

(2014) 01 DEL CK 0037

In the Delhi High Court

Case No : Writ Petition (C) 7505 of 2013 and CM Application 16064 of 2013

M/s. Holystar Natural Resources Pvt. Ltd. and Another

APPELLANT

Vs

Union of India and Another

RESPONDENT

Date of Decision : 17-01-2014

Acts Referred:

Banking Regulation Act, 1949 — Section 21 35-A
Constitution of India, 1950 — Article 14 19(1)(g) 245
Delhi Municipal Corporation Act, 1957 — Section 116 116(3)
Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI) — Section 13 13(2) 13(4) 15 17

Citation : AIR 2014 Delhi 60 : (2014) 3 BC 233 : (2014) 121 CLA 18 : (2015) 191 CompCas 482 : (2014) 207 DLT 396

Hon'ble Judges : N.V. Ramana, C.J.;Manmohan, J

Bench : Division Bench

Advocate : Ramesh Singh and Mr. Nikhil Goel, for the Appellant; Rajeeve Mehra, ASG in W.P. (C) 7505, 7506, 7507, 7508, 7509, 7510 and 7574/2013 and CM Appl. 16064, 16065, 16066, 16067, 16068, 16069 and 16188/2013, Mr. Aditya Malhotra, for UOI in W.P. (C) 7505, 7508, 7510 and 7574/2013 and CM Appl. 16064, 16067, 16069 and 16188/2013, Ms. Praveena Gautam, Advocate for respondent No. 2/BOB in W.P. (C) 7505, 7506, 7507, 7508, 7509, 7510 and 7574/2013 and CM Appl. 16064, 16065, 16066, 16067, 16068, 16069 and 16188/2013, Mr. Sumeet Pushkarna in W.P. (C) 7505, 7506, 7507, 7508, 7509, 7510 and 7574/2013 and CM Appl. 16064, 16065, 16066, 16067, 16068, 16069 and 16188/2013, CGSC and Ms. Sara Sundaram, for UOI in W.P. (C) 7506, 7507, 7509/2013 and CM Appl. 16065, 16066, 16068/2013, for the Respondent

Final Decision : Dismissed

Judgement

N.V. Ramana, C.J.—In this batch of writ petitions, the petitioners are assailing the constitutional validity of Section 2(1)(o) of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (hereinafter referred to as "SARFAESI Act") as well as the legality of the Circular dated 1st July, 2013 of the Reserve Bank of India (hereinafter referred to as "RBI").

Petitioner's submissions

Mr. Ramesh Singh, learned counsel for the petitioners, pointed out that Section 2(1)(o) of the SARFAESI Act defines Non-Performing Asset (for short, "NPA") to mean an asset/account of a borrower, which had been classified by a bank/financial institution as sub-standard, doubtful or loss asset in accordance with the RBI guidelines relating to asset classification or similar guidelines issued by banks/financial institutions. He submitted that the SARFAESI Act did not define or even indicate any guideline for defining as to what is sub-standard, doubtful or loss asset.

2. According to him, the Parliament by delegating such an essential legislative function and that too, in an uncontrolled manner inter alia by not setting the limits of the power delegated or by laying down standards or guidelines had clearly violated Article 14 of the Constitution of India. In support of his submission, Mr. Ramesh Singh relied upon a judgment of the Supreme Court in *Krishna Mohan Pvt. Ltd. Vs. Municipal Corporation of Delhi and Others*, wherein it has been held as under:-

44. The next question that arises for our consideration is whether, following the reasons given by this Court in *New Manek Chowk Spinning and Weaving Mills Co. Ltd. and Others Vs. Municipal Corporation of The City of Ahmedabad and Others*,] it can be held that subsection (3) of Section 116 is invalid for excessive delegation of legislative powers as it vests arbitrary and unguided discretion in the Commissioner to declare any machinery situated in or upon a land or building to be deemed to form part of the land and building for the purpose of determining the rateable value thereof. According to learned counsel for the appellant, the reasons given by this Court in *New Manek Chowk Spinning and Weaving Mills Co. Ltd. and Others Vs. Municipal Corporation of The City of Ahmedabad and Others*,] for striking down Rule 7(2) framed under the BPMC Act, 1949 as invalid on account of excessive delegation of power of the legislature equally apply to sub-section (3) of Section 116.

45. For the respondents, however, it is contended that as long as guidelines for exercise of delegated power are discernible in the statute, it cannot be held to be unconstitutional, however skeletal the parent legislation may be. Our attention was drawn to the judgments of this Court in *J. Jayalalitha v. Union of India* and *Kishan Prakash Sharma v. Union of India*.

46. Learned counsel for the respondents contends that reading the provisions of the DMC Act, particularly the definition of the expressions "land", "building", "premises", "rateable", it is clear that the exclusion contemplated by subsection (3) of Section 116 of the Act can only be of such items which could not normally be included in the concept of land or building. Hence, the Commissioner's power to notify plant or machinery u/s 116(3) must be read as extending only to such things of the same nature as would fall within the definition of "land" as defined in Section 2(24) of the Act. He, therefore, contends that there is thus sufficient

guideline indicated in the statute itself and, therefore, the constitutionality of the statute must be upheld. Despite anxiously scanning the provisions of the statute, we hardly find any such guidelines therein. The contention of the learned counsel for the respondent that the statute indicates the guideline, namely, that the Commissioner's power to notify u/s 116(3) is only in respect of things which are of the same nature as would fall within the ambit of the expression "land", as defined u/s 2(24), appears to be a classic case of post hoc ergo propter hoc. Obviously, the power given to the Commissioner under sub-section (3) of Section 116 is intended to be exercised only in a case where the plant or machinery does not fall within the ambit of the expression "land" or "building" as defined in the Act. It is only in such cases that the question of exercise of the discretion on the part of the Commissioner arises. Thus, the so-called guideline is wholly chimerical.

3. Mr. Ramesh Singh further submitted that Section 2(1)(o) was violative of Article 19(1)(g) of the Constitution of India as it gave uncontrolled discretion and arbitrary power in the hands of financial institutions/RBI to declare any entity as an NPA. He stated that under the SARFAESI Act, the borrower had a very limited right to question the proceedings and the consequences provided in the Act were drastic. Consequently, according to him, by empowering the banks/financial institutions/RBI to determine what NPA is, there had been a disastrous effect on business, profession and trade of the borrowers.

4. Mr. Ramesh Singh also submitted that RBI guidelines were contrary to Section 2(1)(o) of the SARFAESI Act. According to him, while the said Section defined NPA to mean those assets, which had in accordance with RBI guidelines become sub-standard, doubtful or loss assets; RBI guidelines defined sub-standard asset (para 4.1.1) as an asset, which had remained non-performing asset for a period of less than or equal to twelve months. In other words, it was entirely left to the whim and fancy of the banks/financial institutions/RBI as to whether they wanted to declare an account to be an NPA when it had become a sub-standard or doubtful or loss asset. He stated that no guideline had been laid or prescribed according to which the bank/financial institution had to decide whether an account is sub-standard or not. This, in his submission, gave uncanalised/uncontrolled/arbitrary power to the banks/financial institutions to decide whether an NPA became a sub-standard asset one day post becoming NPA or twelve months from the said period. Thus, he submitted that under the RBI guidelines, an account could become an NPA even without becoming a substandard asset.

5. Mr. Ramesh Singh lastly submitted that the guidelines issued by the RBI and other financial institutions like National Housing Bank with regard to sub-standard, doubtful and loss asset were not identical. He also referred to an order dated 08th July, 2013 passed by the Gujarat High Court in Special Civil Application No. 2970/2013 and the interim stay order dated 30th July, 2013 passed by the Supreme Court in SLP (Civil) No. 23094/2013.

6. To put it differently, the sheet anchor of the petitioners' submission is that:-

(i) Section 2(1)(o) of the SARFAESI Act does not define what is a substandard, doubtful or loss asset and such an essential legislative function in an uncontrollable manner has been delegated to banks/financial institutions/RBI, which is contrary to Article 19(1)(g) of the Constitution.

(ii) The impugned provision is also violative of Article 14 of the Constitution, as it undertakes classification between banks and financial institutions, which has no reasonable nexus.

(iii) RBI guidelines, as far as it defines NPA, gives power to banks to decide when and under what circumstances an account is to be declared NPA, basing on the whims and fancies of the bank, which is not only unreasonable but also arbitrary.

(iv) Under the provisions of the SARFAESI Act, the borrower has a very limited right to question the proceedings and the consequences provided in the Act are drastic.

Union of India's submissions

7. On the other hand, Mr. Rajeev Mehra, learned ASG for Union of India, stated that in the wake of the financial reforms undertaken by the Government of India based on the Narasimhan Committee Report I and II, prudential norms were introduced by the RBI to address credit monitoring process being pursued by banks and financial institutions. He contended that in order to reflect a bank's financial health in its balance-sheet and as per the recommendations made by the Committee on Financial System (Chairman Shri M. Narasimhan), the RBI had introduced, in a phased manner, prudential norms for income recognition, asset classification and provisioning for the advances portfolio of the banks.

8. He pointed out that prior to the SARFAESI Act, an asset/account was considered as an NPA based on the concept of "past due". An NPA was defined as credit in respect of which interest and/or instalment of principal had remained due for a specific period of time. He stated that the specific period had been reduced in a phased manner over a period of time.

9. Mr. Mehra stated that the SARFAESI Act introduced in the year 2002, was amended in the year 2004 and the whole concept of classification of an account as an NPA was further clarified. To elucidate the definition of an NPA in 2002 and 2004, he handed over a chart explaining the differences. The chart, for the purpose of better understanding, is reproduced here-in-below:-

10. According to him, amendment in Section 2(1)(o) of the SARFAESI Act was made in 2004 to empower the concerned regulator who was administering or regulating such an entity to lay down classification norms for an NPA. He pointed out that there were financial institutions such as Housing Finance Corporations notified by the Central Government under the SARFAESI Act, which were regulated by National Housing Bank. According to him, the NPAs of these institutions were, therefore, directed to be classified as per guidelines prescribed by National Housing Bank.

11. He pointed out that the plea of excessive delegation had not been pleaded in the writ petition. He submitted that the Parliament had not delegated any essential legislative function to RBI u/s 2(1)(o) of the SARFAESI Act. He referred to Sections 2(1)(j), (l), (o) and 13(2) of the SARFAESI Act to submit that NPA had been precisely defined and sufficient guidelines have been given to RBI to issue a Circular to classify the assets as sub-standard, doubtful and loss assets. Sections 2(1)(j), (l) and 13(2) of the SARFAESI Act are reproduced here-in-below:-

2. Definitions.--(1) In this Act, unless the context otherwise requires,--

...

(j) "default" means non-payment of any principal debt or interest thereon or any other amount payable by a borrower to any secured creditor consequent upon which the account of such borrower is classified as non-performing asset in the books of account of the secured creditor.

(l) "financial asset" means debt or receivables and includes--

(i) a claim to any debt or receivables or part thereof, whether secured or unsecured; or

(ii) any debt or receivables secured by, mortgage of, or charge on, immovable property; or

(iii) a mortgage, charge, hypothecation or pledge of movable property; or

(iv) any right or interest in the security, whether full or part underlying such debt or receivables; or

(v) any beneficial interest in property, whether movable or immovable, or in such debt, receivables, whether such interest is existing, future, accruing, conditional or contingent; or

(vi) any financial assistance;

...

13. Enforcement of security interest.-

...

(2) Where any borrower, who is under a liability to a secured creditor under a security agreement, makes any default in repayment of secured debt or any instalment thereof, and his account in respect of such debt is classified by the secured creditor as non-performing asset, then, the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within sixty days from the date of notice failing which the secured creditor shall be entitled to exercise all or any of the rights under sub-section (4).

12. In support of his submission, Mr. Mehra relied upon the judgment of the

Supreme Court in Vasantlal Maganbhai Sanjanwala Vs. The State of Bombay and Others, wherein it has been held as under:-

4....In dealing with the challenge to the vires of any statute on the ground of excessive delegation, it is, therefore, necessary to enquire whether the impugned delegation involves the delegation of an essential legislative function or power and whether the legislature has enunciated its policy and principle and given guidance to the delegate or not. In applying this test the Court has taken into account the statements in the preamble to the Act, and if the said statements afford a satisfactory basis for holding that the legislative policy and principle has been enunciated with sufficient accuracy and clarity the preamble itself has been held to satisfy the requirements of the relevant tests. In every case, it would be necessary to consider the relevant provisions of the Act in relation to the delegation made and the question as to whether the delegation is ultra vires or not will have to be decided by the application of the relevant tests.

13. Mr. Mehra also submitted that the Madras High Court in M/s. Signal Apparels Pvt. Ltd. v. Canara Bank decided on 06th July, 2010 taking into consideration Section 2(1)(o) of the SARFAESI Act as well as Clause 2.1 of the RBI guidelines had held that the action of the Bank was not arbitrary or unreasonable in declaring the assets of the defaulter as NPAs. The High Court of Madras after considering the guidelines issued by the RBI in 2004 (as applicable at that point of time) wherein an account was declared as an NPA, if the borrower had not produced any income for the secured creditor for more than 180 days (as applicable at that time) and also there was a default on the part of the borrower as provided u/s 13(2) of the SARFAESI Act, which was analogous to the facts of the present cases had found no merit to interfere with the impugned notice and was pleased to dismiss the writ petition.

14. Mr. Mehra submitted that, in any event, the present writ petitions were not maintainable as the petitioners had an alternative remedy of filing applications u/s 17(1) of the SARFAESI Act to challenge the notices issued u/s 13(4) by the respective Banks/Financial Institutions within a period of forty-five days from the date on which measures u/s 13(4) had been taken.

15. He stated that as the time for filing the securitization applications u/s 17(1) had already expired, the petitioners had filed the instant writ petitions under the garb of challenging the legality of Section 2(1)(o) of the SARFAESI Act so as to obtain a stay on the securitization measures taken by the Bank/Financial Institution and thereafter prolong the proceedings by one device or the other.

16. He lastly submitted that the present petitions were not maintainable as the Supreme Court in United Bank of India v. Satyawati Tandon, 2010 (8) SCC 117 had categorically held that when a statutory forum was created by law for redressal of grievance and that too in a fiscal statute, a writ petition should not be entertained ignoring the statutory dispensation.

Bank of Baroda/Respondent No. 2's submissions

17. Ms. Praveena Gautam, learned counsel for respondent No. 2/Bank of Baroda submitted that the present batch of writ petitions was an abuse of the process of Court. She stated that the present writ petitions had been filed by the petitioners only with an intent to delay the recovery of huge public money (Rs. 5271.98 lacs + interest) on untenable grounds.

18. She further submitted that the writ petitions were bad for non-joinder of necessary party, namely, the RBI.

19. She submitted that the reason for enactment of the SARFAESI Act was that the financial sector had been one of the key drivers of India's efforts to rapidly develop its economy and while the banking industry in India was progressively complying with the international prudential norms and accounting practices, there were certain areas in which the banking and financial sector did not have a level playing field as compared to other participants in the world financial market. She stated that prior to 2002, the legal framework relating to commercial transactions was not in tune with international commercial practices and this had resulted in slow pace of recovery of defaulting loans and mounting levels of NPAs of banks and financial institutions.

20. According to her, continuous growth of NPAs threatened repayment capacity of banks and this had an adverse impact on the financial strength of banks which, in the present era of globalisation, were required to conform to international standards. Thus, according to her, the legislature had defined an NPA to mean an asset or account receivable of a borrower, which had been classified by banks or financial institutions in terms of the RBI guidelines as sub-standard, doubtful and loss. These guidelines were issued to improve quality of assets of the banks and to recover the public money speedily. The impugned guidelines of the RBI were not to eliminate NPAs, but to restructure them.

Preamble as well as the impugned provisions and circular

21. Having heard the learned counsel for the parties at length, we are of the view that it would be worthwhile to reproduce the impugned provision of the SARFAESI Act, which reads as under:-

2. Definitions.-(1) In this Act, unless the context otherwise requires,-

...

(o) "non-performing asset" means an asset or account of a borrower, which has been classified by a bank or financial institution as sub-standard, doubtful or loss asset,-

(a) in case such bank or financial institution is administered or regulated by any authority or body established, constituted or appointed by any law for the time being in force, in accordance with the directions or guidelines relating to assets classifications issued by such authority or body;

(b) in any other case, in accordance with the directions or guidelines relating to

assets classifications issued by the Reserve Bank;

(emphasis supplied)

22. Since in the present batch of writ petitions, loans and financial facilities availed of by the petitioners are from Bank of Baroda, which is under the regulatory control of the RBI, in all these cases, Section 2(1)(o)(b) would be attracted.

23. The relevant portion of the RBI guidelines/Circular dated 01st July, 2013 with regard to NPA reads as under:-

2. DEFINITIONS

2.1 Non-performing Assets

2.1.2 A non-performing asset (NPA) is a loan or an advance where;

- i. interest and/or instalment of principal remain overdue for a period of more than 90 days in respect of a term loan,
- ii. the account remains "out of order" as indicated at paragraph 2.2. below, in respect of an Overdraft/Cash Credit (OD/CC),
- iii. the bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,
- iv. the instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops,
- v. the instalment of principal or interest thereon remains overdue for one crop season for long duration crops,
- vi. the amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitisation transaction undertaken in terms of guidelines on securitisation dated February 1, 2006.
- vii. in respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

...

4. ASSET CLASSIFICATION

4.1 Categories of NPAs

Banks are required to classify non-performing assets further into the following three categories based on the period for which the asset has remained non-performing and the realisability of the dues:

- i. Substandard Assets
- ii. Doubtful Assets

iii. Loss Assets

4.1.1 Substandard Assets

With effect from March 31, 2005, a sub-standard asset would be one, which has remained NPA for a period less than or equal to 12 months. Such an asset will have well defined credit weaknesses that jeopardise the liquidation of the debt and are characterised by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.

4.1.2 Doubtful Assets

With effect from March 31, 2005, an asset would be classified as doubtful if it has remained in the sub-standard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, -on the basis of currently known facts, conditions and values-highly questionable and improbable.

4.1.3 Loss Assets

A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

(emphasis supplied)

Purport and Object of the SARFAESI Act

24. Before we proceed to deal with the issues involved, we would like to discuss in detail the purport of the SARFAESI Act. The SARFAESI Act was enacted on the basis of the recommendations of the Narsimhan Committee I and II and ANDHYARUJINA Committee constituted by the Central Government for the purpose of examining banking sector reforms, which were to consider the need for changes in the legal system in respect of these areas. After taking into consideration the recommendations of the Narsimhan Committee(s) and ANDHYARUJINA Committee and after deliberations, the Parliament thought it fit to bring into existence the SARFAESI Act. This decision was related to strengthening the banking and financial sector in the field of recovery of its dues or facilitating securitization of financial assets of banks and financial institutions. The Act has come into existence equally with an object of rapidly developing the economy of the country by creating the effective machinery and system for the purpose of fast recovery of defaulting loans and preventing the mounting up of level of NPAs of banks and financial institutions. The Preamble of the SARFAESI Act is in the following terms:-

STATEMENT OF OBJECTS AND REASONS

The financial sector has been one of the key drivers in India's efforts to achieve success in rapidly developing its economy. While the banking industry in India is progressively complying with international prudential norms and accounting practices there are certain areas in which the banking and financial sector do not have a level playing field as compared to other participants in the financial markets in the world. There is no legal provision for facilitating securitisation of financial assets of banks and financial institutions. Further, unlike international banks the banks and financial institutions in India do not have power to take possession of securities and sell them. Our existing legal framework relating to commercial transactions has not kept pace with the changing commercial practices and financial sector reforms. This has resulted in slow pace of recovery of defaulting loans and mounting levels of non-performing assets of banks and financial institutions. Narasimham Committee I and II and Andhyarujina Committee constituted by the Central Government for the purpose of examining banking reforms have considered the need for changes in the legal system in respect of these areas. These Committees, inter alia, have suggested enactment of a new legislation for securitisation and empowering banks and financial institutions to take possession of the securities and to sell them without the intervention of the court. The provisions of the Ordinance would enable banks and financial institutions to realise long-term assets, manage problem of liquidity, asset liability mismatches and improve recovery by exercising powers to take possession of securities, sell them and reduce non-performing assets by adopting measures for recovery or reconstruction.

2. It is now proposed to replace the Ordinance by a Bill, which, inter alia, contains provisions of the Ordinance to provide for-

(h) empowering banks and financial institutions to take possession of securities given for financial assistance and sell or lease the same or take over management in the event of default, i.e. classification of the borrower's account as non-performing asset in accordance with the directions given or under guidelines issued by the Reserve Bank of India from time to time;

.....

25. As can be seen from the Statement of Objects and Reasons of the SARFAESI Act, the main purpose of the Act is to enable and empower the secured creditors to take possession of their securities and to deal with them without intervention of the Court. Through the scheme of the Act, banks and financial institutions possess more drastic powers and at the same time, the scheme of the Act also ensures to protect the borrower's interest. The SARFAESI Act is arguably the last in the set of measures that the Government has initiated over the past few years for curbing the evil of NPAs as the amnesty scheme announced for settlement, the DRT, etc. failed to provide any comprehensive solution. Now, the SARFAESI Act enables banks and financial institutions to have an identical level playing field compared with other participants in global financial markets, so as to enforce security interest with power to take possession of the securities and to sell them.

It aims at expeditious recovery of NPAs of banks and financial institutions.

Presumption in favour of constitutionality of an enactment

26. Now, we deal with the grievance of the petitioners with regard to Section 2(1) (o) of the SARFAESI Act and the RBI Circular dated 1st July 2013-whether they are violative of Articles 14 and 19(1)(g) of the Constitution of India?

27. It is trite that presumption is always in favour of the constitutionality of an enactment. The Constitution Bench of the Supreme Court in the case of *Chiranjit Lal v. The Union of India*, 1950 SCA 869, has laid down certain guidelines, which may be summarized as follows:

(1) The presumption is always in favour of the constitutionality of an enactment, since it must be assumed that the legislature understands and correctly appreciates the needs of its own people, that its experience and its discriminations are based on adequate grounds.

(2) The presumption may be rebutted in certain cases by showing that on the face of the statute, there is no classification at all and no difference peculiar to any individual or class and not applicable to any individual or class and not applicable to any other individual or class and yet the law hits only a particular individual or class.

(3) The principle of equality does not mean that every law must have universal application for all persons who are not by nature, attainment or circumstances in the same position and the varying needs of different classes of persons often require separate treatment.

(4) The principle does not take away from the State the power of classifying persons for legitimate purposes.

(5) Every classification is in some degree likely to produce some inequality and mere production of inequality is not enough.

(6) If a law deals equally with members of a well defined class, it is not obnoxious and it is not open to the charge of denial of equal protection on the ground that it has no application to other person.

(7) While reasonable classification is permissible, such classification must be based upon some real and substantial distinction bearing a reasonable and just relation to the object sought to be attained and the classification cannot be made arbitrary and without any substantial basis.

Thus, the Apex Court, in the above cited judgment, has laid down the guidelines when the classification is not discriminatory, when equality can be claimed and how a classification becomes arbitrary.

28. The Apex Court in *Municipal Corporation of the City of Ahmedabad and Others Vs. Jan Mohammed Usmanbhai and Another*, has held that "there is always a presumption in favour of constitutionality of an enactment and the

burden is upon him who attacks it to show that there has been a clear violation of the constitutional principles. The Court must presume that the legislature understands and correctly appreciates the claim of its people that its laws are directed against the problems made manifestly by experience and that its discriminations are based on adequate grounds. It must be borne in mind that the legislature is free to recognize degrees of harm and may confine its restrictions to those cases where need is deemed to be cleared and finally that in order to sustain the presumption of constitutionality, the Court may take into consideration the matters of common knowledge, matters of rapport, history of the times and may assume every set of facts which can be conceived to be existing at the time of legislation."

29. It is well settled law that unless it is found that the provision enacted results in palpably arbitrary consequences, Courts refrain from declaring the law invalid as passed by the legislature. The Supreme Court in *R.K. Garg and Others Vs. Union of India (UOI) and Others*, has held as under:-

The first rule is that there is always a presumption in favour of the constitutionality of a statute....This rule is based on the assumption, judicially recognized and accepted, that the legislature understands and correctly appreciates the needs of its own people, its laws are directed to problems made manifest by experience.

.....

Every legislation particularly in economic matters is essentially empiric and it is based on experimentation or what one may call trial and error method.... There may be crudities and inequities in complicated experimental economic legislation but on that account alone it cannot be struck down as invalid. The Courts cannot be converted into tribunals for relief from such crudities and inequities....The Court must therefore adjudge the constitutionality of such legislation by the generality of its provisions and not by its crudities or inequities or by the possibilities of abuse of any of its provisions.

The Court must defer to legislative judgment in matters relating to social and economic policies and must not interfere, unless the exercise of legislative judgment appears to be palpably arbitrary.

(emphasis supplied)

30. The constitutional vires of Sections 13, 15, 17 and 34 of the SARFAESI Act fell for consideration before the Supreme Court in *Mardia Chemicals Ltd. Vs. Union of India (UOI) and Others Etc. Etc.*, . It was contended before the Apex Court that the SARFAESI Act vested arbitrary powers in the banks without any guidelines for the exercise thereof and also without appropriate and adequate mechanism to decide the disputes relating to the correctness of the demand. While dealing with constitutionality of the impugned provisions therein, the Apex Court, with regard to Section 2(1)(o) of the Act, held that declaring an asset as

NPA is not based on the whims and fancies of bank and financial institutions but basing on the guidelines issued by the Reserve Bank of India and upheld the provisions and guidelines. The observations of the Apex Court in *Mardia Chemicals Ltd.*'s case (supra), in our opinion, provide complete answer to the contentions of learned counsel for the petitioners in this case too. The Supreme Court has held as under:-

36. In its Second Report, the Narasimham Committee observed that NPAs in 1992 were uncomfortably high for most of the public sector banks. In Chapter VIII of the Second Report, the Narasimham Committee deals about legal and legislative framework and observed:

.....

37. Next, we come to the question as to whether it is on the whims and fancies of the financial institutions to classify the assets as non-performing assets, as canvassed before us. We find it not to be so. As a matter of fact a policy has been laid down by Reserve Bank of India providing guidelines in the matter for declaring an asset to be a non-performing asset known as "RBI's prudential norms on income recognition, asset classification and provisioning--pertaining to advances" through a circular dated 30-8-2001. It is mentioned in the said circular as follows:

1.1. In line with the international practices and as per the recommendations made by the Committee on the Financial System (Chairman Shri M. Narasimham), Reserve Bank of India has introduced, in a phased manner, prudential norms for income recognition, asset classification and provisioning for the advances portfolio of the banks so as to move towards greater consistency and transparency in the published accounts.

2.1. Non-performing assets

2.1.1. An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. A "non-performing asset" (NPA) was defined as a credit facility in respect of which the interest and/or instalment of principal has remained "past due" for a specified period of time. The specified period was reduced in a phased manner as under:

2.1.2. An amount due under any credit facility is treated as "past due" when it has not been paid within 30 days from the due date. Due to the improvements in the payment and settlement systems, recovery climate, upgradation of technology in the banking system, etc. it was decided to dispense with "past due" concept, with effect from 31-3-2001. Accordingly, as from that date, a non-performing asset (NPA) shall be an advance where

(i) interest and/or instalment of principal remain overdue for a period of more than 180 days in respect of a term loan,

(ii) the account remains "out of order" for a period of more than 180 days, in

respect of an overdraft/cash credit (OD/CC),

(iii) the bill remains overdue for a period of more than 180 days in the case of bills purchased and discounted,

(iv) interest and/or instalment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purposes, and

(v) any amount to be received remains overdue for a period of more than 180 days in respect of other accounts.

4.2.2. Banks should establish appropriate internal systems to eliminate the tendency to delay or postpone the identification of NPAs, especially in respect of high-value accounts. The banks may fix a minimum cut-off point to decide what would constitute a high-value account depending upon their respective business levels. The cutoff point should be valid for the entire accounting year. Responsibility and validation levels for ensuring proper asset classification may be fixed by the banks. The system should ensure that doubts in asset classification due to any reason are settled through specified internal channels within one month from the date on which the account would have been classified as NPA as per extant guidelines.

From what is quoted above, it is quite evident that guidelines as laid down by Reserve Bank of India which are in more details but not necessary to be reproduced here, lay down the terms and conditions and circumstances in which the debt is to be classified as non-performing asset as early as possible. Therefore, we find no substance in the submission made on behalf of the petitioners that there are no guidelines for treating the debt as a non-performing asset.

(emphasis supplied)

31. In the light of the well-settled legal position as aforesaid, we are of the opinion that the submissions of learned counsel for the petitioners are founded on a fundamental misconception regarding the scope and ambit of Section 2(1)(o) of the SARFAESI Act and the Circular of the RBI dated 1st July 2013.

32. Hence, in view of the aforesaid discussion and the law laid down by the Apex Court in catena of cases with regard to constitutionality of enactments, the burden heavily lies on the person who assails the constitutionality of the provision. The petitioner could not place any convincing material to show that Section 2(1)(o) of the Act and the RBI Circular dated 1st July 2013 are unreasonable, arbitrary or otherwise repugnant to the constitutional principle. Consequently, we are of the view that the petitioners are not able to rebut the presumption of constitutionality of Section 2(1)(o) of the SARFAESI Act and the RBI Circular in question.

Constitutional limit of delegated legislation

33. The next contention of learned counsel for the petitioners is that an essential legislative function has been delegated to the banks and financial institutions. Now, we would like to deal with constitutional limit of delegated legislation and the question-whether any essential legislative function has been delegated by the legislature in the facts and circumstances of the present case?

34. In India, legislatures, consistent with their sovereign character, have been held to possess wide powers of delegation. This power is, however, subject to one important limitation. The legislature cannot delegate essential legislative functions, which consist in the determination or choosing of the legislative policy and of formally enacting that policy into a binding rule of conduct. The legislature cannot delegate "uncanalised and uncontrolled power"; the power delegated must not be "unconfined and vagrant", but must be "canalised within banks that keep it from overflowing". The "banks", that set the limits of the power delegated, are to be constructed by the legislature by declaring the policy of the law and by laying down standards for guidance of those on whom the power to execute the law is conferred. So, the delegation is valid only when the legislative policy and guidelines to implement it are adequately laid down and the delegate is only empowered to carry out the policy within the guidelines laid down by the legislature. (See: Principles of Statutory Interpretation by Justice G.P. Singh, 13th Edition 2012).

35. The question, whether any particular legislation suffers from excessive delegation, has to be decided having regard to the subject-matter, the scheme, the provisions of the statute including its preamble, and the facts and circumstances in the background of which the statute is enacted.

36. For instance, although power to tax is a well-recognised legislative power, ample latitude has been allowed to the legislature to leave to a delegatee the power to work out details of a tax policy. In upholding a power delegated to the State Government for amending the Schedule relating to exemptions in a Sales Tax Legislation, Justice Venkatarama Aiyar observed: "Now the authorities are clear that it is not unconstitutional for the legislature to leave it to the executive to determine details relating to the working of taxation laws, such as the selection of persons on whom the tax is to be laid, the rates at which it is to be charged in respect of different classes of goods, and the like." (See Pandit Banarsi Das Bhanot Vs. The State of Madhya Pradesh and Others,

37. The Supreme Court in the case of Harishankar Bagla and Another Vs. The State of Madhya Pradesh, , while sustaining the legality of Section 3 of the Essential Supplies (Temporary Powers) Act, 1946, which gave wide powers to the Central Government to make orders for regulating or prohibiting the production, supply and distribution of essential commodities, was satisfied that it laid a clear principle and offered sufficient guidance. It was held that the power conferred by the Section therein is to be exercised "for maintaining or increasing supplies of any essential commodity, or for securing their equitable distribution and availability at fair prices".

38. In fact, the Constitution Bench of the Supreme Court in *Kishan Prakash Sharma and Others etc. Vs. Union of India and Others*, succinctly laid down the test of constitutional limit of delegated legislation while holding as under:-

18....The legislatures in India have been held to possess wide power of legislation subject, however, to certain limitations such as the legislature cannot delegate essential legislative functions which consist in the determination or choosing of the legislative policy and of formally enacting that policy into a binding rule of conduct. The legislature cannot delegate uncanalised and uncontrolled power. The legislature must set the limits of the power delegated by declaring the policy of the law and by laying down standards for guidance of those on whom the power to execute the law is conferred. Thus the delegation is valid only when the legislative policy and guidelines to implement it are adequately laid down and the delegate is only empowered to carry out the policy within the guidelines laid down by the legislature. The legislature may, after laying down the legislative policy, confer discretion on an administrative agency as to the execution of the policy and leave it to the agency to work out the details within the framework of the policy. When the Constitution entrusts the duty of law-making to Parliament and the legislatures of States, it impliedly prohibits them to throw away that responsibility on the shoulders of some other authority. An area of compromise is struck that Parliament cannot work in detail the various requirements of giving effect to the enactment and, therefore, that area will be left to be filled in by the delegatee. Thus, the question is whether any particular legislation suffers from excessive delegation and in ascertaining the same, the scheme, the provisions of the statute including its preamble, and the facts and circumstances in the background of which the statute is enacted, the history of the legislation, the complexity of the problems which a modern State has to face, will have to be taken note of and if, on a liberal construction given to a statute, a legislative policy and guidelines for its execution are brought out, the statute, even if skeletal, will be upheld to be valid but this rule of liberal construction should not be carried by the court to the extent of always trying to discover a dormant or latent legislative policy to sustain an arbitrary power conferred on the executive....

(emphasis supplied)

39. Justice S.B. Sinha of the Supreme Court in *State of Rajasthan and Others Vs. Basant Nahata*, culled out the relevant case law on the constitution limitation of legislative delegation. The relevant portion of the said judgment is reproduced here-in-below:-

Delegated legislation

19. The necessity of the legislature's delegating its powers in favour of the executive is a part of legislative function. It is a constituent element of the legislative power as a whole under Article 245 of the Constitution. Such delegation of power, however, cannot be wide, uncanalised or unguided. The

legislature while delegating such power is required to lay down the criteria or standard so as to enable the delegatee to act within the framework of the statute. The principle on which the power of the legislature is to be exercised is required to be disclosed. It is also trite that essential legislative functions cannot be delegated.

20. The procedural powers are, therefore, normally left to be exercised by the executive by reason of a delegated legislation.

Law operating in the field

21. We have been taken through a large number of decisions by the learned counsel appearing on behalf of the parties beginning from Delhi Laws Act, 1912, Re In Re: The Delhi Laws Act, 1912, the Ajmer-Merwara (Extension of Laws) Act, 1947 and the Part C States (Laws) Act, 1950, to Andhra Bank Vs. B. Satyanarayana and Others, but it may not be necessary to deal therewith separately in great detail.

...

Analysis

30. There cannot be any doubt whatsoever that the court shall not invalidate a legislation on the ground of delegation of essential legislative function or on the ground of conferring unguided, uncontrolled and vague powers upon the delegate without taking into account the preamble of the Act as also other provisions of the statute in the event they provide good means of finding out the meaning of the offending statute. This aspect of the matter has been considered in some detail in People's Union for Civil Liberties and Another Vs. Union of India (UOI) and Others, and Andhra Bank Vs. B. Satyanarayana and Others, in which one of us was a member.

(emphasis supplied)

40. In Delhi Race Club Ltd. Vs. Union of India (UOI) and Others, , after revisiting the law on the issue of constitutionality of the delegated legislation, the Supreme Court held as under:-

30. From the conspectus of the views on the question of nature and extent of delegation of legislative functions by the legislature, two broad principles emerge viz.

(i) that delegation of non-essential legislative function of fixation of rate of imposts is a necessity to meet the multifarious demands of a welfare State, but while delegating such a function laying down of a clear legislative policy is prerequisite, and

(ii) while delegating the power of fixation of rate of tax, there must be in existence, inter alia, some guidance, control, safeguards and checks in the Act concerned.

It is manifest that the question of application of the second principle will not arise unless the impost is a tax. Therefore, as long as the legislative policy is defined in clear terms, which provides guidance to the delegate, such delegation of a non-essential legislative function is permissible....

(emphasis supplied)

41. Keeping in view the aforesaid legal position, we analyse the provision in question in the present cases. Section 2(1)(o) of the Act defines NPA as an asset or accountable receivable of a borrower, which has been classified by banks or financial institutions in terms of RBI guidelines as sub-standard, doubtful and loss asset. Clause 4.1 of the RBI guidelines classifies NPA into three categories-sub-standard, doubtful and loss asset. Once the account finds place in any of these categories, it becomes an NPA with respect to clause 2.1 of the RBI guidelines. Broadly speaking, the classification of assets into sub-standard, doubtful or loss asset is done taking into account the degree of well-defined credit weakness and extent of dependence on collateral securities for realisation of dues. The Legislature has left it to RBI to identify, define and classify different assets in accordance with current international best practices as well as the changing economic scenario of the country. We are of the opinion that the Legislature has clearly defined NPA u/s 2(1)(o) of the SARFAESI Act and the RBI guidelines are issued to improve quality of assets of the bank and to recover the public money speedily. There is no excessive delegation or scope for the banks to act upon basing on their whims and fancies, but they are governed by the guidelines issued by the RBI which u/s 21 of Banking Regulation Act 1949 is empowered to lay guidelines in the interest of banking policy relating to advances to be followed by the banking companies. It is settled law that in the matters of policy decisions of the Government in respect of economic matters, Courts cannot interfere unless such policy is contrary to the Constitution. In applying the test of reasonableness, the criteria is whether the law strikes a proper balance between social contract on one hand and the rights of the individual on the other hand. A famous American Supreme Court Judge, Frankfurter J. in *Secretary of Agriculture v. Central Rois Refining Co.* (94 L Ed 381)

observed:

However, though while considering economic or most other legislation, the Court gives great latitude to the legislature when adjudging its constitutionality, a very different approach has to be adopted by the Court where the question of civil liberties and the fundamental rights under Part III of the Constitution arise. ...

As regards economic and other regulatory legislation, judicial restraint must be observed by the Court and greater latitude must be given to the legislative while adjudging the constitutionality of the statute, because the court does not consist of economic or administrative experts. It has no experience in these matters and in this age of specialization, when policies have to be laid down with great care

after consulting the specialities in the field, it will be wholly unwise for the court to encroach into the domain of the executive or legislature and try to enforce its views and perception.

The Judgment of the Supreme Court of the U.S. crystallises the scope of judicial review in matters of economic and financial sector and with regard to presumption of constitutionality of the statute.

Parliament while enacting SARFAESI Act has not delegated essential legislative function; validity of Section 2(1)(o) of the SARFAESI Act and RBI Circular dated 1st July, 2013

42. In our opinion, Section 2(1)(o) of SARFAESI Act clearly defines NPA as an asset or an account which has been classified as a sub-standard, doubtful or loss asset. Consequently, the Indian Parliament while enacting SARFAESI Act has not delegated essential legislative function to the RBI/Financial Institution with regard to the concept of NPA.

43. We are also of the view that the impugned Circular issued by the RBI, which provides guidelines for determining NPAs, is in conformity with Section 2(1)(o) of the SARFAESI Act. Clause 2.1 of the RBI Circular is beneficial in nature inasmuch as even though a customer may be a defaulter on account of his failure to pay interest or repay principal in accordance with the contract, yet he would be classified as NPA only if the default continues beyond ninety days.

44. As the concepts of sub-standard, doubtful or loss asset are not static, but dynamic in nature, the Legislature has left it to the Regulators to identify, define and classify assets as sub-standard, doubtful or loss asset in accordance with current international best practices as well as the changing economic scenario of the country.

45. Consequently, the legislative policy and guideline has been laid down by the Parliament and the Regulator (be it the RBI or a Financial Institution) is only empowered to carry out that policy within the guideline laid down by the Parliament.

46. True, the guidelines issued by the RBI and other financial institutions like National Housing Bank are not identical, but, in our opinion, the power to issue guidelines has been rightly vested in the regulator of that particular institution as the said regulator would understand the need of that institution. There can be no quibble over the proposition that if the differentiation is rational, having regard to the objects sought to be achieved, then such differentiation is not discriminatory. Article 14 only forbids unreasonable classification. The burden lies on the petitioners to show that what has been done is irrational and unreasonable. Nothing has been placed before us to show that the classification is irrational or unreasonable. In any event, the classification between different banks and financial institutions is founded on an intelligible differentia and the said differentia has a rational relation to the object sought to be achieved.

47. A reading of the RBI Circular dated 01st July 2013 makes it amply clear that every NPA would fall either in the category of sub-standard or doubtful or loss asset. Thus, the submission of learned counsel for the petitioners that a sub-standard asset may not fall in the definition of NPA is not correct as in all cases where there has been default in repayment of interest and/or principal beyond ninety days, the account would be a substandard account and would also be covered by the definition of NPA.

48. We are also of the view that there is no discretion vested with the Bank u/s 2(1)(o) of SARFAESI Act to pick and choose an account as an NPA at its own whim and fancy. In declaring an account as an NPA, the Banks have to act in accordance with the provisions of the Act and the various Circulars/Guidelines issued by the RBI.

49. Moreover, if the borrower is aggrieved by the action taken by the Banks under Sections 2(1)(o) and 13(4) of the SARFAESI Act, the same can be challenged before the Debt Recovery Tribunal u/s 17 of the SARFAESI Act. Consequently, Section 2(1)(o) of SARFAESI Act is neither unreasonable nor violative of Articles 14 and 19(1)(g) of the Constitution, as alleged by the petitioners.

RBI's directives and guidelines have statutory flavour

50. Also, the RBI's directives and guidelines have statutory flavour and consequently, the Banks have to abide by them. The Supreme Court in ICICI Bank Limited Vs. Official Liquidator of APS Star Industries Ltd. and Others, with regard to the previous NPA issued by the RBI has held as under:-

41. At the outset one needs to know what is NPA? When a borrower who is under liability to pay to secured creditors, makes default in repayment of secured debt or any instalment thereof, the account of borrower is classified as non-performing asset (NPA). Such NPAs cannot be used for any productive purpose. Continuous growth in NPAs threatens the repayment capacity of the banks. They have an adverse impact on the financial strength of the banks which in the present era of globalisation are required to conform to international standards. Thus, NPA means an asset or account receivable of a borrower, which has been classified by banks or financial institutions in terms of the RBI Guidelines as substandard, doubtful etc. These guidelines are issued to improve quality of assets of the banks. The 2005 Guidelines of RBI are not to eliminate NPAs but to restructure.

42. The BR Act, 1949 vide Section 21 empowers RBI in the interest of the banking policy to lay down guidelines in relation to advances to be followed by the banking companies. The 2005 Guidelines have been issued as "a restructuring measure" in order to avoid setbacks in the banking system. NPAs do not generate interest. 85% of the Indian banks' income comes from interest. Thus, NPAs adversely impact profits of the banks and hence, as a matter of banking policy, RBI as regulator seeks through its guidelines u/s 21 read with

Section 35-A to manage these NPAs and not to eliminate them. The said guidelines deal with restructuring of the banking system which is one of the objects behind giving authority to RBI to frame "banking policy.

(emphasis supplied)

In fiscal matters and/or where discretion is conferred on high ranking statutory authorities, Courts don't ordinarily interfere in exercise of power of judicial review

51. This Court in reaching the aforesaid conclusions has kept in mind that the statutes dealing in fiscal matters and/or where discretion is conferred on high ranking statutory authorities like the RBI, should not ordinarily be interfered with in exercise of power of judicial review.

52. The judgment of Krishna Mohan (P) Ltd.'s case (supra), referred to by learned counsel for petitioners, is clearly inapplicable to the facts of the present cases, as in the said case, the Court had held that there was hardly any distinction between the situation envisaged by the Supreme Court in *New Manek Chowk Spinning and Weaving Mills Co. Ltd. and Others Vs. Municipal Corporation of The City of Ahmedabad and Others*, and the one before them in that case. The vice discovered by the Supreme Court in Rule 7(2) framed under the BPMC Act, 1949 equally affected Section 116(3) of the DMC Act. The order of the Gujarat High Court and the interim order passed by the Supreme Court offer no assistance to the petitioners as in the said petitions, the constitutionality of Section 2(1)(o) was not challenged. From a reading of the Gujarat High Court order dated 08th July, 2013, it transpires that the guidelines issued by the regulator of a group of financial institutions has been challenged being arbitrary, discriminatory and violative of Article 14 of the Constitution.

Conclusion

53. In view of the aforesaid elaborate discussion, we are of the considered view that Section 2(1)(o) of the SARFAESI Act and the RBI Circular dated 1st July 2013 are perfectly legal, valid and are not violative of Articles 14 and 19(1)(g) of the Constitution of India. Accordingly, the present batch of writ petitions as well as all pending applications are dismissed, but with no order as to costs.