
(2009) 05 DEL CK 0096
In the Delhi High Court
Case No : Writ Petition (C) 7036 of 2007

Sudarshan Overseas Ltd.

APPELLANT

Vs

Reserve Bank of India and Another

RESPONDENT

Date of Decision : 28-05-2009

Acts Referred:

Income Tax Act, 1961 — Section 132

State Financial Corporations Act, 1951 — Section 32G

Citation : (2009) 160 DLT 77 : (2010) 7 RCR(Civil) 519

Hon'ble Judges : Sanjiv Khanna, J

Bench : Single Bench

Advocate : Aniruddh Chaudhary, for the Appellant; H.L. Tikku, Yashmeet Kaur and H.S. Parihar, for the Respondent

Judgement

Sanjiv Khanna, J.—The petitioner M/s. Sudarshan Over Seas Limited has filed the present writ petition for following reliefs:

In view of the above it is most respectfully prayed as under:

- a) To issue a writ of mandamus or any other Order or directions against the Reserve Bank of India directing them to set aside the Master Circular dated 2.7.07 and declare the same as ultra vires the Constitution
- b) To issue a writ of mandamus or any other Order or directions against the Reserve bank of India directing them not to enlist the Petitioner in the Willful Defaulter List at the instance of the Respondent No. 2.
- c) To issue an appropriate writ and direction against the Respondent No. 2, not to issue any correspondence to the customers of the Petitioner alleging that the Petitioner is a willful defaulter.
- d) Pass any other Order (s)/ direction (s) as this Hon''ble Court may deem fit and proper under the facts and circumstances of the case.

2. Standard Chartered Bank is respondent No. 2 to the present writ petition and

had reported to the Reserve Bank of India respondent No. 1 that in the quarter ending on 30th June, 2007, the petitioner had been declared a willful defaulter. A similar letter was also addressed to Credit Information Bureau (India) Ltd. (CIBIL for short). It is, however, now admitted that the said letter stands withdrawn by respondent No. 2 without prejudice to their rights and contentions to address in future a similar letter to CIBIL. Counsel for the petitioner submits that as the letter written by respondent No. 2 Standard Chartered Bank is withdrawn, the writ petition to this extent is rendered infructuous. He however submits that in case respondent No. 2 on any occasion in future categorizes the petitioner as a willful defaulter, they will be entitled to challenge and question the same. The writ petition in respect of prayers B and C is rendered infructuous and the prayers are not required to be examined in the present case. It is clarified that the legal contentions raised by the parties in respect of prayers B and C are left open.

3. In prayer A the petitioner has questioned the constitutional validity of the Master Circular dated 2nd July, 2007 issued by the respondent No. 1, Reserve Bank of India, on the ground that no one WPC No. 7036/2009 Page 3 can be a judge of his own cause (*Nemo Debet Esse Judex in Propria Sua Causa*) and has submitted that the Master Circular, which permits the lender bank to declare a borrower a willful defaulter, violates the said principle.

4. The Master Circular dated 2nd July, 2007 is in respect of willful defaulters and issues instructions in matters relating to willful defaulters. The said circular was prepared to ensure that all existing instructions on the subject are incorporated and consolidated in a single document and available at the website maintained by the Reserve Bank of India. The Master Circular also spells out the purpose of having a category of willful defaulters. It is stated that in 1999 a scheme was introduced by the Reserve Bank of India under which all banks and notified all India financial institutions were required to give details of willful defaulters of outstanding of Rs. 25 lacs or above. This was pursuant to instructions issued by Central Vigilance Commission. The Circular seeks to prescribe norms for declaring a borrower a willful defaulter, measures required to be taken against a willful defaulter and roles and responsibilities of an audit and inspecting team that deals with such accounts.

5. The circular, states that after introduction of the 1999 Circular, the banks and financial institutions were required to report the cases of default which were detected after 31st March, 1999 on quarterly basis. It was observed that there was another scheme of disclosure of information on Defaulting Borrowers of the Banks and FIs.

6. The need and necessity to issue the circular is explained in the Master Circular for the following reasons:

This circular prescribed the norms for declaring an individual borrower a willful defaulter, penal measures that can be taken against a willful defaulter, roles and

responsibilities of a audit and inspecting teams while they deal with such accounts and a mechanism by which the grievance can be addressed if any party feels aggrieved on account of inclusion of its name in the willful defaulters list. The circular also deals with the criminal action that a bank can take against the willful defaulters and precautions a bank can take in this regard before giving credit facilities to the borrowers.

7. After noticing the working of the earlier schemes, in Clause 2.1, the term "willful default" has been redefined in supersession of the earlier definition as under:

A "willful default" would be deemed to have occurred if any of the following events is noted:

(a) The unit has defaulted in meeting its payment/ repayment obligations to the lender even when it has the capacity to honour the said obligations

(b) The unit has defaulted in meeting its payment/ repayment obligations to the lender and has not utilized the finance from the lender for the specific purposes for which finance was availed of but has diverted the funds for other purposes.

(c) The unit has defaulted in meeting its payment/ repayment obligations to the lender and has siphoned off the funds so that the funds have not been utilized for the specific purpose for which finance was availed of, nor are the funds available with the unit in the form of other assets.

8. The terms "diversion" and "siphoning of funds" have also been defined in the said Master Circular. The Circular explains the term "cut of limit for use of funds" and stipulates the "penal measures" which are required to be taken to prevent the access to the capital markets by the willful defaulters. The Master Circular enumerates the ?penal measures? which can be initiated by a bank against willful defaulters. The said penal measures read as under:

The following measures should be initiated by the banks and FIs against the willful defaulters identified as per the definition indicated at paragraph 2.1 above;

a) No additional facilities should be granted by any bank/ FI to the listed willful defaulters. In addition, the entrepreneurs/ promoters of companies where banks/ FIs have identified siphoning/ diversion of funds, misrepresentation, falsification of accounts and fraudulent transactions should be debarred from institutional finance from the scheduled commercial banks, Development Financial Institutions, Government owned NBFCs, investment institutions etc. for floating new ventures for a period of 5 years from the date the name of the willful defaulter is published in the list of willful defaulters by the RBI.

b) The legal process, wherever warranted, against the borrowers/ guarantors and foreclosure of recovery of dues should be initiated expeditiously. The lenders may initiate criminal proceedings against willful defaulters, wherever necessary.

c) Wherever possible, the banks and FIs should adopt a proactive approach for a

change of management of the willfully defaulting borrower unit.

d) A covenant in the loan agreements, with the companies in which the banks/ notified FIs have significant stake, should be incorporated by the banks/ FIs to the effect that the borrowing company should not induct a person who is a promoter or director on the Board of a company which has been identified as a willful defaulter as per the definition at paragraph 2.1 above and that in case, such a person is found to be on the Board of the borrower company, it would take expeditious and effective steps for removal of the person from its Board.

9. Immediately after mentioning the penal measures in the Master Circular it is mentioned that it would be imperative on the part of the banks and financial institutions to put in place a transparent mechanism for the entire process so that the ?penal provisions? are not misused and the scope of such discretionary powers are kept to the barest minimum.

10. To ensure that the identification of willful defaulter is transparent and objective so as not to cause inconvenience to borrowers, the Master Circular in Clause 3 has set out grievances redressal mechanism. The said clause reads as under:

3. Grievances Redressal Mechanism

Banks/FIs should take the following measures in identifying and reporting instance of willful default:

(i) With a view to imparting more objectivity in identifying cases of willful default, decisions to classify the borrower as willful defaulter should be entrusted to a Committee of higher functionaries headed by the Executive Director and consisting of two GMs/DGMs as decided by the Board of the concerned bank/ FI.

(ii) The decision taken on classification of willful defaulters should be well documented and supported by requisite evidence. The decision should clearly spell out the reasons for which the borrower has been declared as willful defaulter vis-?-vis RBI guidelines.

(iii) The borrower should thereafter be suitably advised about the proposal to classify him as willful defaulter along with the reasons therefor. The concerned borrower should be provided reasonable time (say 15 days) for making representation against such decision, if he so desires, to a Committee headed by the Chairman and Managing Director.

(iv) A final declaration as "Willful defaulter" should be made after a view is taken by the Committee on the representation and the borrower should be suitably advised.

11. A bare perusal of the aforesaid clause indicates that safeguards have been provided to protect the borrowers by ensuring that the decision to classify a borrower as a willful defaulter is entrusted to a Committee, which is headed by the Executive Director of the concerned bank/financial institution. Before a

borrower is classified as a willful defaulter, he is required to be issued notice along with the documents and other evidence. The borrower is to be provided with reasonable time to make representation against the proposed action. Thereafter decision has to be taken whether a borrower is to be declared as a willful defaulter and the borrower is to be informed. Thus there are number of stipulations and safeguards in the said Master circular to protect the interest of the borrowers.

12. The object and purpose behind issuing the Master Circular is obvious and the desire to maintain a list of willful defaulters as defined is perse justified. One scheme or other in this regard has existed from 1994. The Master Circular has been issued to remove loopholes and rectify defects and problems noticed in the past. It is a policy decision, which has been taken after careful thought, past experience, problems faced by the banks and financial institutions. The foundation of the scheme is explained in the Mater Circular as:

2. Guidelines issued on Wilful defaulters (May 30, 2002)

Considering the concerns expressed over the persistence of willful default in the financial system in the 8th Report of the Parliament's Standing Committee on Finance on Financial Institutions, the Reserve Bank of India, in consultation with the Government of India constituted in May 2001 a working group on Willful Defaulters (WGWD) under the Chairmanship of Shri S.S. Kohli, the then Chairman of the Indian Banks' Association, for examining some of the recommendations of the committee. The group submitted its report in November 2001. The recommendations of WGWD were further examined by an In House Working Group constituted by the Reserve Bank. Accordingly, the banks/FIs were advised in May 30, 2002 for implementation, with immediate effect, as under.

13. A borrower who is a willful defaulter can otherwise go to different banks or financial institution and obtain loans. Past conduct of willful default by way of diversion and siphoning of funds etc. is always a relevant consideration for deciding whether or not additional funds/facilities should be granted. Past conduct as a willful defaulter should be in the knowledge of bank/financial institutions advancing the money. The Master Circular obviously has a laudatory purpose behind it and cannot be rejected. Clauses of the Master Circular quoted above disclose that the Reserve Bank of India has after careful and due consideration defined the terms "willful default" and "diversion" and "siphoning of funds". It has also taken care to prescribe a detailed procedure, which requires issue of notice with documents and evidence and a speaking order after considering the representation made by the borrower before he is declared a willful defaulter. The Master Circular was introduced by the Government and Reserve Bank of India to deal with the problem of non-performing assets and with losses caused to the financial institutions/banks. It will be appropriate to refer to the observations made by the Supreme Court in *Mardia Chemicals Ltd. Vs. Union of India (UOI) and Others Etc. Etc.*, upholding the constitutional validity of Securitization and Reconstruction of Financial Assets and Enforcement

of Security Interest Act, 2002. In the said judgment, the problem faced by the banks and financial institutions due to non-recovery of dues in spite of existing laws was considered. Reports given by various committees were examined and it is observed:

34. Some facts which need to be taken note of are that the banks and the financial institutions have heavily financed the petitioners and other industries. It is also a fact that a large sum of amount remains unrecovered. Normal process of recovery of debts through courts is lengthy and time taken is not suited for recovery of such dues. For financial assistance rendered to the industries by the financial institutions, financial liquidity is essential failing which there is a blockade of large sums of amounts creating circumstances which retard the economic progress followed by a large number of other consequential ill effects. Considering all these circumstances, the Recovery of Debts Due to Banks and Financial Institutions Act was enacted in 1993 but as the figures show it also did not bring the desired results. Though it is submitted on behalf of the petitioners that it so happened due to inaction on the part of the Governments in creating Debts Recovery Tribunals and appointing presiding officers, for a long time. Even after leaving that margin, it is to be noted that things in the spheres concerned are desired to move faster. In the present-day global economy it may be difficult to stick to old and conventional methods of financing and recovery of dues. Hence, in our view, it cannot be said that a step taken towards securitisation of the debts and to evolve means for faster recovery of NPAs was not called for or that it was superimposition of undesired law since one legislation was already operating in the field, namely, the Recovery of Debts Due to Banks and Financial Institutions Act. It is also to be noted that the idea has not erupted abruptly to resort to such a legislation. It appears that a thought was given to the problems and the Narasimham Committee was constituted which recommended for such a legislation keeping in view the changing times and economic situation whereafter yet another Expert Committee was constituted, then alone the impugned law was enacted. Liquidity of finances and flow of money is essential for any healthy and growth-oriented economy. But certainly, what must be kept in mind is that the law should not be in derogation of the rights which are guaranteed to the people under the Constitution. The procedure should also be fair, reasonable and valid, though it may vary looking to the different situations needed to be tackled and object sought to be achieved.

14. In the said judgment, the Court also observed that in financial policy matters there is limited and minimal scope for interference by courts and the courts should examine the question by generalities and not crudities or inequities or by possibility of abuse of provision. The Reserve Bank of India by issuing the said Circular has taken positive steps to protect the interests of the banks and financial institutions and ensure that a list of willful defaulters is known and made available for other banks and financial institutions. The said purpose cannot be said to be an arbitrary and unjustified.

15. Mere categorization as a willful defaulter does not entitle the bank/financial institution to immediately recover their due from the said borrower. Proceedings in accordance with law have to be initiated and thereupon recovery has to be effected. The order passed by the banks or financial institutions declaring a borrower a willful defaulter is an administrative or a quasi judicial order. The Doctrine that no man can be a judge in his own cause has its limitation specially when doctrine of necessity is applicable. Some relaxation and exception have been carved out by applying doctrine of necessity. As held by Frank J. of the United State of Linahan, Inere:

If, however, "bias" and "partiality" be defined to mean the total absence of preconceptions in the mind of the judge, then no one has ever had a fair trial, and no one ever will. The human mind, even at infancy, is no blank piece of paper. We are born with predispositions and the processes of education, formal and informal, create attitudes which precede reasoning in particular instances and which, therefore, by definition, are prejudices.

16. Recently, in the case of Union of India (UOI) and Others Vs. Vipin Kumar Jain and Others, the Supreme Court has held that an officer who has carried out search u/s 132 of the Income Tax Act, 1961 is competent to act as an assessing officer and there is no inherent unconstitutional in permitting the assessing officer to gather information and assess the value of the information himself. While rejecting the above contention the Supreme Court referred to decision of the U.S. Supreme Court in the case of Harold Withrow versus Duane Larken 43 L.ED.2 712 and has been opined:

Even though it could be said that in a sense since the Assessing Officer was acting on behalf of the Revenue, in discharging the functions as an Assessing Officer, he was a party to the dispute, nevertheless there is no presumption of bias in such a situation. As said in H.C. Narayanappa v. State of Mysore SCR at p 753:

It is also true that the Government on whom the duty to decide the dispute rests, is substantially a party to the dispute but if the Government or the authority to whom the power is delegated acts judicially in approving or modifying the scheme, the approval or modification is not open to challenge on a presumption of bias. The Minister or the officer of the Government who is invested with the power to hear objections to the scheme is acting in his official capacity and unless there is reliable evidence to show that he is biased, his decision will not be liable to be called in question, merely because he is a limb of the Government.

There is nothing inherently unconstitutional in permitting the assessing officer to gather the information and to assess the value of the information himself. The issue as to the constitutional validity of a provision which permitted an examining board not only to hold an inquiry but also to take action against doctors was raised before the Supreme Court of the United States in Harold Withrow v. Duane

Larkin. In negating the challenge the Court said: (US p.47)

The contention that the combination of investigative and adjudicative functions necessarily creates an unconstitutional risk of bias in administrative adjudication has a much more difficult burden of persuasion to carry. It must overcome a presumption of honesty and integrity in those serving as adjudicators; and it must convince that, under a realistic appraisal of psychological tendencies and human weakness, conferring investigative and adjudicative powers on the same individual poses such a risk of actual bias or prejudgment that the practice must be forbidden if the guarantee of due process is to be adequately implemented.

It is true that there may be cases where the outcome of the assessment may be influenced by the fact that the raiding Assessing Officer had himself in the course of the raid been witness to any incriminating material against the assessee. The Assessing Officer's decision on the basis of such material is not the final word in the matter. The assessment order is appealable under the provisions of the statute itself and ultimately by way of judicial review.

18. In *Delhi Fin. Corpn. and Another Vs. Rajiv Anand and Others*, , the Supreme Court examined the said principle, with reference to Section 32-G of the State Financial Corporation Act, 1951, as the State Government had appointed the Managing Director of the State Financial Corporation as the authority to adjudicate the claims of the State Financial Corporation and issue certificates of recovery. In *Delhi Financial Corporation case (Supra)* after referring to the several case laws on the subject, it was held as under:

9. Faced with this authority, it was submitted that the observations made by the Constitution Bench are per incuriam inasmuch as this authority has not taken note of the judgment in *Gullapalli Nageswara Rao case*. We are unable to accept this submission. It is to be seen that there is a big difference in the facts of the two cases. The doctrine that "no man can be a judge in his own cause" can be applied only to cases where the person concerned has a personal interest or has himself already done some act or taken a decision in the matter concerned. Merely because an officer of a corporation is named to be the authority, does not by itself bring into operation the doctrine "no man can be a judge in his own cause". Of course, in individual cases bias may be shown against a particular officer but in the absence of any proof of personal bias or connection merely because officers of a particular corporation are named as the authority does not mean that those officers would be biased. As has been held by the Constitution Bench, a Managing Director is a high-ranking officer. He is not personally interested in the transaction. There is no question of any bias or conflict between his interest and his duty. In *Gullapalli Nageswara Rao case* the Secretary who had framed the Scheme then proceeded to hear the objections and advise the Chief Minister. It is because of the personal involvement of the Secretary that the majority took the view. Even then two Judges held that it did not follow that he was an improper person to hear the objections.

14. Thus, the authorities disclose that mere appointment of an officer of the corporation does not by itself bring into play the doctrine that 'no man can be a judge in his own cause'. For that doctrine to come into play it must be shown that the officer concerned has a personal bias or a personal interest or has personally acted in the matter concerned and/or has already taken a decision one way or the other which he may be interested in supporting. This being the law it will have to be held that the decision of the Delhi High Court is erroneous and cannot be sustained and the view taken by the Punjab and Haryana High Court is correct. It will, therefore, have to be held that Managing Director of a financial corporation can be appointed as an authority u/s 32-G of the Act.

19. State Financial Corporation are a Public Sector Undertaking; where as the second respondent is a Private bank. However, in the present case no adjudication order for recovery is being made. Banks and financial institutions are required to follow the guidelines of Master Circular introduced by the Reserve Bank of India before declaring a borrower a willful defaulter and communication has to be sent to the borrower. In case of violation, complaint to Reserve Bank of India can be made. Action to declare a borrower as willful defaulter is an internal action of the bank in question and declaration to the same effect is required to be made after giving hearing and right to representation. The borrower is also entitled to receive documents and evidence relied upon by the bank/financial institution. The Master Circular has taken precaution to ensure that genuine borrowers or others, who have committed defaults in making the payment of money are not categorized as willful defaulters. In case of wrong classification, aggrieved person can move to Court or approach Reserve Bank of India in case there is breach of the conditions mentioned in the Master Circular.

20. In these circumstances, I do not find any merit in the contention of the petitioner that the Master Circular dated 2nd July, 2007 is constitutionally invalid. To this extent the petition is dismissed. No order as to costs.