

739/99(F)

**IN THE COURT OF APPEAL OF THE DEMOCRATIC SOCIALIST REPUBLIC
OF SRI LANKA**

J.A.X.Fernando and Company (Pvt) Ltd,
No. 388, Union Place, Colombo 2.

Plaintiff

C.A.Case No:-739/99(F)

D.C.Colombo Case No:-4131/SPL

V.

Hatton National Bank Limited,
No. 481, T.B.Jaya mawatha,
Colombo 10.

Defendant

AND

Hatton National Bank PLC.,
No. 481, T.B.Jaya Mawatha,
Colombo 10.

Defendant-Appellant

V.

J.A.X. Fernando and Company (Pvt) Ltd
No.388, Union Place, Colombo 2.

Plaintiff-Respondent

Before:- H.N.J.Perera, J.

Counsel:-Shammil Petera P.C with Shamil Fernando & D.Perera

For the Defendant-Appellant

Respondent absent and unrepresented.

Argued On:-28.10.2013

Written Submissions:-24.10.2013

Decided On:-04.11.2015

H.N.J.Perera, J.

The plaintiff-respondent instituted action in the District Court of Colombo against the defendant-appellant praying, inter alia, for a declaration that the defendant-appellant is not entitled to debit the plaintiff-respondent's current account No. 18054-01 with equivalent Indian Rs. 1,131,250/-as per defendant's letter of 1st July 1994.

The plaintiff-respondent in its plaint pleaded inter alia that

(a)On or about 1st July 1994, Sri Aravindh Steel (Pvt) Ltd of Trichy, India opened a Letter of Credit No.092/9/94-95 for supply of 250 tons of Heavy Metal Scraps.

(b)the plaintiff-respondent on 6th July 1984 loaded the said goods on county craft bearing No.TTN 195 which was named Maria Anthony Clayton Raj.

(c)the plaintiff-respondent presented documents to the defendant-appellant and obtained a sum of Sri Lanka Rupees equivalent to Indian Rs. 1,131,250/-.

(d)on or about 15th July 1984, the plaintiff-respondent was informed by the defendant-appellant that the said buyer was refusing to accept

the documents pertaining to shipment on the basis that there are discrepancies in compliance with the conditions of Letter of Credit.

(e) the defendant-appellant subsequently informed the plaintiff-respondent that its current account would be debited with a sum equivalent to Indian Rs. 1,131,250/-

The defendant-appellant filed answer and stated inter alia that

(a) due to discrepancies in compliance in the Letter of Credit, the Indian Overseas Bank who issued the Letter of Credit, refused to pay the sum referred to in the Letter of Credit.

(b) the plaintiff-respondent failed to tender a Certificate to the Beneficiary, under clause in the Letter of Credit.

(c) the defendant-appellant paid a sum of Rs. 1,709,658/12 to the plaintiff-respondent when the said document tendered to the defendant-appellant to be forwarded to the Indian Overseas Bank, since the plaintiff-respondent issued a Letter of Indemnity marked 'E' and whereby promised to repay the defendant-appellant Bank, on demand, the value of the Bill of Exchange which was paid to the plaintiff-respondent, notwithstanding the discrepancies.

In the circumstances, the plaintiff-respondent is obliged to repay the said sum of Rs.1,709,658/12 to the defendant-appellant under the said Letter of Indemnity signed by the plaintiff-respondent.

The defendant-appellant claimed following in reconvention against the plaintiff-respondent.

- a. A sum of Rs. 420,000/- being the balance due on a sum of Rs. 627,000/- lent and advanced to the plaintiff-respondent
- b. A sum of Rs. 371,000/- being the balance due on a sum of Rs.1.621,000/-lent and advanced to the plaintiff-respondent

- c. A sum of Rs.1,079,000/-being the sum lent and advanced to the plaintiff-respondent
- d. Alternatively , the defendant-appellant claimed the sum of Rs. 1,709,000/-on the said Letter of Indemnity marked as V7 signed by the plaintiff-respondent

At the trial the plaintiff-respondent led the evidence of two witnesses, the defendant-appellant did not call any witness to give evidence and learned trial judge on 20th May 1999 entered judgment in favour of the plaintiff-respondent and dismissed all the claims in reconvension of the defendant-appellant. The learned trial Judge has held that the defendant-appellant is estopped from claiming the payment made by them to the plaintiff-respondent on the basis that there were discrepancies on the part of the defendant-appellant in complying with the terms and conditions of the Letter of Credit. Aggrieved by the said judgment of the learned trial Judge the defendant-appellant had preferred this appeal to this court.

In the instant case the witness of the plaintiff-respondent had admitted that once the documents were handed over by them to the defendant-appellant, thereafter the said documents were examined and the payment had been made by the defendant-appellant to the said plaintiff-respondent. The said witness had admitted the following documents had been tendered by them to the defendant-appellant for the purposes of negotiating the aforesaid Letter of credit marked P1.

1. Document marked as P2 which is the Certificate issued by the Sri Lanka National Chamber of Commerce.
2. Document marked as P3, which is the Bill of Lading issued by te shipper concerned, and
3. Document marked as P4, which is a telegraph sent by the plaintiff-respondent to the New India Assurance Company giving out the

name of the vessel, the Letter of Credit number, weight of the metal scrap shipped and the value of the goods therein.

The witness of the plaintiff-respondent had admitted under cross examination that they have in fact sent only a telegraph to the New India Assurance Company , whereas they had been required to send in a Certificate to the said Company , in accordance with the terms and conditions of the Letter of Credit marked P1.

In the Letter of Credit marked P1 "Sree Aravindh Steel (Pvt) Ltd Company " has been named as the Applicant/Buyer of the said Letter of credit , the plaintiff-respondent has been named as the Beneficiary/ Seller of the same , the defendant-appellant has been named as the Advising/Nominated Bank of the same, and the Indian Overseas Bank has been named as the Issuing/confirming Bank of the same.

The defendant-appellant had examined all documents handed over by the plaintiff-respondent, and in return accordingly made payment to the said plaintiff-respondent in compliance with the terms and conditions of the Letter of Credit marked P1.

It was the contention of the Counsel for the defendant-appellant that by Letter of Indemnity marked V6 the plaintiff-respondent agreed to refund on demand all payments made by the defendant-appellant to the plaintiff-respondent notwithstanding the discrepancies in the Bill. This position had been admitted by the witness for the plaintiff-respondent whilst giving evidence in court. It was further submitted by the Counsel for the defendant-appellant that the plaintiff-respondent had by special Letter of Indemnity marked as V7, notwithstanding the discrepancies , which were namely, the fact that the on board date being incorrect on the cable copy, and that the beneficiary's certificate with regard to the shipment details sent by cable not being submitted , but instead a copy of the telegraph being submitted , agreed to refund the defendant-

appellant a sum of Rupees equivalent to Indian Rupees 1,131,250/- paid by the defendant-appellant to the plaintiff-respondent. This position too had been admitted by the witness for the plaintiff-respondent in his testimony before court. It is to be noted that the Letter of Indemnity marked V7 is a Special Letter of Indemnity given by the plaintiff-respondent wherein the said plaintiff-respondent had admitted the following discrepancies in conforming with the terms of credit therein, but nevertheless proceeded to give the Appellant the said Special Letter of Indemnity.

- a. "on board date incorrect on cable copy."
- b. Beneficiary's certificate with regards to shipment details sent by cable not submitted. Instead copy telegraph submitted.

On a perusal of the said Special Letter of Indemnity marked V7 the plaintiff-respondent had unconditionally agreed to reimburse the defendant-appellant upon demand, the local currency equivalent of the amount of the said bill or Rupee amount of the said bill. Therefore it is very clearly seen that the plaintiff-respondent had therein expressly agreed that the amount of the claim paid by the defendant-appellant in connection with the bill shall be accepted by the said plaintiff-respondent without equivocation dispute , or delay as correct and just; and that the said plaintiff-respondent had waived all rights to contest the amount or nature of the defendant-appellants claims against the said plaintiff-respondent in respect of the amounts paid by the defendant-appellant under such guarantees or indemnities.

The said witness the Managing Director of the plaintiff-respondent under cross examination had admitted that by the Special Letter of Indemnity marked V7 the plaintiff-respondent therein agreed to refund the defendant-appellant a sum of Sri Lankan Rupees equivalent to

Indian Rupees 1,131,250/- paid by the defendant-appellant notwithstanding the aforementioned discrepancies .

It was contended by the Learned President's Counsel for the defendant-appellant that the defendant-appellant had upon the security of the said Letters of Indemnity marked V6 and V7 , and also upon the security of the Bill of Exchange marked V4, paid a sum of Sri Lankan Rupees equivalent to Indian Rupees 1,131,250/- to the plaintiff-respondent when the plaintiff-respondent had presented the relevant documents to the defendant-appellant. Thereafter on or about the 6th July 1994, the defendant-appellant had proceeded to dispatch the aforesaid negotiated documents by courier to the Issuing Bank in the said transaction, the Indian Overseas Bank, to obtain the payment with regards to the same. In turn the said Indian Overseas Bank had detected a discrepancy in the documents submitted and refused payment upon the same, due to the said discrepancy. Therefore it was submitted that the value of the bill negotiated between the parties had remained to be unpaid. The defendant-appellant had duly issued a Notice of Dishonour, dated 1st September 1994 marked as P15 to the plaintiff-respondent and had brought the said fact to their attention, along with the right of recourse available to the defendant-appellant against the said plaintiff-respondent, and gave notice to the said plaintiff-respondent that the defendant-appellant shall be debiting their account with the Rupee equivalent of the said bill.

In the instant case the plaintiff-respondent has clearly admitted that the defendant-appellant had paid the sum of Sri Lanka Rupees equivalent to Indian Rupees of 1,131,250/- to the said plaintiff-respondent in accordance with the terms of the said Letters of Indemnity marked as V6 and V7.

In Hyderabad Industries Ltd V. Idac Trading (Pvt) Ltd and Two Others (1995) 2 SLR 304 Ranaraja, J observed as follows:-

“...A contract of Indemnity is a contract express or implied, to keep a person who has entered into or who is about to enter into a contract or incur any other liability, indemnified against loss, independent of the question whether a 3rd party person makes default (Halsbury’s Laws of England). The letters of indemnity issued by the 1st respondent to the 2nd respondent as carrier of the cargo guaranteed by the 3rd respondent is independent of the contract between the petitioner and the 1st respondent.

As in the case of an irrevocable or confirmed letter of credit, a letter of indemnity obliges the 3rd respondent bank to pay the 2nd respondent on it irrespective of any dispute between the petitioner and the 1st respondent on the contract regarding the goods. It is an irrevocable obligation with which courts will not interfere with except when there is fraud by one of the parties to the underlying contract and the bank had notice of that fraud. Edward Owen Engineers Ltd V. Barclays Bank International Ltd 1978 1 AER 976. In the instant case there is no prima facie evidence that the 3rd respondent bank was aware of any such fraud. Fraud must be clearly proved...”

The attention of this court has been drawn by the Learned Counsel for the defendant-appellant to the pages 206 and 207 in “Schmitthoffs Export Trade”, 10th edition by Leo D’Arcy, Carole Murray and Barbara Cleave wherein it is stated as follows:-

“...Where the seller tenders non-conforming documents, the advising bank, instead of refusing to accept them, as it is entitled to do, may ask the seller to supply an indemnity and, on the strength of such indemnity, may make the credit available. Sometimes, where the advising bank is not identical with the exporter’s bank, it will ask for an indemnity from

the exporter's bank. This procedure is adopted where there are discrepancies between the documents presented by the exporter and the instructions received by the advising bank, or when documents are presented after the expiry date of the credit and no arrangements have been made for its extension. An indemnity which the seller gives to the advising bank cannot be transferred or extended by that bank to the issuing bank without the seller's consent

The exporter, when giving an indemnity in order to avail himself of the credit, should be aware that the bank may have recourse against him and may hold him liable on the indemnity, he should therefore endeavor to settle the point which has given rise to the discrepancy forthwith by agreement with the overseas buyer."

In the instant case the plaintiff-respondent in paragraph 22 of the plaint has pleaded that it has duly performed the terms and conditions of the contract for the shipment of the 250 metric tons of heavy metal scrap to Sree Aravindth Steels (Pvt) Ltd. The consignee, Sree Aravindth Steels (Pvt) Ltd has failed and neglected to adhere to the terms and conditions of the said shipment by not insuring the said scrap iron. Therefore due to consignee's failure to insure the scrap iron the consignee is wrongfully and illegally refusing to accept the documents in respect of this shipment. The plaintiff-respondent should have settled the said dispute forthwith by agreement with the overseas buyer.

Therefore in the instant case the defendant-appellant has clearly suffered loss whereupon the said Issuing bank, namely the Indian Overseas Bank, had stated that the applicant of the Letter of Credit transaction had refused to accept the said negotiated documents due to the discrepancy detected therein. The value of the bill negotiated by the defendant-appellant has remained to be unpaid up to date.

The evidence led in this case clearly proves that the defendant-appellant had granted the plaintiff-respondent a loan of Rs.627,000/- repayable on or before 26th July 1994, together with interest thereon at the rate of 27%per annum. The witness of the plaintiff-respondent had admitted the above mentioned claim of the defendant-appellant and went on to admit that the sum of Rs.420,000/- was due and payable on the related loan under the 1st claim in reconvention and the plaintiff-respondent had failed to pay the said sum though it had been demanded by the appellant.

The Promissory Notes marked V2 and V3 formed the basis of the defendant-appellant's 2nd and 3rd claims in reconvention in respect of a loan of Rs. 1,621,000/-and of Rs. 1,079,000/- granted to the plaintiff-respondent. The plaintiff-respondent's witness had admitted under cross examination that the said sums were borrowed by the plaintiff-respondent and that a sum of Rs.371,000/- was due and payable under the 2nd claim of reconvention and that he was unable to state whether the other sum of Rs. 1,079,000/- claimed under the 3rd claim in the reconvention although borrowed by the plaintiff-respondent, was repaid or not.

The said witness of the plaintiff-respondent Mr.Fernando also had admitted that the Bill of Exchange marked V4 had been drawn , accepted and signed by the plaintiff-respondent for valuable consideration and that the said Bill had been duly presented by the defendant-appellant to the relevant Indian Overseas Bank ,to obtain payment, and that the payment in turn not been made by the said Indian Overseas Bank, the drawee of the said Bill, and that thereby the plaintiff-respondent had been subsequently informed that this Bill of Exchange marked V4 had been dishonoured by the defendant-appellant by his letter marked P15.

The Learned trial Judge erred in law in holding that there was no demand by the defendant-appellant when the Managing Director expressly admitted that the defendant-appellant demanded the repayment of the monies due under the 1st, 2nd, 3rd claims in Reconvention and demanded the money under the fourth claim in Reconvention by the letter marked P15.

In his judgment the learned trial Judge has held that the defendant-appellant would not be entitled to rely on the said Letters of Indemnity marked V6 and V7. It was contended by the Learned Counsel for the defendant-appellant that the learned trial Judge has taken the quotation from Justice Weeramantry referred to at pages 190 and 191 in "The Law of Contract", Vol.1, out of context. Page 190 is as follows:-

Contracts which charge a person with the debt, default or miscarriage of another are contracts of suretyship or guarantee. By such contracts the surety or guarantor undertakes to discharge the liability of the principal debtor in the event of the principal debtor failing to do so. The only formality required under our law for a contract of suretyship is a writing signed by the party making the same, as required by section 18.

Contracts of guarantee must be distinguished from contracts of indemnity. In a guarantee a promise is made by the guarantor to the creditor which is collateral to the contract already existing between the creditor and the debtor. The obligation of the guarantor is conditional on the failure of the principal debtor to pay. It will thus be seen that in cases of guarantee there are two contracts and three parties.

In cases of indemnity, on the other hand, there is only one contract-the contract between the person indemnifying and the creditor. It is a promise to see that the promisee does not suffer by entering into the transaction. To illustrate the difference- if two persons enter a shop and one buy goods and the other promises the seller "if he does not pay you

I will,” this is a contract of guarantee. If on the other hand he says “let him have the goods- I will pay you,” this is a contract of indemnity. There is only one contract and it is not dependent on the existence of another.”

It is not in dispute in the instant case the defendant-appellant had upon security of the said Letters of Indemnity marked V6 and V7, paid a sum of Sri Lankan Rupees equivalent to Indian Rupees 1,131,250/- to the plaintiff-respondent when the said plaintiff-respondent had presented the relevant documents to the defendant-appellant. (admission No. 3) Thereafter on or about the 6th July 1994 , the defendant-appellant had proceeded to dispatch the said documents by courier to the Issuing Bank in the said transaction., the Indian Overseas Bank, to obtain payment with regards to the same. In turn the Issuing Bank had detected a discrepancy in the documents submitted and refused payment upon the same, due to the said discrepancy. The obligations agreed upon by the plaintiff-respondent in the aforesaid Letters of Indemnity marked V6 and V7 have not been duly performed and discharged by the said plaintiff-respondent.

By Letters of Indemnity marked V6 and V7 the plaintiff-respondent had clearly given an indemnity to the defendant-appellant in respect of the Bills drawn under the Letter of Credit marked P1 in the instant case. The defendant-appellant had upon the security of the said Letters of Indemnity marked V6 & V7 and also upon the security of the Bill of Exchange marked V4 had paid a sum of Sri Lankan Rupees equivalent to Indian Rupees 1,131,250/- to the plaintiff-respondent.

The learned District Judge in his judgment has clearly held that the said plaintiff-respondent is liable to pay to the defendant-appellants all the sums claimed in the claim in reconvention. In his judgment he has held that the plaintiff-respondent has accepted clearly that the plaintiff-respondent is liable to pay to the defendant-appellants as set out in the

said defendant-appellants claim in reconvention. Therefore after considering the evidence led in this case I am of the view that the plaintiff-respondent is not entitled to a declaration as prayed for in prayer (a) of the plaint and that the defendant-appellant is entitled to be repaid the said sums of monies due to it and therefore is entitled to a judgment as prayed for in the claim in reconvention in its answer.

For the foregoing reasons I set aside the judgment of the learned District Judge dated 20th May 1999 and dismiss the plaint of the plaintiff-respondent with costs and enter Judgment in favour of the defendant-appellant as prayed for in paragraphs (a), (b), (c), (d) (e) and (f) of the answer.

Appeal allowed.

JUDGE OF THE COURT OF APPEAL