CASE NO.:
Appeal (civil) 9 of 2008

PETITIONER:
Reserve Bank of India

RESPONDENT:
M.Hanumaiah & Ors.

DATE OF JUDGMENT: 04/01/2008

BENCH:
G.P.Mathur & Aftab Alam

JUDGMENT:
J U D G M E N T
(Arising out of SLP) No.13664/2005)

AFTAB ALAM,J.

Leave granted.

Whether the principles of natural justice have any application at the stage when the Registrar Co-operative Societies, on being so required in writing by the Reserve Bank of India passes an order removing the Committee of Management of a Co-operative Bank and appointing an Administrator to manage its affairs for such period, as may be specified by the Reserve Bank of India? This is the question that falls for consideration in this case.

The facts and circumstances in which the question arises are brief and simple and may be stated thus :

On inspection of Kalidasa Cooperative Bank Ltd. (respondent No.16) (hereinafter referred to as the \021Cooperative Bank\022 or \021the Bank\022) made on June 30, 1994 under Section 35 read with Section 56 of the Banking Regulation Act the Reserve Bank of India (the appellant before us) found a number of serious irregularities in its affairs. It sent a copy of the inspection report to the Cooperative Bank and called the members of its board of directors for discussion on the findings in the report. It also forwarded a copy of the inspection report to the Joint Registrar, Cooperative Societies. The Joint Registrar advised the Reserve Bank to make requisition for supersession of the committee of management of the Bank. The Reserve Bank, however, withheld any action in that regard but called the members of the board of directors of the Bank for several rounds of discussions at different levels. The board of directors was repeatedly urged to take stringent actions to improve the financial health of the Bank. Apparently, no remedial measures were taken and the affairs of the Cooperative Bank continued in a state of financial distress. Finally, the Reserve Bank issued a requisition to the Registrar Cooperative Societies, Karnataka on January 22, 2002 requiring him to supersede the board of directors of the Cooperative Bank and to appoint an Administrator for a period of one year as provided under Section 30(5) of the Karnataka Cooperative Societies Act. The requisition was made in public interest and for preventing the affairs of the Bank being conducted in a manner detrimental to the interest of the depositors and for securing proper management of the Bank.

In compliance with the requisition made by the Reserve Bank the Registrar Cooperative Societies issued an order on January 31, 2002 superseding the board of directors of the Bank

and appointing an Administrator in its place.

The order of supersession issued by the Registrar was challenged before the Karnataka High Court by respondents 2 to 13 (members of the committee of management of the Cooperative Bank that was in existence at that time) in W.P.No.6706 of 2003 (CS-RES). The writ petition was allowed by a learned Single Judge of the Court by order dated September 21, 2002. It is a brief order in which after noticing the relevant provision as contained in Section 30(5) of the Karnataka Cooperative Societies Act, the learned Judge simply observed as follows :

\023From the order, I find that the supersession is at the instance of the Reserve Bank of India since it is referred to in the impugned order. Further, the reason given by the Reserve Bank of India in order to supersede the Committee of Management in the public interest has not been disclosed in the impugned order. Further, no opportunity of hearing also has been afforded before passing an order by the Cooperative Bank. In the result, I pass the following order :

(a) Writ Petition is allowed.
(b) The impugned order is quashed.\024
(Emphasis added)

Against the order passed by the learned Single Judge, the Reserve Bank of India preferred Writ Appeal No.6120 of 2002 (CS-RES). When the appeal was taken up on March 31, 2003, the Court was told that fresh elections for the committee of management were to take place on March 20. The Division Bench took the view that this development had rendered the writ appeal infructuous and disposed it of as such, leaving it open \021to the Reserve Bank to proceed against the Bank, if necessary, in accordance with law\022.

Mr.R.N.Trivedi, learned senior counsel, appearing on behalf of the appellant, submitted that both the learned Single Judge and the Division Bench of the High Court seriously erred in the matter, the learned Single Judge by introducing the elements of natural justice where none existed and the Division Bench by treating the appeal as infructuous.

The learned counsel submitted that the Division Bench overlooked the main issue and failed to appreciate that as long as the Registrar was held obliged to give an opportunity of hearing to the cooperative bank it was pointless to say that it \021would be open to Reserve Bank of India to proceed against the bank, if necessary, in accordance with law\022. Counsel further submitted that the learned Single Judge had set aside the supersession order on two grounds. The first ground was wrong on facts and the second was flawed legally. It was incorrect to say that the order of the Registrar did not disclose the reasons for supersession. The reasons were stated in the preamble of the order. Moreover, the reasons for supersession were stated in detail in the requisition made by the Reserve Bank. But it was the second ground in regard to the opportunity of hearing to the cooperative bank that was fundamentally bad as it tended to defeat the very object and purpose of supersession of the managing committee of the bank. Learned counsel submitted that the order of the learned Single Judge would in effect give rise to a process of adjudication at the level of the Registrar. In other words, the Reserve Bank which is the apex expert body in the country in regard to banking affairs would be required to go to the Registrar and satisfy him about the need for supersession of the management of the bank. What is worse is that this process of adjudication might take a few weeks\022 time and thus completely

frustrate the need for an urgent intervention by the Reserve Bank in order to protect the interests of small depositors.

We are satisfied that Mr.Trivedi is right in his submission and though the managing committee of the Cooperative Bank for the supersession of which action was taken by the Reserve Bank may no longer be in existence the issue involved in the case needs to be decided as it is likely to crop up in future in regard to the respondent-bank or other cooperative banks.

In order to examine the question it would be best to begin with the legal provision. Section 30 of the Karnataka Co-operative Societies Act, 1959 is as follows :

\02330. Supersession of committee \026 (1) If, in the opinion of the Registrar \026

(a) the committee of a co-operative society persistently makes default or is negligent in the performance of the duties imposed on it by this Act or the rules or the bye-laws or commits any act which is prejudicial to the interests of the society or its members, or is otherwise not functioning properly; or

(b) a co-operative society is not functioning in accordance with the provisions of this Act, the rules or bye-laws or any order or direction issued by the State Government or the Registrar, \023including the direction issued under Section 30B\024.

the Registrar may, after giving the committee an opportunity to state its objections, if any, by order in writing remove the said committee, and appoint an administrator to manage the affairs of the society for such period, not exceeding [six months], as may be specified by the Registrar. The Registrar may for the reasons to be recorded in writing extend the period of such appointment for a further period of six months at a time and in any case such extension shall not exceed one year in aggregate.

(2) The administrator so appointed shall, subject to the control of the Registrar and such instructions as he may give from time to time, exercise all or any of the functions of the committee or of any [office bearer] of the co-operative society and take such action as he may consider necessary in the interest of the society.

(3) The administrator shall, before the expiry of his term of office arrange for the constitution of a new committee after holding the election in accordance with this Act, the rules and the bye-laws of the co-operative society.

Provided that in such an election, no member of the committee removed under sub-section (1) shall, notwithstanding anything contained in this act, the rule or the bye-laws, be eligible for being elected as a member of the Committee, for a period of four years from the date of supersession of the committee under the said sub-section.

(4) Before taking any action under sub-section (1) in respect of a co-operative society, the Registrar shall consult the financial banks to which it is indebted.

(5) Notwithstanding anything contained in this Act, the Registrar shall, in the case of a co-operative bank, if so required in writing by the Reserve Bank of India in public interest or for preventing the affairs of the co-operative bank being conducted in a manner detrimental to the interest of the depositors or for securing the proper management of the co-operative bank, by order in writing, remove the committee of that co-operative bank and appoint an administrator to manage the affairs of the co-operative bank for such period as may, from time to time, be specified by the Reserve Bank of India.\024

(Emphasis added)

Sub-sections (1) to (4) relate to removal of the committee of the cooperative society and sub-section (5) relates to supersession of the managing committee of a cooperative bank. It is to be seen that in case of removal of the committee of a cooperative society compliance with the principles of natural justice is expressly required inasmuch in sub-section (1) it is stipulated that the Registrar would pass the order of removal only \021after giving the committee an opportunity to state its objections\022. On the other hand the requirement of any hearing is absent in sub-section (5) which starts with a non-obstante clause that also covers the provisions of the earlier sub-sections of Section 30. Mr.Trivedi submitted that in case of supersession of the management of a cooperative bank there was no application of the principles of natural justice for two reasons; one was that the Reserve Bank of India was the apex expert body in the country in banking matters and once the Reserve Bank of India was satisfied in regard to the need of supersession of the bank\022s management, the Registrar cooperative societies who had no experience in the affairs of banks was simply obliged to carry out the instructions of the Reserve Bank; secondly, once the decision of supersession was taken it was necessary to have it effected speedily because any delay would cause irreparable loss and harm to the interests of small depositors of the bank. It was, therefore, by design that no opportunity of hearing was mentioned in sub-section (5) even though it was stipulated earlier (in sub-section (1)) in the same section.

Mr.Trivedi submitted that a similar question arose before this Court when the validity of section 38 of the Banking Companies Act, 1956 came in question in the case of Joseph Kurnvilla Velukunnel vs. Reserve Bank of India & Ors. [AIR 1962 SC 1371] relating to the winding up of the Palai Central Bank Ltd., Kerala. The Reserve Bank of India made an application in the High Court of Kerala under Section 38 of the Banking Companies Act read with some allied provisions of the Indian Companies Act for the winding up of the Palai Central Bank Limited and for appointment of the official liquidator etc. The High Court allowed the application and the decision of the High Court came to be challenged before this Court in appeal in which the main question related to the constitutional validity of Section 38 of the Banking Companies Act. A Constitution Bench upheld the validity of the provision by a majority of 3 to 2.

Section 38 of the Banking Companies Act laid down as follows :

\02338(1). Notwithstanding anything contained in Section 391, Section 392, Section 433 and Section 583 of the Companies Act, 1956, but without prejudice to its powers under sub-section (1) of Section 37 of this Act, the High Court shall order the winding up of a banking company \026

(a) if the banking company is unable to pay its debts; or

(b) if an application for its winding up has been made by the Reserve Bank under Section 37 of this Section.

(2) The Reserve Bank shall make an application under this section for the winding up of a banking company if it is directed so to do by an order under clause (b) of sub-section (4) of Section 35.

(3) The Reserve Bank may make an application under this section for the winding up of a banking company ---

xxx xxx xxx xxx
(b) if in the opinion of the Reserve Bank --
xxx xxx xxx xxx
(iii) the continuance of the banking company is prejudicial to the interests of its depositors.

Mr.Trivedi argued that in case of Palai Bank the issue was far more fundamental and grave than the issue in the case in hand. In Palai Bank the provision of Section 38 ousted the authority and power of the High Court and not merely that of a Registrar, Cooperative Societies; furthermore, the provision allowed for the winding up of a banking company and thus interfered with the fundamental right to carry on business. In the case in hand the business of the cooperative bank would go unhindered and interference was limited only to the management of the bank.

One of the grounds on which the validity of Section 38 was challenged was that it offended the principles of natural justice. In paragraphs 30 to 31 of the judgment this Court noticed the grounds on which the provisions were assailed and observed as follows :

\023(30) The main ground of attack is the way Ss.38(1) and (3)(b)(iii) make it mandatory for the High Court to pass an order winding up a banking company whenever the Reserve Bank under its powers or under an order of the Central Government makes an application for the winding up a banking company. It is argued that such a power to the Reserve Bank is an uncontrolled and despotic power and to crown all, access to Courts is not possible because the Court itself must pass an order without deciding whether the affairs of the banking company are being conducted in a manner detrimental to the interests of the depositors \026 a fact capable of being proved like any other fact. It is argued as a matter of principle that any law which bars a decision by the Court is itself unreasonable without more. Mr.Pathak, in supplementing the above contentions of Mr.Nambiar, also contends that by the law in question a judicial process has been converted into

an executive action, and subjective determination has taken the place of judicial determination. He also contends that the Reserve Bank accuses a banking company, and then tries the issue to the complete exclusion of Courts.

(31) It must not be overlooked that the winding up of a banking company takes place before the High Court and under the process of law. The judicial process is excluded only to respect of the momentous decision whether a winding up order should be made or not. This opinion is left to the Reserve Bank, and the Court merely passes an order according to the Reserve Bank\022s opinion, and then proceeds to wind up the banking company according to law. The narrow question is whether in leaving this decision to the Reserve Bank the law offends the principles of natural justice and becomes so unreasonable, viewed in the light of Art.19, as to become void. This is the point on which the respective parties joined issue and had much to say, and this is the crucial point in this case.\024

(emphasis added)

Rejecting the submissions the majority decision referred to an earlier decision of this Court in Virendra vs. The State of Punjab [1958 SCR 308] relied upon by the Attorney General and in paragraphs 44 and 45 observed as follows :

\023(44) These observations lay down clearly that there may be occasions and situations in which the legislature, may with reason, think that the determination of an issue may be left to an expert executive like the Reserve Bank rather than to Courts without incurring the penalty of having the law declared void. The law thus made is justified on the ground of expediency arising from the respective opportunities for action. Of course, the exclusion of Courts is not lightly to be inferred nor lightly to be conceded. The reasonableness of such a law in the total circumstances will, if challenged, have to be made out to the ultimate satisfaction of this Court and it is only when this Court considers that it is reasonable in the individual circumstance that the law will be upheld.

(45) In the present case, in view of the history of the establishment of the Reserve Bank as a central bank for India, its position as a Bankers\022 Bank, its control over banking companies and banking in India, its position as the issuing bank, its power to license banking companies and cancel their licenses and the numerous other powers, it is unanswerable that between the court and the Reserve Bank, the momentous decision to wind up a tottering or unsafe banking company in the interest of the depositors, may reasonably be left to the Reserve Bank. No doubt, the Court can also, given the time perform this task. But the decision has to be taken without delay, and the Reserve Bank already knows intimately the affairs of the banking companies and has had access to their books and accounts. If the Court were called upon to take immediate action, it would almost always

be guided by the opinion of the Reserve Bank. It would be impossible for the Court to reach a conclusion unguided by the Reserve Bank if immediate action was demanded. But the law which gives the same position to the opinion of the Reserve Bank is challenged as unreasonable. In our opinion such a challenge has no force. The situation that arose in this case is typical of the occasions on which this extraordinary power would normally be exercised, and, as we have said already, if the power is abused by the Reserve Bank, what will be struck down would be the action of the Reserve Bank but not the law. An appeal against the Reserve Bank\022s action or a provision for an ex post fact finding by the Court is hardly necessary. An appeal to the Central Government will be only an appeal from Caesar to Caesar, because the Reserve Bank would hardly act without the concurrence of the Central Government and the finding by the Court would mean, to borrow the macabre phrase of Raman Nayar,J. a post-mortem examination of the corpse of the banking company.\024
(emphasis added)

The decision in the case of Palai Bank undoubtedly goes a long way to support the contention of the appellant in the case in hand.

Mr.Trivedi also submitted that the Maharashtra Cooperative Societies Act, 1960 had a similar provision in Section 110A like the one contained in Section 30(5) of the Karnataka Act. Sub-section (ii) of Section 110A provided that an order for the winding up of the bank would be made by the Registrar, if so required by the Reserve Bank of India in the circumstances referred to in section 13-D of the Deposit Insurance Corporation Act, 1961. Dealing with the provisions the Bombay High Court had held that the power conferred under Section 110A of the Maharashtra Cooperative Societies Act should not be hindered by reading into it the requirement of show cause notice. Learned counsel cited before us two decisions of the Bombay High Court. One in Mahendra Husanji Gadkari vs. State of Maharashtra & Ors. [1992 Mah.L.J.1442] and the other in Ishwardas Premkumar Choradiya & Anr. vs. State of Mahrashtra & Ors. [2002 (2) Mah.L.J.844]. In the latter decision, a learned Single Judge of the Bombay High Court held as follows :

\023The question is : whether under Section 110A of the Maharashtra Cooperative Societies Act, 1960, respondent No.5 was duly bound to give a show cause notice to the petitioners herein. In the first instance, the section does not provide for a show cause notice. Once that be so, the question is : whether it can be implied in the absence of provision of show cause notice whether by implication it is required that a show cause notice must be issued as it involves civil consequences. Sub-section (3) of Section 110A of the Mahrashtra Cooperative Societies Act, 1960, came up for consideration before a Division Bench of this Court in the case of Mahendra Husanji vs. State of Maharashtra, 1992 Mah.L.J.1442. The Division Bench of this Court, after considering the provisions of sub-section (3) of Section 110A of the Maharashtra Cooperative Societies Act, has held that the Reserve Bank of India can issue

directions only when the situation contemplated by Section 110A of the Act exists. The directions issued are binding on the Registrar. In other words, once a direction is issued by the Reserve Bank of India, the Registrar has no discretion in the matter, but to supersede and appoint an Administrator. Once that be so, and as there is no discretion left in respondent No.5, it must mean that the right of hearing is excluded. Once that be so, there was no question of issuing a show cause notice to the petitioner herein before passing the impugned order. In fact, though not directly in issue in the case of L.V.Sasmile vs. State of Maharashtra 1992 CTJ 729, another Division Bench, considering the material on record, had directed the appointment of an Administrator under Section 110A of the Maharashtra Cooperative Societies act. That also would indicate that there is no requirement under Section 110 for hearing.\024

In our opinion the Bombay High Court has taken the correct view of the matter.

On hearing Mr.Trivedi, counsel for the appellant, and on a careful consideration of the relevant provisions of law and the decisions cited before us we have no hesitation in accepting the submissions made on behalf of the appellant. We accordingly answer the question (framed in the beginning of the judgment) in the negative and hold and find that on receipt of a requisition in writing from the Reserve Bank of India the Registrar Cooperative Societies is statutorily bound to issue the order of supersession of the committee of management of the cooperative bank. At that stage the affected bank/its managing committee has no right of hearing or to raise any objections.

The question may here arise whether the principles of natural justice are completely excluded from the process or it may be that against the requisition, the affected bank may move the Reserve Bank itself and try to show that it had wrongly arrived at the decision for its supersession. The other course may be that after the supersession order was issued by the Registrar that may be challenged before a court of law and in that proceeding one of ground for assailing the order might be that the decision of the Reserve Bank was arrived at without giving the affected cooperative bank a proper opportunity of hearing. We, however, refrain from going into that question as it does not arise in the facts of the present case.

In light of the discussions made above, both the orders passed by the learned Single Judge and the Division Bench appear quite untenable. Both the orders are accordingly set aside. However, since the matter has become quite old it needs to be clarified that the order of supersession passed by the Registrar on January 31, 2002 shall not be automatically revived but in case the Reserve Bank of India is of the opinion that the situation so warrants it may issue a fresh requisition to the Registrar Cooperative Societies, Karnataka, who would on that basis pass the order of supersession as held in the judgment.

The appeal is, accordingly, allowed but with no order as to costs.