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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

% *Date of Decision: 25th May, 2023*

+ **LPA 564/2019, CM APPL. 39454/2019, CM APPL. 5264/2020 & CM APPL. 5307/2020**

UDAY J DESAI & ORS

..... Appellants

Through: Mr. Malak Bhatt, Ms. Neeha Nagpal & Mr. Siddharth Kumar, Advs.

versus

UNION OF INDIA & ORS

..... Respondents

Through: Mr. Ravi Prakash, CGSC with Mr. Farman Ali, Mr. Varun Aggarwal, Mr. Aman Rewaria & Mr. Yasharth Shukla, Advs. for R-1/UoI.
Mr. Arun Aggarwal, Adv. for R-4 & R-10.
Mr. Sudarsh Menon, Adv. for R-6.
Ms. Manya Hasija, Adv. for R-16

CORAM:

HON'BLE MR. JUSTICE VIBHU BAKHRU

HON'BLE MR. JUSTICE AMIT MAHAJAN

VIBHU BAKHRU, J. (Oral)

1. The appellants have filed the present appeal impugning an order dated 26.07.2019 (hereafter 'the impugned order') delivered by the learned Single Judge in **W.P.(C) 8092/2019** captioned ***Uday J Desai & Ors. v. Union of India & Ors.***, whereby the said Writ Petition preferred by the appellants was

rejected. The appellants had preferred the aforesaid Writ Petition



seeking several reliefs but had confined the same to prayer clauses D & F. The relevant prayer clauses are set out below:

“In the circumstances, it is therefore most respectfully prayed that this Hon'ble Court may graciously be pleased to:

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D. Pass a writ of certiorari or any other writ, direction or order in the nature of a writ of certiorari for quashing and setting aside the decision taken by the Respondent Banks at the consortium meeting held on 07.01.2019 allowing the individual banks to decide on the course of action basis the forensic audit, and

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F. Pass a writ of certiorari or any other writ, direction or order in the nature of a writ of certiorari for quashing and setting aside the declaration of the Petitioner No.5 as Fraud contained in 1A filed by Respondent No. 6 before the Hon'ble Supreme Court in Writ Petition [Civil] No 1316 of 2018. on the basis of the Haribhakti Report dated 05.01.2019 and its addendum.”

2. As is apparent from the above, the appellants had confined their petition to, essentially, assail the decision of the consortium of respondent banks taken in the meeting held on 07.01.2019 without affording the appellants any opportunity to be heard. According to the appellants, the said decision of the consortium of banks has wide ramifications as it permitted the lending banks to proceed on the basis of the Forensic Audit Report submitted by M/s Haribhakti & Co. LLP. It further declared appellant no. 5's account as a fraud account, thus, adversely affecting the ability of the appellants (who were guarantors / borrowers) to raise any funds from the banks in the future. According to the appellants, the impugned decision is erroneous on several grounds. However, the appellants had confined their challenge to the said decision of the banks, on the sole ground that it was made in violation of the principles of natural justice.

3. According to the appellants, it was necessary for the respondent banks to have provided a copy of the Forensic Audit



Report to the appellants and also afford them an opportunity to be heard before taking any adverse decision. This contention was stoutly resisted on behalf of the respondents. According to them, the banks had acted in accordance with the Master Circular issued by the Reserve Bank of India and the said circular did not provide for any such procedure of hearing the borrowers before taking a decision to declare their account as 'Fraud'.

4. It was also contended on behalf of the respondent banks that sufficient opportunity was granted to the appellants to respond to the observations made by the Forensic Auditors (M/s Haribhakti & Co. LLP). Thus, the Forensic Audit Report had also taken into consideration the response of the appellants to various audit observations.

5. In view of the rival contentions, the learned Single Judge observed that *"the only issue, which arises for consideration is whether principles of natural justice need to be followed before declaring the account of respondent No. 5 as fraud."*

6. The learned Single Judge answered the said question in the negative. The learned Single Judge referred to paragraphs 8.9.4 - 8.9.6 of the Master Circular dated July 3, 2017 and has observed that the aforesaid paragraphs of the Circular do not stipulate issuance of a Show Cause Notice or sharing of the Forensic Report with a concerned entity. Accordingly, the Court proceeded to reject the stand of the appellants that they were required to be heard by the concerned banks before any adverse decision was taken holding the account in question to be a fraud account.

7. The learned Single Judge also accepted the contention of the respondents that during the course of the Forensic Audit, the



appellants had an opportunity to interact with the Auditors, and the draft reports were discussed by the Forensic Auditor with the appellants.

8. The learned Single Judge also held that since the appellants had accepted the appointment of M/s Haribhakti & Co. LLP as a forensic auditor without protest and had participated in deliberations with the said auditors, they were precluded from challenging its report on the ground that it was arbitrary and full of conjectures and surmises. The Court held that the challenge to the conclusion of the Forensic Auditor was not permissible.

9. We have heard the counsel for the parties.

10. The principal question involved in the present appeal is no longer *res integra* in view of the authoritative decision of the Hon'ble Supreme Court in ***State Bank of India & Others v. Rajesh Agarwal & Others*: 2023 SCC OnLine SC 342**. Considering the nature of the order declaring borrowers to be fraud, the Supreme Court observed as under:

“71. Audi alteram partem, therefore, entails that an entity against whom evidence is collected must : (i) be provided an opportunity to explain the evidence against it; (ii) be informed of the proposed action, and (iii) be allowed to represent why the proposed action should not be taken. Hence, the mere participation of the borrower during the course of the preparation of a forensic audit report would not fulfil the requirements of natural justice. The decision to classify an account as fraud involves due application of mind to the facts and law by the lender banks. The lender banks, either individually or through a JLF, have to decide whether a borrower has breached the terms and conditions of a loan agreement, and based upon such determination the lender banks can seek appropriate remedies. Therefore, principles of natural justice demand that the borrowers must be served a notice, given an opportunity to explain the findings in the forensic audit report, and to represent before the account is classified as fraud under the Master



Directions on Frauds.”

11. It is also relevant to set out the conclusions summarised by the Hon’ble Supreme Court in the said decision. The same are set out below:

“87. The conclusions are summarized below:

- i. No opportunity of being heard is required before an FIR is lodged and registered;
- ii. Classification of an account as fraud not only results in reporting the crime to investigating agencies, but also has other penal and civil consequences against the borrowers;
- iii. Debarring the borrowers from accessing institutional finance under Clause 8.12.1 of the Master Directions on Frauds results in serious civil consequences for the borrower;
- iv. Such a debarment under Clause 8.12.1 of the Master Directions on Frauds is akin to blacklisting the borrowers for being untrustworthy and unworthy of credit by banks. This Court has consistently held that an opportunity of hearing ought to be provided before a person is blacklisted;
- v. The application of audi alteram partem cannot be impliedly excluded under the Master Directions on Frauds. In view of the time frame contemplated under the Master Directions on Frauds as well as the nature of the procedure adopted, it is reasonably practicable for the lender banks to provide an opportunity of a hearing to the borrowers before classifying their account as fraud;
- vi. The principles of natural justice demand that the borrowers must be served a notice, given an opportunity to explain the conclusions of the forensic audit report, and be allowed to represent by the banks/JLF before their account is classified as fraud under the Master Directions on Frauds. In addition, the decision classifying the borrower's account as fraudulent must be made by a reasoned order; and



vii. Since the Master Directions on Frauds do not expressly provide an opportunity of hearing to the borrowers before classifying their account as fraud, audi alteram partem has to be read into the provisions of the directions to save them from the vice of arbitrariness.

12. In view of the abovesaid decision, the conclusion of the learned Single Judge that it was not necessary to afford the appellants any opportunity to be heard before the impugned decision was taken by the consortium of banks, is liable to be set aside. Further, the conclusion that no opportunity is required to be given for the reason that the Master Circular issued by the RBI does not entail any such procedure, is also unsustainable in view of the decision of the Hon'ble Supreme Court in *State Bank of India & Others* (supra).

13. We are also of the view that the learned Single Judge has erred in holding that the appellants are precluded from challenging the report furnished by the Forensic Auditor because they had participated in the appointment of M/s Haribhakti & Co. LLP as Forensic Auditors without demur and had participated in deliberations with the said auditor.

14. Merely because a party participates in a proceeding or in a deliberation before any authority is not a ground to preclude the party from challenging the final decision that may be rendered by said authority. We find no basis in law for the proposition where a party who participates in the proceedings is precluded from challenging the report or decision rendered pursuant to the said proceedings and, are unable to concur with the said view. A party who has participated in a proceeding before an authority unreservedly, may be precluded from challenging the procedure



or the constitution of the Authority; but it would not preclude the party from challenging the conclusion drawn by the concerned authority.

15. It is not in dispute that the appellants were not afforded any opportunity of hearing by the respondent banks prior to the decision dated 07.01.2019, which is impugned by way of the Writ Petition.

16. It is also not disputed that the Forensic Report of M/s Haribhakti & Co. LLP, Forensic Auditor, was not shared with the appellant prior to the same being considered at the meeting held on 07.01.2019.

17. Concededly, the appellants had no opportunity to address the consortium of banks on the contents of the Forensic Report on the basis of which an adverse decision was taken.

18. In view of the above, the decision of the respondents to the extent that it holds the account of appellant No. 5 (Frost International Limited) as 'fraud', is set aside.

19. It is clarified that this would not preclude the consortium of banks or any of the banks from independently taking action in accordance with the law and after affording the appellants an opportunity to be heard.

20. The appeal is allowed in the aforesaid terms.

VIBHU BAKHRU, J

AMIT MAHAJAN, J

MAY 25, 2023

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