

01
18.09.2020
Sc/pg.

IN THE HIGH COURT AT CALCUTTA
CIVIL APPELLATE JURISDICTION
APPELLATE SIDE

FMA 906 of 2020
(MAT 494 of 2020)
with
IA No. CAN 3 of 2020
(CAN 4730 of 2020)

Axis Bank Limited
Vs.
Gaurav Dalmia & Ors.

with
COT 36 of 2020
CAN 1 of 2020
(CAN 5809 of 2020)

Axis Bank Limited
Vs.
Gaurav Dalmia & Ors.

With
FMA 907 of 2020
(MAT 495 of 2020)
with
IA No. CAN 3 of 2020
(CAN 4734 of 2020)

Axis Bank Limited
Vs.
Raghu Hari Dalmia & Ors.

with
COT 35 of 2020
IA No. CAN 1 of 2020
(CAN 5804 of 2020)

Axis Bank Limited
Vs.
Raghu Hari Dalmia & Ors.

Mr. Jayanta Kumar Mitra, Sr. Advocate
Mr. Debnath Ghosh
Mr. Sanjay Ginodia
Mr. S. D. Majumder Advocates
.....For the Appellant

Mr. Jishnu Saha, Sr. Advocate
 Mr. Anirban Roy
 Mr. Jisnu Chowdhury
 Ms. Chandrani Das Advocates
For the Writ Petitioner

Mr. Debdatta Sen
 Ms. S. Chatterjee Ghosh
 Mr. M.K. Seal Advocates
For the Respondent No.2

The appeal arises out of an order passed on two petitions under Article 226 of the Constitution. The common judgment and order was passed on March 18, 2020. The bank which extended credit facilities to a unit that was found to be a wilful defaulter is the common appellant. Two cross-objections have been filed by the writ petitioners.

The matter pertains to the Reserve Bank's Master Circular on wilful default. The latest edition of such Master Circular was published on July 1, 2015. The facts are not much in dispute.

The writ petitioners were promoters of a company by the name of Pro Minerals Pvt. Ltd. (hereafter referred to as "the said company") and the writ petitioners were, in fact, in control of such entity. Appellant Axis Bank granted credit facilities to the said company in 2012 and later discovered that the funds made available to the said company had been diverted by its promoters for purposes other than for which the credit facilities had been accorded. In due course, show-cause notices

followed and proceedings were held in terms of the Master Circular of 2015 for the adjudication as to whether the relevant lending unit and its promoters were wilful defaulters within the meaning of the expression used in the relevant Master Circular.

For the present purpose, it may only be said that the ultimate finding as to the said company and its promoters being wilful defaulters has attained finality. A Division Bench order of this Court, confirming the finding of wilful default, was carried by way of a Special Leave Petition to the Supreme Court. By such time, however, the said company was sold to new promoters in insolvency proceedings before the National Company Law Tribunal. In such situation, the order of the Supreme Court of May 8, 2019, passed at the admission stage of the petition for special leave to appeal, records as follows :-

“The petitioners state that the assets of the company have since been sold in liquidation of the companies debts. The petitioners wish to make a representation to the Review Committee of the Axis Bank as to whether, in the light of these subsequent events, they should be continued to be classified as wilful defaulter. Such representation will be made within two weeks from today. The Review Committee under the Master Circular dated 01.07.2015 of the Reserve Bank of India, will then decide the said representation and give its reasons in accordance with our judgment delivered today, on 8th May, 2019, in Civil Appeal No.4776 of 2019.”

The principal parties here agree that the liquidation referred to in the Supreme Court order,

in fact, pertains to the insolvency proceedings before the NCLT. The parties also agree that the Review Committee was of Axis Bank and not of Reserve Bank.

Pursuant to the leave granted by the Supreme Court as evident from the said order of May 8, 2019, the writ petitioners approached the Review Committee of Axis Bank and sought to reopen the entire matter, including the previous finding as to the petitioners being wilful defaulters. Quite appropriately, the Review Committee did not permit the matters which had attained finality to be re-agitated; but only went into the subsequent event of the unit having been sold and the consequence thereof. The Review Committee opined that notwithstanding the unit being sold, the writ petitioners continued to be regarded as wilful defaulters in terms of the relevant Master Circular of July 1, 2015.

It was such decision of the Review Committee passed on October 25, 2019 which was challenged before this Court in proceedings under Article 226 of the Constitution that culminated in the order under appeal. The Single Bench upheld the first part of the order of the Review Committee not allowing matters which had been concluded between the parties to be

reopened. However, the Single Bench was of the opinion that since the loans had been obtained in connection with the affairs of Pro Minerals Private Limited and the writ petitioners had been divested of their control over and association with such company, the writ petitioners ceased to be wilful defaulters any further. It is such view of the Single Bench which is challenged in the appeals. The cross-objections are limited to the Single Bench accepting the Review Committee's decision to not allow the past and concluded transactions to be reopened.

In all fairness, the writ petitioners have not laboured much over the Review Committee's decision to not allow the concluded matters to be reopened. In any event, in view of the limited scope of the adjudication allowed by the Supreme Court order of May 8, 2019 and such order not setting aside the judgment and order that was challenged before the Supreme Court, the writ petitioners virtually accept that the only relevant consideration before the Review Committee of Axis Bank was whether the subsequent event of the lending unit having been sold in insolvency proceedings absolved the promoters of the lender company of the wilful default stigma under the relevant Master Circular.

The Master Circular of 2015 is somewhat of a departure from the immediate previous circular of July

1, 2014. However, for the present purpose, the most important clause appears to be sub-clause (a) of clause 2.5 of the 2015 Master Circular:-

“2.5 Penal Measures

The following measures should be initiated by the banks and FIs against the wilful defaulters identified as per the definition indicated at paragraph 2.1.3 above:

a. No additional facilities should be granted by any bank/FI to the listed wilful defaulters. In addition, such companies (including their entrepreneurs/promoters) where banks/FIs have identified siphoning/diversion of funds, misrepresentation, falsification of accounts and fraudulent transactions should be debarred from institutional finance from the scheduled commercial banks, Financial Institutions, NBFCs, for floating new ventures for a period of 5 years from the date of removal of their name from the list of wilful defaulters as published/disseminated by RBI/CICs.

b. ...”

On a meaningful reading of the relevant Master Circular, it is evident that any juristic entity can be labelled as a wilful defaulter though the *mens rea* element of the wilfulness of the default has, per force, to fasten onto some human agency. In other words, the human agencies in control of an inanimate juristic entity have to be found guilty of wilful default within the meaning of such expression as used in the Master Circular for the penal measures to attach to the juristic entity in default and also to the human agencies found responsible for the wilful default.

There could be myriad situations covered by the Master Circular and the finding of wilful default. There could be a case where credit facilities were granted without any securities being obtained or personal guarantees being sought. In such a case, even though the human agencies responsible for the actions of the inanimate juristic entity may be found to be in wilful default along with the juristic entity, that is, the borrower, no independent financial obligation would fasten to the human agencies since they may not have extended any guarantee or created any mortgage of their personal properties. There could be other situations where the human agencies found to be in wilful default may also be guarantors or may be mortgagors. In such a scenario, the human agencies found to be in wilful default would wear the badge of wilful defaulters and also carry the burden of the financial obligation to ensure repayment.

In the present case, the human agencies found to be in wilful default had neither executed any personal guarantee nor had furnished any property by way of security or mortgage.

It must be understood that the more important word in the expression “wilful default” is “default”. If there is no default in repayment, the question of any adjudication of any act being wilful or otherwise would

not arise. It is possible, say, that money lent for a particular purpose was diverted for use otherwise and the promoters promptly repay the lender. In such an event, the lender would not be required to go into the question as to whether there was any diversion of funds since the money was returned and there is no default. Thus, the entire purpose of the Master Circular and the larger goal that it seeks to achieve is to identify defaulters and such defaulters who have wilfully defaulted, where wilful default includes diversion of funds, not paying despite having the ability, siphoning off of funds and the like.

When an inanimate juristic entity like a company is found to be in wilful default within the meaning of the relevant expression in the Master Circular, the human agencies in control of such company and who may have caused the wilful default may also be branded as wilful defaulters along with the borrower company. As long as the human wilful defaulters continue to be associated with the borrower company and the repayment has not taken place, such human agencies continue as wilful defaulters along with the borrower. It is possible that the promoter wilful defaulters (the human agencies found guilty of diversion of funds or siphoning off thereof or the like) may voluntarily sell off their stake in the borrower company. In such a situation, such human agencies continue as wilful defaulters till the

debt due to the lender is discharged; whereupon, they qualify to have their names removed from the list of wilful defaulters. This would govern a situation where the human agencies identified as wilful defaulters have no personal obligation to repay the lender other than to cause the borrower to make such repayment. The situation is entirely different if the promoters are required under any law or by any authority on the basis of any law in force to divest their shares in the borrower company. In such a situation, when the human wilful defaulters no longer exercise any control over the wilful defaulter company and also have no personal obligation to the lender, such human wilful defaulters cease to be wilful defaulters upon being divested of their shares in and their control over the wilful defaulter company. This is because such human agencies can no longer cause the wilful defaulter company to make the repayment; and, their names are liable to be taken off the list of wilful defaulters maintained by the credit companies and monitored by the Reserve Bank.

As it transpires in the present case, the relevant company, Pro Minerals, was referred to NCLT under the Insolvency and Bankruptcy Code, 2016. In course of the proceedings before such tribunal, the company changed hands and the final resolution was approved. Such resolution was approved on or about February 22, 2019. In terms of the resolution, Axis Bank has received

the money that was due to it from Pro Minerals, albeit a lesser amount than what was due, in terms of the scheme which provided for a haircut for all creditors. Thus, as on date, there is no default on the part of Pro Minerals in respect of the relevant transaction, though it is the undeniable position that the money lent for a particular purpose had once been diverted for some other purpose by the then promoters of Pro Minerals.

The writ petitions were instituted late in 2019 upon the names of the human agencies who had caused the wilful default on the part of Pro Minerals not being removed from the list of wilful defaulters. The appellant herein opposed the writ petitions before the Single Bench and says that once a wilful defaulter, the person continues to be a wilful defaulter. Axis Bank is also quick to point out that the default in this case was not made good by the writ petitioners but by a third party on behalf of Pro Minerals in terms of the resolution as approved by the tribunal. The underlying submission of Axis Bank appears to be that persons who are found guilty of siphoning off funds or diversion of funds or not paying despite having the ability to repay should not qualify to obtain future credit facilities from other banks or financial institutions in view of their deplorable conduct. However, at the same time, Axis Bank, in all fairness, points out to the limitation of

the penal measures that can be taken under the Master Circular.

The Master Circular is somewhat unhappily worded as to how the name of a wilful defaulter ought to be removed upon such name being appropriately once included in the list. In other words, once a person is appropriately condemned, the Master Circular does not adequately indicate how the person may make good the loss that he may have brought about and not carry the stigma for any longer than necessary.

The relevant sub-clause under the heading “penal measures” can be seen to be in two parts. The first part is covered by the first sentence. The prohibition envisaged in the first sentence is co-terminus with the name of the wilful defaulter being removed from the list. However, the second part of the penalty in the rest of the sub-clause, in essence, prohibits a wilful defaulter from setting up any new commercial enterprise with the aid of finance made available by FIs or NBFCs or scheduled banks. The second limb of the penalty continues for a period of five years after the name is removed from the list of wilful defaulters; and, thereafter no other prohibition applies.

There is also the stigma which attaches to a person or an entity having been found to be a wilful defaulter. Whether or not the name of the wilful

defaulter is removed from the list or the default is made good, the fact that a person was once found to be a wilful defaulter would weigh with future lenders approached by such person for credit facilities. It is quite like a one-time smoker being liable to pay more premium for insurance policies despite kicking the habit. It is also akin to a convict wearing a badge of disqualification in certain cases for the rest of his life after having served out the period of punishment.

In the present case, since no personal guarantee was furnished by any of the writ petitioners, the moment the money due to Axis Bank was paid in full or was agreed to be received by way of a compromise, the writ petitioners stood rid of their burden as wilful defaulters and their names were liable to be removed from the relevant list. If, however, the writ petitioners continued in their capacity as guarantors in respect of the relevant transactions, the writ petitioners would have continued to be liable till the entire debt was discharged. But as the writ petitioners did not have any personal liability, the moment the resolution was approved and Axis Bank received the payment or is deemed to have received the payment, the names of the petitioners ought to have been taken off the list of wilful defaulters. As a consequence, the moment the writ petitioners were entitled to have their names removed from the list, the first sentence in the relevant sub-

clause would not apply. In other words, the writ petitioners qualified to obtain additional credit facilities from banks and financial institutions. However, the second limb of the prohibition under clause 2.5(a) continued and still continues.

Since the resolution was given effect to on February 22, 2019, it is reasonable to expect that the writ petitioners' names should have been removed from the list of wilful defaulters by the end of that month. Thus, the writ petitioners' names would be deemed to have been removed from the list of wilful defaulters with effect from March 1, 2019. With effect from March 1, 2019, there is no embargo on the writ petitioners obtaining additional credit facilities from banks and financial institutions. However, the embargo in terms of the second limb of clause 25(a) of the Master Circular will apply to the writ petitioners for a period of five years from February 28, 2019.

Though the Reserve Bank has appeared at a belated stage, it has appropriately indicated the position in terms of its Master Circular of July 1, 2015. Accordingly, the Reserve Bank should take immediate steps to ensure that the names of the writ petitioners are removed from the list of wilful defaulters and the deletion will take effect from February 28, 2019.

In view of the above, the appeals are disposed of by modifying the order under appeal as indicated above.

FMA 906 of 2020 (MAT 494 of 2020) with IA No: CAN 3 of 2020 (CAN 4730 of 2020), FMA 907 of 2020 (MAT 495 of 2020) with IA No: CAN 3 of 2020 (CAN 4734 of 2020), COT 36 of 2020 with IA No: CAN 1 of 2020 (CAN 5809 of 2020) and COT 35 of 2020 with IA No: CAN 1 of 2020 (CAN 5804 of 2020) are disposed of.

There will be no order as to costs.

(Sanjib Banerjee, J.)

(Aniruddha Roy, J.)