
(2003) 05 AHC CK 0040

In the Allahabad High Court

Case No : Civil Miscellaneous Writ Petition No. 18361 of 2003

Garlon Polyfab Industries Ltd. and Others

APPELLANT

Vs

State Bank of India and Another

RESPONDENT

Date of Decision : 08-05-2003

Acts Referred:

Constitution of India, 1950 — Article 14, 226
Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI) — Section 13, 13(2), 13(4), 13(9), 2

Citation : (2003) 5 AWC 4291 : (2003) 3 BC 626 : (2003) 2 UPLBEC 1785

Hon'ble Judges : R.S. Tripathi, J;M. Katju, J

Bench : Division Bench

Judgement

M. Katju, J.—This writ petition has been filed praying for a writ of mandamus declaring Section 13 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (hereinafter referred to as "the Act) as ultra vires and for quashing the notices dated 31.12.2002 Annexures 2 and 3 to the writ petition.

2. We have heard the learned Counsel for the parties.

3. The petitioner No. 1 is a private limited company. The petitioner No. 1 took loans from respondent No. 1 (the State Bank of India) and U.P. Financial Corporation. It is alleged that the present secured loan outstanding from U.P. Financial Corporation is Rs. 137.89 lakhs as principal amount, and from respondent No. 1 is Rs. 39 lakhs as principal amount. The petitioner No. 1 was having a total cash credit limit of Rs. 37 lakhs from the respondent No. 1. A dispute arose between the petitioners and the respondent No. 1 in June 1995 owing to clean bill limits (discounting) facility and the Bank stopped accepting the same for discounting. It is alleged that for this reason the company stopped operations with the Bank and offered to settle the same by way of one time settlement in 1999 at Rs. 32 lakhs. It is alleged in paragraph 6 of the writ petition that this was agreed and recommended by the Branch, and the

promoters got Rs. 10 lakhs deposited from a third party in no lien account with the Bank to facilitate the same.

4. Misalleged in paragraph 7 of the writ petition that the respondent No. 1 later on realised and did not make one time settlement at Rs. 32 lakhs on the principal amount, and the petitioners increased the offer upto Rs. 37 lakhs. However, the total head office of the Bank did not accept this and rejected the offer by the order dated 3.8.2000, Annexure 4 to the writ petition. Thereafter the respondent No. 1 filed a petition for recovery in the Debt Recovery Tribunal, Allahabad on 18.9.2000, which is pending. It is alleged in paragraph 9 of the writ petition that in 1998 the unit of the petitioner was closed on account of a series of searches by the Central Excise Authorities as a result of which the company could not function for about eight months and subsequently became sick.

5. The petitioner was referred to BIFR in January, 2001 and the reference is still pending there. The proceeding before the Debt Recovery Tribunal had been suspended in view of the reference pending before the BIFR. It is alleged in paragraph 11 of the writ petition that the Peak Net Worth of the company is Rs. 628.63 lakhs and accumulated losses are Rs. 717.46 lakhs as on 31.10.2000. In April 2002 the BIFR allowed conducting proceedings before the Debt Recovery Tribunal but restrained it from taking any recovery till the pendency of the reference. On 2.1.2003 the State Bank of India issued six draft notices to the petitioners u/s 13(4) of the Act.

6. In Paragraph 14 of the writ petition it is alleged that the total loan component of State Bank of India constitutes less than 75% and it proceeded without having consent of the main lender U.P. Financial Corporation whose dues comes to Rs. 4.50 crores. It is contended that in view of Section 13(9) of the Act no secured creditor is entitled to exercise any right u/s 13(4) of the Act unless such right is agreed upon by secured creditors representing not less than 3/4 of the total value of amount outstanding. Hence it is alleged that the impugned notices are bad. It is alleged in paragraph 18 of the writ petition that the proceeding under the Act are not maintainable.

7. It is alleged in paragraph 19 of the writ petition that Section 13 of the Act is in express derogation of Sections 69 and 69A of the Transfer of Property Act. In paragraph 20 of the writ petition it is alleged that Section 13 of the Act provides for enforcement of security without intervention of the Court or Tribunal. It is alleged that there is no adjudicatory forum for settlement of any dispute which may be genuine, and the Bank (secured creditor) has been made Judge in its own cause which is against the fundamental principle of law and violative of Article 14 of the Constitution. In paragraph 21 of the writ petition it is alleged that u/s 13 there is no provision for considering any explanation by the borrower in reply to the notice u/s 13(2) which means that no opportunity of hearing need be given to the borrower. Hence it is alleged that Section 13(4) of the Act is ultra vires Article 14 of the Constitution. It is alleged in paragraph 22 of the writ petition that before the Debt Recovery Tribunal the Bank will have to prove its

case and a judicial decision would be taken. However, u/s 13 the Bank besides being the plaintiff is also the judge of its own case which is a drastic provision. No appeal is provided under the Act.

8. We are of the opinion that there is no merit in the challenge to Section 13(4) of the Act. It may be mentioned that there is always a presumption in favour of the constitutional validity of an Act vide *Chiranjit Lal Chowdhuri Vs. The Union of India (UOI) and Others*, *Madhu Limaye Vs. Sub-Divisional Magistrate, Monghyr and Others*, *Hamdard Dawakhana and Another*, *Kalipada Deb and Another*, *Lakshman Shripati Itpure @ Lakshman Shripati Impore and A.B. Choudhri and Another Vs. The Union of India (UOI) and Others*, *Sunil Batra Vs. Delhi Administration and Others etc.*, *Rt. Rev. Msgr. Mark Netto Vs. State of Kerala and Others*, etc. A heavy burden lies on the person who challenges the constitutional validity of a statute. We do not see any constitutional invalidity in Section 13 of the Act.

9. No doubt Section 13 is a drastic provision but it appears to have been enacted in view of the grave financial position in the country that huge amounts of loans of Banks are outstanding which the borrowers have avoided repaying by various devices. Unless loans of the Bank are returned the Bank or the financial institution cannot again advance money to someone else. Money must be kept in circulation, but that is not possible if loans are not repaid.

10. Section 2(zd) of the Act defines a secured creditor as follows :

"secured creditor" means by Bank or financial institution or any consortium or group of Banks or financial institutions and includes-

(i) debenture trustee appointed by any Bank or financial institution; or

(ii) Securitisation company or reconstruction company; or

(iii) any other trustee holding securities on behalf of a Bank or financial institution, in whose favour security interest is created for due repayment by any borrower of any financial assistance."

11. Thus the respondent No. 1 is a secured creditor and hence Section 13 will apply in its case.

12. In our opinion it is not correct that the loanee does not get any opportunity of hearing before the action is taken u/s 13(4) of the Act. Section 13(2) itself mentions that where a borrower who is under a liability to a secured creditor under a security agreement makes any default in repayment of a secured debt or instalment thereof, the secured creditor may require the borrower by notice to discharge in full his liabilities to the secured creditor within sixty days failing which the secured creditor shall be entitled to exercise all or any of the rights under Sub-section (4).

13. In *The Maharashtra State Financial Corporation Vs. M/s. Suvarna Board Mills and another*, it was held by the Supreme Court that where a notice is given to a

defaulter to pay the dues failing which possession of the property will be taken, no further show-cause notice is required. Such notice itself fulfils the requirements of natural justice.

14. The aforesaid decision of the Supreme Court is a clear proposition that once a notice is given to the borrower to pay his dues failing which possession of the property will be taken, this itself amounts to compliance of the principle of natural. In response of this notice it is open to the borrower to give any explanation which he requires and obviously this explanation must be considered by the required creditor before taking action u/s 13(4).

15. u/s 13(10) of the Act where dues of the secured creditor are not fully satisfied with the sale proceeds of the secured assets, the secured creditor may file an application before the Debt Recovery Tribunal. This implies that the Debt Recovery Tribunal is not totally out of the picture but it is open to the secured creditor to take action u/s 13 for recovering debt dues after sale of the secured assets.

16. In *Maganlal Chhaganlal (P) Ltd. Vs. Municipal Corporation of Greater Bombay and Others*, it was held by the Supreme Court, while reversing its own earlier decision in *Northern India Caterers Private Ltd. and Another Vs. State of Punjab and Another*, that where a statute providing for a more drastic procedure different from the ordinary procedure and covers the whole field covered by the ordinary procedure without any guidelines as to the class of cases in which either procedure is to be resorted to, the statute will be hit by Article 14. However, the Supreme Court went on to say that the necessary guidelines could be inferred from the preamble and surrounding circumstances as well as the provisions of the statute and in such a case the statute will not be hit by Article 14. Then again, where the statute itself covers only a class of cases the statute will not be bad. The fact that in such cases the executive will choose which cases are to be tried under the special procedure will not affect the validity of the statute. Hence the contention that the mere availability of two procedures will vitiate one of them is not supported by reason or authority.

17. In the present case the impugned Act itself mentions the class of cases which will be covered by Section 13 of the Act. In the first place, there must be a secured interest created in favour of a secured creditor. Secondly, there must be a secured agreement under which the borrower will have the liability. Thirdly, the borrower must make a default for repayment of a secured debt or any instalment thereof and then again such debt has to be classified by the secured creditor as a non-performing asset.

18. A non-performing asset has been defined in Section 2(o) of the Act as follows :

"Non-performing asset means an asset or account of a borrower, which has been classified by a Bank or financial institution as substandard, doubtful or less assets, in accordance with the directions or under guidelines relating to assets

classification issued by the Reserve Bank."

19. The Act of 2002 is thus a special Act and it will override any provision to the contrary in the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 or any other earlier Act of Parliament or the State Legislature pertaining to the field it covers.

20. It may be noted that u/s 13(2) of the 2002 Act the secured creditor has to first classify the debt as a non-performing asset, and only then can action be taken u/s 13(4). There is no such requirement in the Recovery of Debts Due to Banks and Financial Institutions Act, 1993. In fact the 1993 Act is not restricted to non-performing assets. Thus the field covered by the 2002 Act and the 1993 Act are different. The 1993 Act does not refer to non-performing assets at all, and such assets have not to be classified in accordance with the Reserve Bank guidelines and directives.

21. The obvious purpose of enacting the impugned Act was that the loans of Banks and financial institutions were not being recovered promptly and this was adversely affecting the financial health of the nation. Unless loans are repaid promptly money will not remain in circulation, and the Banks and financial institutions may get into trouble. In fact already many Banks and financial institutions are in financial difficulty due to non-repayment of the loans.

22. We see no constitutional invalidity in Section 13 of the Act No. 54 of 2002. Rather, it serves a salutary purpose. The challenge to the aforesaid provision therefore fails.

23. However, a regards the petitioner's plea relating to Section 13(9) of the Act, the provision itself makes it clear that where there are more than one secured creditors, no secured creditor can exercise the right u/s 13(4) unless the secured creditors representing not less than three-fourth of the outstanding amount agree. The petitioners have relied on the letter of the Regional Magistrate of the U.P. Financial Corporation dated 11.12.2002 (Annexure 5) to demonstrate that the U.P. Financial Corporation is not agreeable to take action u/s 13(4) against petitioner No. 1.

24. We are not going into the factual controversy as to whether the U.P. Financial Corporation is now agreeable to take action u/s 13(4) or not, and whether the secured creditors representing three-fourth or more of the loan amount are agreeable to take action u/s 13(4). However, we make it clear that action u/s 13(4) cannot be taken in violation of Section 13(9) of the Act.

With these observations the petition is disposed of finally.