13th May, 2024
(AK)
20

W.P.A 13341 of 2024

Amit Kumar Kejriwal
Vs.
UCO Bank and others

Mrs. Noelle Banerjee
Mr. Dipak Dey
Ms. S. Mitra
Mr. Aniket Ojha
…for the petitioner.

Mr. Shashwat Nayak
Mr. Santosh Kr, Ray
Ms. Antalina Guha
…for the respondents.

1. The petitioner challenges a show-cause notice issued under the Master Directions on Frauds-Classification and reporting by commercial Banks and selected FIs dated July 1, 2016 (updated as on July 3, 2017) issued by the Reserve Bank of India (RBI).
2. Learned counsel for the petitioner argues that the impugned show-cause notice has only quoted some of the observations made in a transaction audit report, which was not authored within the purview of the Master Directions.
3. As such, mere reliance on such observations cannot justify action to be taken under the Master Directions for classification as fraud.

4. Learned counsel for the petitioner places specific reliance on the timelines stipulated in the Master Directions, which require reports to the Board to be ensured, quarterly review of frauds, annual review of frauds etc.

5. As specific timelines are given for such compliances by the Bank, in the absence of adherence to the same, the notice under the Master Directions stands vitiated.

6. It is argued on the premise of Chapter IV of the Master Directions that in the absence of compliance of such reviews and other acts on the part of the Bank, not only is the Bank subject and amenable to penal action within the provisions of the Master Directions but the same vitiates any step taken for classification as fraud.

7. Learned counsel appearing for the petitioner next argues that the show-cause notice is vitiated and barred by the principle of *res judicata* since in a proceeding before the NCLT (National Company Law Tribunal) under the provisions of Sections 43, 44, 45, 46, 48, 49, 66 and 67 of the Insolvency and Bankruptcy Code, 2016, the applications made by the Bank were disposed of without any observation that the petitioners are guilty of fraud or fraudulent activities under any of the said provisions.

8. The issue having thus been decided in favour of the petitioner, the petitioner cannot be vexed twice on the self-same cause of action by issuance of a notice under the Master Directions, which also operates on the premise of fraud.
9. Learned counsel next argues that even the audit report which has been relied on by the petitioner was held in a different proceeding by this court not to be a valid basis for issuance of notice under the Master Circular of the RBI on Willful Defaulters.
10. Hence, having been held to be vitiated, the said audit report cannot be the premise of a different proceeding under the Master Directions on Fraud as well.
11. Learned counsel specifically places reliance on the General Guidelines and the provisions of the Master Directions, in particular Clause 4.4 thereof, which contemplates that a Special Committee of the Board as enumerated therein has to be constituted by the Bank in order to monitor and follow up cases of frauds.
12. Hence, the impugned show-cause notice issued by the zonal head of the respondent-Bank is bad in law.
13. Learned counsel for the petitioner argues that if a statute mandates a particular procedure in which an action has to be taken, in the absence of such

action being taken adhering to the said procedure, the action itself is vitiated.

14. Learned counsel appearing for the petitioner also cites a judgment of the Supreme Court rendered in *(1954) 1 SCC 691 (Shankar Sitaram Sontakke and another vs. Balkrishna Sitaram Sontakke and others*) where it was observed that a consent decree is as binding upon the parties thereto as a decree passed by invitum.

15. Thus, it is argued that a decree passed on consent has the binding force of *res judicata*.

16. The same principle, it is argued, should apply vis-à-vis the order passed by the NCLT in the present context.

17. Learned counsel appearing for the Bank refutes all the submissions made by the petitioner and argues that it would be premature for this court to enter into the veracity of the Forensic Audit Report.

18. In the previous proceeding where it was held by this court that the said report could not be a valid basis, the challenge was against an order passed by the Review Committee which had affirmed the Willful Defaulter Identification Committee decision.

19. The said stage was a mature one whereas in the present case, at the inception of issuance of show-cause, the present writ petition has been preferred.

20. Insofar as the NCLT order is concerned, it is argued that the questions raised in the show-cause notice were not decided conclusively by the said forum and, as such, the principle of *res judicata* does not operate.

21. Regarding the timelines given in the Master Directions, it is argued that the said mandate is upon the Bank to follow and the accused person under the Master Directions on Fraud cannot set up a defence on the basis of the same, as even non-adherence to such timelines does not vitiate a show-cause notice issued under the said Master Directions.

22. In respect of the show-cause notice not being issued by the Special Committee as envisaged in the Master Directions, it is argued that the Special Committee comes into operation only after declaration of fraud.

23. It is argued that, in any event, the Master Directions do not even contemplate issuance of any notice.

24. It is only in the judgment of *State Bank of India and others vs. Rajesh Agarwal and others* reported at *(2023) 6 SCC 1* that the Supreme Court has read the principle of *audi alteram partem* into the Master Directions.

25. However, the fact remains that the Bank is the authority which has to issue a notice under the said Directions and the same need not be authored by a Special Committee.

26. In reply, learned counsel for the petitioner argues that in *Rajesh Agarwal's* case, the Bank had complied with the timeline given in the Master Directions and the Forensic Audit Report under consideration was authored under the directions of the JLF within the confines of the Master Directions.

27. Upon a careful consideration of the arguments made by the parties, it is seen that the impugned show-cause notice quotes certain observations of the Transaction Audit Report, which was not authored at the behest of the JLF.

28. The said Audit Report was apparently used in the NCLT proceeding as well.

29. Although in a previous writ petition, this court had cast certain doubts on the Audit Report as a basis for action taken under the Master Circular on Willful Defaulters issued by the RBI, in the said writ petition, the court was considering the validity and legality of a decision by a Review Committee, affirming that of a Willful Defaulter Identification Committee.

30. In such context, the observations were made therein.

31. The present proceeding, however, is at an inchoate stage only, where merely a show cause notice has been issued and no decision declaring the petitioner's account as fraud has been taken as yet.

32. Taken in proper context, the present challenge against the show-cause notice is premature on such count, as upon a consideration of the representation of the petitioner, it is for the concerned authorities to take a decision as to whether to declare the account of the petitioner as fraud at all.

33. As opposed to the previous judgment, no decision has been taken on such count at this stage and as such the court need not go into a detailed scrutiny of the Transaction Audit Report as a valid basis in such proposed declaration of fraud.

34. Regarding the argument of *res judicata*, the same is not tenable in the eye of law.

35. A bare perusal of the NCLT order indicates that the NCLT recorded the submission of both parties and ultimately the contention of the present writ petitioner, who was the respondent therein, that the respondents had complied with the reliefs as prayed for in the application therein.

36. On such submission, the applicant/Bank submitted that the reliefs prayed for in the application before the NCLT had been complied in totality and no other reliefs were pending for compliance, in view of which submission it was recorded by the NCLT that nothing survived for the consideration of the NCLT and the applications were disposed of.

37. The said observations clearly point out that the NCLT was of the opinion that nothing survived for its consideration and the matter was disposed of as infructuous in view of the reliefs claimed having already been complied with.

38. Thus, there is no scope of applying the ratio laid down in *Shankar Sitaram (supra)*, as the NCLT order was not an adjudication on merits at all on any of the issues involved therein, but merely a recording that the matter had become infructuous, on which ground the same was disposed of, in fact specifically observing that "nothing survived for its consideration".

39. Thus it cannot be said that the NCLT or any other forum has decided on merits any of the issues raised in the impugned show-cause notice.

40. With regard to the issue of timelines raised by the petitioner, it is seen from a comprehensive consideration of the Master Directions on Fraud

that the timelines are mandates on the Banks, to ensure that all frauds above Rs.0.1 million are reported to the Boards promptly on their detection.

41. It is also observed in Clause 4.1 of the Master Directions that such report should among other things take note of the failure on the part of the concerned branch officials and controlling authorities, and give details of action initiated against the officials responsible for the fraud.

42. The purpose enumerated in Clause 1.3 of the Master Directions makes it clear that the directions are issued with an intention to provide a framework to Banks to detect and report frauds early and take timely consequential actions.

43. They are also to enable faster dissemination of information by the RBI to Banks on the details of frauds, unscrupulous borrowers and related parties etc.

44. Thus, the timelines operate as against the Banks, casting the liability on Banks to pay penalty if not followed, and an accused person under the said Master Directions cannot take advantage of the same.

45. Non-compliance of the said timelines does not vitiate a show-cause notice or an action taken for classification of fraud under the Master Directions but those timelines are merely for the Bank to

comply with, not to contradict an action taken under the Master Directions for declaration of fraud but to facilitate the same.

46. The converse, thus, cannot be argued by the petitioner.

47. However, the petitioner has made out a strong case inasmuch as the show-cause notice was not issued by the Special Committee envisaged under the Master Directions.

48. The Bank argues that it is only in *Rajesh Agarwal (supra)* that the principles of natural justice have been read into the Master Directions and there is no specific provision in the Master Directions as to issuance of notice or which authority has to issue notice.

49. Learned counsel for the Bank has also argued that the Bank itself can issue such notice through his zonal head or otherwise.

50. However, a through perusal of the Master Directions leaves no other option for the court but to hold that it is only the Special Committee which is to be instrumental in authoring the show-cause notice for declaration of an entity as fraud.

51. In Clause 2.1, under the General Guidelines, it is provided that the Chairman and Managing Director/Chief Executive Officers (CMD/CEOs) of

Banks must provide focus on the fraud prevention and management function.

52. Clause 2.1.2 stipulates that the fraud risk management, monitoring and investigation function must be owned by the Bank's CEO, Audit Committee of the Board and the Special Committee of the Board.

53. Even Clause 4.4.1 of the Master Directions indicates that the Audit Committee of the Board (ACB) shall monitor all cases of frauds in general and Banks are required to constitute a Special Committee of the Board for monitoring and follow up of cases of fraud involving amounts of Rs.10 million and above exclusively.

54. The expressions "follow up of cases of frauds" and "monitoring", coupled with the expression "fraud monitoring" and "fraud investigation function" clearly indicates the scope of functioning of the Special Committee also to incorporate proceedings taken under the Master Directions for declaring an account or an entity as fraud.

55. The issuance of a show-cause notice is the primary pre-requisite and first step of such action and falls within the domain of such action.

56. Thus, there cannot be any doubt that the Special Committee has, among other things, to author the show-cause notice issued for declaration of an

entity or account as fraud under the Master Directions.

57. As such, the impugned show-cause notice dated April 10, 2024, issued by the Zonal Head of the Bank and not the Special Committee, is vitiated on the last above mentioned ground and not on the other grounds.

58. In such view of the matter, the show-cause notice cannot stand the test of judicial scrutiny.

59. Accordingly, WPA 13341 of 2024 is allowed, thereby setting aside the impugned show-cause notice dated April 10, 2024 on the ground of lack of authority of the DGM & Zonal head of the respondent-Bank to issue the same.

60. Nothing in the above order, however, shall preclude the respondent-Bank, through the Special Committee formed under Articles 4.4 of the Master Directions on Fraud, to issue a fresh notice, thereby initiating a de novo proceeding against the petitioner for declaration of the petitioner's account as fraud under the concerned Master Directions of the RBI.

61. The merits of the allegations and counter–allegations in the writ petition have not been gone into at this stage and it will be open to the concerned authorities, subject to issuance of a

proper notice, to decide such issues if raised before it independently and in accordance with law.

62. There will be no order as to costs.

63. Urgent photostat copies of this order, if applied for, be given to the parties upon compliance of all requisite formalities.

(Sabyasachi Bhattacharyya, J.)