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

\+   W.P.(C) 6835/2023 & CM APPL. 25139/2024

ARUN MITTAL & ANR. ..... Petitioners

Through: Mr. Anshuman Sharma and Mr. Azad Ahmed, Advocates
Mob: 9910207302
Email: info@aslaws.in

versus

PUNJAB NATIONAL BANK & ANR. ..... Respondents

Through: Mr. Santosh Kumar Rout, Ms. Dharna Veragi, Advocates for R-1.
Email: skrlawfirms@gmail.com
Mob: 9990432878

% ***Date of Decision: 30th April, 2024***

CORAM:
HON'BLE MS. JUSTICE MINI PUSHKARNA

JUDGMENT

MINI PUSHKARNA, J: (ORAL)

CM APPL. 25139/2024

1. The present is an application for early hearing and disposal, in view of the counter affidavit filed on behalf of the respondent.

2. Considering the submissions made in the present application, the present petition is taken up for hearing today itself.

3. The next date of hearing, i.e., 11th September, 2024 stands cancelled.

4. With the aforesaid directions, the present application is disposed of.

W.P.(C) 6835/2023

5. The present writ petition has been filed seeking quashing and setting

aside of the impugned order dated 26th August, 2022 and all connected proceedings prior and subsequent thereto, including the proceedings of Minutes of the Meeting dated 31st December, 2020 of the respondent no. 1-Punjab National Bank ("PNB"). By way of the said order dated 26th August, 2022, the respondent no. 1-bank has declared the petitioners' account as 'Fraud' in terms of the Reserve Bank of India ("RBI") Master Directions on Frauds - Classification and Reporting by Commercial Banks and Select FIs.

6. It is submitted that the aforesaid declaration of the petitioners' account as 'Fraud', is in complete violation of the Principles of Natural Justice and also in complete disregard to the binding judgment passed by the Supreme Court in the case of ***State Bank of India and Others Versus Rajesh Agarwal and Others, 2023 SCC OnLine SC 342***.

7. Learned counsel appearing for the petitioners submits that as per the aforesaid judgment passed by the Supreme Court, for the purposes of following the Principles of fair play and equality, the respondent-bank was required to issue a Show Cause Notice to the petitioners and the petitioners were required to be granted due opportunity of representation to put forth their defence before the respondent-bank.

8. However, it is submitted that the procedure as laid down by the Supreme Court, has not been followed. Thus, it is submitted that the declaration of the account of the petitioners as 'Fraud', is totally illegal and cannot stand the test of law.

9. Attention of this Court has been drawn to the judgment dated 8th May, 2023 passed by the Division Bench of this Court in *W.P.(C) 1213/2023* and *W.P.(C) 1153/2023*, wherein the Division Bench of this Court has categorically held that in case an opportunity of hearing and the process as

envisaged by the Supreme Court in the case of ***Rajesh Agarwal (Supra),*** is not followed, then such an order cannot be sustained.

10. Responding to the same, learned counsel appearing for the respondent submits that declaration of the accounts of the petitioners as 'Fraud', has been done on the basis of the procedure as envisaged in Master Directions of the RBI. He refers to the counter affidavit filed on behalf of respondent no. 1-Punjab National Bank, to submit that the petitioners are in breach of the terms and conditions of the loan agreements, therefore, the respondent-bank has rightly exercised its power to declare the loan account of petitioners, as 'Fraud'. It is further submitted that the said action was taken after duly considering the Forensic Audit Report and the Transaction Audit Report, in terms of the stipulation of the Master Directions of the RBI.

11. He further submits that the account of the petitioners was declared as 'Fraud', much prior to the judgment of the Supreme Court in the case of ***Rajesh Agarwal (Supra)***.

12. Having heard learned counsel appearing for the parties, it is manifest that the impugned order has been passed without following the procedure as laid down by the Supreme Court in the case of ***Rajesh Agarwal (Supra).*** Thus, the impugned order declaring the accounts of the petitioners as 'Fraud', cannot be sustained.

13. Division Bench of this Court in the case of ***Aditya Malhotra and Another Versus Reserve Bank of India and Ors.***, vide order dated 8th May, 2023 in *W.P.(C) No. 1213/2023*, while referring to the judgment of the Supreme Court in the case of ***Rajesh Agarwal (Supra)***, has held as follows:

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4. Thus, to summarise, the Hon"ble Supreme Court in its judgment has held as under:

(i) No opportunity of being heard is required before an FIR is lodged and registered against the borrower;

(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 practical 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 make representations before 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.

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14. It is to be noted that the Hon'ble Supreme Court in the aforesaid case of ***Rajesh Agarwal,*** has categorically held that the Principles of Natural

Justice and *Audi Alteram Partem*, have to be read into the Master Directions, as issued by the RBI. Thus, it has been held as follows:

> *"xxx xxx xxx*
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> ***81.** 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.*
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> ***D.4. Challenge to constitutional validity***
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> ***82.** The borrowers have argued that the Master Directions on Frauds will have to be struck down as arbitrary and unconstitutional for conferring unguided and unbridled powers on banks. To counter the submission, RBI and lender banks have relied upon the decision in Delhi Cloth & General Mills Co. Ltd. v. Union of India [Delhi Cloth & General Mills Co. Ltd. v. Union of India, (1983) 4 SCC 166] to submit that the provisions of the Master Directions on Frauds are not arbitrary as they have a reasonable nexus to the object sought to be achieved. It was further argued that the Courts should not interfere with and supplant their wisdom in an economic policy decision unless there is blatant perversity, arbitrariness, or mala fides.*
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> ***83.** RBI has the right to take all such measures as are necessary to protect the health of the banking system. Hence, the Master Directions on Frauds lay down the procedure for banks, who in case of a breach of loan agreements by the borrowers, can seek appropriate remedies by approaching law-enforcement agencies and debarring borrowers from accessing further institutional finance. However, any policy decision which contemplates serious civil consequences for any person will be open to challenge for being arbitrary if the principles of natural justice are not applied during the process.*
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> *xxx xxx xxx"*

15. Considering the aforesaid, the order declaring the account of the petitioners as 'Fraud', is hereby set aside.

16. However, liberty is granted to the respondent-bank to proceed ahead in accordance with law, in the light of the judgment of the Supreme Court in the case of ***Rajesh Agarwal (Supra)***.

17. Accordingly, the present petition is disposed of, with the aforesaid directions.

MINI PUSHKARNA, J

APRIL 30, 2024
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