M/S Sachdeva & Sons Rice Mills Ltd vs Kotam Mahindra Bank Ltd And Others on 8 April, 2013

Bench: Hemant Gupta, Ritu Bahri

CWP No. 7187 of 2013 -1-

IN THE HIGH COURT OF PUNJAB & HARYANA AT
CHANDIGARH

CWP No. 7187 of 2013 (O&M)

Date of decision: 08.04.2013

M/s Sachdeva & Sons Rice Mills Ltd. ...Petitioner

versus

Kotam Mahindra Bank Ltd and others ...Respondents

CORAM: HON'BLE MR. JUSTICE HEMANT GUPTA
HON'BLE MS. JUSTICE RITU BAHRI

Present: Mr. Ashok Aggarwal, Senior Advocate with
Mr. Rohit Suri, Advocate, for the petitioner.

HEMANT GUPTA, J. (Oral)

Challenge in the present writ petition is to the possession notice dated 20.09.2012 (P-19) consequent to deed of assignment executed by a secured creditor in favour of respondent No.1 - Bank on 27.09.2007.

The petitioner is a part of Group of Companies namely M/s Sachdeva & Sons Industries Pvt. Ltd.; M/s Sachdeva & Sons Rice Mills Ltd. and M/s Pari Foods Pvt. Ltd. M/s Sachdeva & Sons Industries Pvt. Ltd. availed financial assistance from consortium of Banks i.e Punjab National Bank, State Bank of India, Central Bank of India, Canara Bank, Bank of India and Standard Chartered Bank. The aforesaid accounts have been taken over by M/s J.M. Financial Assets Reconstruction Company Limited, Mumbai on 30.06.2010.

The petitioner-company also availed financial assistance from the Bank of Punjab since merged into Centurian Bank of Punjab and thereafter into HDFC Bank Limited. The account of the petitioner was declared Non- Performing Asset (NPA) in the year 2004. In the year 2007, one time settlement was arrived at for a sum of Rs.7.40 crore and in furtherance of the said settlement, Rs.40 lacs was

deposited in the "No Lien Account" with the said Bank. Some where, in May 2006 the petitioner approached the respondent No. 1-Bank and desired fresh working capital funding for the 3rd company i.e M/s Pari Foods Pvt. Ltd. It was in February, 2007 the contract styled as "Indicative Terms Sheet for Fund Raising and Corporate Reconstructing" was entered upon by the petitioner with respondent No. 1- Bank whereby in terms of the said agreement, the respondent No. 1 was engaged to facilitate the one time settlement on behalf of the petitioner with the secured creditors.

Lateron, vide notice dated 28.09.2007 (P-8), the petitioner was informed that by deed of assignment on 27.09.2007, the Centrurion Bank of Punjab has assigned the total debts due from the petitioner to respondent No. 1. The letter reads as under:-

> "By a deed of Assignment dated September 27, 2007, we have assigned teh total debts due from your pursuant to the various financial facility/ies granted by us from time to time alongwith underlying financial documents together with our rights, benefits and obligations thereunder to Kotak Mahindra Bank Limited, 36-38A, Nariman Bhavan, 227 Nariman Point, Mumbai-400021, whereby the total debts due from you to us will now become payable to Kotak Mahindra Bank Limited. Further, Kotak Mahindra Bank Limited shall now stand subrogated in our place and shall be entitled to institute/continue all and any proceedings against you or enforce the rights and benefits under the financial documents including guarantee and security documents (if any) executed for the purpose of availing the financial facility.
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> Please treat this letter as a notice intimating you of the assignment of the debts due from you and the financial documents including guarantee and securing documents (if any) together with our rights, benefits and obligations thereunder to Kotak Mahindra Bank Limited. Please note that on and from the date of the Deed of Assignment, we stand released from the ownership under the Financial Instruments as per the terms of the Deed of Assignment, and you shall look only to Kotak Mahindra Bank Limited in respect of repayment of the Debt and references in the financial documents including guarantee and security documents (if any) to Bank of Punjab Ltd (now merged with Centurion Bank Ltd. to form Centurian Bank of Punjab Ltd.) shall be construed accordingly as references to Kotak Mahindra Bank Limited. All agreements, representations and warranties made in the financial documents including guarantee and security documents (if any) shall survive any transfers and/or assignments made pursuant to the Deed of Assignment."

Consequent to the said letter, the petitioner addressed the communication on 19.10.2007 (P-9) offering settlement with respondent No. 1. The relevant extract of the communication given by the petitioner, reads as under:-

> "We have learned that our loan account in CBOP has been bought over by KMBL, without prejudice, in response we would like to make a settlement offer on the following terms:
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> Settlement amount- Rs.10.00 crores

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Interest servicing @ 16%
Tenure-12 months from October 15, 2007
Payment any time during 12 months
The interest will be charged on reducing balance
The Company shall be permitted to sell the securities now
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charged to Kotak with the prior consent from Kotak. The sale proceeds shall be used to pay the settlement amount of Kotak.

In addition to the above, the Company agrees to pay management fees of Rs.16 lacs by 31st March, 2008 of the sanction of the aforesaid settlement by Kotak We request you to kindly approve the settlement on the above lines and issue us the sanction letter as well as file the consent terms."

Since the petitioner failed to discharge the loan accounts, a notice was served culminating with the notice of possession (P-19), which is the subject matter of challenge in the present writ petition.

Learned counsel for the petitioner has vehemently argued that respondent No. 1 is not registered with the Reserve Bank of India as provided under Section 3 in terms of Section 2(1)(z) and (za) of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (for short 'the Act'), therefore, the assignment of assets in favour of the said respondent is an offence under Section 29 of the Act. In respect of such argument, learned counsel for the petitioner relies upon an order passed by a Division Bench of Madhya Pradesh High Court in a case " Kotak Mahindra Bank Ltd. and others vs. State of Madhya Pradesh and others" M.CR.C.No. 7310 of 2011 decided on 23rd January 2012 arising out of a petition seeking quashing of proceedings initiated by the Chief Judicial Magistrate under Section 156 (3) Cr.P.C. The reference of learned counsel for the petitioner is on para No. 26 of the aforesaid judgment which reads as under:-

"26. Learned counsel for respondent No. 3 and 4 has submitted that the applicant bank has claimed to be a secured creditor as the applicant bank has stepped in the shoes of BOB and BOI. It was quoted in para 5.4 of plaint filed by the applicant bank before the Debt Recovery Tribunal but the assets of a bank relating to the borrower-companies could be purchased within the limits of the provision enumerated in the Special Act 2002. In Section 2(1)(z) of the Special Act, the definition of word "securitization" is given and in sub-section (za) the definition of "securitization company" is given. Looking to the those definitions, it would be clear that the financial assets are to be purchased from one financial company by another one then it is a process of securitization and therefore, purchase of assets from BOI and BOB amounts to be a process of securitization but according to the Section 3 of the Special Act, 2002, for such activities the concerned company should be a registered company with RBI and if it is not registered then it is a violation of the provisions of Section 3 of the Special Act, 2002 punishable under Section 29 of that Act. Under such circumstances, the purchase of the assets of borrower from BOI and BOB by the applicant bank is an offence under Section 29 of the Special Act, 2002."

It is also argued that vide document (P-1), respondent No. 1- bank was appointed as an agent, therefore, agent cannot be assigned debts so as to take over the asset of the borrower.

We have heard learned counsel for the petitioner and finds no merit in the present petition.

The assignment of debt is permissible in terms of Section 130 of the Transfer of Property Act, 1882. Learned counsel for the petitioner could not point out any prohibition in the documents of loan prohibiting assignment of debt in favour of an another Banking company. It is not disputed that respondent No. 1 is a Banking Company registered under the Banking Regulation Act, 1949 with the Reserve Bank of India. We are not able to agree with the observations of Madhya Pradesh High Court in the aforesaid judgment as the Court has proceeded on the assumption that assignment of debt could only be under the provisions of the Act. The Court has not examined the provisions of the Transfer of Property Act. In fact, the Gujarat High Court has not noticed the judgment of Supreme Court reported as ICICI Bank Limited v. Official Liquidator of APS Star Industries Limited, (2010) 10 SCC 1. The view as reproduced above, was set aside by the Supreme Court. We find that reliance on the judgment of Gujarat High Court in view of the Supreme Court order is rather unfortunate. The Supreme Court was examining the question as to "Whether the Gujarat High Court was right in holding that assignment of debts by the banks inter se is not an activity permissible under the BR Act, 1949 and consequently all executed contracts of assignment of debts were illegal?" The Supreme Court observed as under:

> 38. The BR Act, 1949 basically seeks to regulate banking business. In the cases in hand we are not concerned with the definition of banking but with what constitutes "banking business". Thus, the said BR Act, 1949 is an open-

ended Act. It empowers RBI (regulator and policy framer in matter of advances and capital adequacy norms) to develop a healthy secondary market, by allowing banks inter se to deal in NPAs in order to clean the balance sheets of the banks which guideline/policy falls under Section 6(1)(a) read with Section 6(1)(n). Therefore, it cannot be said that assignment of debts/NPAs is not an activity permissible under the BR Act, 1949. Thus, accepting deposits and lending by itself is not enough to constitute the "business of banking". The dependence of commerce on banking is so great that in modern money economy the cessation even for a day of the banking activities would completely paralyse the economic life of the nation. Thus, the BR Act, 1949 mandates a statutory comprehensive and formal structure of banking regulation and supervision in India.

39. The test to be applied is--whether trading in NPAs has the characteristics of a bona fide banking business. That test is satisfied in this case. The Guidelines issued by RBI dated 13-7-2005 itself authorises the banks to deal inter se in NPAs. These guidelines have been issued by the regulator in exercise of the powers conferred by Sections 21 and 35-A of the Act. They have a statutory force of law. They have allowed the banks to engage in trading in NPAs with the purpose of cleaning the balance sheets so that they could raise the capital adequacy ratio. All this comes within the ambit of Section 21 which enables RBI to frame the policy in relation to advances to be followed by the banking companies and which empowers RBI to give directions to banking companies under Section 21(2). These guidelines and directions following them have a statutory force.

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43. One more aspect needs to be kept in mind. In this batch of cases we are dealing with assets in the hands of the banks. NPAs are "account receivables". The impugned guidelines show that RBI considers inter se NPA assignment between banks to be a tool for resolving the issue of NPAs and in the interest of banking policy under Section 21 of the BR Act, 1949. The object is to minimise the problem of credit risk. The corporate debt restructuring is one of the methods for reducing NPAs. Thus, such restructuring as a matter of banking policy cannot be treated as "trading". One has to keep in mind the object behind enactment of the BR Act, 1949. Thus, the said guidelines fall under Section 21 of the 1949 Act. These guidelines are a part of credit appraisal mechanism. Thus, in our view the impugned guidelines are not ultra vires the BR Act, 1949. Dealing in NPAs as part of the credit appraisal mechanism and as a part of restructuring mechanism falls within Section 21 read with Section 35-A of the Act. Hence, it cannot be said that "transfer of debts/NPAs" inter se between banks is an activity which is impermissible under the 1949 Act. The BR Act, 1949 is an Act enacted to consolidate and amend the law relating to banking. Thus, while interpreting the Act one needs to keep in mind not only the framework of the banking law as it stood in 1949 but also the growth and the new concepts that have emerged in the course of time. (emphasis supplied) xxx xxx

46. As stated above, an outstanding in the account of a borrower(s) (customer) is a debt due and payable by the borrower(s) to the bank. Secondly, the bank is the owner of such debt. Such debt is an asset in the hands of the bank as a secured creditor or mortgagee or hypothecatee. The bank can always transfer its asset. Such transfer in no manner affects any right or interest of the borrower(s) (customer). Further, there is no prohibition in the BR Act, 1949 in the bank transferring its assets inter se. Even in the matter of assigning debts, it cannot be said that the banks are trading in debts, as held by the High Court(s). The assignor Bank has never purchased the debt(s). It has advanced loans against security as part of its banking business. The account of a client in the books of the bank becomes non-performing asset when the client fails to repay. In assigning the debts with underlying security, the bank is only transferring its asset and is not acquiring any rights of its client(s). The bank transfers its asset for a particular agreed price and is no longer entitled to recover anything from the borrower(s). The moment ICICI Bank Ltd. transfers the debt with underlying security, the borrower(s) ceases to be the borrower(s) of the ICICI Bank Ltd. and becomes the borrower(s) of Kotak Mahindra Bank Ltd. (assignee).

47. At this stage, we wish to once again emphasise that debts are assets of the assignor Bank. The High Court(s) has erred in not appreciating that the assignor Bank is only transferring its rights under a contract and its own asset, namely, the debt as also the mortgagee's rights in the mortgaged properties without in any manner affecting the rights of the borrower(s)/ mortgagor(s) in the contract or in the assets. None of the clauses of the impugned deed of assignment transfers any obligations of the assignor towards the assignee.

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51. In view of the above exposition of law, we find that under the impugned deed of assignment only the account receivables in the books of ICICI Bank Ltd. has been transferred to Kotak Mahindra

Bank Ltd. The obligations of ICICI Bank Ltd. towards its borrower(s) (customer) under the loan agreement secured by deed of hypothecation/mortgage have not been assigned by ICICI Bank Ltd. to the assignee Bank, namely, Kotak Mahindra Bank Ltd. Hence, it cannot be said that the impugned deed of assignment is unsustainable in law. The obligations referred to in the impugned deed of assignment are the obligations, if any, of ICICI Bank Ltd. towards Kotak Mahindra Bank Ltd. (assignee) in the matter of transfer of NPAs. For example, when an account receivable is treated as NPA and assigned to the assignee Bank, the parties have to follow certain guidelines issued by RBI. If there is a breach of the guidelines or statutory directions issued by RBI by the assignor in regard to transfer of NPA then the assignee Bank can enforce such obligations vis-à-vis the assignor Bank. It is these obligations which are referred to in the impugned deed of assignment. That, an account receivable becomes an NPA only because of the default committed by the borrower(s) who fails to repay. Lastly, it may be mentioned that the said SARFAESI Act, 2002 was enacted enabling specified SPVs to buy NPAs from the banks. However, from that it does not follow that the banks inter se cannot transfer their own assets. Hence the said SARFAESI Act, 2002 has no relevance in this case.

52. Before concluding, we may state that NPAs are created on account of the breaches committed by the borrower. He violates his obligation to repay the debts. One fails to appreciate the opportunity he seeks to participate in the "transfer of account receivable" from one bank to the other." The Gujarat High Court has not only failed to notice the above judgment but also the provisions of the Transfer of Property Act. In view of the above judgment of the Supreme Court, the assignment of debt by a Bank to another Bank in not impermissible under the Banking Regulation Act, 1949. Therefore, the challenge to the assignment of debt is wholly devoid of merit.

The other argument that respondent No. 1 was an agent and thus could not be assigned of the debt, is again not tenable. The petitioner and also that group companies of the petitioner have approached the respondent Bank for assisting it in raising funds. The assistance of respondent No.1 was sought to liquidate the funds raised by the petitioner. There is no embargo in the documents produced that the respondent Bank cannot act in any other capacity. Since there was no restriction of respondent No.1 to seek assignment of the debt, we do no find that assignment of debt by secured creditors in favour of the respondent bank, suffers from any patent illegality. In fact at the very first instance, in the communication dated 19.10.2007, the petitioner submitted settlement to respondent No. 1. It is too late in the date, almost after 6 years to say that respondent No.1 is not competent to take the possession from the petitioner in exercise of the powers confers under Section 13 of the Act.

The present petition is consequently dismissed.

(HEMANT GUPTA) JUDGE (RITU BAHRI) JUDGE April 08, 2013 G.Arora/Vimal