniform Customs and Practice for Documentary Credit (1993 Revision) as published in International Chambers of Commerce Publication No.500.

According to the Appellant-Bank, the beneficiary presented the documents indicated by the Letter of Credit for negotiation to the Appellant-Bank on 6th April, 1998 and on the basis thereof the Appellant-Bank made payment under the Letter of Credit to the beneficiary M/s.Frobevia S.A. and informed the Respondent-Banks accordingly.

On 22nd July, 1998, the Respondent-Bank informed the Appellant-Bank that its documents for U.S. Dollars 1,320,900 referred to in the Letter of Credit had been accepted to mature on 23rd September, 1998 on which date the funds would be remitted as per the instructions of the Appellant-Bank. By a subsequent communication dated 21st August, 1998, the Respondent-Bank informed the Appellant-Bank that the beneficiary had agreed to extend the maturity date of the Letter of Credit from 23rd September, 1998 to 21st March, 1999. The Appellant-Bank was requested to confirm such extension. In response to the said communication, the Appellant-Bank by its communication

dated 31st August, 1998 confirmed the extension of the reimbursement date till 21st March, 1999.

As indicated hereinbefore, notwithstanding the fact that the Appellant-Bank had made payment to the beneficiary under the Letter of Credit as far back as on 6th April, 1998, and had informed the Respondent-Bank accordingly, the Respondent-Bank caused a letter dated 3rd February, 1999 to be written by its learned advocate stating that certain frauds perpetrated by its constituent, M/s. Hamco Mining & Smelting Ltd., M/s. Frobevia and one M/s. Solo Industries Ltd., had been brought to its notice by several other banks which had established Letters of Credit at the instance of M/s. Hamco Mining & Smelting Ltd. It was also mentioned that the clear implication was that the Letters of Credit were fraudulently encashed by production of bogus Bills of Lading and other shipping documents. By the said letter the Appellant-Bank was put 'on caution' not to negotiate the export bills, if any, presented by M/s. Frobevia and further not to make any payment whatsoever to M/s. Frobevia in respect of the Letter of Credit.

While considering the application filed by the Appellant- Bank for summary judgment, the High Court took note of the fraud said to have been perpetrated by M/s.Hamco Group of Industries and that it was the case of the Defendant-Bank that they had been defrauded by their constituent in obtaining the Letter of Credit. The learned Single Judge also took note of the submission made on behalf of the Defendant-Bank that it had come to its notice that the Letter of Credit had been sought to be encashed without import of any goods, on the basis of bogus documents and that even the Bill of Lading and shipping documents used for obtaining the Letter of Credit and subsequent encashment thereof were fraudulent.

The learned Single Judge also took note of the submission made on behalf of the Plaintiff-bank that since the Letter of Credit was a written contract, on the date of maturity the Defendant-Bank was bound to honour the commitment made therein. The learned Judge also noted that it was the case of the Plaintiff-Bank that even before communication by the Respondent-Bank of the fraud said to have been perpetrated by the constituent of the Respondent-Bank, the Appellant-Bank had already paid over the amount to the beneficiary which amount was to be reimbursed by the Respondent-Bank.

On consideration of the submissions made, the learned Single Judge was of the view that the suit raises serious triable issues and in that view of the matter unconditional leave was granted to the Defendant-Banks to defend their respective suits.

The reasoning of the learned Single Judge of the High Court in granting such leave has been questioned in these appeals on the ground that the High Court had completely misconstrued the law relating to Letters of Credit which is sometimes referred to as the life-blood of international commerce.

The main contention raised on behalf of the Appellant- Bank is that since it had no knowledge of any fraud perpetrated by the constituent of the Respondent-Bank before making payment under the Letter of Credit in question, the Respondent-Bank could not refuse to reimburse the Appellant-Bank of payments already made to the beneficiary under the Letter of Credit before such intimation

was received. It was also the case of the Appellant-Bank that since it had no knowledge of the fraud said to have been committed with regard to the Bills of Lading and the Letter of Credit itself, it negotiated documents presented before it by the beneficiary and made payment accordingly as per the instructions of the Respondent-Bank.

Appearing for the Appellant-Bank, Mr. Ashok Desai, learned senior advocate, referred to and relied on the decision of this Court in *Oil & Natural Gas Corporation Ltd. vs. SBI, Overseas Branch, Bombay*, wherein while dealing with a summary suit under Order XXXVII and a similar question involving leave to defend in respect of a bank guarantee, this Court held that an unconditional bank guarantee must be given effect to even where there is a dispute between the parties and that unless there is a plea relating to fraud the Court does not have jurisdiction to grant unconditional leave to defend. Mr. Desai submitted that in the instant case the plea relating to fraud was taken by the Respondent-Bank against its own constituent and such fact was intimated to the Appellant-Bank long after the payment under the Letter of Credit had been made to the beneficiary. Similar sentiments were expressed by this Court in *Dwarikesh Sugar Industries Ltd. vs. Prem Heavy Engineering Works (P) Ltd. and Anr.*, 6, wherein while dealing with a bank guarantee this Court held that the principle of undue enrichment was not applicable to encashment of bank guarantees.

Mr. Desai also referred to another decision of this Court in *Federal Bank Ltd. vs. V.M. Jog Engineering Ltd. and Ors.*, 9, wherein it was observed that in the case of a bank guarantee or letter of credit the Court should not issue an order of injunction restraining encashment thereof on ground of breach of the main contract between the buyer and the seller. A contract of bank guarantee or letter of credit is independent of the main contract and the only exceptions are when fraud is committed by the seller or where encashment results in irretrievable damage. This Court went on further to hold that where the negotiating bank makes payment to the seller after obtaining confirmation from the issuing bank about the genuineness of the letter of credit, bill of exchange and other related documents and seeks reimbursement from the issuing bank, the encashing bank cannot be restrained by injunction from obtaining reimbursement.

Mr. Desai also referred to the relevant provisions of the UCP 500, and in particular Article 14 thereof, which deals with reimbursement on negotiation of documents presented to the Confirming-Bank on the instructions of the Issuing-Bank. It was urged that the Respondent-Bank had no defence since no triable issues arise in the suits as filed.

The stand taken on behalf of the Respondent-Bank was that the Appellant-Bank could claim reimbursement only on the due date of payment as stipulated in the Letter of Credit agreed upon between the issuing bank and the confirming bank. It was urged that since the fraud committed by M/s. Hamco Mining & Smelting Ltd. had been discovered and intimated to the Appellant-Bank before the due date of reimbursement, the Respondent-Bank was entitled to withhold payment under the Letter of Credit. It was also urged that several triable issues arise in the suit, which had been taken note of by the High Court while granting unconditional leave to defend the suit.

Mr. R.F. Nariman, learned senior advocate, appearing for the Respondent-Bank contended that one such triable issue was whether payment had at all been made by the Appellant-Bank to the

beneficiary under the Letter of Credit before being informed of the fraud perpetrated by M/s. Hamco Mining & Smelting Ltd. It was contended that in the correspondence exchanged between the two banks, except for intimation that the documents presented by the beneficiary had been negotiated by the Appellant-Bank, there was nothing else on record to indicate that payment had, in fact, been made on 6th April, 1998, the same date on which the documents were presented for negotiation.

Apart from the above, it was submitted that the Court would have to consider whether the Appellant-Bank had satisfied itself about the genuineness of the documents presented and had obtained confirmation from the Respondent-Bank before making payment to the beneficiary of the Letter of Credit. In fact, one of the points urged on behalf of the Respondent-Bank was that payment, if any, made by the Appellant-Bank to M/s. Frobevia S.A. may have been under some private agreement and not under the Letter of Credit.

It was contended that it was sufficient to indicate to the Court before which a suit was pending, that there was a triable issue for which leave to defend the suit was required to be given.

Reference was made to the decision of this Court in Raj Duggal vs. Ramesh Kumar Bansal, , where a question had been raised regarding leave to defend in a suit under Order XXXVII of the Code of Civil Procedure. While considering the said question, this Court set out the principles to decide whether leave should be granted or denied in the following manner :-

*"3. Leave is declined where the court is of the opinion that the grant of leave would merely enable the defendant to prolong the litigation by raising untenable and frivolous defences. The test is to see whether the defence raises a real issue and not a sham one, in the sense that if the facts alleged by the defendant are established there would be a good or even a plausible defence on those facts. If the court is satisfied about that leave must be given. If there is a triable issue in the sense that there is a fair dispute to be tried as to the meaning of a document on which the claim is based or uncertainty as to the amount actually due or where the alleged facts are of such a nature as to entitle the defendant to interrogate the plaintiff or to cross-examine his witnesses leave should not be denied. Where also, the defendant shows that even on a fair probability he has a bona fide defence, he ought to have leave. Summary judgments under Order 37 should not be granted where serious conflict as to matter of fact or where any difficulty on issues as to law arises. The court should not reject the defence of the defendant merely because of its inherent implausibility or its inconsistency."*

It was urged that the defence was not required to show that it would inevitably succeed in the suit, but that a plausible defence, capable of being tried, was sufficient to grant leave to a defendant to defend a suit of this nature. The principle in such matters was to grant leave to a defendant to defend a suit if there was the slightest possibility of a triable defence.

In addition, it was contended that the appeals were not maintainable as the impugned order of the High Court granting leave to the Defendant-Banks to defend their respective suits did not amount to

a judgment against which an appeal would lie. Placing reliance on the decision of this Court in *Shah Babulal Khimji vs. Jayaben D. Kania and Anr.*, (distinguished), Mr. Nariman submitted that no civil right of the Appellant-Bank had been adversely affected by grant of such leave and that as far as the Appellant-Bank was concerned, the suits filed by it remained and the defendants therein would only get an opportunity to defend the same. On consideration of the submissions made on behalf of the respective parties, we are unable to agree with the submissions advanced on behalf of the Respondent-Bank in these appeals. While the principles indicated by Mr. Nariman in matters relating to grant of leave to a defendant to defend a suit under Order XXXVII of the Code of Civil Procedure are undoubtedly sound, in the facts of this case, however, no triable issue can be raised which would warrant grant of unconditional leave to the Respondent-Bank to defend the suit filed by the Appellant-Bank. International commerce operates on trust and relies to a large extent on arrangements between banks on behalf of their respective clients, giving rise to 'UCP 500' which governs the Letter of Credit involved in the instant case. Prior to 3rd February, 1999, when the advocate for the Respondent-Bank wrote to the petitioner-bank, there is nothing on record to suggest that any fraud had been perpetrated by the applicant and the beneficiary or that the Appellant-Bank had been requested not to negotiate the documents to be presented by the beneficiary. In fact, four and a half months after 6th April, 1998, when the Letter of Credit had already been negotiated, the Respondent-Bank requested the Appellant-Bank to extend the maturity date of the Letter of Credit from 23rd September, 1998 to 21st March, 1999.

The facts of these three appeals are clear and simple. The Letters of Credit were issued by the issuing bank to the confirming-bank with a request to inform the beneficiary that an irrevocable Letter of Credit had been established for the sum indicated therein to be paid by the Appellant-Bank on negotiation of documents to be presented by the beneficiary. Such documents having been presented by the beneficiary to the Appellant-Bank, it made payment under the Letter of Credit to the beneficiary and was entitled to receive reimbursement for the same from the Respondent-Bank. If the fraud had been detected earlier and the Appellant-Bank had been informed of such fraud and put on caution prior to making payment, the Respondent-Bank may have had a triable issue to go to trial. That is not so in these three cases. In these cases, the fraud was detected after the Letters of Credit had been negotiated and hence such fraud alleged to have been committed by the constituent of the Respondent-Bank cannot be set up even as a plausible defence in the suit filed by the Appellant-Bank.

The High Court, appears to have been persuaded to hold that serious triable issues arise in the present suits since the record reveals that a fraud had been committed in obtaining the Letter of Credit. Even if the constituent of the Respondent-Bank had committed fraud in obtaining the Letter of Credit, the same would not be a triable issue to decide whether the Appellant-Bank was entitled to reimbursement under the Letter of Credit before such fraud was brought to its notice. The High Court has wrongly interpreted Clause 8 of the Letter of Credit in holding that the plaintiff's claim for encashment of the Letter of Credit could not be accepted because prima facie Clause 8 of the said Letter of Credit did not provide for discounting of the said Letter of Credit and in view of such discounting the plaintiff would not be entitled to claim reimbursement on the ground that the said amount had been paid to the beneficiary. The Letter of Credit itself shows that the same was to be negotiated as had been done by the Appellant-Bank.

As far as the submission regarding the maintainability of the appeals are concerned, we are satisfied

that the principles enunciated in Babulal Khimji's case (supra) which apply to Letters Patent Appeals, will not apply to appeals for which special leave is granted under Article 136 of the Constitution. In such circumstances, these appeals succeed and are allowed. The judgment and order of the High Court in these three appeals are set aside and the unconditional leave granted to the Respondent-Bank to defend the suit is revoked.