

# M/s Rajshree Sugars and Chemicals v. M/s Axis Bank Limited (2019) | 14 Nov 2024

## Introduction

- This is a landmark judgment relating to the legality of derivative contracts.
- This judgment was delivered by a single judge bench comprising of Justice V Ramasubramaniam.

## Facts

- The Parties & Background:
  - The plaintiff is a listed company that manufactures and exports sugar
  - They have foreign loans (External Commercial Borrowings) and deal in foreign currencies
  - The defendant is UTI Bank (later became AXIS Bank)
- Initial Agreement:
  - On May 14, 2004, both parties signed an ISDA Master Agreement
  - This is a standard international agreement for financial trading
  - The agreement included a schedule specifying Mumbai High Court's jurisdiction
  - The plaintiff's Chief Financial Officer (P.K. Viswanathan) was authorized to handle derivative transactions
- The Disputed Transaction:
  - Out of 10 deals between the parties, 9 went smoothly
  - The dispute is about the 10th deal (Contract No. OPT 727) from June 22, 2007
  - It was a complex currency option deal involving US Dollars and Swiss Francs
  - The deal included specific conditions about exchange rates and payments
- Key Events:
  - The bank paid USD 100,000 to the plaintiff on June 27, 2007
  - In December 2007, the plaintiff claimed the contract was terminated
  - The bank disagreed, saying the contract was still valid
  - The bank offered to work out risk mitigation options
- Legal Action:
  - The plaintiff filed a lawsuit seeking several declarations:
    - To declare the contract void and illegal
      - To declare it violates RBI Guidelines
    - To declare it beyond the company's authority
- They also requested injunctions to:
  - Stop the bank from recovering any money
  - Force the bank to deposit all related documents in court
- Court Proceedings:
  - The court initially ordered a status quo

- This was later modified to prevent the bank from enforcing the contract
- The bank filed counter-applications requesting:
  - Prevention of the plaintiff from selling assets
  - Restriction on transactions with other banks
  - Bank guarantee of Rs. 40 crores
  - Various other procedural requests
- The case essentially revolves around a complex financial derivative contract that the plaintiff wants to void, while the bank wants to enforce it.

## Issue Involved

Whether the derivative contract is void or valid in the eyes of law?

## Observations

- A derivative transaction is considered a 'debt' under banking laws
- Banks can handle derivative transactions as part of their normal banking business.
- Just because something is a 'debt' doesn't automatically prevent someone from filing a civil lawsuit. People can still file civil suits in certain limited situations.
- However, if the borrower's case is closely tied to the bank's claim, the case should go to the Debt Recovery Tribunal (DRT).
- In this case, it wasn't transferred only because the bank didn't ask for it
- A High Court cannot stop proceedings in courts that aren't "subordinate" to it
- The DRT is not considered subordinate to the High Court. Therefore, the High Court cannot stop someone from going to the DRT. However, the High Court can still hear the case for other aspects
- A wagering agreement must have all these four elements:
  - Two parties must have opposite views about a future uncertain event
  - One party must win and the other must lose when the event happens
  - The parties shouldn't have any real interest in the event itself
  - Neither party should intend the contract to be legally binding (it's just a cover for betting)
- Key Findings in This Case:
  - The derivative transaction here was not considered betting because:
    - **It served a real business purpose (like insurance)**
    - **It helped the company manage its financial risks**
- The transaction was considered legal because:
  - It's specifically allowed by various laws and rules
  - What's legally permitted cannot be against public policy
- Important Principle:
  - If something is explicitly allowed by law, it cannot be considered against public policy
- This case essentially established that derivative transactions are legal financial instruments when used for business purposes like risk management, rather than mere speculation or

betting.

## **Conclusion**

- The judgment discusses the complex topics of derivative contracts.
- It is one of the first instances where the legality of derivative contracts was challenged.