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* IN THE HIGH COURT OF DELHI AT NEW DELHI

Date of Decision: 13th May, 2021

+ **W.P.(C) 5309/2021 with CM APPLs. 16327-16329/2021**

SHANTANU PRAKASH

..... Petitioner

versus

UNION BANK OF INDIA & ORS.

..... Respondents

+ **W.P.(C) 5313/2021 with CM APPLs. 16351-16353/2021**

JAGDISH PRAKASH

..... Petitioner

versus

UNION BANK OF INDIA & ORS.

..... Respondents

Present: Mr. Dayan Krishnan, Sr. Adv. with Mr. Aditya Dewan &
Mr. Siddharth Chechani, Advocates for the petitioners.

Mr. O.P. Gaggar, Advocate for the Respondent-Bank.

CORAM:

HON'BLE MR. JUSTICE PRATEEK JALAN

PRATEEK JALAN, J. (ORAL)

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The proceedings in the matter have been conducted through
video conferencing.

CM APPLs. 16328-16329/2021 (exemption) in W.P.(C) 5309/2021

CM APPLs. 16352-16353/2021 (exemption) in W.P.(C) 5313/2021

Exemptions allowed, subject to all just exceptions.

The applications are disposed of.

W.P.(C) 5309/2021 with CM APPLs. 16327/2021 (interim relief)
W.P.(C) 5313/2021 with CM APPLs. 16351/2021 (interim relief)

1. Issue notice. Mr. O.P. Gaggar, learned counsel for respondent no. 1-Union Bank of India [“the Bank”], accepts notice. In view of the order which I propose to pass, it is not necessary to issue notice to the other respondents. The petitions are taken up for disposal with the consent of learned counsel for the parties.

2. These proceedings arise out of actions taken by the Bank against the petitioners under the Master Circular on Wilful Defaulters dated 01.07.2015 [“the Master Circular”], issued by the Reserve Bank of India. The petitioners have challenged a show cause notice dated 22.10.2020 issued to them, the order of the Identification Committee dated 04.02.2021, and the order of the Review Committee dated 06.04.2021. [The terms “Identification Committee” and “Review Committee” refer to the committees constituted under Clauses 3(b) and 3(c) of the Master Circular, respectively.]

A. Facts

3. The petitioners, Mr. Shantanu Prakash [“SP”] and Mr. Jagdish Prakash [“JP”], were promoter-directors of M/s Educomp Solutions Ltd. [hereinafter, “the Company”], a borrower of the Bank, and guarantors of loans taken by the Company from the Bank. JP claims to have resigned as a director in 2014. It is undisputed that corporate insolvency resolution proceedings have commenced against the Company, and the matter is pending before the National Company Law Tribunal [“NCLT”].

4. In the meanwhile, the Bank issued the impugned show cause notice dated 22.10.2020 to the Company and to the guarantors of the Company's debts, including the petitioners herein. The show cause notice contemplated declaration of the noticees as wilful defaulters in terms of the Master Circular. The petitioners were required to furnish their objections, failing which the Bank intended to take action in terms of the Master Circular.

5. SP responded to the impugned show cause notice by a communication dated 03.12.2020. He requested the Bank to supply him with a copy of the minutes of the Identification Committee meeting dated 07.02.2020, upon which the impugned show cause notice was based, and any other documents which were relied upon in the show cause notice. However, he also responded to the allegations on merits, without prejudice to his rights and contentions. JP, who is the father of SP, claims that he did not receive the impugned show cause notice at all, and therefore did not respond to it. It is undisputed that neither of the petitioners participated in the personal hearing offered to them by the Identification Committee. They have stated that they failed to participate in the hearing *inter alia* due to COVID-19 infection and other medical issues.

6. The Identification Committee, however, considered the issue at a meeting on 22.01.2021, in the absence of the petitioners, and passed an order dated 04.02.2021. It classified the petitioners as 'wilful defaulters' based upon the grounds mentioned in the show cause notice dated 22.10.2020, which were reproduced in its order. The relevant extracts of the impugned order of the Identification

Committee are as follows:

“After careful examination of the facts of the case and the submission from borrower/representative and Bank, the Identification Committee in its meeting held on 22.01.2021 passed the order as under:

The Committee observed that in spite of providing sufficient opportunity of personal hearing, the borrower/ promoters/ whole time directors/ guarantors have failed to appear for personal hearing. Hence, the committee decided to classify them as wilful defaulters based on the grounds mentioned in the show cause notice served to them which are reproduced herein below:-

- The company has provided loans amounting to Rs.3.75 crores to related party M/s Authorgen Technologies Ltd. during January-March 2013 even when it itself was under huge debt. Subsequently, the loan was written off by ESL and Authorgen was sold off.
- The company made investment in subsidiaries/ associate concerns outstanding at Rs.1684.40 crores as on 31.03.2016. Thus, the company diverted lenders' fund by investing in other companies/ subsidiaries.
- Upon review of customer ledger of Edu Smart Services Pvt. Ltd. (ESSPL), it was noted that ESSPL has been one of the largest debtors to ESL for the FY 2015-16 & 2016-17 despite being a related party of ESL.
- It was observed that retail sales amounting to Rs.2.53 cr. was booked without contractual obligations and the company did not receive the payments pertaining to these sales.
- Upon review of financial statements and customer ledger accounts of related parties for the period 31.05.2015 to 30.05.2017, it was noted that a knock-

off entry of Rs. 0.50 crore where ESL's customer viz. ESSPL made a direct payment to ESL's vendor viz. Rational Business Corporation Pvt. Ltd. which resulted in the set off of ESL's debtor with that of operations creditor. ESL was supposed to receive this payment from ESSPL which was directly used to pay Rational Business Corporation. Thus, an operational creditor was made a payment before making payments to outstanding secured creditors. This payment has been categorized under preferential payments.

- *The following transactions have been categorized as a preferential transactions as payments were made prior to making payment to outstanding secured creditors:*
 - ✓ *Payment of Rs.7.00 crores made to a related party Educomp Learning Hour Pvt. Ltd. on behalf of Edu Smart Services Pvt. Ltd. prior to making payments to outstanding secured creditors.*
 - ✓ *Three payment transactions aggregating to Rs.5.10 crores were made during period 31.05.2016 to 30.05.2017 to HP Financial Services Private Limited ("HP Financial") against unsecured loans from HP Financial.*
 - ✓ *Six Payment transactions to SKS Fincap Private Limited (SKS) aggregating to Rs. 1.14 crore were made between 29.06.2016 and 07.03.2017.*

In light of the above facts, the committee is of the view that borrower/ promoters/ whole time directors/ guarantors have indulged in the act of wilful default by diversion/ siphoning off banks' funds.

Hence, the committee concluded that the said borrower/ its promoters/ directors/ guarantors be declared as wilful defaulters.

The Committee directed that the order be served on the borrower/ its promoters/ whole time directors/

guarantors allowing them to file appeal against the order of Identification Committee within 15 days to place the same before Review Committee for final view. Ordered accordingly.”

(Emphasis supplied.)

7. The aforesaid order of the Identification Committee was communicated to the petitioners on 09.02.2021. Both the petitioners approached the Review Committee on 19/20.02.2021. The Review Committee thereafter passed the impugned order dated 06.04.2021, noting that the order of the Identification Committee and the representations made by the noticees were placed before it. The operative portion of the order of the Review Committee reads as follows:

“The said order of Identification Committee and representations made by company/ promoters/ directors/ guarantors were placed before "Review Committee for Non Cooperative Borrowers and Wilful Defaulters" for taking a decision in the matter.

The "Review Committee" in its meeting held on 22.03.2021 considered the entire material brought on record including contentions/ appeal of the borrower/promoters/directors/ guarantors and views of Identification Committee. After careful examination of the facts of the case, the Review Committee observed that there is unimpeachable evidence/s against the promoters/ directors/ guarantors and their act would fall under the purview of RBI guidelines on "Wilful Defaulter".

Hence, the Review Committee confirmed the order passed by Identification Committee on Wilful Defaulters in its meeting held on 22.01.2021, declaring the promoters/

whole time directors/ guarantors (mentioned below) as Wilful Defaulters.”

(Emphasis supplied.)

8. The petitioners have challenged the show cause notice, as well as the orders of the Identification Committee and the Review Committee by way of these writ petitions.

B. Relevant clauses of the Master Circular

9. Clauses 2.5 and 3 of the Master Circular are relevant for adjudication of the disputes raised in these petitions. Clause 2.5 enumerates the penal provisions which would be visited upon an account-holder upon classification as a “wilful defaulter”. It thereafter states as follows:

“It would be imperative on the part of the banks and FIs to put in place a transparent mechanism for the entire process so that the penal provisions are not misused and the scope of such discretionary powers are kept to the barest minimum. It should also be ensured that a solitary or isolated instance is not made the basis for imposing the penal action.”

(Emphasis supplied.)

The requirements of the mechanism referred to in the above provision are elaborated in Clauses 3(a) to 3(c) of the Master Circular in the following terms:

“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.”

C. Submissions of counsel

10. Mr. Dayan Krishnan, learned Senior Counsel for the petitioners, submits that the procedure adopted by the Bank in the present case was in violation of the principles of natural justice and the provisions of the Master Circular. He submits that the documents referred to in the impugned show cause notice dated 22.10.2020 were not supplied

to the petitioners, despite their requests. [The petitioners do not however dispute that the forensic/transaction audit report referred to in the show cause notice was available with them.] He has taken me through the impugned orders of the Identification Committee and the Review Committee to contend that neither committee has considered the representations of the petitioners, nor disclosed the reasons for rejection of their contentions. In support of his arguments, Mr. Krishnan relies upon the judgments of the Supreme Court in *State Bank of India vs. Jah Developers* (2019) 6 SCC 787 and *Indian Commodity Exchange Limited vs. Neptune Overseas Limited & Ors.* (2020) SCC Online SC 967 [Civil Appeal No. 9037/2019, decided on 27.11.2020], and of a coordinate bench of this Court in *Aap Infrastructures Ltd. Vs. Bank of Baroda and Anr.* (2019) 177 DRJ 252.

11. Mr. Gaggar, who appears for the Bank on advance notice, submits that the documents referred to in the show cause notice dated 22.10.2020 are principally the accounts of the Company itself to which the petitioners had access. As such, he submits that there was no occasion to supply the same documents to the petitioners again. He distinguishes the judgment in *Indian Commodity Exchange* (supra) on the ground that the Bank is not undertaking judicial or quasi-judicial proceedings for which adherence to the principles of natural justice, as elucidated in the aforesaid judgment, would be required.

D. Analysis

(i) Infirmities in the impugned orders

12. Having heard learned counsel for the parties, I am of the view

that the matter requires to be remanded to the Bank for reconsideration in view of infirmities in the impugned orders of the two committees. Clause 2.5 of the Master Circular itself emphasises the importance of transparency in the identification of a “defaulter”, and the checks and balances necessary to avoid misuse of discretionary exercise of power. The interpretation of the Master Circular in *Jah Developers* (supra) also underscores the requirements of natural justice in the context of the consequences contemplated upon identification as a “wilful defaulter” under the Master Circular. The following observations of the Court are directly applicable:

“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.)

13. The judgment of this Court in *Aap Infrastructures* (supra) is

also instructive as to the requirement of consideration of the noticees' submissions by the committees constituted under the Master Circular:

“13. Insofar as the plea of Mr. Nandrajog that the petitioner in his reply to show cause has admitted the allegations made against it is concerned, the same is not appealing. This I say so, for two reasons; firstly which has already been noted by me above that the copy of the order passed by the First Committee dated February 20, 2018 has not been given to the petitioner. Secondly, it is clear that both the Committees have neither considered nor dealt with the stand taken by the petitioner in its reply to the show cause notice. The said Committees or at least the Review Committee was required to refer to the reply and dealt with the same while rejecting the reply of the petitioner to the show cause notice. This would have been in compliance of principles of natural justice as reasons would indicate, application of mind, that too what were the relevant considerations for the authorities to reject the reply of the petitioner to the show cause notice.”

(Emphasis supplied.)

The Division Bench decision of this Court in *Indian Oil Corporation Ltd. Vs. SPS Engineering Ltd.* (2006) 128 DLT 417 (paragraph 32) also lays down that an authority is required to deal, at least in brief, with the explanation given in response to a show cause notice.

14. Applying these principles to the facts of the present case, it is clear that both the impugned orders fall short. The order of the Identification Committee dated 04.02.2021 does not reveal any consideration of SP's reply dated 03.12.2020 to the impugned show cause notice. Without prejudice to his request for supply of documents, the representation offered various responses to the allegations made by the Bank. Although the order of the Identification

Committee refers to the submissions of the borrower, it has confirmed the allegations in the show cause notice merely on the basis that the petitioners did not appear for the personal hearing. The judgment in *Aap Infrastructure* (supra) makes it clear that consideration of the noticees' response is necessary. The order of the Identification Committee is, under the Master Circular, subject to review, which is characterized by the Supreme Court in *Jah Developers* as “a full representation on facts and law (if any)”. Such an exercise requires the Identification Committee to give reasons, which are subject to review. A mechanical reproduction of the allegations is, in these circumstances, entirely inadequate.

15. The impugned order of the Review Committee quoted above is similarly laconic. The Review Committee refers to the representations made by the petitioner, but does not record any reasons for coming to the conclusion that there was “*unimpeachable evidence/s against the promoters/ directors/ guarantors and their act would fall under the purview of RBI guidelines on "Wilful Defaulter"*”. That such an order is unacceptable is beyond the pale of doubt in view of the specific observation in *Jah Developers* that the Review Committee must pass a reasoned order. Assertion of the Committee's conclusions cannot substitute for an expression of reasons.

16. For the reasons aforesaid, the impugned orders of the Identification Committee and the Review Committee dated 04.02.2021 and 06.04.2021 respectively are required to be set aside, and the matter remanded to the Bank for a fresh decision in accordance with law.

(ii) Disclosure of documents

17. What remains to be considered is the contention of Mr. Krishnan regarding the supply of documents relied upon in the impugned show cause notice. Clauses 3(a) and (b) of the Master Circular require the Identification Committee to examine the evidence of wilful default on the part of the borrowing company and its promoter/whole-time directors and come to a conclusion as to whether a show cause notice is to be issued. In the present case, the impugned show cause notice reveals that such an exercise was undertaken by the Identification Committee in its meeting on 07.02.2020. The meeting was held on the basis of the recommendation received from “IFB Delhi”. [According to Mr. Gaggar, this refers to the Industrial Finance Branch, Delhi, which was the dealing branch of the Bank.] The allegations against the Company, presumably based on the evidence brought before the Identification Committee, have been set out in the impugned show cause notice.

18. Mr. Krishnan’s contention is that the documents referred to in the show cause notice are required to be supplied to the noticees. For this purpose, he relies upon the following observations in the judgment of the Supreme Court in *Indian Commodity Exchange* (supra):

“32. We have no doubt that a proper show cause notice was served on Respondent No. 2 herein. The moot point, however, remains as to what is the effect of not serving him with the documents he sought for and within the compass of time, which was given to him to respond.

33. Once again, it may be stated that a large part of the documents would have been within the custody of the Respondent No. 2 herein or for that matter with Respondent No. 1 herein. However, this would not encompass all the documents. Not only that, when reliance is placed on as many as 4,000 pages of documents, it would not be fair to expect that the party in question ferrets through its own record trying to locate the documents, when on basis of formation of an opinion for issuance of the show cause notice, logic and requirement of law both would dictate that the show cause notice should be comprehensive enough with full supporting documents being handed over. The answer cannot be that they are free to inspect 4,000 pages on their own! In fact, in so many terms, ultimately most of those documents were made available and it would not be appropriate to go back into the issue of whether the documents should have been supplied or not. In a sense, that chapter closed with the supply of documents on 5.7.2011 even though some more documents were sought thereafter.

34. We fail to appreciate why there should have been a cussedness in handing over mere copies of documents when serious allegations and serious consequences which would flow to the respondents herein. Not only that, the endeavour to conclude the proceedings within a span of two weeks thereafter cannot, in our view, be said to be an adequate opportunity as has been found by the SAT. An opportunity of hearing is not a mere nicety but a valuable right. That it does not fall in a straitjacket formula is no doubt the accepted legal position [Dharampal Satyapal Ltd.]. The question is whether there was substantial compliance of the principles of natural justice

[Chairman, Board of Mining Examination] and whether there were unnecessary adjournments being sought, which were declined [Titaghur Paper Mills Co. Ltd. and Cement Workers Karamchari Sangh]”

19. In view of the fact that the matter is being remanded to the Bank for a fresh consideration of the issue, it is not necessary to conclusively decide this issue at this stage. Suffice it to say that the Bank is required to disclose the documents and evidence which the Identification Committee has relied upon to arrive at the decision to issue the show cause notice. The disclosure must be such as to enable the noticee to appreciate the scope of the allegations made against it and, if the allegations are based upon documents which the Bank states are already in the possession of the noticee, such as its own accounts, to identify the transactions upon which the Bank seeks to rely.

20. The fundamental principle, as laid down by the Supreme Court in *Natwar Singh vs. Director of Enforcement* (2010) 13 SCC 255 (paragraph 30) is that “*nothing should be used against the person which has not been brought to his notice*”. In paragraph 26 of the said judgment, the Court also reiterated the flexible approach to be adopted while considering claims of violation of natural justice. Upon a consideration of the applicable statutory and regulatory scheme, the Court held that the petitioner therein was entitled to the documents relied upon by the authority, but not to other documents in its possession.

21. In the facts of the present case Mr. Gaggar may be correct in

submitting that the Bank will not be required to supply copies of the Company's own accounts to the Company itself. However, at the very least, the transactions based upon which the Bank has arrived at its conclusion must be identifiable from the disclosure. Mr. Krishnan points out that the petitioners in the present case are not the Company itself, which is under the control of a resolution professional, but its erstwhile directors – one who claims to have resigned in 2014 and the other who was a director until the Company went under the resolution process.

22. Mr. Gaggar's submission regarding the distinction between an administrative decision and a quasi-judicial/ judicial decision does not persuade me to a contrary conclusion. It is now well settled that the principles of natural justice are applicable to administrative decisions as well. Reference may be made, for this purpose, *inter alia* to the decisions of the Supreme Court in *Canara Bank vs. Debasis Das* (2003) 4 SCC 557 (paragraph 19) and *Manohar vs. State of Maharashtra* (2012) 13 SCC 14 (paragraph 17). The determination rests not upon such a classification of the decision, but upon the entire statutory scheme, the nature of the inquiry and other relevant factors, as indicated, by way of example, in paragraph 26 of *Natwar Singh* (supra).

23. As the proceedings are being remanded to the Bank, it is for the Bank to take a call as to the extent of disclosure required in law, if any, bearing the aforesaid observations in mind. The rights and contentions of the parties in this regard are reserved.

E. Conclusion

24. The petitions are therefore disposed of with the following directions:

- a. The impugned orders of the Identification Committee and the Review Committee dated 04.02.2021 and 06.04.2021 respectively are set aside.
- b. The matter is remanded to the Identification Committee of the Bank for a fresh decision pursuant to the impugned show cause notice dated 22.10.2020.
- c. Prior to the Identification Committee taking a fresh decision, the Bank will address a communication to the petitioners disclosing any documents which it considers necessary in accordance with law, or alternatively stating its conclusion that no further disclosure of documents is required.
- d. The Bank will give the petitioner at least 15 days' time to submit an additional representation after the aforesaid communication.
- e. The Bank will also give the petitioners an opportunity of a personal hearing before the Identification Committee, which may pass a fresh order in accordance with law thereafter.
- f. In the event the Identification Committee reaches a conclusion adverse to the petitioners, the petitioners will have 15 days' time to submit a representation for consideration of the Review Committee, which will thereafter proceed in accordance with the procedure laid down in law, and give a reasoned decision.
- g. The question of adequacy of the disclosure made by the Bank pursuant to this judgment is left open.

h. It is made abundantly clear that this Court has not expressed any opinion on the merits of the parties' contentions.

25. The pending applications are also disposed of.

PRATEEK JALAN, J

MAY 13, 2021

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