REPORTABLE

IN THE SUPREME COURT OF INDIA
CIVIL ORIGINAL JURISDICTION

WRIT PETITION (CIVIL) NO. 355 OF 2011

CENTRE FOR PUBLIC LITIGATION .... PETITIONER

VERSUS

UNION OF INDIA & ORS ..... RESPONDENTS

J U D G M E N T

Dr D Y CHANDRACHUD, J

Centre for Public Interest Litigation, while invoking the jurisdiction of this Court under Article 32 of the Constitution sought diverse reliefs in relation to the conduct of business and affairs of Industrial Finance Corporation of India. The reliefs which have been sought in these proceedings are for :

(i) The removal of Atul Kumar Rai, the Respondent No. 4 from the post of Chief Executive Officer and Managing Director;

(ii) An independent investigation into allegations of administrative and financial irregularities of IFCI;

(iii) A direction to the Union of India to exercise its powers under the "surviving provisions" of the Industrial Finance Corporation;

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Date: 2018.09.23 16:18:49 IST
Reason:

(iv) Transfer of Undertaking and Repeal Act, 1993, in particular by enforcing its

rights for conversion of an investment of Rs. 523 crore in Optional Convertible Debentures into equity.

2 Industrial Finance Corporation of India (IFCI) was established as a statutory Corporation under the Industrial Finance Corporation of India Act, 1948 by the provisions of the Industrial Finance Corporation of India (Transfer of Undertaking and Repeal) Act, 1993. The Act of 948, was repealed and the Corporation was converted into a Company. The Statement of Objects and Reasons accompanying the introduction of the Bill in Parliament indicated that the conversion of IFCI from a statutory Corporation to a Company was necessitated in view of the decline in the availability of concessional funds from government and the Reserve Bank of India. As a result of the developments which took place in the financial sector, it had become necessary for IFCI to raise resources from the market.

3 A major shareholder of IFCI was the Industrial Development Bank of India which was essential in a competing market position. As a result of the repeal enactment a new Company governed by the Companies Act 1956 was established to which the entire undertaking business and functions of IFCI as well as its assets and liabilities were transferred. The financial position of IFCI painted a dismal picture. On 31 March 2002, its accumulated losses were over Rs. 1100 crore; its net worth stood at a negative Rs. 31 crore and non-performing assets were officially estimated at 32 per cent.

4 A group of Ministers was formed in July 2002 to work out a restructuring package following its recommendations. A note was placed before the Cabinet in

November 2002 stating that 56 per cent of the equity was held by public sector institutions and the nationalized banks. The restructuring package was approved by the Union Cabinet on 17 February 2005 and until 2006-07 a total amount of Rs. 2932.31 crore was provided by way of assistance to IFCI of which an amount of Rs. 523 crore was in the form of Optional Convertible Debentures. As on 31 March 2011, IFCI had outstanding loans to the Union Government of Rs. 923 crore, grants-in-aid of Rs. 2409.31 crore and outstanding guarantees of Rs. 2797.06 crore. Under the package which was approved by the Union Government a total amount of Rs. 2932.31 crore was released to IFCI. In or about December 2009, the Union Government received several complaints from Members of Parliament and from the employees association of IFCI alleging gross irregularities in certain investments made and generally in regard to the accountability of IFCI to the Government of India. Among the irregularities is the role ascribed to the Respondent No. 4, Atul Kumar Rai. The Respondent No. 4 belongs to the IES cadre and had joined the banking division (later known as the Department of Financial Services) as a Director on 1 November 2002. On 7 November 2002, he was appointed as a Director (Industrial Finance), in the Department of Financial Services, Ministry of Finance *inter alia* dealing with the operational, policy and budgetary matters relating to financial institutions including IFCI. On 21 August 2005, he was nominated as Government Director on the Board of IFCI in which capacity he continued until taking voluntary retirement. In February 2007, the Respondent No. 4 sought voluntary retirement with effect from 28 February 2007 following a cadre clearance, his voluntary retirement was approved with effect

from 31 May 2007. Before being relieved the Respondent No. 4 addressed a note of 30 April 2007 stating that the Board of Directors had offered him a post of a whole Time Director by Board's resolution dated 7 March 2007. Approval for his accepting the position was conveyed on 1 January 2007 subject to his furnishing a mandatory declaration in terms of the instructions under Rule 10 of the CCS (Pension) Rules dated 5 December 2006. The Respondent No. 4 is stated to have submitted the declaration on plain paper on 31 March 2007 and joined IFCI as its Chief Executive Officer and Managing Director on 1 June 2007.

5 A Committee of Privileges of the Rajya Sabha raised certain issues in the matter of a breach of privilege by the Respondent No. 4, with the Secretary (Financial Services) on 19 August 2010. While instituting these proceedings, the petitioners have sought to highlight the role played by the Respondent No. 4 in the financial misdemeanour and irregularities committed in the conduct of business by IFCI. Among the irregularities which have been highlighted by the petitioners are the following :

> "(i) Purchase of 5% stake in the MCX-SX by IFCI management on a much higher price of Rs. 35 per share whereas the Union Bank of India and the Bank of India acquired the shares of the same company at Rs. 10 per share, thereby inflicting a loss of Rs. 168 crores on the IFCI;
> (ii) Notice dated 22.4.2009 issued by the Registrar of Companies, NCT Delhi and Haryana to the IFCI, calling for an explanation from the IFCI on various irregularities/allegations, appalling corruption including the questionable acquisition of 17.4% shareholding of Rajus of the Satyam in MAYTAS Infrastructure, it has come to light that Shri Ramalinga Raju had borrowed a loan of Rs. 85 crores after pledging 10 lakh shares of the Satyam and the MAYTAS barely 72 hours before he had confessed to irregularities in the Satyam;
> (iii) Sanction of Rs. 225 crores to Blue Coast Hotels Ltd., whose name has been put up on the wilful defaulters list by the Reserve Bank of India" (Id. at p-D)

These proceedings were entertained by the court while issuing a notice on 5 September 2011. Directions were issued for the submission of counter affidavits. On 1 August 2013, this Court noted the statement which was made before it to the effect that the Respondent No. 4 had since been removed from the post of CEO and MD of IFCI as a result of which that part of the relief had been rendered infructuous.

6 The second prayer, as the court noted was for the initiation of the investigation into various allegations of administrative and financial irregularities in IFCI. This Court noted that an investigation by the Registrar of Companies was underway. As regards the third prayer for the exercise of control by the Union Government, the court was informed that this was being done. In pursuance of the order dated 1 August 2013, this Court was informed on 8 March 2016 by the learned counsel appearing on behalf of the Union Government in the Ministry of Corporate Affairs that the report had been submitted by the Registrar of Companies, Noida. The report has since been filed on 29 June 2016. This Court was informed by the Solicitor General on the basis of an affidavit of the Joint Director in the Ministry of Corporate Affairs that the Board of IFCI "is being reconstituted and the process overhauled". This Court accordingly stood over for the hearing so as to enable the Union Government to apprise it on whether the reconstituted board had looked into the allegations of mismanagement and financial irregularities which were referred to in the recommendations contained in the report dated 8 January 2013 and on whether any action was initiated on the basis thereof.

7 During the course of the hearing, counter affidavits have been filed in these proceedings including on behalf of the Union Government, IFCI as well as the Respondent No. 4. The petitioners have availed the opportunity to traverse the material contained in the counter affidavits in rejoinder. The material which has been placed before this Court on the record *inter alia* contains : (i) a copy of the inspection report under Section 209(A) of the Companies Act 1956 dated 10 April 2012 submitted by the Joint Director (Inspection) ; (ii) a copy of the report of the Registrar of Companies, Delhi and Haryana dated 8 January 2013; (iii) a copy of the letter dated 4 June 2013 addressed by the Secretary to the Government of India in the Ministry of Finance (Department of Financial Services) to the Secretary, Ministry of Corporate Affairs. The report of the ROC dated 8 January 2013 notes that the complaints against IFCI commenced with a reference from the Lok Sabha Secretariat (Standing Committee on Finance) having forwarded the complaints against affairs of the Companies. IFCI refused to furnish information and challenged the jurisdiction of the ROC by filing Writ Petitions in the Delhi High Court, after the disposal of those Writ Petitions, the ROC submitted its reports to the Ministry of Corporate Affairs in 2009, 2010 and 2011. The findings in the reports are as follows: (i) acquisition of 5 per cent stock in July 2009 by IFCI in MCX-SX at the rate of Rs. 35 per share at an alleged loss of Rs. 168 crore. The findings in the reports are as follows :

> "The issue of acquisition of 5% stake in MCX-SX in July 2009 from TCIL by IFCI @ of Rs. 35/- per share while Union Bank of India acquired @ Rs. 10/- per share inflicting a loss of Rs. 168 crores (approximately) to IFCI, a Public Financial Institution, was raised in a complaint against the company in a complaint filed by Sh. Mohammad Ajeeb , Hon'ble Member of Parliament (Rajya Sabha) addressed to the Hon'ble Prime Minster and various other

> authorities including this office enclosing therewith a complaint signed by 54 shareholders of the Company. This office had submitted a detailed report vide this office letter dated 13.5.2011 on examination of the said complaint received by this office. The detailed factual information and prima facie findings were given by this office in the said report dated 13.5.2011. The allegation was prima facie found to be correct. Copy of this office letter dated 13.5.2011 along with a copy of the complaint received from the Hon'ble MP are enclosed for ready reference and collectively marked as Annexure-I. Ministry had ordered inspection under Section 209A of the Companies Act,1956 of the Books of Account and other records of the captioned Company vide Ministry letter No. 3/235/2009-CL.II dated 16.9.2011 on the basis of report under Section 234(b) dated 13.5.2011 submitted by this office. The inspection was conducted by an officer from the office of Regional Director (NR). He has given his comments on this issue vide para 17 in Annexure A attached to his report. The Company had claimed that the amount of premium @ Rs. 25/- per share along with interst @ 9.5% per annum has been returned by Financial Technologies (India) Limited (FTIL), the co-promoter of MCX-SX, as MCX was not able to come out with an IPO before 31.3.2011. It is not clear from the inspection report as to under which head FTIL has returned this amount whereas the amount was paid to MCX under the head "share premium amount" which cannot be refunded in this manner. It is also pertinent to mention here that this office has reported vide on para 14 to the Notes to Account to the Balance Sheet as at 31.3.2010 of FTIL that FTIL has earned profit of Rs. 2,36,82,81,250/- (net of directly attributable brokerage expenses of Rs. 7,54,68,750/-) whereas the Company has refused to give any information on the payment of brokerage to the IO as noted in his comments vide para 24 in Annexure A to his report dated 10.4.2010. Thus, this transaction, prima facie smacks of lack due diligence and is prejudicial to the interest of the Company and its members/stakeholders. (id. at p-172-173)

Loss of Rs. 225 crore granted to Blue Coast Hotels and Resource Limited. The findings are as follows :

> "(a) The hotel is associated with Morpen Laboratories Limited and Sh. Sushil Suri, the Managing Director of Morpen, hold 0.37% stake in the said hotel and is also the Chairman and Managing Director of Morpen Laboratories Limited against whom the Ministry is indulges in a court case on account of default in repayment of deposits and interest to about 85,000 depositors. Certain Directors in BCH and its subsidiaries are Directors in Morpen group of companies or their near relatives are the Directors of Morpen Group of Companies. It was reported that the term loan of Rs. 150 Crore obtained from IFCI Limited

is prima facie, utilized for repayment of secured term loans of Rs. 72.49 crore to its existing lenders and in making further investments of Rs. 85 crore in the subsidiary Company of BCH namely Silver Resort Hotel India Private Limited (SRH). IFCI is also a major shareholder in SRH. It was further reported that on the basis of such examination the contention of IFCI that being on NBFC the loans are extended having commercial objective of the Company in mind is prima facie wrong and misleading particularly keeping into consideration the fact that IFCI had made investment of Rs. 85 crore in a newly incorporated (incorporated in 2010) subsidiary of BCH i.e. SRH. It was also noted that the promoters and group shareholding in BCH had decreased significantly in the financial year 2009-10 as compared to previous year shareholding following the loans/investments made by IFCI. This office had reported that this was one of the instances which show that the main objective of IFCI is to divert funds to real estates or auxiliary business that too in the garb of loan by NBFC. On this point this office also recived a complaint from All India Finance Corporation Employees Assistance on 27.3.2010 and accordingly a report No.5/367/2009/TC/COMP/719 dated 16.4.2010 was sent to the Minstry. Thus, this office had preliminary found that IFCI had made loans to wilful defaulters….

(c) However this office reiterates that the loan to BCH was not on the basis of adequate due diligence and lack of commercial prudence on the sanction of the loans as well as utilization of sanctioned loan and cannot be prima facie stated to be a loan by an NBFC whose motive is to finance for industrial infrastructure particularly in view of the track record of the Directors and promotoers of Morpen Group of Companies and further diversion of funds by BCH. (Id at p-173-175)

Financial dealings with Satyam Group of Companies. The findings are as follows :

"(a) This point of loans to Satyam group was also raised by the complainant in the above referred ocmplaint under the head *"Raju dug hole in IFCI too"*. The Hon'ble MP has referred to a news item published in newspaper wherein it was reported that "barely 72 hours before Satyam computer founder Sh. Ramalinga Raju confessed his crime he dug a hole in the fiancés of a public sector Industrial Finance Corporatin of India by borrowing loans of Rs. 85 crores after pledging 10 Lacs shares of Satyam and Mytas and 72 acres of land situated in Nagallore Vilalge….."This office had given a detailed report on this point vide para 9(f) of this office report dated 13.5.2011 referring to admission of the Company in its reply to the order under Section 324(1) issued by this office on the basis of reference received from Lok Sabha Secretariat (Standing Committee of Finance Branch) wherein the Company had admitted having securities of 17.45 Lacs shares in Mytas Infrastructure Limited by involving the pledge which it

> held as security for the loans sanctioned to "certain companies of Mytas Infrastructure Limited" but had not revealed the name of such 'certain companies'. IFCI had specifically denied furnishing the information as called for by this office on the contention that ROC has no reason to pass directions for furnishing information of cumulative shares pledge by the promoters and the list of loans granted to Satyam furnish the information/documents called by this office under Section 234 of the Companies Act, 1956.
> (b) The IO has given his findings on this issue as per para 23 in Annexure A to his report dated 10.4.2012. (Id at p- 175).

8 Besides these aspects the report deals with various other matters including investments in unquoted shares worth Rs. 2,500 crore; loss due to investments made otherwise than in the normal course of business; bad and doubtful debts written off to the extent of Rs. 279.85 crore, 284.66 crore and 512.81 crore during 2008-09, 2009-10 and 2010-11. The report has adverted to the lack of due diligence in various investments made by IFCI. Following the report, it appears that a communication was addressed by the Ministry of Corporate Affairs on 13 February 2013 to the Ministry of Finance (Department of Financial Services) in response, by letter dated 4 June 2013 the Secretary in the Ministry of Finance informed the Secretary in the Ministry of Corporate Affairs that the Respondent No. 4 has submitted his resignation which was accepted with effect from 31 May 2013. The letter stated that the Union Government was in the process of overhauling and reconstituting the entire Board of IFCI which was expected to be completed shortly. The letter stated that it was appropriate if the charges were looked at impartial by the reconstituted board of IFCI.

9 An affidavit has been filed in these proceedings on 13 July 2016 on behalf of the Union Government in the Ministry of Corporate Affairs (Department of Financial Services) it has been stated before the court that the report was forwarded to IFCI on

27 June 2013. The report was placed before the reconstituting board of IFCI on 30 July 2013 and 12 November 2013 earlier, as on 11 December 2012. The Board of IFCI consisted of 13 members as on 12 November 2013. The reconstituted board consisted of 8 members of whom 2 were on the previous board. The reconstituted board examined the report. The affidavit submitted on behalf of the Ministry of Finance contains the following summary of the observations of the board of IFCI.

> "(9) That the response of IFCI Ltd. inter-alia indicated no loss in share purchase; action under debt recovery laws where warranted; investment in unlisted equity made after appraisal with personal guarantees and pledge of shares; NPAs, wherever occurring were fully provided for and investment in debentures were done after due diligence, with ongoing action in some cases. (Id at p- 2-3)

10 The learned Solicitor General, while adverting to the findings in the report over the violation of the provisions of the Companies Act 1956 stated that where the violations are of a nature that is capable of being compounded, orders for compounding have been passed by the Company Law Board in five cases on 27 August 2013, 25 September 2013. In other cases, it has been stated that proceedings have been dropped. The Solicitor General submits that the prayer for the removal of the Respondent No.4 as CEO and MD will not survive since in the meantime, he has resigned from the post. As regards the exercise of the option for the conversion of OCD, into equity, it has been stated that due steps have been taken by the Union Government in this regard, reference has been made in the report submitted by the ROC on 8 January 2013 to the following :

> "(c) Allotment of Equity Shares to Central Government:- The Company has filed form No.2 vide SRN No. S15353568 on 31.10.2012 for allotment of 40 crores Equity Shares of Rs. 10/- each amounting to Rs. 400 crore to Govt. of India, Ministry of

> Finance, Deparment of Financial Services, Jeevan Deep Building, Parliament Street, Delhi- 110 001 vide allotment dated 17.10.2012 on conversion of Optionally Convertible Debentures held by Govt. of India amounting to Rs. 400 crore into 40 crore Equity Shares of the Company at par i.e. @ Rs. 10/- per shares ranking pari-passu with the existing Equity Shares. The Company has enclosed list of allottees certified copy of the extracts of the minutes of the meeting of the committee of Directors held on 17.10.2012 and also a copy of the extracts of the minutes of the 9th AGM of the Company held on 23.9.2002 (copies enclosed collectively marked as **Annexure 9).** The Company has filed another Form 2 vide SRN No. S19735174 on 1.1.2013 for allotment of 52.30 crore Equity Shares of Rs. 10/- each amounting to Rs. 523 crore to Govt. of India, Ministry of Finance, Department of Financial Services, Jeevan Deep Building, Parliament Street, Delhi- 110 001vide allotment dated 20.12.2012 on conversion of Optionally Convertible Debentures held by Govt. of India amounting to Rs. 523 crore into 52.30 Crore Equity Shares of the Company having face value of Rs. 10/- each ranking pari-passu with the existing Equity Shares. (Id at p- 186-187)

11 The material which has been placed before this Court during the course of the hearing is such as would, in our view, necessity close scrutiny and action by an independent regulatory. Learned counsel appearing on behalf of the petitioners has in fact supported this line of action, submitting that it would not be adequate or sufficient to rest on the response submitted by IFCI for the inspection and the report of the ROC. As we have noted earlier following the receipt of the report of the ROC, the Ministry of Corporate Affairs eliciting the response to the inspection report dated 8 January 2013 of the ROC. The Department of Financial Services in turn forwarded the report to IFCI. IFCI Board considered the report and came to the conclusion essentially that there were no irregularities. The position which has been adopted before this Court by the Department of Financial Services is that it would be sufficient in itself, once IFCI through its newly constituted board had not found anything untoward or remits. This

in our view is not a satisfactory method of resolving the issues which have been raised and the serious concerns which emerge from the inspection report of the ROC. As of it now emerges, the object and purpose of such an enquiry is to scrutinize serious allegations which have been levelled in regard to the investments which were made by IFCI and particularly in regard to the role of its erstwhile CEO and MD, a scrutiny of the report by the Board of IFCI would not suffice to the affairs and impartial investigation. IFCI has a huge financial commitment to the Union Government in terms of loans, grants and guarantees. A dire financial position of IFCI led the Union Government to commit resources to raise the company from a position of serious financial distress. There is a vital element of public interest in ensuring that a full, fair and objective scrutiny is carried out by an independent regulatory with a view to ensure a degree of accountability. If it is found that the conduct of any of the officers or employees of IFCI led to the sustain of a loss, such conduct must be subjected to scrutiny and action in accordance with law. The whole purpose of an independent regulatory is to ensure that an entity in the financial sector whose conduct is in question does not have a final or decisive voice in determining whether there has been a violation of law and if so what action is necessary. In fact, we may not at this stage that the affidavit which has been filed in these proceedings on behalf of the Ministry of Finance (Department of Financial Services) specifically draws attention to the fact that IFCI, being a public financial institution and NBFC, listed with stock exchanges falls within the regulatory purview of various agencies. The affidavit of the Union Government states that :

> " (8). It is stated that IFCI is a Public Limited Company and Notified as Public Finance Institution under Section 4(A) of the Companies Act, 1956, it is also registered as systemically important NBFC and listed with stock exchanges. As such it comes under the regulatory purview of Ministry of Corporate Affairs, RBI, SEBI, NSE and BSE. Therefore, investigation into financial irregularities, it any, may be ordered by the respective regulatory agencies. (Id. at p- 313)

12 In fairness, we may also note that the Solicitor General has not opposed a direction required a further independent scrutiny by competing regulator. In view of the matter and for the aforesaid reasons we are of the view that it is necessary and proper to issue a direction both to the Union Ministry of Finance and Union Ministry of Corporate Affairs to ensure that a proper scrutiny is carried out in respect of the allegations which form the subject matter of these proceedings as narrated in the earlier part of this judgment including on the basis of the inspection report of the ROC dated 8 January 2013 The Union Ministry of Finance and Corporate Affairs respectively shall ensure that all aspects of the matter which duly looked into by the regulators competing to do so in areas entrusted to their respective domains. We direct the Union Government to ensure a due and proper scrutiny into all aspects of the matter by the (i) serious frauds investigation officer; (ii) Reserve Bank of India; and (iii) Security and Exchange Board of India (SEBI). The scrutiny, it is needless to add shall be conducted with due observance of norms of procedural fairness that would include an opportunity to IFCI to respond to the allegations This exercise shall be initiated not later than a period of one month from the receipt of a copy of this judgment and shall be completed not later than a period of four months thereafter. Upon receipt of the reports of the respective agencies, the Union Government shall determine what action is necessary to ensure compliance of law expeditiously.

13 The Writ Petition shall accordingly stand disposed of. There shall be no order as to costs.

.....CJI
[T S THAKUR]

……..J
[Dr D Y CHANDRACHUD]

New Delhi
September 23, 2016.

ITEM No. 1C Court No. 1 SECTION PIL(W)
(For Judgment)

S U P R E M E C O U R T O F I N D I A
RECORD OF PROCEEDINGS

WRIT PETITION (CIVIL) 355 of 2011

CENTRE FOR PUBLIC INTEREST LITIGATION **Petitioner(s)**

VERSUS

UNION OF INDIA AND ORS. **Respondent(s)**

Date : 23.09.2016 **This matter was called on for pronouncement of judgment today.**

For Appellant(s) **Mr. Prashant Bhushan, Adv.**

For Respondent(s) **Ms. Sushma Suri, Adv.**

Mr. Shreekant N.Terdol, Adv.

Mr. D.S.Mahra, Adv.

Mr. Arvind Kumar Sharma, Adv.

Ms. Ruchi Kohli, Adv.

Hon'ble Dr. Justice D.Y.Chandrachud pronounced judgment of the Bench comprising Hon'ble the Chief Justice and Hon'ble Dr. Justice D.Y.Chandrachud.

In terms of the signed judgment, the writ petition shall stand disposed of in terms of the signed reportable judgment. No costs.

(Shashi Sareen) **(Veena Khera)**
AR-cum-PS **Court Master**
(Signed reportable judgment is placed on the file)