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2021 PLRonline 5107 = (2022-3)207 PLRIJ 018 (Del.) (SN)

High Court Of Delhi
Before: Justice Prateek Jalan.
FROST INTERNATIONAL LIMITED & Ors. - Petitioners
versus
PUNJAB NATIONAL BANK – Respondent.
W.P.(C) 4295/2020 & CM APPL. 15453/2020

(i) Wilful defaulter – Banking - Declaration - Although the allegations against the petitioners have been summarised while enumerating the grounds put up by the Convenor of the Committee - Do not find adequate discussion as to the representation of the petitioners and the reports submitted by them - The minutes of the meeting in the present case contain a recital that the financial statements of the company have been discussed, and that the reasons put up by the Convenor of the Committee are justified, but record conclusion without prescribing any meaningful reasons - Orders of both, the Identification Committee and the Review Committee, must be reasoned orders - In the case of the Identification Committee, this is further necessary because the party concerned has been provided with a domestic remedy of representation before the Review Committee - If the constituent of a bank is inadequately apprised of the reasons which have weighed with the Identification Committee, its opportunity of filing a representation will become meaningless - The provisions of Clause 3 (c) of the Master Circular have been interpreted in *Jah Developers* to be in the nature of a full appeal on facts and law for which purpose, the party against whom the order is passed, is given an opportunity of making a representation.

(ii) Wilful defaulter – Banking - Declaration – Order of the Review Committee being unreasoned - The recital of conclusions does not substitute for an expression of reasons The least that is expected of the Review Committee is to consider, howsoever briefly, the representations made by the petitioners against the order of the Screening Committee and to give its reasons for rejection of the representation - This order is wholly unsatisfactory to meet the requirements of natural justice - RBI Master Circular on Wilful defaulter.

Mr. Malak Bhatt, Advocate.Mr. Vipin Jai, for the parties

JUDGMENT

Prateek Jalan, J. (Oral) - *(13th July, 2021)* - The proceedings in the matter have been conducted through video conferencing.

1. The petitioners assail an order dated 30.03.2020, passed by the respondent-Punjab National Bank ["the Bank"], by which the petitioners have been declared as 'wilful defaulters' under the Master Circular issued by the Reserve Bank of India ["RBI"] dated 01.07.2015.

Facts

2. The Bank issued a show cause notice to the petitioners in this regard on 19.07.2019. The petitioners responded to the show cause notice by a communication dated 24.07.2019. The Screening Committee (stated to be constituted under Clause 3 (a) of the Master Circular) held two meetings on 14.10.2019 and 14.11.2019, at which the petitioners were permitted to present their case.

3. It appears that at the meeting on 14.11.2019, the Screening Committee decided to declare the petitioners as wilful defaulters. However, this was communicated to the petitioners only on 31.01.2020. The communication dated 31.01.2020 stated as follows:-

> "With regard to the subject we inform you that your matter along with show cause notice and all other records along with your representation, if any, and record of hearing / proceeding was placed in the meeting of the Screening Committee held on 14.11.2019 and after giving careful consideration on the matter and perusal of record, it was ob-

[Para 12, 13]

served that incidence of wilful default is apparent on the face of the record and the above account is eligible to be identified as Wilful Defaulter. In view of the above the Committee decided that the matter be placed before the Review Committee of The Board on Non Coperative Borrower and Wilful Defaulters to declare you as Wilful Defaulter. As such, the matter was placed before the Review Committee of the Board on Wilful Defaulters and Non Co operative Borrowers on 17.12.2019. The Committee has decided in terms of Hon'ble Supreme Court decision in State Bank of India vs Jah Developers Pvt. Ltd on 08.05.2019 to give final opportunity to submit written submission on the subject matter.

In view of above, we inform you may submit, if deem fit, a written submission within 15 days from the date of this letter. So submitted written submission, if any, received by us with in the stipulated time as above will be placed before the Review Committee of the Board on Wilful Defaulters and Non Co operative Borrowers in its next meeting for their consideration and final decision. Please note no further opportunity shall be provided to you for this purpose and if we do not receive any written submission within the stipulated time the Review Committee of the Board on Wilful Defaulters and Non Co operative Borrowers will decide the matter on the merit on the basis of record available with the Bank. If may also be noted that no personal hearing shall be afforded before the Review Committee of the Board on Wilful Defaulters and Non Co operative Borrowers and only written submission will be accepted."

4. Pursuant to the aforesaid communication, the petitioners filed a representation dated 18.02.2020 before the Review Committee, constituted under Clause 3 (c) of the Master Circular of the RBI. The Review Committee, at its meeting on 19.03.2020, rejected the petitioners' representation and confirmed the decision of the Screening Committee. This has been communicated to the petitioners by the impugned order dated 30.03.2021, which, according to the petitioners, was received on 25.06.2020.

Submissions

5. Mr. Malak Bhatt, learned counsel for the petitioners, submits that the aforesaid procedure undertaken by the Bank is wholly contrary to the procedure contemplated by the Master Circular and elaborated by the Supreme Court in **State Bank of India v. Jah Developers Private limited and Others** (2019) 6 SCC 787. He makes the following submissions in support of this contention:-

(a) Mr. Bhatt submits that the order of the Identification Committee as incorporated in the minutes of its meeting dated 14.11.2019, is devoid of reasons, inasmuch as the petitioners' representation dated 24.07.2019 has not been dealt with at all.

(b) Mr. Bhatt points out that the minutes dated 14.11.2019, were not communicated to the petitioners until 31.01.2020. It appears from the communication dated 31.01.2020 itself that, even prior to communicating the order to the petitioners, the matter was placed before the Review Committee. The Review Committee then decided to give the petitioners an opportunity of making their submissions in terms of the decision in Jah Developers (supra). According to Mr. Bhatt, the practice of placing the matter before the Review Committee prior to communication to the petitioners was itself not in accordance with the Master Circular and shows that the Review Committee had pre-judged the matter.

(c) Mr. Bhatt further submits that the Review Committee has also passed an unreasoned order.

6. Mr. Vipin Jai, learned counsel for the Bank, on the other hand, submits that the minutes dated 14.11.2019 and the Review Committee's order dated 30.03.2020, disclose adequate reasons for rejection of the petitioners' case. It is Mr. Jai's submission that the procedure contemplated by the Master Circular, as interpreted by the Supreme Court in Jah Developers, has been scrupulously followed in the present case.

Analysis

7. Before adverting to the facts of the case, the provisions of the Master Circular in this regard may be noticed, which are as follows:-

"3. Mechanism for identification of Wilful Defaulters The mechanism referred to in paragraph 2.5 above should generally include the following:

(a) The evidence of wilful default on the part of the borrowing company and its promoter whole-time director at the relevant time should be examined by a Committee headed by an Executive Director or equivalent and consisting of two other senior officers of the rank of GM / DGM.

(b) If the Committee concludes that an event of wilful default has occurred, it shall issue a Show Cause Notice to the concerned borrower and the promoter / whole time director and call for their submissions and after considering their submissions issue an order recording the fact of wilful default and the reasons for the same. An opportunity should be given to the borrower and the promoter / whole-time director for a personal hearing if the Committee feels such an opportunity is necessary.

(c) The Order of the Committee should be reviewed by another Committee headed by the Chairman / Chairman & Managing Director or the Managing Director & Chief Executive Officer/CEOs and consisting, in addition, to two independent directors / non-executive directors of the bank and the Order shall become final only after it is confirmed by the said Review Committee. However, if the Identification Committee does not pass an Order declaring a borrower as a wilful defaulter, then the Review Committee need not be set up to review such decisions."

8. The Master Circular was interpreted by the Supreme Court inter alia in **Jah Developers,** wherein the Court incorporated the Rules of Natural Justice into the procedure. The relevant observations of the Court are reproduced below:-

"24. Given the above conspectus of case law, we are of the view that there is no right to be represented by a lawyer in the in-house proceedings contained in Para 3 of the Revised Circular dated 1-7-2015, as it is clear that the events of wilful default as mentioned in Para 2.1.3 would only relate to the individual facts of each case. What has typically to be discovered is whether a unit has defaulted in making its payment obligations even when it has the capacity to honour the said obligations; or that it has borrowed funds which are diverted for other purposes, or siphoned off funds so that the funds have not been utilised for the specific purpose for which the finance was made available. Whether a default is intentional, deliberate, and calculated is again a question of fact which the lender may put to the borrower in a show-cause notice to elicit the borrower's submissions on the same. However, we are of the view that Article 19(1)(g) is attracted in the facts of the present case as the moment a person is declared to be a wilful defaulter, the impact on its fundamental right to carry on business is direct and immediate. This is for the reason that no additional facilities can be granted by any bank/financial institutions, and entrepreneurs/promoters would be barred from institutional finance for five years.

Banks/financial institutions can even change the management of the wilful defaulter, and a promoter/director of a wilful defaulter cannot be made promoter or director of any other borrower company. Equally, under Section 29-A of the Insolvency and Bankruptcy Code, 2016, a wilful defaulter cannot even apply to be a resolution applicant. Given these drastic consequences, it is clear that the Revised Circular, being in public interest, must be construed reasonably. This being so, and given the fact that Para 3 of the Master Circular dated 1-7-2013 permitted the borrower to make a representation within 15 days of the preliminary decision of the First Committee, we are of the view that first and foremost, the Committee comprising of the Executive Director and two other senior officials, being the First Committee, after following Para 3(b) of the Revised Circular dated 1-7-2015, must give its order to the borrower as soon as it is made. The borrower can then represent against such order within a period of 15 days to the Review Committee. Such written representation can be a full representation on

facts and law (if any). The Review Committee must then pass a reasoned order on such representation which must then be served on the borrower. Given the fact that the earlier Master Circular dated 1-7-2013 itself considered such steps to be reasonable, we incorporate all these steps into the Revised Circular dated 1-7-2015...."

(Emphasis supplied.)

9. Applying these principles to the facts of the present case, it appears that in the show cause notice dated 19.07.2019, the Bank raised various factual grounds in support of its proposal to declare the petitioners as wilful defaulters including inter alia, allegations regarding diversion of funds and related party merchant trade transactions. The reply of the petitioners dated 24.07.2019 included the petitioners' contention with respect to the Forensic Audit Report relied upon by the Bank. The petitioners also made submissions with regard to a detailed fact finding exercise conducted at their instance by Price Waterhouse Coopers.

10. The minutes of the meeting of the Screening Committee dated 14.11.2019, record the following conclusions:-

"Moving forward, the convener of the committee has put up the proposal for declaring the borrower as Wilful Defaulter on following submitted grounds: Ø After examining financial papers, statements and record, it is observed that the FIL has rigorously misused the Bank's fund by granting unsecured loans to parties with whom they had no business relations and the same was given without entering into any agreement. As such, the Company has not used the bank's fund for the purpose it was sanctioned but diverted the funds for other purposes. Ø The unit has defaulted in meeting its payment / repayment obligations to the lender and has siphoned off the funds so that the funds have not been utilised for the specific purpose for which finance was availed of, nor are the funds available with the unit in the form of other assets. Ø It is also informed by the borrower that a writ petition filed by them which is pending for disposal. On inquiry it is informed that no stay / restrain order is passed by the Hon'ble High Court, Delhi till date. After looking into the facts, it is decided that in the absence of any stay / restrain order, the matter heard and decided on merit.

After discussion the financial statements of the company during the meeting, it was observed that the facts and documents presented by the convener of the Committee for declaring the borrower as wilful defaulter are based on justified reasons. The borrower has not utilized the finance availed from the lender for the specific purposes for which finance was sanctioned but has diverted the funds for some other purposes.

After deliberating the above facts the committee opined that the criteria for declaring the borrower as Wilful Defaulter as perscribed by the RBI are met with, therefore, the borrower may be identified as Wilful Defaulter. In view of the above the Committee decided to place the matter before the Review Committee of the Board on Wilful Defaulters and Non Co operative Borrowers for their necessary consideration and deliberation for declaring the borrower as Wilful Defaulter.

Simultaneously, the borrower be supplied with the copy of this order under the signature of the Dy. General Manager R&L with a information that they can make, it deem fit, written submission to be placed before the Review Committee of the Board on Non Co-operative Borrower and Wilful Defaulters within 15 days of the letter, Failing which the Bank will inform the Credit Information Companies after above stipulated time."

11. Although the allegations against the petitioners have been summarised while enumerating the grounds put up by the Convenor of the Committee, I do not find adequate discussion as to the representation of the petitioners and the reports submitted by them. The extract of the Supreme Court's judgment in Jah Developers quoted above clarifies the scope of consideration required before classifying a party as a wilful defaulter. The minutes of the meeting in the present case contain a recital that the financial statements of the company have been dis-

cussed, and that the reasons put up by the Convenor of the Committee are justified, but record conclusion without prescribing any meaningful reasons. The Supreme Court in Jah Developers has made it clear that the orders of both, the Identification Committee and the Review Committee, must be reasoned orders. In the case of the Identification Committee, this is further necessary because the party concerned has been provided with a domestic remedy of representation before the Review Committee. If the constituent of a bank is inadequately apprised of the reasons which have weighed with the Identification Committee, its opportunity of filing a representation will become meaningless.

12. The second ground urged by Mr. Bhatt, with regard to the matter having been placed before the Review Committee prior to the order being communicated to the petitioners, is however, in my view, insubstantial in the facts of this case. It is evident from the letter dated 31.01.2020 extracted above, that the matter was placed before the Review Committee which decided to call for a representation from the petitioners. The provisions of Clause 3 (c) of the Master Circular have been interpreted in Jah Developers to be in the nature of a full appeal on facts and law for which purpose, the party against whom the order is passed, is given an opportunity of making a representation. It is evident that the Review Committee did not proceed to decide the petitioners' case prior to the representation having been sought. Mere placing of file before the Review Committee at that stage was therefore of no prejudice to the petitioners.

13. Mr. Bhatt's third submission, with regard to the order of the Review Committee being unreasoned, is however, justified. The order of the Review Committee reprises the course of the proceedings and then proceeds to record its conclusion in the following terms:-

> "In response to our letter dated 30.01.2020, we have received written Representation from Mr Uday Jayant Desai (HUF), M/s N.S.D Nirman Pvt. Ltd., Mr Nipum Verma, Mr Sunil Verma (HUF), Ms Poonam Vadera, M/s R.S. Builders Pvt. Ltd., the Borrower Company, Comet Overseas Pvt. Ltd., Mr Saral Verma, M/s Globiz Exim Pvt. Ltd., Ms. Sanjana U Desai, Ms Reeta Verma, Ms Neelima U Desai.
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> Thereafter, the Review Committee of the Board on Non- Cooperative Borrowers and Willful Defaulters in its meeting held on 19.03.2020 has reviewed the orders of the Screening Committee and perused records of the matter and written representation submitted by Mr Uday Jayant Desai (HUF), M/s N.S.D Nirman Pvt. Ltd., Mr Nipum Verma, Mr Sunil Verma (HUF), Ms Poonam Vadera, M/s R.S. Builders Pvt. Ltd., the Borrower Company, Comet Overseas Pvt. Ltd., Mr Saral Verma, M/s Globiz Exim Pvt. Ltd., Ms Sanjana U Desai, Ms Reeta Verma, Ms Neelima U Desai. Thereafter considering all the above papers, the Review committee has approved your Name/Account for declaration as willful defaulter.
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> Accordingly your name is being reported as willful defaulter to the Credit Information Companies. Further, in the course photographs of the borrower / guarantor / mortgaged of account will be published in news papers in accordance with the policy of the Bank, which please be noted."

14. This order is wholly unsatisfactory to meet the requirements of natural justice, as elucidated in the judgment of the Supreme Court in Jah Developers. The recital of conclusions does not substitute for an expression of reasons. The least that is expected of the Review Committee is to consider, howsoever briefly, the representations made by the petitioners against the order of the Screening Committee and to give its reasons for rejection of the representation.

15. For the reasons aforesaid, the petitioner has made out a good case for setting aside of the orders of the Screening Committee and the Review Committee and a direction to the Bank to decide the case afresh.

Conclusion

16. In the facts and circumstances aforesaid, the petition is allowed, and the impugned actions of the Screening Committee and Review Committee of the Bank under the Master Circular are set aside.

17. The matter is remanded to the Screening Committee for a fresh decision in accordance with law. The Screening Committee may seek a further representation, written or oral, from the petitioners, if it considers it necessary. The Screening Committee is also at liberty to proceed on a consideration of the petitioners' reply dated 24.07.2019 to the show cause notice, and the submissions made by the petitioners at the hearings which were accorded to them.

18. After the Screening Committee passes a fresh reasoned order, it will be communicated to the petitioners, and the petitioners will be given a period of 15 days to make their representations against the said orders to the Review Committee, if necessary. The Review Committee will thereafter, consider petitioners' representation and proceed in accordance with law.

19. The writ petition, alongwith pending application, stands disposed of in these terms. There will be no order as to costs

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