Insolvency and Bankrutpcy Board of India 7th Floor, Mayur Bhawan, Connaught Place, New Delhi -110001

2nd April, 2019

Subject: Judgementⁱ dated 2nd April, 2019 of the Hon'ble Supreme Court in the matter of Dharani Sugars and Chemicals Ltd. Vs. Union of India & Ors. [Transferred Case (Civil) No. 66 of 2018 in Transfer Petition (Civil) No. 1399 of 2018 with several Writ Petitions and Transferred Cases and a SLP].

While declaring the circular dated 12th February, 2018 issued by RBI as *ultra vires* of section 35AA of the Banking Regulation Act, 1949, the Hon'ble Supreme Court of India made several important findings and rulings as under:

Sl. No.	Issues	Held	Para /Page
1	Constitutional validity of sections 35AA and 35AB introduced by the Banking Regulation (Amendment) Act, 2017.	a. The provisions are not excessive in any way nor do they suffer from want of any guiding principle. These are in the nature of amendments which confer regulatory powers upon the RBI to carry out its functions under the Act and are not different in quality from any of the sections which have already conferred such power. For example, section 21 makes it clear that the RBI may control advances made by banking companies in public interest, and in so doing, may not only lay down policy but may also give directions to banking companies either generally or in particular. Similarly, under section 35A, vast powers are given to issue necessary directions to banking companies in public interest, in the interest of banking policy, to prevent the affairs of any banking company being conducted in a manner detrimental to the interest of the depositors or in a manner prejudicial to the interest of the banking company, or to secure the proper management of any banking company. Therefore, these provisions which give the RBI certain regulatory powers cannot be said to be manifestly arbitrary.	
		b. As regards guidelines for exercise of powers, such guidance can be obtained not only from the Statement of Objects and Reasons and the Preamble to the Act, but also from its provisions. Sections 22, 25, 29, 30, and 31 give guidance as to how the RBI is to exercise these powers under the newly added provisions. There is no dearth of guidance for the RBI to exercise the powers delegated to it by these provisions.In view of the above, sections 35AA and 35AB are constitutionally valid.	17/38 & 44

2	Scope of power of the RBI under section 35AA vis-a-vis the impugned circular.	a. A cursory reading of section 35A makes it clear that there is nothing in the aforesaid provision which would indicate that the power of the RBI to give directions, when it comes to the Insolvency Code, cannot be so given. The width of the language such as 'public interest', 'banking policy', etc. used in section 35A makes it clear that if otherwise available, use of section 35A as a source of power for the impugned circular cannot be interdicted on the ground that the Insolvency and Bankruptcy Code, 2016 (Code) could not have been in the contemplation of Parliament in 1956, when section 35A was enacted.	24/52
		b. If a specific provision of the Banking Regulation Act makes it clear that the RBI has a specific power to direct banks to move under the Code against debtors in certain specified circumstances, it cannot be said that they would be acting outside the four corners of the statutes which govern them, namely, the RBI Act and the Banking Regulation Act.	26/55
		c. Section 35AA makes it clear that the Central Government may, by order, authorise the RBI to issue directions to any banking company or banking companies when it comes to initiating the insolvency resolution process under the provisions of the Code. Therefore, without authorisation of the Central Government, no such directions can be issued by the RBI.	29/60
		d. Prior to the enactment of section 35AA, it may have been possible for the RBI to issue directions under sections 21 and 35A to a banking company to initiate insolvency resolution process under the Code. But after introduction of section 35AA, it may do so only within the four corners of section 35AA.	30/65
		e. If a statute confers power to do a particular act and has laid down the manner in which that power has to be exercised, it necessarily prohibits the doing of the act in any manner other than that which has been prescribed.	31/65
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f. The RBI can only direct banking institutions to move under the Code if two conditions precedent are specified, namely, (i) that there is a Central Government authorisation to do so; and (ii) that it should be in respect of specific defaults. The section, therefore, by necessary implication, prohibits this power from being exercised in any manner other than the manner set out in section 35AA.	31/66
g. The words "without prejudice" appearing in a section make it clear that powers that are enumerated are only illustrative of a general power and do not restrict such general power. The power to issue directions given by section 35AB is, therefore, in addition to the power under section 35A.	35/71
 h. The scheme of sections 35A, 35AA, and 35AB is as follows: (i) When it comes to issuing directions to initiate the insolvency resolution process under the Code, section 35AA is the only source of power. (ii) When it comes to issuing directions in respect of stressed assets, which directions are directions other than resolving this problem under the Code, such power falls within section 35A read with section 35AB. 	38/73
i. When one section of a statute grants general powers, as opposed to another section of the same statute which grants specific powers, the general provisions cannot be utilised where a specific provision has been enacted with a specific purpose in mind.	39/74
j. Stressed assets can be resolved either through the Code or otherwise. When resolution through the Code is to be effected, the specific power granted by section 35AA can alone be availed by the RBI. When resolution <i>de hors</i> the Code is to be effected, the general powers under sections 35A and 35AB are to be used. Any other interpretation would make section 35AA otiose.	40/75

3	Constitutional validity of	a. Section 35 AA enables the Central Government to authorise the RBI to issue such directions	41-42/
5	the impugned circular		76-78
	issued by the RBI.	and payable and is not paid by the corporate debtor. Therefore, what is important is that it is a	1010
		particular default of a particular debtor that is the subject matter of section 35AA. Any	
		directions which are in respect of debtors generally would be <i>ultra vires section</i> 35AA.	
		b. The power to be exercised under the authorisation of the Central Government requires "due	44/80
		deliberation and care" and hence refer to specific defaults.	
		c. There is nothing to show that the provisions of section $45L(3)$ have been satisfied in issuing	45/83
		the impugned circular. The impugned circular nowhere says that the RBI has had due regard	
		to the conditions in which and the objects for which such institutions have been established,	
		their statutory responsibilities, and the effect the business of such financial institutions is likely to have on trends in the money and capital markets.	
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		d. The impugned circular applies to banking and non-banking institutions alike. Non-banking	45/83
		financial institutions are inseparable from banking institutions insofar as the application of the	15/05
		impugned circular is concerned. It is very difficult to segregate the non-banking financial	
		institutions from banks so as to make the circular applicable to them even if it is ultra vires	
		insofar as banks are concerned.	
		e. In view of the above, the impugned circular is ultra vires, and has no effect in law.	45-46/84
		Consequently, all actions taken under the said circular, including actions by which the Code	
		has been triggered must fall along with the said circular. As a result, all cases where debtors	
		have been proceeded against by financial creditors under section 7 of the Code, only because	
		of the operation of the impugned circular, are non-est.	

ⁱ Prepared by Legal Division for the sole purpose of creating awareness and must not be used as a guide for taking or recommending any action or decision, commercial or otherwise. One must do its own research or seek professional advice if it intends to take any action or decision using the material covered here.