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Case Commentary: Impact of Bank of India vs. M/s Sri Nangli Rice Mills Pvt. Ltd. — Supreme Court Judgment Delivered on 23 May 2025

by Shrikumar Pillai

The SARFAESI Act, 2002 is a vital law that has resolved a large number of non-performing asset accounts across the banking and NBFC credit space. Its impact is far-reaching, helping banks, NBFCs and borrowers alike determine their rights in the recovery process.

In implementing the Act, banks and NBFCs sometimes turn adversaries — where two lenders have each advanced credit to the same borrower against the same collateral. This battle between creditors not only hampers recovery but can erode the value of the asset itself. DRAT rulings in *Federal Bank Ltd. v. LIC Housing Finance* (2010 SCC OnLine DRAT 138) and *Standard Chartered Bank v. LIC Housing Finance Ltd.* (2011 SCC OnLine DRAT 112) had widened this loophole, holding that Section 11 of the SARFAESI Act was not mandatory, and that arbitration under it required a written arbitration agreement.

Factual Background

The borrower, M/s Sri Nangli Rice Mills Pvt. Ltd., a rice and paddy manufacturing unit, had availed credit facilities from Bank of India (the appellant) since 2003 by hypothecating paddy stock, formalised through a Credit Facility Agreement dated 23.09.2006. It later also availed facilities from Punjab National Bank (respondent no. 2), pledging warehouse receipts for paddy and rice stock through collateral manager National Bulk Handling Corporation. On default, both banks asserted competing claims of priority over the same stock.

The DRT-I (Delhi) held that since the real dispute was between two banks, it had no jurisdiction, and directed arbitration under Section 11 of the SARFAESI Act. The High Court of Punjab and Haryana upheld this (CWP No. 13538 of 2020), leading to the present appeal.

The Legal Question

These questions, framed by the Supreme Court as issues for its consideration, needed a definitive answer:

- What is the meaning of "any dispute relating to securitization or reconstruction or non-payment of any amount due including interest" in Section 11?
- What is the significance of "arises amongst any of the parties, namely, the bank or financial institution or asset reconstruction company or qualified buyer" in Section 11 read with Section 2?
- What is the object behind prescribing arbitration for such disputes under Section 11?
- Is a written arbitration agreement required under Section 11 — and is there a conflict between Oriental Bank of Commerce and Federal Bank (supra)?
- Should Section 11 be construed as mandatory or directory?

What the Court Held

The Supreme Court held that Section 11 is attracted only where the dispute relates to (i) securitisation, (ii) reconstruction, or (iii) non-payment of any amount due, including interest — and only where it arises between a bank, financial institution, asset reconstruction company or qualified buyer. Both conditions must be satisfied together; where they are, the DRT has no jurisdiction, and the only recourse is arbitration under Section 11 read with the Arbitration and Conciliation Act, 1996.

This category of disputes covers the rights of secured creditors inter se — including disputes from third-party default — in relation to enforcement of a security interest, independent of the borrower's own liability. It does not cover disputes relating to recovery proceedings or measures taken under the Act itself.

Significantly, the Court also carved out an exception: where the relationship between the two disputing entities is itself that of lender and borrower — for instance, where one bank has independently borrowed from another — Section 11 does not apply at all, since the Act's wide definition of "borrower" under Section 2(f) includes "any person," even a bank or financial institution.

On the written-agreement question, the Court held that Section 11 creates a legal fiction as to the existence of an arbitration agreement, regardless of whether one actually exists — in other words, the law treats the parties as if they had signed an arbitration agreement, using the phrase "as if the parties have consented in writing." This dispenses with the need for an actual agreement and binds the parties to arbitration or conciliation under the Arbitration and Conciliation Act, 1996.

On the mandatory/directory question, the Court held that the use of "shall" makes Section 11 mandatory — the prescribed mechanism cannot be bypassed by seeking recourse elsewhere.

The AMRCD Memorandum Argument — Rejected

The respondent bank argued, for the first time before the Supreme Court, that as a dispute between two public sector banks, it should instead be resolved under the Finance Ministry's AMRCD Memorandum (Office Memorandum dated 14.12.2022) governing inter-CPSE commercial disputes. The Court rejected this for two reasons: first, Clause 3.3 of the Memorandum is confined to disputes over commercial contracts between CPSEs, and this dispute arose instead from two separate agreements each bank had independently executed with the borrower; and second, an executive memorandum cannot in any event override a statutorily mandated arbitration mechanism such as Section 11.

The Outcome

Finding no infirmity in the High Court's order, the Supreme Court dismissed the appeal, holding that the dispute between Bank of India and Punjab National Bank over the pledged and hypothecated paddy stock must proceed to arbitration or conciliation under Section 11, and could not be entertained by the DRT. The parties were left to bear their own costs.

Analysis and Critical Evaluation

For Banks and NBFCs it should now build institutional readiness for ad hoc arbitration under Section 11 under SARFAESI Act, since the absence of a signed agreement is no longer a valid argument. Public sector Banks in-house counsel should note that internal government mechanisms such as the AMRCD Memorandum will not be read to displace a statutory arbitration mandate, even where both disputants are CPSEs. It is imperative that Credit and Legal teams should also conduct thorough charge-search and asset-verification diligence

before hypothecation or pledge is taken, given that priority disputes of this kind arise precisely from undetected competing security interests.

The ruling is a course-correction as it resolves the Federal Bank–Oriental Bank of Commerce conflict in favour of a mandatory, agreement-independent arbitration regime, the Court removes the loop-hole which led to delay intentionally or otherwise. A common ploy which a lender facing an adverse Section 11 route was to simply deny the existence of a written arbitration agreement and force the dispute into slower DRT or civil litigation, during which the value of the contested security often eroded.

The observation that deeming an arbitration agreement to exist "as if" the parties had consented in writing is a significant departure from Section 7 of the Arbitration and Conciliation Act, 1996, which ordinarily requires actual written consent. The Court treats this as legislative fiat within a specialized statute, significant.

That carve-out made for determining whether the jural relationship between two disputing banks/NBFC or regulated entities is genuinely one of "lender and borrower" (taking the dispute outside Section 11) or one of competing secured creditors (keeping it within Section 11) will not always be as clean and clear as it in this case, where the two credit relationships ran independently to a common borrower. Parties may now re-characterise their inter se relationship as one of lending, inviting exactly the kind of jurisdictional skirmish this judgment was meant to end.

One question the judgment leaves open is its effect on part-heard DRT proceedings already underway between competing lenders at the time of this ruling — whether they must now be aborted in favour of arbitration, or may continue to conclusion under a savings principle, is likely to be tested in the lower fora before long.

Conclusion

The judgment delivered on 23.05.2025 provides much-needed clarity on resolving inter se disputes between banks, NBFCs, ARCs or other eligible entities enforcing action under the SARFAESI Act, 2002. Where such a dispute does not arise from action taken under the Act itself, but from the apportionment of security interest between competing lenders, Section 11 mandates arbitration or conciliation as the sole route, to the exclusion of the DRT. **Citation**

- *Bank of India v. M/s Sri Nangli Rice Mills Pvt. Ltd. & Ors., Civil Appeal No. 7110 of 2025, arising out of SLP(Civil) No. 16735 of 2022, 2025 INSC 765 (Supreme Court of India, decided 23.05.2025).*
- *Standard Chartered Bank v. LIC Housing Finance Ltd., 2011 SCC OnLine DRAT 112.*
- *Federal Bank Ltd. v. LIC Housing Finance Ltd., 2010 SCC OnLine DRAT 138.*

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