IN THE HIGH COURT AT CALCUTTA
(Constitutional Writ Jurisdiction)
APPELLATE SIDE

Present:

The Hon'ble Justice Krishna Rao

W.P.A. No. 12897 of 2026

VFS Capital Limited & Ors.

Vs.

Small Industries Development Bank of India & Ors.

Mr. Jishnu Chowdhury, Sr. Adv.
Mr. Chayan Gupta
Mr. Joydeep Guha
Mr. Abhideepta Tarafdar

....for the petitioners.

Mr. Ratnanko Banerji, Sr. Adv.
Ms. Urmila Chakraborty
Ms. Gunja Pachisia
Md. Minhajuddin

....for the respondent nos. 1 & 2.

Hearing Concluded On : 09.07.2026

Judgment Delivered On : 15.07.2026

Judgment Uploaded On : 15.07.2026

Krishna Rao, J:

1. The petitioners have filed the present writ petition challenging the Show Cause Notice dated 20th November, 2025, and the impugned order dated 11th March, 2026, wherein the account of the petitioners have been declared as fraud on account of misappropriation of funds and criminal breach of trust.

2. On 18th January, 2024, a Partnership Agreement was entered between the Petitioner No.1 and the Respondent No.1 for implementation of "Prayaas Scheme 2.0" for Direct Credit to Micro Enterprises. The Petitioner No.1 was appointed as partner to provide services. Under the Scheme, credit availed by the Petitioner No.1 from the Respondent No.1 was to be disbursed to borrowers, and upon collection of the repayment from such borrowers/customers, the Petitioner No.1 was required to deposit the collected amounts in a designated Collection Account and remit the same to the Respondent No.1, for credit to the borrowers' loan accounts.

3. The stated objective of the scheme was to assist microfinance clients seeking to upscale or diversify their business with loans ranging from Rs. 50,000 to Rs.5 lakh, commonly known as "Missing Middle Segment", to improve access to affordable finance and reduce the interest rate for borrowers otherwise charged interest as high as 20% or more, and to improve livelihood opportunities for such borrowers.

4. In accordance with Clause 5 of the Partnership Agreement dated 18th January, 2024, the petitioner no.1 submitted/created fixed deposits with the respondent No.1. Under Schedule-II of the Partnership Agreement and the modality of conduct of business contained therein that money collected from the end of the customers by the petitioner No.1 were required to be immediately made over to the Respondent No.1. The petitioners' case is that the Petitioner No.1 had no obligation to pay the respondent No.1 except to the extent of sums actually collected from customers/borrowers, and that, in case of default by end of the customers, its obligation was limited to the extent of the fixed deposits placed.

5. On 29th to 30th October, 2025, officials of the Respondent No.1 visited the office of the Petitioner No.1. The Petitioner No.1 shared data on Prayaas borrowers. The petitioners showed a portfolio outstanding of Rs. 56.87 Crores as on 30th October, 2025, whereas the books of the respondent No.1 reflected an outstanding portfolio of Rs.74.63 Crores in respect of Prayaas borrowers under Petitioner No.1. There is a shortfall of Rs.17 Crores in between both portfolio authorities of Prayaas. According to the respondents, upon being questioned, Petitioner No.1 responded that some recoveries from Prayaas borrowers had not been transferred to the Respondent No.1.

6. Consequently, the respondent No.1 issued a notice dated 20th November, 2025, calling upon the petitioner No.1 to show cause as to why its account should not be classified as "fraud" in terms of the

Reserve Bank of India's Directions, granting 21 days for submission of a representation. The petitioners have submitted detail reply to the show cause notice to the respondents on 10th December, 2025.

7. A notice for personal hearing dated 19th December, 2025, was issued pursuant to which a personal hearing was held on 5th January, 2026, attended by the Petitioner No.2. According to the respondents, the Petitioner No.2, namely, Shri Kuldip Maity, the Managing Director of the Petitioner No.1 admitted at the said hearing that collections from Prayaas borrowers were not transferred to the Respondent No.1 within the stipulated timelines and were instead utilised by Petitioner No.1 to service its debt obligations to other lenders, and that the same is audio-recorded and acknowledged in the petitioners' written representation.

8. By an order dated 11th March, 2026, the competent authority of the respondent No.1 classified the account of Petitioner No.1 as a "fraud account" under paragraph 6.1 of the RBI Master Directions on Fraud Risk Management dated 15th July, 2024, on the ground of alleged misappropriation of funds and criminal breach of trust, relying substantially on the alleged admission at the hearing dated 5th January, 2026.

9. Being aggrieved, the petitioners have preferred the present writ petition challenging the show cause notice dated 20th November, 2025 and the order dated 11th March, 2026, seeking, inter alia, quashing thereof on the grounds of violation of the principles of natural justice, non-application of mind and arbitrariness.

10. Mr. Jishnu Chowdhury, Learned Senior Advocate representing the petitioners submits that the Partnership Agreement dated 18th January, 2024, shows that the Petitioner No.1 was only required to collect money from customers and make over the same to the Respondent No.1, and that even where customers failed to pay, the petitioners' exposure was limited to a security deposit/guarantee to the extent of 5% of the total sanctioned value. The petitioners' consistent stand is that they have not collected and retained any money that was due and payable but could not be collected from the customers.

11. Mr. Chowdhury submits that under Clause 6.1 of the RBI Master Circular on Fraud dated 15th July, 2024, an account can be termed "fraud" only where the petitioners collect money from customers and does not make over to the Respondent No.1. Clause 2.1.1.1 of the Circular further requires a show cause notice to provide complete details of the transactions/actions/events on the basis of which declaration and reporting of fraud is contemplated. He submits that the show cause notice dated 20th November, 2025, does not meet this requirement. The first paragraph on merely records an outstanding/ gap, while the succeeding paragraphs rely on expressions such as 'deep apprehension', 'it is possible', 'if VFSCL' and 'we apprehend', reflecting surmise and conjecture rather than any direct allegation, particulars, documents or instances. Allegations of breach of trust, dishonest misappropriation and cheating cannot be sustained on such basis.

12. Mr. Chowdhury submits that in the reply dated 10th December, 2025, the Petitioner No.1 categorically denied any history of fraudulent conduct, wilful default, diversion of funds or misrepresentation, diversion or misuse of collections, and affirmed diligence in remitting amounts to the designated collection account. The order dated 11th March, 2026, records no independent satisfaction and proceeds entirely on an alleged admission attributed to Shri Kuldip Maity, the Managing Director of the Petitioner No.1. No such admission was in fact made, despite the respondents' claim of an audio recording, none has been produced, and the respondents did not act upon the petitioners' willingness to seek a review/deletion of the alleged admission. He submits that in any event, even as recorded, the alleged admission is, at best, that collections were not transferred within the stipulated timelines i.e., a delay/contractual breach and does not establish collection and retention of money, which alone would constitute fraud.

13. Mr. Chowdhury submits that if a gap exists between the parties' figures, this shows only that collections have not been made, and does not prove that money has been collected and withheld an outstanding or gap is, by itself, meaningless for this purpose. He submits that the petitioner's willingness to pay towards the First Loss Default Guarantee (FLDG) has no bearing on the allegation of fraud and merely reflects a request for time to pay the 5% guarantee.

14. Mr. Chowdhury has relied upon the judgment in the case of ***Hemant Kanoria Vs. Bank of India*** reported in ***2024 SCC OnLine Cal 1012*** and submits that specific instances of allegations are to be mentioned in the show cause notice and to ensure that an effective opportunity of hearing is given to the petitioner.

15. Mr. Ratnanko Banerji, Learned Senior Advocate representing the respondents submits that the petitioners are challenging the show cause notice dated 20^{th} November, 2025 and the order dated 11^{th} March, 2026, classifying the account of the petitioner No.1 as a "fraud account", raises two contentions that is absence of evidence for the fraud declaration, and reliance on surmise and conjecture - both of which are wholly misconceived and not maintainable.

16. Mr. Banerji submits that under the Partnership Agreement dated 18^{th} January, 2024 for the Prayaas Scheme, the Petitioner No.1 was obliged to deposit amounts collected from the borrowers into a designated Collection Account and remit the same to the Respondent No.1. The Petitioner No.1 failed to do so and misappropriated the collected amounts, leading to the show cause notice dated 20^{th} November, 2025.

17. Mr. Banerji submits that the show cause notice records that during a visit on 29^{th} to 30th October, 2025, data shared by the Petitioner No.1 showed a Prayaas portfolio outstanding of Rs.56.87 Crores, whereas the Respondent No.1's books showed Rs.74.63 Crores, a shortfall of Rs.17 Crores. There being no inappropriate receipt at the Respondent

No.1's end, the Petitioner No.1, on being questioned, responded that some recoveries had not been transferred to the respondent No.1. The notice was issued with 21 days for representation, in compliance with natural justice and the RBI Master Directions on Fraud Risk Management dated 15th July, 2024.

18. Mr. Banerji submits that in its reply dated 10th December, 2025, Petitioner No.1 admitted defaults, mismatch in data and discrepancies, admitted "elevated delinquencies" in the portfolio managed by it, and admitted temporary manpower shortage/staff turnover causing delays/ inconsistencies in submission of collection data, without denying the portfolio mismatch or seeking further documents rather, it volunteered to furnish further clarification. The allegation of non-supply of documents is accordingly an afterthought, raised for the first time in the petition.

19. Mr. Banerji submits that at the personal hearing held on 5th January, 2026, pursuant to notice dated 19th December, 2025, the petitioner No.2, the Managing Director of the Petitioner No.1, admitted that collections from Prayaas borrowers were not transferred to Respondent No.1 within the stipulated time and were misutilised by the Petitioner No.1 to service its debts/obligations to other lenders, an admission also acknowledged in the Petitioner No.1's written representation and which is audio-recorded, the transcript whereof is in the respondents' custody.

20. Mr. Banerji submits that the reasoned order dated 11th March, 2026, classifying the account as "fraud" under paragraph 6.1 of the RBI Master Directions, was passed after due compliance with natural justice, based on documents submitted by the petitioners themselves, on account of misappropriation of funds and criminal breach of trust.

21. Mr. Banerji has also relied upon the judgment in the case of ***Hemant Kanoria (supra)***, for the proposition that a balance must be struck between adherence to technicalities and speed in reporting, with emphasis under the Master Directions on the place of reporting to protect the banking system from frauds; delay in reporting, and consequent delay in alerting other banks/disseminating caution advice, would enable similar fraud elsewhere, and banks are cautioned to strictly adhere to the prescribed time frame for reporting frauds to the RBI, time being of the essence.

22. Mr. Banerji submits that the ultimate sufferers are the Prayaas borrowers who repaid their loans to the Petitioner No.1 but continue to be shown as defaulters in the Respondent No.1's books, since the Petitioner No.1 has not repaid to the Respondent No.1 despite having misappropriated the collected funds.

23. Heard the Learned Counsel for the respective parties, perused the materials on record and the judgment relied by the parties. As per the scheme, the credit availed by the petitioner no.1 from the respondent no.1 was to be disbursed to the borrowers and upon collection of the repayment money from the said borrowers, the same was to be deposited by the petitioner no.1 in the collection account and remit the same to the respondent no.1. The First Loss Default Guarantee (FLDG) to the tune of 5% of sanctioned partnership limit will have to be provided by the petitioner no.1, which would be in the form of maintenance of minimum 2% in the form of fixed deposit and further built up on incremental basis till stipulated FLDG i.e. 5% is exhausted.

24. The Show Cause notice was issued to the petitioners on the following allegations:

> *"During our recent visit on October 29-30, 2025 to your office, VFSCL shared certain data on Prayaas borrowers. While VFSCL showed a portfolio outstanding of Rs.56.87 crore under Prayaas as on October 30, 2025, SIDBI's books had outstanding portfolio of Rs.774.63 crore in respect of Prayaas borrowers under VFSCL. This shows that the overall Prayaas portfolio at VFSCL is lowered by a very large amount of Rs17.00 crore. As there were no unappropriated receipts at SIDBI's end, the matter was raised with VFSCL. VFSCL responded that some of the recoveries from Prayaas borrowers have not been transferred to SIDBI.*
>
> *Meanwhile, we also have seen that some dues are transferred to SIDBI with substantial delay by VFSCL, Further, we also contacted some defaulting Prayaas borrowers under VFSCL who informed that dues have been paid on time by them to VFSCL. SIDBI notes, with deep apprehension, that VFSCL has been defaulting on transfer of collected dues to SIDBI in respect of the Prayaas borrowers. The loan accounts of these borrowers show default which will adversely impact their credit record and their ability to mobilise funds in future from banking system including SIDBI. VFSCL is solely responsible for creating this fully avoidable situation. Apart from the deep distress created for the Prayaas borrowers who have already repaid*

their dues, VFSCL is using their money for other purposes of which SIDBI is not aware, It is possible that VFSCL is using these collections from Prayaas customers to service its borrowings from lenders for micro finance operations. This throws a much larger question on the micro finance operations of VFSCL for which VFSCL has separate credit facilities from other lenders including SIDBI. If VFSCL is collecting the dues of Prayaas borrowers and misuse them for debt servicing of its borrowings for micro finance operations, the company's ability to carry its operations sustainably is in question."

25. The data shared by the petitioner no.1 to the respondent no.1, the portfolio outstanding of Rs. 56.87 crores under Prayaas as on 30th October, 2025 but as per the books of accounts of the respondent no.1, the outstanding portfolio of Rs. 74.63 crores in respect of Prayaas borrowers under the petitioner. The petitioner has not denied the said difference of figure of Rs. 17.00 crores. The petitioner in its show cause reply stated as follows:

"As your goodselves are aware, the microfinance sector has, in recent months, been facing an exceptionally challenging operating environment owing to socio-political disruptions and operational constraints in several regions. These external factors have adversely affected borrower cash flows, repayment behaviour and overall credit discipline across the sector. Given that Prayaas borrowers primarily belong to bottom-of-the-pyramid segments, their repayment capacity has also been affected, resulting in elevated delinquencies in the portfolio managed by VFSCL. We submit that these are credit-risk driven developments, and not in any manner indicative of fraud-risk or wilful intent.

At the beginning of the current financial year, both the on-book and off-book portfolios of the Company were performing strongly. However, temporary manpower shortages and staff turnover

> *in a few branches led to delays or inadvertent inconsistencies in consolidation and submission of collection data. These were operational lapses, arising from short-term constraints, and not systemic or intentional. Importantly, there has been no diversion or misuse of collections and the Company has been diligent in remitting all amounts to the designated Collection Account as per the Agreement."*

26. The petitioners have submitted detailed show cause reply but the petitioners have not stated anything with regard to supply of any documents. The petitioners in their reply have requested for personal hearing and accordingly, the respondents have granted personal hearing to the petitioners. During the personal hearing on 5th January, 2026, the petitioner no.2 admitted that the collections from the prayaas borrowers were not transferred to the respondent no.1 within the stipulated time and were utilised by the petitioner no.1 for servicing its debt obligations to other lenders.

27. Mr. Banerji during hearing of the case has handed over the copy of the communication made by the petitioner no.2 to the respondent no.1 on 30th October, 2025, which reads as follows:

> *"Dated: 30.10.2025*
>
> ***The General Manager,***
> ***SIDBI***
> ***Mumbai***
>
> *Dear Sir,* ***Kind Attn: Mr Radha Ramana***
>
> ***Sub: Repayment of Prayaas***
>
> *As discussed with you on date, please be informed that on or before 14 November 2025, we shall be repaying you Rs. 10 crores.*

In between whatever possible we shall be repaying you in phases along with the daily collection.

In this context, request you, if you can kindly adjust our FLDG kept with you in the form of FD against the pending Prayaas repayment amount.

Look forward for your kind cooperation in this regard.

Thanking you!
Yours faithfully,
Kuldip Maity
MD & CEO."

28. Mr. Chowdhury has relied upon Clause 2.1.1.1 of Chapter-II of the Master Directions on Fraud Risk Management in commercial Banks (including Regional Rural Bank) and All India Financial Institutions dated 15th July, 2024 and submits that in the show cause notice complete details of transactions has not been provided. The petitioners have submitted reply to the show cause notice. In the said reply, the petitioners have not asked for any details. The petitioners only asked for personal hearing and the same was provided. The petitioners in the show cause reply even not denied with regard to the details of data of Prayaas borrowers. In the show cause notice, it is also mentioned that on 29th/30th October, 2025, the respondent no.1 visited the office of the petitioner no.1 and the letter produced by Mr. Banerji is dated 30th October, 2025. In the said letter, the petitioner no. 2 admitted that he will repay an amount of Rs. 10 Crores on or before 14th November, 2025, and remaining amount shall be repaying in phase along with daily collection and the show cause notice was issued on 20th November, 2025 but the petitioners have not paid the said amount.

29. The judgment relied by the petitioners and the respondents in the case of ***Hemant Kanoria (supra)*** wherein the Hon'ble Coordinate Bench of this Court held that:

> *"**60.** Hence, what has to be ensured is that specific instances of allegations are to be mentioned in the show-cause notice, although all particular documents which are to be relied on and/or intricate details of the frauds alleged need not be given at the show-cause notice stage. The show-cause is a mere indicator of the allegations made against the borrower and its Director/management. It is to ensure that an effective opportunity of hearing is given to the accused."*

In the present case, in the show cause notice, details have been given regarding the difference amount of Rs. 17.00 Crores after considering the portfolios maintained by the petitioner no.1 and the respondent no.1. The petitioners have not denied with regard to the said figure and even in reply to the show cause notice, have not demanded any further documents or details. As per request of the petitioner no.1, personal hearing was also provided to the petitioners. Thus the judgment relied by the petitioners is not applicable to the petitioners' case though it is squarely applicable to the respondents.

30. This Court did not find any justification to interfere with the show cause notice dated 20th November, 2024 and the impugned order dated 11th March, 2026.

31. **WPA No. 12897 of 2026** is thus **dismissed**.

Parties shall be entitled to act on the basis of a server copy of the Judgment placed on the official website of the Court.

Urgent Xerox certified photocopies of this judgment, if applied for, be given to the parties upon compliance of the requisite formalities.

(Krishna Rao, J.)