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IN THE HIGH COURT AT CALCUTTA
Constitutional Writ Jurisdiction
ORIGINAL SIDE

Present:
The Hon'ble JUSTICE MOUSHUMI BHATTACHARYA

I.A.No.G.A.1 of 2020
With
(Old G.A.1062 of 2020)
With
W.P.O.236 of 2020

Sandip Kumar Bajaj & Anr.
Vs.
State Bank of India & Anr.

For the Petitioners	:	Mr. Sabyasachi Chowdhury, Sr. Adv. Ms. Sanjukta Ray, Adv.
For the Respondents	:	Mr. Om Narayan Rai, Adv.
Last Heard on	:	04.09.2020.
Delivered on	:	15.09.2020.

Moushumi Bhattacharya, J.

1. The challenge in this writ petition is to a notice issued by the respondent State Bank of India to the petitioners by which the petitioners have been called upon to show cause and make submissions in writing within 30 days from the date of receipt of the notice as to why their names

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should not be included in the list of wilful defaulters as per the Reserve Bank of India (RBI) Guidelines. The Show Cause Notice dated 14th November, 2019 was followed by correspondence between the parties culminating in a notice for personal hearing dated 6th August, 2020 by which the petitioners were called upon to personally appear before the Wilful Defaulter Identification Committee on 24th August, 2020 at a specific time. Both these notices have been challenged in this writ petition and the petitioners seek cancellation of these notices.

2. The petitioners claim to be the erstwhile promoters/directors of Mohan Motors Udyog Private Limited (the Company) which is presently in a Corporate Insolvency Resolution Process (CIRP) under the relevant provisions of The Insolvency and Bankruptcy Code 2016 (IBC). The insolvency proceedings commenced on 17th March, 2020 by an order of the National Company Law Tribunal, Kolkata Bench.

3. The contentions of Mr. Sabyasachi Chowdhury, learned counsel appearing for the petitioners, are two-fold. Counsel submits that by reason of the moratorium under section 14 of the IBC being operational in respect of the Company, proceedings under the master circular of the RBI for being declared as wilful defaulters should be stayed during the operation of the moratorium period. The second limb of Mr. Chowdhury's argument is that the impugned Show Cause Notice dated 14th November, 2019 and the notice of hearing dated 6th August, 2020 are bad by reason of the fact that they have not been issued by the committee which is empowered to do so under

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the RBI Master Circular on Wilful Defaulters, 2015. Counsel submits that a notice was initially given on 13th September, 2019 on an "appropriate committee" examining the conduct of the account of the Company and concluding that a wilful default has been committed. The notice had the heading "Gujarat NRE Coke Ltd". On the mistake being pointed out to the Bank by the Company by its letter dated 31st October, 2019, the respondent no. 1 (State Bank of India) issued a fresh notice dated 14th November, 2019 which is the impugned notice in this case. Counsel submits that the notice does not disclose the particulars of the "appropriate committee" which has allegedly examined the conduct of the account and the credit facilities of the Company and also fails to disclose the particulars of the alleged meeting where the conduct of the Company has been examined. It is submitted that the notices do not disclose the satisfaction of the Identification Committee and is not in consonance with the relevant clause of the RBI circular. Counsel relies on *Atlantic Projects Limited versus Allahabad Bank*, a decision of a learned Single Judge of this court in W.P. No. 7471 (W) of 2019 where the court held that the requirement of clause 3(b) of the Master Circular must be discharged by the Identification Committee before a show-cause notice can be issued. According to counsel, *Atlantic Projects* held that clause 3(b) requires application of mind by the Identification Committee "at all stages" before a show-cause notice can be issued on a defaulting borrower.

4. Mr. Om Narayan Rai, learned counsel appearing for the respondents/SBI and its Deputy General Manager, relies on a Division Bench judgment of this Court in CAN 5340 of 2019 in MAT 787 of 2019:

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Union Bank of India versus Sudhir Kumar Patodia/Pawan Kumar Patodia, which, according to counsel, has overruled the Single Bench decision in *Atlantic Projects* by implication. Counsel submits that the Division Bench held that even if the power to issue a show cause notice has been delegated, the notice itself would not be invalidated. It is also argued that the petitioners have not pleaded any prejudice consequent to issue of the show cause notice and the challenge thereto must therefore fail. Counsel points to the delay in filing of the writ petition as the impugned notice is dated 14th November, 2019. Counsel raises the additional point of ratifying an act subsequent to its commission in that the show cause notice can be approved anytime by the Identification Committee. In this connection, *Maharashtra State Mining Corporation versus Sunil:* (2006) 5 SCC 96 and *National Institute of Technology versus Pannalal Choudhury*: (2015) 11 SCC 669 are relied on.

5. I have considered the contentions urged on behalf of the parties. But first, a brief explainer on the RBI guidelines contained in the Master Circular. The scheme framed by the RBI was to identify events of wilful default by borrowers where the particular unit has defaulted in its payment obligations to the lender despite having a capacity to pay or has diverted the borrowed funds for some other purpose other than the specific purpose for which the funds were made available. The scheme evolved a mechanism of identifying such defaults by various methods of monitoring and prevention. The first point in this writ petition is whether the Company and the petitioners can be subjected to proceedings for identification of Wilful

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Defaulters under the RBI Master Circular, 2015 in the face of the ongoing CIRP under the Insolvency and Bankruptcy Code, 2016. Section 14 of the IBC is relevant. Paragraph 1 of the writ petition describes the petitioners as the erstwhile directors as well as the erstwhile promoters and guarantors of the Company, Mohan Motor Udyog Private Limited, which is presently undergoing CIRP by virtue of an order dated 17th March, 2020 passed by the NCLT, Kolkata Bench. By the said order, Moratorium was declared for the purposes as referred to under Section 14 of the IBC. The order of Moratorium is to remain effective from the date of admission till the completion of the CIRP.

6. The second issue is validity of the impugned Show-Cause Notice on the ground that the said notice does not comply with the RBI guidelines relating to wilful defaults by an entity as expressed in the Master Circular which is binding on the respondent Bank. According to the petitioner, the impugned show-cause notice belies not only the formation and constitution of the "Committee" under clause 3(a) of the Master Circular but also sub-clause (b) which requires formation of opinion by the Committee before a show-cause notice is issued to the intended party.

7. I will first deal with the preliminary issue which is that any proceedings initiated against the petitioners as guarantors of the Company would meet a roadblock in the form of section 14 of the IBC under which Moratorium has been declared against the Company. The argument sought to be urged on behalf of the petitioners is that after declaration of the

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Moratorium on 17th March, 2020, subjecting the petitioners to initiation of proceedings under the Master Circular by way of the impugned Show-Cause Notice issued subsequent to the declaration of Moratorium would be contrary to the provisions of the IBC. For testing the strength of this submission, the relevant part of section 14 of the IBC is required to be set out;

"***14. Moratorium.*** *– (1) Subject to provisions of sub-sections (2) and (3), on the insolvency commencement date, the Adjudicating Authority shall by order declare moratorium for prohibiting all of the following, namely :-*

(a) the institution of suits or continuation of pending suits or proceedings against the corporate debtor including execution of any judgment, decree or order in any Court of law, tribunal, arbitration panel or other authority;

……………………………

(3) The provisions of sub-section (1) shall not apply to –

(a) such transaction as may be notified by the Central Government in consultation with any financial regulator;

(b) a surety in a contract of guarantee to a corporate debtor.

(4) The order of moratorium shall have effect from the date of such order till the completion of the corporate insolvency resolution process:

Provided that where at any time during the corporate insolvency resolution period, if the Adjudicating Authority approves the resolution plan under sub-section 1 of section 31 or passes an order liquidation of corporate debtor under Section 33, the moratorium shall cease to have effect from the date of such approval or liquidation order as the case may be."

It is clear from section 14(3)(b) that the prohibition on institution or continuation of suits and other proceedings against the corporate debtor do not extend to a surety. It is undisputed that both the petitioners are erstwhile guarantors of the Company, namely, the corporate debtor. Since

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counsel for the petitioners has also relied on sections 29-A and 31 of the IBC, these provisions should also be seen in the context of what the petitioners seek. Section 29-A (Persons not eligible to be Resolution Applicant) lists the categories of persons who are not eligible to submit a resolution plan and includes a wilful defaulter under the RBI guidelines (clause (b)) as well as "a connected person" enumerated under clause (j) including a promoter of the resolution applicant (the Company in this case). Against these provisions, the case sought to be made out on behalf of the petitioners is that the petitioners would altogether be excluded from participating in the resolution process despite being inextricably linked to the fate of the corporate debtor. In other words, the petitioners would suffer a double-whammy as it were and be left to fend for themselves even when a moratorium is declared under section 14 while being deprived of the fruits of a successful resolution process. However attractive this argument may be in the context of the apparent unfair treatment meted out to promoters of a corporate debtor, section 128 of the Indian Contract Act, 1872 must be kept in mind where the liability of the surety is co-extensive with that of the principal debtor unless the contract provides to the contrary. This also finds place in clause 2.6 of the Master Circular which is extracted below:

"2.6 Guarantees furnished by individuals, groups companies & non-group companies

While dealing with wilful default of a single borrowing company in a Group, the banks / FIs should consider the track record of the individual Company, with reference to its repayment performance to its lenders. However, in cases where guarantees furnished by the companies within the Group on behalf of the wilfully defaulting units are not honoured when invoked by the banks / FIs, such Group companies should also be reckoned as wilful defaulters.

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In connection with the guarantors, in terms of Section 128 of the Indian Contract Act, 1872, the liability of the surety is co-extensive with that of the principal debtor unless it is otherwise provided by the contract. Therefore, when a default is made in making repayment by the principal debtor, the banker will be able to proceed against the guarantor / surety even without exhausting the remedies against the principal debtor. As such, where a banker has made a claim on the guarantor on account of the default made by the principal debtor, the liability of the guarantor is immediate. In case the said guarantor refuses to comply with the demand made by the creditor / banker, despite having sufficient means to make payment of the dues, such guarantor would also be treated as a wilful defaulter. This treatment of non-group corporate and individual guarantors was made applicable with effect from September 9, 2014 and not to cases where guarantees were taken prior to this date. Banks/FIs may ensure that this position is made known to all guarantors at the time of accepting guarantees."

8. Hence the argument that section 29-A or 31 would provide a shield against the operation of section 14(3)(b) and that the petitioners would come under the immunity-blanket of section 14 is contrary to the law governing insolvency resolution process and the RBI guidelines for dealing with wilful defaults of corporate entities. Although *State Bank of India vs. Jah Developers (P) Ltd. (2019) 6 SCC 787* threw a light on the harsh consequences of being declared a wilful defaulter, it was a decision on whether legal representation can be permitted before a declaration of wilful default is made. The Supreme Court held that the proceedings under the Master Circular, being essentially in the nature of in-house proceedings and of an administrative character, cannot permit legal representation.

9. The next issue urged is that the Show Cause Notice is against the mandate of the Master Circular in terms of the composition/constitution of the Committee which has been empowered to identify wilful defaulters. The petitioner has urged that the requirements of clause 3 of the Master Circular

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have not been complied with. To put the argument in context, the relevant part of clause 3 is set out below:

"3. Mechanism for identification of Wilful Defaulters

The mechanism referred to in paragraph 2.5 above should generally include the following:

(a) The evidence of wilful default on the part of the borrowing company and its promoter / whole-time director at the relevant time should be examined by a Committee headed by an Executive Director or equivalent and consisting of two other senior officers of the rank of GM / DGM.

(b) If the Committee concludes that an event of wilful default has occurred, it shall issue a Show Cause Notice to the concerned borrower and the promoter / whole-time director and call for their submissions and after considering their submissions issue an order recording the fact of wilful default and the reasons for the same. An opportunity should be given to the borrower and the promoter / whole-time director for a personal hearing if the Committee feels such an opportunity is necessary.

(c) The Order of the Committee should be reviewed by another Committee headed by the Chairman / Chairman & Managing Director or the Managing Director & Chief Executive Officer / CEOs and consisting, in addition, to two independent directors / non-executive directors of the bank and the Order shall become final only after it is confirmed by the said Review Committee. However, if the Identification Committee does not pass an Order declaring a borrower as a wilful defaulter, then the Review Committee need not be set up to review such decisions.

Clause 3(a) specifies the composition of the Committee which is entrusted with the task of first identifying and then examining the evidence of wilful default. The petitioners' case is that the Show Cause Notice which was issued by the Deputy Managing Director and signed by the Deputy General Manager, falls short of clause 3(a) and that any deviation from the prescribed composition would warrant quashing of the Show Cause Notice. To test this contention, it would help to reproduce the relevant paragraph from the impugned Show Cause Notice;

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> *2. You are hereby called upon to show cause and make submissions in writing within 30 days from the date of receipt of this letter as to why your name should not be included in the list of wilful defaulters as per RBI guidelines.*

10. The question which would arise is whether the post of Deputy Managing Director (mentioned as the head of the 'appropriate committee' in the impugned notice) is equivalent to that of the Executive Director (under clause 3(a)) of the Master Circular. The stress on equivalence would be justified from the use of this very expression in clause 3(a) which allows for a loosening of the composition of the Committee by prescribing "*…headed by an Executive Director <u>or equivalent</u>…*" (underlined for emphasis). It is also significant that the show cause notice clarifies that the composition of the Committee- or the departure from the recommended composition- is "*as approved by RBI".* It is also significant that clause 3 of the Master Circular slackens the rigour of the requirements by using the expression "*…should generally include the following*" and puts the stress more on a pyramidal power structure of the Committee of a head who is ranked higher than the two senior officers of the rank of GM/DGM who form the base of the structure. This court also takes judicial notice of the fact that there are presently no Executive Directors on the Board of the State Bank of India which is comprised of a Chairman, Managing Directors and Directors. As on 7th September, 2020, the Board of Directors of SBI comprises of a Chairman, 2 Managing Directors, 2 Shareholder Directors and 2 Nominee Directors. The State Bank of India Act of 1955 also does not contemplate a post of Executive Director. Therefore, the first contention with regard to an

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improperly constituted Committee under a Deputy Managing Director instead of the recommended Executive Director, fails.

11. The next issue is of the appointed Committee not applying its mind or making such non-application evident in the Show Cause Notice thus rendering it vulnerable. Clause 3(b) starts with "*If the Committee concludes that an event of wilful default has occurred…*" thereby implying that the condition precedent to issuing a Show Cause Notice to the concerned borrower is of the Committee forming an opinion on the basis of available evidence as to whether there has been a "wilful default" under clause 3(a). The petitioners contend that the impugned Notice is devoid of any indication that the 'appropriate Committee' has indeed done what it is supposed to do under clause 3, namely apply its mind to the materials which would identify the petitioners for the purposes of the Show Cause Notice. For assessing the worth of this contention, the impugned Notice should be seen against the mandate of clause 3(b). While it is correct that the first page of the Notice is opaque in terms of making the workings of the Committee's mind known to the petitioners/recipients of the Notice, the lacuna is addressed by the Annexure to the Notice stating the "*Justification/Reasons for declaring the Borrower as Wilful Defaulter*". The accompanying tabulated statement lists the criteria for classification as Wilful Defaulter as per the RBI Master Circular dated 1st July, 2015 with further references to the "*Events of Default*" and *"Evidences and documents substantiating each event of wilful default"*. It should also be mentioned that the respondent has furnished a Resolution of the Wilful Defaulter Identification Committee dated 17th June,

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2019 in relation to the Company which contains a Proposal *"For approval for identification of Wilful Defaulters and issuance of Show Cause Notices"*. The Resolution further encloses "*Agenda Item No. 2080"* followed by factual events of default corresponding to the relevant clauses of the Master Circular. The Resolution bears the signatures of the Deputy Managing Director as the Chairman of the "Wilful Defaulter Identification Committee-I" and two General Managers as the other Members of the said Committee. The Resolution was filed later in court on behalf of the respondents and forwarded to the petitioners on the same day.

12. In this background, the questions which would naturally arise are:

a) It is necessary for a Show Cause Notice to disclose the basis of the conclusion arrived at by the Committee under clause 3(a)? and

b) If yes, how can such application of mind/formation of opinion be made apparent on the face of the Show Cause Notice?

13. Both these questions can be answered from a plain reading of clause 3 of the Master Circular. First, the clause does not mandate that the Show Cause Notice must disclose the basis of the satisfaction of the concerned Committee or the conclusion arrived at from the evidence before it. What clause 3(a) requires is that the Committee and its members must *"examine"* the evidence of wilful default of a borrower before proceeding to sub-clause (b). Clause 3(b) comes at the stage of completion of examination of the available evidence whereupon the Committee may or may not conclude that

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an event of default has occurred. If it does, only then will it take steps for issuing a Show Cause Notice under the said clause.

14. In the facts of the present case, the contention of the petitioners of the impugned Notice being devoid of any indication of application of mind by the Committee is not acceptable on two grounds. First, the Master Circular does not require it and more important, the Annexure to the Show Cause Notice coupled with the Resolution of the Committee dated 17th June, 2019 provides sufficient material (and particulars specific to the Company of which the petitioners are guarantors) to satisfy that the Committee had indeed fulfilled its mandate under both sub-clauses (a) and (b) of clause 3. One of the most obvious ways in which working of the mind or some sort of deliberation by the persons concerned can be shown is by articulation of the findings arrived at with reference to a meeting (including of minds) where such deliberation palpably took place and the findings being relatable to the materials/evidence before the Committee entrusted with the duty to sift through the evidence to come to the conclusions.

15. Now to the decisions cited in support of the arguments advanced. *Atlantic Projects,* decided on 3rd May, 2019 was on a challenge to a Show Cause Notice in which the petitioner had contended that the function of issuing a Show Cause Notice cannot be delegated to a person who is not a member of the Identification Committee. The Learned Single Judge held that an identified administrative authority cannot delegate its power to issue a Show Cause Notice under clause 3 of the Master Circular. The finding in

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that case was that the Identification Committee must apply its mind at all stages to the materials before it before arriving at a conclusion pertaining to the wilful default and further that the borrower (described as 'the delinquent' in the decision) must have the entire material that was before the Identification Committee for the purpose of giving a complete response. The Division Bench judgment in *Sudhir Kumar Patodia/ Pawan Kumar Patodia* pronounced on 28th February, 2020 was also concerned with a challenge to a Show Cause Notice on the ground of improper constitution of the Identification Committee and non-application of mind in classifying the writ petitioner as a wilful defaulter. The Division Bench construed the RBI Guidelines and held that there had not been any delegation of the functions of the Identification Committee as the power only involved identifying a wilful defaulter and a final order in that regard would have to be made by the Review Committee. The decision proceeded on the basis that identifying a wilful defaulter is essentially a fact-finding exercise followed by an administrative decision. The Division Bench accordingly was of the view that the Regional Office of the appellant/respondent being delegated the task of issuing the Show Cause Notice would not by itself invalidate the proceedings which had been initiated under the Master Circular for declaring the petitioners as wilful defaulters. Relying on *The Secretary, Ministry of Defence vs Prabhash Chandra Mirdha; (2012) 11 SCC 565,* it was additionally held that a Show Cause Notice does not give rise to a cause of action unless a strong case of abuse of process is made out.

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16. The decision in *Pawan Kumar Patodia* is relevant for the present case for the following reasons. First, the challenge mounted to the Show Cause Notice is on the same plank, namely that the issuing authority lacked jurisdiction under the governing guidelines and that there had been delegation of power to a lesser authority. Second, the aspect of a decision having been taken by the concerned committee implying application of mind to the material at hand was considered by the court. The Court, however, held that omission to refer to the decision of the identification committee would not render the Show Cause Notice vulnerable to challenge. Third, the question of prejudice consequent to a Show Cause Notice was addressed by the Division Bench and it was held that the purpose of such a notice was to make the charges known to the borrower so that it could give a comprehensive explanation to and defend the same in the form of a hearing etc. Besides these, *Pawan Kumar Patodia* is a later decision compared to the Single Bench decision in *Atlantic Projects* and considered the same issues which were canvassed in the latter. It is significant that in *Pawan Kumar Patodia,* the Division Bench refused to interfere with the Show Cause Notice despite finding that the Notice was issued by an entity not prescribed under clause 3(a) of the Master Circular. The fact that the Division Bench was also of the view that the Show Cause Notice need not reflect the decision taken by the concerned committee effectively takes care of both the points urged by the petitioners in this case with regard to clause 3 of the Master Circular. It should also be pointed out that the Division Bench considered *Jah Developers* (relied on by the petitioners here) and expressed its reservations

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on the decision being of assistance to the writ petitioners/respondents before the Division Bench.

17. The conduct of the petitioners as would appear from the facts of the present case would further lend credence to the 'prejudice' point as considered in *Pawan Kumar Patodia*; or in other words, whether the petitioners have suffered any prejudice by issuance of the impugned Show Cause Notice. The scheme of clause 3 of the Master Circular (Mechanism for Identification of Wilful Defaulters) contemplates a two-tier system of identification where the decision of the first Committee under clause 3(b) would be subject to review by a second Committee under clause 3(c). Hence, no finality is attached to the decision of the first/identification Committee and more so at the stage of a Show-Cause Notice. Further, the Petitioners in this case received the impugned show-cause notice dated 14th November, 2019 together with the Annexure on 18th November, 2019. The date of receipt would appear from the reply of the petitioners dated 19th December, 2019 to the Show-Cause Notice. In the said letter, the petitioners contended, *inter alia,* that the appropriate Committee had not been formed in keeping with the RBI guidelines and called for withdrawing of the Show-Cause Notice. The respondent Bank thereafter issued a "Notice for Personal Hearing" dated 17th July, 2020 calling upon the petitioners to appear before the "Wilful Defaulter Identification Committee" on 29th July, 2020 at 11 a.m. for making appropriate submissions. The petitioners were given the option to make submissions through video conferencing on the specified date. On receiving the notice for personal hearing, a chain of correspondence followed

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between the parties on 28th July, 2020 whereby the respondents asked the petitioners to be present for the personal hearing on 17th July, 2020 to which the petitioners requested to keep the meeting after August due to the prevailing lockdown in the State. The petitioners sent another e-mail on 29th July, 2020 to the respondents stating that it would be inconvenient for the petitioner no.2 to attend the personal hearing. This was followed by a reply from the respondent attaching a copy of the revised letter for personal hearing dated 6th August, 2020 by which the petitioners were given the opportunity to make their submissions through video conferencing before the concerned Committee on 24th August, 2020 at 12.15 p.m. The present writ petition was filed on 17th August, 2020. From the trail of correspondence, it is evident that the petitioners were initially not averse to appearing before the concerned Committee for making their submissions with regard to the impugned show-cause notice. The reason given for the petitioners' inability to appear on 29th July, 2020 was the pandemic and the petitioners requested for a date in August 2020. The correspondence indicates that the petitioners were not averse to a personal hearing, *per se.*

18. A few decisions have been cited on behalf of the respondent on whether an improper act / decision can be cured by subsequent ratification, including *Marathwada University Vs. Seshrao Balwant Rao Chavan (AIR 1989 SC 1582).* Since this Court is of the view that there was no defect in the act of issuing the impugned Show Cause Notice by reason of the composition of the issuing authority under the guidelines, this court refrains from dealing with the decisions as it would become an academic exercise.

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19. For the reasons as stated above, the challenge to the impugned Show Cause Notice dated 14th November, 2020 and the Notice dated 6th August, 2020, fails. The petitioners are not entitled to the reliefs claimed in WPO 236 of 2020 which is accordingly dismissed without any order as to costs.

20. I.A. No: G.A. 1 of 2020 (Old No: G.A. 1062 of 2020) is disposed of by this judgment.

Urgent Photostat certified copy of this Judgment, if applied for, be supplied to the parties upon compliance of all requisite formalities.

(MOUSHUMI BHATTACHARYA, J.)