



## Balancing Act: SC Navigates Arbitration and Bank Guarantee Conundrum



### Introduction

The legal arena often witnesses a delicate dance between seemingly conflicting principles. One such intricate interplay exists between the sanctity of arbitration agreements, designed to minimize judicial intervention, and the robust mechanism of bank guarantees, instruments intended to be both independent and unconditional. While courts generally exercise restraint in interfering with the invocation of these guarantees, the scales of justice sometimes demand intervention, particularly when faced with the specter of egregious fraud or the certainty of irretrievable harm. This very tension was at the heart of a recent decision by the Supreme Court of India.

In *Jindal Steel And Power Limited V. Bansal Infra Projects Pvt. Ltd. & Others*<sup>1</sup>, a division bench comprising Justices JB Pardiwala and R Mahadevan grappled with the question of how far a High Court can, and indeed should, step in under its supervisory jurisdiction under Article 227 of the Constitution in matters involving bank guarantees, especially within the framework of the Arbitration Act<sup>2</sup>.

The case unfolded with a significant advance payment of ₹3.73 Crore, secured by an



unconditional bank guarantee. The Appellant, Jindal Steel, citing project delays and alleged poor performance, sought to invoke this guarantee. Bansal Infra Projects Pvt. Ltd., the Respondent, resisted, leading to a legal challenge.

The core issue that reached the Supreme Court was whether the High Court had overstepped its boundaries by intervening to prevent the encashment of this guarantee, especially considering the alternative remedies available under the Arbitration Act. The Supreme Court's decision hinged on the argument of “**irreversible harm**” – the potential fallout from the guarantee's encashment.

This article delves into the Supreme Court's judgment, analyzing the nuanced jurisprudence that governs judicial intervention in disputes involving bank guarantees within the realm of arbitration law.

The Supreme Court's recent engagement with the intricate relationship between arbitration law and bank guarantees was sparked by an appeal challenging a High Court's interim order. This order had restrained the appellants from invoking a bank guarantee during the pendency of proceedings under **Section 9 of the Arbitration Act**.

The appellants, aggrieved by the High Court's intervention, raised a series of fundamental legal questions. These questions challenged the very jurisdiction and propriety of the High Court's action, touching upon core tenets of arbitration law and the limits of judicial review.

The appellants questioned whether the High Court, while exercising its supervisory jurisdiction under Article 227 of the Constitution, could delve into the merits of the case, and whether it was appropriate for the High Court to intervene at all in matters concerning the encashment of an unconditional bank guarantee.

They also raised questions on the interplay between orders under the CPC<sup>3</sup> and Sections under the Arbitration Act, specifically asking whether an interim order under **Order XXXIX Rule 3 CPC** accompanying a **Section 9 Petition** should be treated as an order under Section 9, and thus appealable under Section 37(1)(b) of the Arbitration Act.

A key thrust of their argument was whether the High Court could invoke its extraordinary writ jurisdiction under **Article 227** when an alternative remedy, an appeal under **Section 37(1)(b) of the Arbitration Act**, was available. The appellants further questioned the permissibility of filing interim applications under the CPC in a Section 9 petition, given the Arbitration Act's claim to be a self-contained and exhaustive code.



They also argued against allowing parties to pursue parallel proceedings under Article 227 while simultaneously invoking arbitration, which they said would cause delays in the arbitral process.

Finally, they posed questions about the appealability of interlocutory orders, arguing that an order rejecting an ex parte interim stay under **Order XXXIX Rule 3 CPC** with a Section 9 Petition, may be appealable under **Section 37** of the Arbitration Act, or barred from challenge under **Order XLIII Rule 1(r)** read with **Section 104 CPC**, thus limiting recourse to Article 227 of the Constitution.

At the heart of the dispute were conflicting claims arising from a work order dated 24.01.2022. The appellants had made an advance payment of ₹3,73,95,490 to the respondent, who had furnished an irrevocable and unconditional bank guarantee for this amount. The appellants, citing delays and poor performance, terminated the work order and sought to encash the bank guarantee.

The respondent, however, countered that the delays were attributable to the appellants' own failures, such as delays in supplying materials and releasing payments, and a failure to provide adequate facilities for workers. It was this contention that led the respondent to approach the **Commercial Court**, seeking an ex parte interim order to restrain the encashment of the bank guarantee. While the Commercial Court rejected the respondent's application under Order XXXIX Rule 3 CPC, the High Court, in the exercise of its powers under Article 227 of the Constitution, granted the interim protection sought by the respondent.

It is important to note that the Supreme Court, in its analysis, reiterated the established legal principle that courts should be wary of interfering with the invocation of a bank guarantee. The Court emphasized that such interference should be limited to exceptional cases involving egregious fraud or the likelihood of irretrievable injustice.

The Court drew attention to its previous ruling in **Hindustan Construction Co. Ltd v. State of Bihar and others**<sup>4</sup>, where it had affirmed the crucial role of bank guarantees in commercial transactions and the need to honor them as per their terms. The Supreme Court in this case also referred to several other cases that have consistently upheld this principle, including **U.P. Coop. Federation Ltd v. Singh Consultants & Engineers (P) Ltd**<sup>5</sup>, **Bolivinter Oil SA v. Chase Manhattan Bank**<sup>6</sup>, **Svenska Handelsbanken v. Indian Charge Chrome**<sup>7</sup>. Despite the numerous legal questions posed by the appellants, the Supreme Court noted a crucial fact: the High Court had disposed of the respondent's writ petition with the consent of both parties, through





the issuance of an interim order. The High Court justified its intervention on the ground that allowing the bank guarantee to be encashed would render the respondent's pending Section 9 arbitration petition meaningless. The High Court directed the Commercial Court to adjudicate the petition on its merits, without being influenced by any observations made in its order, and extended the interim protection against the encashment of the bank guarantee until the petition was disposed of, contingent on the respondent extending the guarantee's validity.

The Supreme Court characterized this High Court order as an interim measure intended to safeguard the interests of both parties. The court also took cognizance of the ongoing arbitration proceedings initiated by the respondent, including the constitution of an Arbitral Tribunal.

Given these circumstances, the Supreme Court concluded that maintaining the status quo regarding the bank guarantee was necessary until the Section 9 petition was finally decided. The Supreme Court also acknowledged that the respondent had extended the validity of the bank guarantee, ensuring that the appellants did not suffer any prejudice. Consequently, the court opted not to rule on the broader legal issues raised in the appeal, leaving them open for future determination. The Supreme Court disposed of the appeal, directing the Commercial Court to expedite the proceedings and issue a decision within eight weeks, and ordered that the bank guarantee remain valid and subject to the outcome of the Section 9 arbitration petition.

### **Conclusion and Future Implications**

This judgment, while not definitively resolving the core legal questions surrounding the invocation of bank guarantees in the context of arbitration, provides important practical guidance. The Supreme Court's emphasis on maintaining the status quo, particularly when arbitration proceedings are underway, signals a cautious approach. It underscores the judiciary's inclination to balance the sacrosanct nature of bank guarantees with the need to protect parties genuinely pursuing dispute resolution through arbitration. The decision also highlights the importance of the High Court's role in exercising its supervisory jurisdiction under Article 227 of the Constitution, especially in situations where strict adherence to legal procedure might lead to injustice. The ruling could lead to more parties seeking interim relief in similar situations, potentially influencing how lower courts handle such matters.

However, the deliberate deferral of a conclusive ruling on the substantial legal questions indicates that the debate is far from over. A key question that remains is: To what extent





should courts interfere with the invocation of unconditional bank guarantees when such interference is sought to protect the arbitration process, and what are the precise parameters for determining “irreparable harm” in such cases? Future cases will likely need to address this, further refining the boundaries between judicial intervention and the principles of party autonomy in arbitration.

**Citations**

1. *Jindal Steel And Power Limited V. Bansal Infra Projects Pvt. Ltd. & Others Slp (Civil) No. 21916 of 2024*
2. *Arbitration and Conciliation Act, 1996*
3. *Code of Civil Procedure, 1908*
4. *Hindustan Construction Co. Ltd v. State of Bihar and others(1999) 8 SCC 436*
5. *U.P. Coop. Federation Ltd v. Singh Consultants & Engineers (P) Ltd.(1988) 1 SCC 174*
6. *Bolivinter Oil SA v. Chase Manhattan Bank(1984) 1 All ER 351 (CA)*
7. *Svenska Handelsbanken v. Indian Charge Chrome(1994) 1 SCC 502*

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