Journal Section

Relationship between a bank and its financial subsidiary - some legal issues

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A bank or a financial institution floating a subsidiary is a very common occurrence in the present times. The subsidiary system is now well-established in practice and is also well-anchored in law. Currently, subsidiaries have been set-up for conducting a host of activities. These are basically financial activities and the risk of their financial position turning adverse looms heavily in respect of their activities. Existence of such risk gives rise to certain pertinent questions. What exactly is the relationship between the parent institution and its financial subsidiary? More importantly, whether the liabilities of a subsidiary can be enforced against the parent institution? It would appear that till now no case requiring judicial determination of this issue, has reached the Court of Law. A day, however, is not far off when the issue will arise for serious consideration and may also require judicial determination.

Recently, there have been cases particularly in the mutual fund sector, where the parent institutions have bailed out, or rather were required to bail out, their mutual fund units by paying for the shortfall in the "assured returns" schemes run by such mutual funds. Number of such instances is on the increase. In fact, a recent report had predicted a shortfall in respect of eighty such schemes, and the amount involved to be more than Rs.2500 crores (Report prepared by Price Waterhouse under the USAID – Sponsored Financial Institution Reforms and Expansion Project).

Legal grounds on which the parent institutions in these cases had discharged, or were required to discharge, the liability of their mutual fund units, are not known. The reasons could perhaps be attributed to the parent institution acting in its capacity as "Sole Trustee". If that were so, it would mean that the parent subsidiary angle was not a factor for fastening this liability on the parent institution. There had, however, been a general impression that requiring the parent banks to meet the shortfall of their mutual fund units, was by way of lifting their "corporate veil" and fastening the liability on the parent institution on that basis. In this background, it is felt appropriate to examine generally the legal position with respect to the holding company-subsidiary relationship and in particular, the principles on which a claimant of a subsidiary can enforce his claim against the holding company.

Independence of the entity

The true legal position in regard to the character of a company which owes its incorporation to a statutory authority/provision, is not in doubt or dispute. A company in law is equal to a natural person and has a separate legal entity of its own. The company operates in its own name; its assets are separate and distinct from those of its members; it can sue and be sued exclusively for its own purpose; its creditors cannot obtain satisfaction from the assets of its members; the liability of the members of shareholders is limited to the capital invested by them; similarly, the creditors of the shareholders have no right to the assets of the company. This position has been well-established ever since the decision in the case of Saloman v. Saloman and Co. (1897) AC 22 was pronounced in 1897; and indeed, it has always been the

well-recognised principle of common law. This holds equally good in the case of a holding company and its subsidiary. Accordingly, the holding company and its subsidiary are, in law, treated as two different distinct and Independent entities.

Lifting the corporate veil

Over a period of time, the doctrine has been subjected to certain exceptions. " The ghost of Saloman case still visits frequently the bounds of company law, but the veil has been pierced in many cases". Demanded by the situation, the Courts have to an increasing extent shown themselves to be prepared to strip aside (or lift, pierce, remove, put aside, or tear as the different terms go) the corporate veil in order to perceive the real person in the corporate entity. In Tata Engineering and Locomotives Company Ltd. vs. State of Bihar (AIR 1965 SC 40), the Supreme Court has observed as under :

> "The doctrine of the lifting of the veil thus marks a change in the attitude that law had originally adopted towards the concept of the separate entity or personality of the corporation. As a result of the impact of the complexity of economic factors, judicial decisions have sometimes recognised exceptions to the rule about the juristic personality of the Corporation. It may be that in course of time these exceptions may grow in number and to meet the requirement of different economic problems, the theory about the personality of the corporation may be confined more and more."

These are words of wide amplitude, and can be said to be toned down by the later judgement in State of UP vs. Renusagar Power Company (AIR 1988 SC 1737), wherein the Supreme Court observed as under:

> "It is the high time to reiterate that, in the expanding horizon of modern jurisprudence, the lifting of the corporate veil is permissible. Its frontiers are unlimited. It must, however, depend primarily on the **realities of the situation**. "

It is, however, distinctly recognised that it would not be possible to evolve a rational, consistent and inflexible principle which can be invoked in determining the question as to whether the veil of the corporation should be lifted or not. Examining the American decisions on the subject in the article "Piercing the Veil of Corporate Entity" [published in (1912) XII Colombia Law Review 496], Wormser summarised the position in the following words.

> " The various classes of cases where the concept of corporate entity should be ignored and the veil drawn aside have now been briefly reviewed. What general rule, if any, can be laid down? The nearest approximation to generalisation, which the present state of the authorities would warrant is this : When the conception of corporate entity is employed to defraud creditors, to evade an existing obligation, to circumvent a statute, to achieve or perpetuate monopoly, or to protect knavery or crime, the courts will draw aside the web of entity, will regard the corporate company as an association of live, up-and-doing, men and women shareholders, and will do justice between real persons."

In the context of this article, it is not necessary to refer to all the exceptions. One of the exceptions pertains to the relationship between the parent institution and its subsidiary. It is proposed to confine this article to the principles relevant in this regard.

Examining the circumstances in which the fundamental principle of corporate personality is disregarded, Professor Gower has cited examples under two categories, namely, (i) under express statutory provisions, and (ii) under case law. Regarding (i), as stated by him, the main categories in which the legislature has made inroads into the corporate entity principle, are –

a) in the interest of the company's creditors where the company has not complied with certain provisions of the Companies Act, which historically, were regarded as essential conditions of incorporation or where the company has traded fraudulently;
b) again in the interest of the company's creditors, where there is a group of interconnected companies which it thought should be treated as one; and
c) to protect the interests of the Revenue.

As under the English Law, the Indian Companies Act also contains a number of provisions qualifying the principle that company is to be treated as a separate entity and instead recognising the group as the true entity. The most important of these relates to accounts which require the holding company's balance-sheet and profit and loss account to be presented in the form of group account, normally by consolidating the subsidiary's figures with those of the holding company. These statutory provisions have, however, no relevance while considering the question of fastening the subsidiary's liability on the parent company.

Under the second category, the exceptional cases in which the Courts have lifted the corporate veil have been on the grounds of agency or fraud. There have been cases which show a tendency to recognise the substance rather than the legal form by treating the whole group of holding and subsidiary companies as one entity. Much, however, seems to depend on the extent of the control exercised by the parent company and the degree of financial independence of the subsidiary. In both cases, still more seems to depend on the nature of legal issue involved and on whether the Courts are being asked to lift the veil in the interest of the members or group or in the interest of their creditors, or in General Public Interest.

The example of the application of agency principle is afforded by Firestone Tire and Rubber Company vs. Llewellin in which it was held that although the English subsidiary was a separate legal entity which was selling its own goods, nevertheless, the sales were the means whereby the American parent company carried out its European business so that it was trading in the U.K. through the agency of the subsidiary.

The question whether the subsidiary can be regarded as agent of the parent entity is very difficult to answer, more so, since the attitude of the Court is unpredictable. In Smith, Stone & Knight Ltd. vs. Birmingham Corporation, Atkinson J. reviewed the early tax cases and made an attempt to extract some principles or guidelines. He concluded that while it was a question of fact in each case whether the subsidiary was carrying on the parent company's business or its own, six points were relevant in determining that question: (1) Were the profits treated as those of the parent company? (2) Were the persons conducting the business appointed by the parent company? (3) Was the parent company the head and brain of the trading venture? (4) Did the parent company govern the adventure and decide what should be done and what capital should be embarked on it? (5) Were the profits made by its skill and direction? (6) Was the parent company in effectual and constant control? The difficulty with this criteria, as pointed out by Professor Gower is that "in all cases of parent and subsidiary companies, the criteria will nearly always be satisfied, either by application of statutory

provisions and at any rate where the Board of directors or the Managing Directors of parent and subsidiary are the same. Therefore, the criteria may provide useful guidelines but they do not seem to be decisive."

Judicial approach in India

So far as the Indian case law is concerned, there are very few cases dealing with the question of lifting the corporate veil as between the holding and the subsidiary company. In Life Insurance Corporation of India vs. Escorts Ltd., AIR 1986 SC 1370, Justice O. Chinappa Reddy had emphasised that the corporate veil should be lifted where the associated companies are inextricably connected as to be in reality, part of one concern. He, however, did not find it necessary or desirable to enumerate the classes of cases where lifting the veil is permissible, "since that must necessarily depend on the relevant statutory or other provisions, the object sought to be achieved, the impugned conduct, the involvement of the element of public interest and the effect on the parties who may be affected." In that case, in view of certain schemes introduced by the Union of India, 13 NRI companies purchased shares. The argument was that all the 13 companies were a façade and Mr. Swaraj Paul was the real investor. The Supreme Court refused to investigate into this question by observing that when the legislature required lifting of the corporate veil for a particular purpose, the Court would lift the veil only to that extent and no more.

A more direct instance relating to the nexus between the parent and subsidiary companies is to be found in Renusagar case, *supra*. In that case, the Supreme Court lifted the corporate veil to hold that Hindalco, the holding company and Renusagar Power Company, its subsidiary, should be treated as one concern and the Power Plant of Renusagar must be treated as the own source of generation of Hindalco and on that basis, Hindalco would be liable to pay electricity duty. As the judgement discloses, the conclusion was based on the facts thereof as is clear from the Court's following observations:

> " Here, indubitably, we are of the opinion that it is correct that Renusagar was brought into existence by Hindalco in order to fulfil the condition of industrial licence of Hindalco through production of aluminium. It is also manifest from the facts that the model of the setting up of a power station through the agency of Renusagar was adopted by Hindalco to avoid complications in case of take over of the power station by the State or the Electricity Board. As the facts make it abundantly clear that all the steps for establishing and exapanding the power station were taken by Hindalco, Renusagar is a wholly owned subsidiary of Hindalco and is completely controlled by Hindalco. Even the day-to-day affairs of Renusagar are controlled by Hindalco. Renusagar has, at no point of time, indicated any independent volition. Whenever felt necessary, the State or the Board have themselves lifted the corporate veil and have treated Renusagar and Hindalco as one concern and the generation in Renusagar as the own source of generation of Hindalco. In the impugned order, the profits of Renusagar have been treated as the profits of Hindalco. In the aforesaid view of the matter, we are of the opinion that the corporate veil should be lifted and Hindalco and Renusagar be treated as one concern."

Post-Renusagar, the issue of lifting the corporate veil had been considered in a couple of other cases. For this, reference may be made to the Supreme Court Judgements in Delhi Development Authority vs. Skipper Construction Co. (P) Ltd. (1997) 89 Com Cas 362, and New Horizons Ltd. vs. Union of India (1997) 89 Com Cas 849. The question in these cases,

however, did not relate to the parent-subsidiary relationship. In Skipper case, the issue related to the adoption of the device of incorporation by certain individuals for committing illegalities and to defraud people. After referring to the authorities and the case law, the Court reiterated the proposition that where the corporate character is employed for the purpose of committing illegality or for defrauding others, the Court would ignore the corporate character and will look at the reality behind the corporate veil so as to enable it to pass appropriate orders to do justice between the parties concerned. "The fact that Tejwant Singh and members of his family have created several corporate bodies does not prevent this court from treating all of them as one entity belonging to and controlled by Tejwant Singh and family if it is found that these corporate bodies are mere cloaks behind which lurks Tejwant Singh and/or members of his family…….".

The case of New Horizons Ltd. (NHL) presented very interesting situation. New Horizons was a joint venture company, which had submitted a tender for printing, etc. of telephone directories for the Department of Telecommunications, Telecom District, Hyderabad. The company claimed to possess the requisite experience, which was actually the experience of its promoter companies. The Department rejected the offer on the ground of non-fulfillment of the condition by the applicant company. This rejection was upheld by the High Court. In the view of the High Court, it could not be said that the authorities had failed in their duty to look behind the façade of corporateness of NHL, and it was none of their duty and they rightly examined the experience, etc., of NHL and came to the conclusion that it did not satisfy the eligibility conditions. Disagreeing with the High Court, the Supreme Court found that the facts and the "**realities of the situation**", required departing from the narrow legalistic view. "Once it is held that NHL is a joint venture, as claimed by it in the tender, the experience of its various constituents, namely, TPI, LMI and WML as well as IIPC, had to be taken into consideration if the tender evaluation committee had adopted the approach of a prudent businessman". According to the Court, the conclusion would not be different even if the matter was approached purely from the legal standpoint.

Bank's subsidiary vis-à-vis lifting of corporate veil

It is now time to consider the "realities of the situation" in the case of a financial subsidiary of a bank. Following the amendments to the Banking Regulation Act, 1949, effected in 1983, banks both in public and private sector have diversified their activities into a host of financial services areas like merchant banking, equipment leasing, hire purchase, venture capital, housing finance, factoring, mutual funds, etc., by setting up subsidiaries. The subsidiary is incorporated as a private company under the Companies Act and the entire share capital is held by one bank (the parent bank). Generally, the Board of the subsidiary is constituted by ex-officio/nominee officials of the parent bank. The articles also empower the parent bank to give directions to the subsidiary. The Managing Director of the subsidiary is appointed by the parent bank. The business of the subsidiary, however, is carried out mostly by professional staff recruited by the subsidiary. The subsidiaries of banks generally, and those of the subsidiaries offering merchant banking and other financial services in particular, prominently project the name of the parent bank in their dealings, especially in inviting investments/deposits from the public. Operationally, the business of the subsidiary is carried out entirely as a separate entity and its assets and liabilities are kept distinct and separate.

These features show a "close connection" between the parent bank and its subsidiary. But then these are also the very features that make the company, a subsidiary. Those attributes,

which make it a subsidiary, cannot be relied on also to disregard the separate corporate existence of the company. Therefore something more would be required.

Fraud as a ground to lift the corporate veil of the bank's subsidiary is clearly ruled out. Incorporation of such subsidiary is well-regulated and there is no question of the bank employing the corporate character for committing illegalities or for defrauding others, as was found by the Supreme Court in the Skipper case.

Whether the subsidiary can be treated as carrying on business as agent of the parent bank? The argument would be that in terms of Section 19 of the Banking Regulation Act, 1949 a bank could float a subsidiary for undertaking a business which the bank is permitted by Section 6 of the Act to undertake. It is, therefore, the business of the bank itself which is carried on by it through the medium of a subsidiary. This argument would not be tenable. In this connection, it needs to be noted that it was initially pursuant to Reserve Bank's directions that certain businesses could be undertaken by a bank through subsidiary only. This must have been considered necessary in public interest, in the interest of the depositors and of the bank itself. The Reserve Bank guidelines further clearly envisaged the bank maintaining the arm's length relationship with its subsidiary. Even otherwise, if this argument is to be accepted, there would hardly be any subsidiary carrying on business independently as its own. That would militate against the basic reasons for the constitution of subsidiary by a bank. Considering from all angles, it would not be possible to establish the subsidiary conducting its business as agent of the parent bank.

The principle of *estoppel* also would not help the claimant. Under that principle, a person who by some statement or representation of fact causes another to act to his detriment in reliance of the truth of it is not allowed to deny it later, even though it is wrong. Where no representation is made by the parent bank as regards meeting the liabilities of its subsidiary, no case based on estoppel can be made out against it. Even assuming that the subsidiary has made some representation, the silence on the part of the parent bank in regard thereto would not be sufficient to attribute it to the parent bank or to invoke the principle of *estoppel* against the parent bank.

A few latest developments may also be taken note of in this context. Basle Committee on Banking Supervision has asked all member banks to put in place a new set of supervisory norms for financial conglomerates whereby the entities have to exclude intra-group holding of regulatory capital while calculating capital adequacy. According to the norms, if a financial intermediary has set up a bank, an insurance company or mutual fund, all the capital it has advanced towards these has to be 'provided for' before calculating the capital adequacy of the financial intermediary. Once implemented, this would add one more factor by way of 'close connection' between the banks and the subsidiary. Another development relates to the new accounting norms aimed at transparency in the published bank accounts. Once the accounting and disclosure norms commence to operate, the emerging picture is more likely to present the bank operating as a financial conglomerate. These developments may however, be treated as adding to the principles and guidelines as formulated by Atkinson J., but cannot be said to be decisive on the issue of parent-subsidiary relationship.

Conclusion

Finally to say, no general proposition can be laid down that the corporate veil of the financial subsidiary would be lifted just because it happens to be a subsidiary. In other words, there

cannot be any such proposition that the subsidiary's liability would always be treated as the liability of the holding company. Saying so would amount to wiping out the very corporate existence of the subsidiary. It may be that on the facts and circumstances of a given case, the parent bank may be held liable, whether by lifting the corporate veil on the ground of agency, or on other principles of equity, to meet the liabilities of its financial subsidiary vis-à-vis the particular claimant. That would however be an exceptional situation. Even in such a case, on what grounds the liability would be so shifted to the parent bank, remains unpredictable.

On the question of applicability of the above principles operating in the field of the company law to statutory corporations like the public sector banks, this much can be said that the Judiciary is sure to be guided by these very principles.

One should respect public opinion insofar as is necessary to avoid starvation and to keep out of prison, but anything that goes beyond this is voluntary submission to an unnecessary tyranny,
and is likely to interfere with happiness in all kind of ways.

— RUSSELL, Bertrand A., The Conquest of Happiness (New York : Liveright Publishing Corporation 1930), p. 136.

Laws are made for men of ordinary understanding, and should, therefore be construed by the ordinary rules of common sense. Their meaning is not to be sought for in metaphysical subtleties, which may make anything mean everything or nothing, at pleasure. It should be kit to the sophisms of advocates, whose trade it is, to prove that a defendant is a plaintiff, though dragged into court, toro collo, like Bonaparte's volunteers, into the field in chains, or that a power has been given, because it ought to have been given, et alia talia. The States supposed that by their tenth amendment, they had secured themselves against constructive powers.

— JEFFERSON, Thomas, Letter dated Junr 12, 1823 to United States Supreme Court Associate Justice William Johnson, appointed by Jefferson in 1804. Reprinted in Padover, Saul K., The Complete Jefferson (New York; Duell, Sloan & Pearce, Inc., 1943), p. 323.

Mother's Right to Guardianship and Minor's Investments —Recent Findings of the Supreme Court and Beyond

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Introduction

1. The recent judgement of the Supreme Court (Githa Hariharan Vs. Reserve Bank of India [1999] 2 SCC 228) on the mother's right to guardianship (in the context of investments for the minor), is path breaking and in line with the proactive role adopted by the Court for tackling legal issues, keeping pace with socio-economic realities. The judge-ment, however, is not a wholesale solution for the issues related to the mother's right to guardianship. This article examines the implications of the judgement and the issues resolved as well as the wider issues remaining to be tackled.

Personal laws and guardianship

2.1 A guardian, as understood in common parlance, is a person who has the duty to guard or protect the person or property of another person, in particular a minor. The parents of a child are the persons naturally duty bound to take care of the child's interests.. Guardianship involves a host of duties coupled with certain rights. While meeting the needs of care and protection of the person and property of a minor involves onerous duties, the guardian also exercises the right of taking decisions pertaining to education and upbringing, investment of moneys etc. of the minor. As the matters pertaining to guardianship are governed by personal laws, there is no uniformity in the laws applicable to all and the religion / community of the minor determines the laws applicable in a given case.

2.2 While under the Hindu law the father and after father, the mother are entitled to guardianship of a Hindu minor (both person and property), the Muslim law does not confer any rights of guardianship of property on the mother. The natural guardian of the property of a Muslim minor are the father, the executor of the will appointed by the father, the father's father and the executor appointed under a will by the father's father, in that order. The personal laws applicable to Indian Christians, Parsees and Jews do not recognise the authority of any person to be guardian of the minor's property. To act as guardian and deal with the minor's property, even father should seek an order of the Court.

Hindu law — Some statutory provisions

2.3 Section 6 of the Hindu Minority and Guardianship Act, 1956 (HMG Act) which deals with the guardianship of a Hindu Minor provides as under:

> "The natural guardians of a Hindu minor, in respect of the minor's person as well as in respect of the minor's property (excluding his or her undivided interest in joint family property), and -
>
> (a) in the case of a boy or an unmarried girl - the father, and after him, the mother provided that the custody of a minor who has not completed the age of five years shall ordinarily be with the mother;

(b) in the case of an illegitimate boy or an illegitimate unmarried girl - the mother, and after her, the father;
(c) in the case of a married girl - the husband;"

The proviso to the section further stipulates that no person shall be entitled to act as the natural guardian of a minor under the provisions of this section if he has ceased to be a Hindu, or if he has completely and finally renounced the world becoming a hermit (vanaprastha) or an ascetic (yati or sanyasi). Further, the expression "father" and "mother" do not include a "step-father and a step-mother."

The expression `natural guardian' is defined in Section 4 [c] of HMG Act as any of the guardian mentioned in Section 6 thereof. The term 'guardian' is defined in Section 4 (b) of HMG Act as a person having the care of the person of a minor or of his property or of both, his person and property, and includes a natural guardian among others. Another relevant provision is Section 19 of the Guardians and Wards Act, 1890 which deals with appointment of guardian by Courts. Clause (b) of this section stipulates that the Court shall not appoint a guardian of the person of a minor whose father is alive and in the opinion of the Court, not unfit to be guardian of the person of the minor.

3. Constitution and Personal Laws

The Constitution provides for equality before the law and equal protection of the laws. However, the personal laws which apply to any person based on his religion are not treated as discriminatory but as making a reasonable classification and are therefore not inconsistent with the Constitution. In fact, unification of persoonal laws (a uniform civil code) appears in the Directive Principles of State Policy (Art. 44 of the Constitution) as an ideal to be achieved in future and not justiciable. The idea of unification of civil laws is on the basis that in a civilised society there is no necessary connection between religion and personal laws (see, Sarala Mudgal vs. Union of India (1995) 3SSC 635.

4.1 Challenge to constitutionality

Recently, the Supreme Court had occasion to consider the issue of mother's right to guardianship of a minor in the context of investments proposed to be made on behalf of the minor in Githa Hariharan's case and in the context of custody of the minor in another case. As in both the cases, the constitutionality of Section 6 (a) of HMG Act and Section 19 of the Guardians and Wards Act were challenged, these cases were heard together and disposed of by a common judgement.

4.2 Githa Hariharan's case

In this case, the petitioners had applied to the Reserve Bank of India (first respondent) on 10.12.1984 for 9% Relief Bonds in the name of their minor son Rishab Bailey for Rs.20,000/-. They had stated expressly that both of them agreed that the mother of the child, i.e., the first petitioner would act as the guardian of the minor for the purpose of investments made with the money held by their minor son. Accordingly, in the prescribed form of application, the first petitioner had signed as the guardian of the minor. The first respondent replied to the petitioners advising them either to produce the application form signed by the father of the minor or a certificate of guardianship from a competent authority in favour of the mother. This was on the basis that the first petitioner is not the natural guardian of the minor as under

Section 6 (a) of the HMG Act the father of a Hindu minor is the only natural guardian. Aggrieved by this, the petitioners filed this writ petition with prayers to strike down Section 6 (a) of the HMG Act and Section 19 (b) of the Guardians and Wards Act, 1890 (GW Act) as violative of Articles 14 & 15 of the Constitution and to quash and set aside the decision of the first respondent refusing to accept the deposit from the petitioners and to issue a mandamus directing the acceptance of the same after declaring the first petitioner as the natural guardian of the minor.

4.3 Discrimination against Mother

The petitioners alleged that Section 6 (a) of the HMG Act and Section 19 (b) of the GW Act are violative of the equality clause of the Constitution, inasmuch as the mother of the minor is relegated to an inferior position on ground of sex alone since her right, as a natural guardian of the minor, is made cognisable only `after' the father. Hence, according to the petitioners, both the sections had to be struck down as unconstitutional.

Observations of the Court

4.4.1 Father and `after' him, mother

The court observed that the definitions of 'guardian' and 'natural guardian' do not make any discrimination against mother and she being one of the guardians mentioned in Section 6 would undoubtedly be a natural guardian as defined in Section 4 (c). The only provision to which exception is taken is found in Section 6 (a) which provides for "father, and after him the mother" to be natural guardian. That phrase, on a cursory reading, does give an impression that the mother can be considered to be natural guardian of the minor only after the life time of the father. It is well settled that welfare of the minor in the widest sense is the paramount consideration and even during the life time of the father, if necessary, he can be replaced by the mother or any other suitable person by an order of court, where to do so would be in the interest of the welfare of the minor. In any dispute concerning the guardianship of a minor, between the father and mother of the minor before a Court of law, the word 'after' in the Section would have no significance, as the Court is primarily concerned with the best interests of the minor and his welfare in the widest sense while determining the question regarding custody and guardianship of the minor. The question, however, assumes importance when the mother acts as guardian of the minor during the life time of the father, without the matter going to Court, and the validity of such an action is challenged on the ground that she is not the legal guardian of the minor in view of Section 6 (a) of the HMG Act.

4.4.2 Gender equality

If the word 'after' in the Section is construed to mean only 'after the life time', the section has to be struck down as unconstitutional as it undoubtedly violates gender-equality, one of the basic principles of our Constitution. As the HMG Act came into force in 1956, six years after the Constitution, the Parliament could not have intended to transgress the constitutional limits or ignore the fundamental rights guaranteed by the Constitution which essentially prohibits discrimination on grounds of sex. It is also well settled that if on one construction a given statute will become unconstitutional, whereas on another construction, which may be open, the statute remains within the constitutional limits, the Court will prefer the latter on the

ground that the Legislature is presumed to have acted in accordance with the Constitution and courts generally lean in favour of the constitutionality of the statutory provisions.

4.4.3 Not after father's life time

The Court held that Section 6 (a) of HMG Act is capable of such construction as would retain it within the Constitutional limits. The word 'after' need not necessarily mean 'after the life time'. In the context in which it appears in Section 6 (a), it means ' in the absence of'; the word 'absence' therein referring to the father's absence from the care of the minor's property or person for any reason whatever. If the father is wholly indifferent to the matters of the minor even if he is living with the mother or if by virtue of mutual understanding between the father and the mother, the latter is put exclusively in charge of the minor, or if the father is physically unable to take care of the minor either because of his staying away from the place where the mother and the minor are living or because of his physical or mental incapacity, in all similar situations, the father can be considered to be absent and the mother being a recognized natural guardian, can act validly on behalf of the minor as the guardian. Such an interpretation will be the natural outcome of harmonious construction of Sections 4 and 6 of the HMG Act, without causing any violence to the language of Section 6 (a).

4.4.4 Precedents

The Court observed that the above interpretation had already been adopted to some extent in Jijabai Vithalrao Gajre vs. Pathankhan and others, 1970 (2) SCC 717. In that case, the question was whether a lease deed executed by a tenant in favour of the appellant's mother, during the minority of the appellant and when her father was alive, was valid or not? The Court found that it was the mother who was actually managing the affairs of her minor daughter who was under her care and protection and though the father was alive, he was not taking any interest in the affairs of the minor. In the peculiar circumstances of the case, the father was treated as if non-existent and therefore, the mother was considered as the natural guardian of the Minor's person as well as the property having the power to bind the minor by dealing with her immovable property. The Court distinguished another judgement, Pannilal vs. Rajinder Singh and another, 1993 (4) SCC 38 wherein the sale of property belonging to the respondents who were minors by their Mother, acting as Guardian and attested by Father was held invalid. There was no evidence to show that the father of the minor-respondents was not taking any interest in their affairs or that they were in the care of the mother to the exclusion of the father. An inference was drawn from the factum of attestation of the sale deed that the father was very much 'present' and in the picture. The Court also noted that Pannilal's case had turned mainly on the fact that the sale was not supported by legal necessity; was not for the benefit of the minor and the same had been effected without the permission of the Court. That judgement, therefore, does not run counter to the interpretation now placed on Section 6, as that case was decided on its peculiar facts and is clearly distinguishable.

4.4.5 International Instruments

The Convention on the Elimination of All Forms of Discrimination Against Women, 1979 ("CEDAW") and the Beijing Declaration direct all State parties to take appropriate measures to prevent discrimination of all forms against women. India is a signatory to CEDAW having accepted and ratified it in June, 1993. The Court observed that the interpretation placed on Section 6 (a) gives effect to the principles contained in these instruments. The domestic

courts are under an obligation to give due regard to International Conventions and Norms for construing domestic laws when there is no inconsistency between them. [See, Jolly vs. Bank of Cochin (1980) 2 SCC 360; Valsamma Paul vs. Cochin University (1996) 3 SCC 545; Apparel Export Promotion Council vs. A.K. Chopra, Civil Appeal Nos. 226-227 of 1999 decided on January 20, 1999]. Similarly, Section 19 (b) of the GW Act would also have to be construed on the same lines.

5. Findings of the court

The court has vide paras 16 to 19 of the majority judgement (by Dr.A.S.Anand CJI for himself and M.Srinivasan J) held as under: "16. While both the parents are duty bound to take care of the person and property of their minor child and act in the best interest of his welfare, we hold that in all situations where the father is not in actual charge of the affairs of the minor either because of his indifference or because of an agreement between him and the mother of the minor (oral or written) and the minor is in the exclusive care and custody of the mother or the father for any other reason is unable to take care of the minor because of his physical and/or mental capacity, the mother, can act as natural guardian of the minor and all her actions would be valid even during the life time of the father, who would be deemed to be `absent' for the purposes of Section 6(a) of HMG Act and Section 19 (b) of GW Act.

17. Hence, the Reserve Bank of India was not right in insisting upon an application signed by the father or an order of the Court in order to open a deposit account in the name of the minor particularly when there was already a letter jointly written by both petitioners evidencing their mutual agreement. The Reserve Bank, now ought to accept the application filed by the mother.

18. We are conscious of the fact that till now many transactions may have been invalidated on the ground that the mother is not a natural guardian, when the father is alive. Those issues cannot be permitted to be reopened. This judgement, it is clarified, will operate prospectively and will not enable any person to reopen any decision already rendered or question the validity of any past transaction, on the basis of this judgement.

19. The Reserve Bank of India and similarly placed other organisations, may formulate appropriate methodology in the light of the observations made above to meet the situations arising in the contextual facts of given case."

Implications of the judgement

6.1 Prospective

The judgement is only prospective and does not purport to reopen old decisions where transactions by the mother might have been invalidated (on the ground that the mother was not the natural guardian when father is alive).

6.2 Concurrent Guardianship

The judgement does not have the effect of declaring the mother to be guardian of her minor child concurrently with the father. It rather makes it clear that the mother can act as natural guardian even during the lifetime of the father in certain circumstances. This means that the

provision to act as guardian "after father" does not mean "after the death of the father", but when the father is not available to act and hence, the mother is in charge.

6.3 Actual Charge

The situations where the mother can act as guardian, as specified by the court are —

(i) when the father is not in actual charge of the affairs of the minor and the minor is in exclusive custody of the mother.

This can be because of father's indifference or because of agreement between him and the mother.

Such agreement can be oral or in writing.

(ii) when father is by any reason unable to take care of the minor because of his physical and/or mental capacity.

In such cases the father would be deemed to be absent for the purposes of section 6 (a) of HMG Act and section 19 (b) of GW Act and the mother can act as natural guardian and all her actions would be valid even during the lifetime of the father.

6.4 Formulation of methodology

The Court has also directed the Reserve Bank and other similarly placed organisation to formulate appropriate methodology in the light of the Courts' observations to meet the future situations. Accordingly, any person or organisation having to deal with minors or their guardians like banks and financial institutions while accepting investments or making payments etc. will have to decide on and formulate the methodology for accepting the guardianship of the mother. Where there is a written agreement between the father and the mother or where the father gives consent or concurrence in writing the matter is simple. However, where nothing documentary is available insisting on strict proof of actual care would amount to defeating the very spirit of the judgement. Relying on a declaration duly made by the mother would be a reasonable course.

6.5 Disputed Cases

The situations specified above where the mother can act as guardian during the life time of the father are factual. Hence, there is much scope for dispute between the parents if they are not actually acting in tandem. Issues like exclusive custody of mother, inability of father to take care owing to physical or mental incapacity are fertile grounds for disputes.

7. Scope & Limitations

The reformative construction of guardianship laws as above has been made in the context of the laws applicable to a Hindu minor, and on the interpretation of the HMG Act. Hence, apparently this decision has no effect on the minors and mothers belonging to other communities. Personal law reforms are normally matters of legislation but such reforms are fraught with the danger of evoking community sentiments and hence there is reluctance to make any serious move towards a uniform Civil Code (see, Jorden vs. S.S. Chopra AIR 1985

SC 935). Accordingly, this judgement is in line with the Court's view that the judiciary must step in and provide a solution in cases of legislative lacunae or executive inaction until the same is addressed (see Vineet Narain vs. UOI [1988] 1SSC 226, Vishaka vs. Rajasthan [1997] 6SCC 241).

8. Conclusion

In short, the judgement provides great relief to the vast majority of those mothers who have to take care of their minor children in the absence of the father, as they will now be able to act as guardian with full authority. Perhaps, one may have to wait for another judicial intervention for the next step ahead, for taking care of those who are not covered by this verdict as quick legislative reforms are not expected.

Supreme Court on Interpretation of Statutes
Some Extracts.

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Statute is an authentic expression of the legislative will[1]. For initiating a thinking process, this paper extracts some of the observations of the Supreme Court which throw light on the difficulties encountered by the legislature while expressing its will and some of the rules followed by the courts while interpreting legislation. Interpretation of statutes calls for many varied talents and is not a subject, which can be confined to rules[2]. However, the rules of interpretation of statutes guide in understanding the law.

Task of a Judge

2. Justice Chinnappa Reddy[3] has quoted with approval, the following observations of Lord Denning which outline the task of a judge while interpreting a statute.

> "12. In Seaford Court Estates Ltd. v. Asher ((1949) 2 All ER 155, 164), Lord Denning, who referred to Plowden's Reports already mentioned by us, said :
>
> Whenever a statute comes up for consideration it must be remembered that it is not within human powers to foresee the manifold sets of facts which may arise, and, even if it were, it is not possible to provide for them in terms free from all ambiguity. . . . (A) judge, cannot simply fold his hands and blame the draftsman. He must set to work on the constructive task of finding the intention of Parliament, and he must do this not only from the language of the statute, but also from a construction of the social conditions which gave rise to it and of the mischief which it was passed to remedy, and then he must supplement the written words so as to give "force and life" to the intention of the legislature. . . . Put into homely metaphor, it is this : A judge should ask himself the question how, if the makers of the Act had themselves come across this ruck in the texture of it, they would have straightened it out? He must then do as they would have done. *A judge should not alter the material of which the Act is woven, but* ***he can and should*** *iron out the creases.*" (Emphasis added)

Why is the Task Difficult ?

3. The following passage from the judgement of the Supreme Court[4] very clearly states the difficulties that arise in drafting of legislation and its interpretation.

> "6. It may be worthwhile to restate and explain at this stage certain well-known principles of interpretation of statutes : Words are but mere vehicles of thought. They are meant to express or convey one's thoughts. Generally, a person's words and thoughts are coincidental. No problem arises then, but, not infrequently, they are not. It is common experience with most men, that occasionally there are no adequate words to express some of their thoughts. Words which very nearly express the thoughts may be found but not words which will express precisely. There is then a

great fumbling for words. Long-winded explanations and, in conversation, even gestures are resorted to. Ambiguous words and words which unwittingly convey more than one meaning are used. Where different interpretations are likely to be put on words and a question arises what an individual meant when he used certain words, he may be asked to explain himself and he may do so and say that he meant one thing and not the other. But if it is the legislature that has expressed itself by making the laws and difficulties arise in interpreting what the legislature has said, a legislature cannot be asked to sit to resolve those difficulties. The legislatures, unlike individuals, cannot come forward to explain themselves as often as difficulties of interpretation arise. So the task of interpreting the laws by finding out what the legislature meant is allotted to the courts. Now, if one person puts into words the thoughts of another (as the draftsman puts into words the thoughts of the legislature) and a third person (the court) is to find out what they meant, more difficulties are bound to crop up. The draftsman may not have caught the spirit of the legislation at all; the words used by him may not adequately convey what is meant to be conveyed; the words may be ambiguous; they may be words capable of being differently understood by different persons. How are the courts to set about the task of resolving difficulties of interpretation of the laws ? The foremost task of a court, as we conceive it, in the interpretation of statutes, is to find out the intention of the legislature. Of course, where words are clear and unambiguous no question of construction may arise. Such words ordinarily speak for themselves. Since the words must have spoken as clearly to legislators as to judges, it may be safely presumed that the legislature intended what the words plainly say. *This is the real basis of the so-called golden rule of construction that where the words of statutes are plain and unambiguous effect must be given to them.* A court should give effect to plain words, not because there is any charm or magic in the plainness of such words but because plain words may be expected to convey plainly the intention of the legislature to others as well as judges. *Intention of the legislature and not the words is paramount.* Even where the words of statutes appear to be prima facie clear and unambiguous it may sometimes be possible that the plain meaning of the words does not convey and may even defeat the intention of the legislature; in such cases there is no reason why the true intention of the legislature, if it can be determined, clearly by other means, should not be given effect. Words are meant to serve and not to govern and we are not to add the tyranny of words to the other tyrannies of the world." (Emphasis added)

Words and legislative intent

4. The first lesson to learn from the above is that the words in a statute should be understood in their plain and ordinary sense. Second lesson is that if the words of a statute are ambiguous and not plain, the legislative intent has to be found out and given effect to. The third lesson is that if the legislative intent is clear, it is not necessary to stick to the literal interpretation, which may not give effect to the legislative intent or even defeat it.

Need to Deviate from 'Literal Rule'

5. The Supreme Court[5] has illustrated the need for deviating from the literal rule of construction as under.

"67. The literal rules of construction require the wording of the Act to be construed according to its literal and grammatical meaning whatever the result may be.

However, the Law Commission 21 of England has struck a note of caution that "to place undue emphasis on the literal meaning of the words of a provision is to assume an unattainable perfection in draftsmanship". In Whitely v. Chappell ((1868-69) QBD 147 : 1868 LR 4), a statute concerned with electoral malpractices made it an offence to personate 'any person entitled to vote' at an election. The defendant was accused of personating a deceased voter and the court, using the literal rule, found that there was no offence as the personation was not of person entitled to vote. A dead person was not entitled to vote. A deceased person did not exist and had no right to vote and as a result the decision arrived at was contrary to the intention of Parliament. As it was pointed out in Prince Ernest of Hanover v. Attomey General (1956 Ch D 188), the Golden Rule in the form of modified literal rule, according to which the words of statute will as far as possible be construed according to their ordinary and plain and natural meaning, unless this leads to an absurd result. Where the conclusion reached by applying the literal rule is contrary to the intention of Parliament, the Golden Rule is helpful."

Finding the Legislative Intent

6. The question that arises next is how to determine the legislative intent. This is answered by Justice Chinnappa Reddy in these words.

"7. Parliamentary intention may be gathered from several sources. First, of course, it must be gathered from the statute itself, next from the preamble to the statute, next from the Statement of Objects and Reasons, thereafter from parliamentary debates, reports of committees and commissions which preceded the legislation and finally from all legitimate and admissible sources from where there may be light. Regard must be had to legislative history too."[6]

7. How the supreme court finds out the intention of the legislature is explained[7] as under.

"231 … We now look for the "intention" of the legislature or the 'purpose' of the statute. First, we examine the words of the statute. If the words are precise and cover the situation in hand, we do not go further. We expound those words in the natural and ordinary sense of the words. But, if the words are ambiguous, uncertain or any doubt arises as to the terms employed, we deem it as our paramount duty to put upon the language of the legislature rational meaning. We then examine every word, every section and every provision. We examine the Act as a whole. We examine the necessity which gave rise to the Act. We look at the mischiefs which the legislature intended to redress. We look at the whole situation and not just one-to-one relation. We will not consider any provision out of the framework of the statute. We will not view the provisions as abstract principles separated from the motive force behind. We will consider the provisions in the circumstances to which they owe their origin. *We will consider the provisions to ensure coherence and consistency within the law as a whole and to avoid undesirable consequences.*

233. For this purpose, we call in external and internal aids

> External aids are : the Statement of Objects and Reasons when the Bill was presented to Parliament, the reports of the Committee, if any, preceding the Bill, legislative history, other statutes in pari materia and legislation in other States which pertain to the same subject matter, persons, things or relations.
>
> Internal aids are : Preamble, scheme, enacting parts of the statutes, rules of languages and other provisions in the statutes."

Text & Context

8. The following observations of the Supreme Court[8] are of great guidance for determining the intention of the legislature from the statute.

> "Interpretation must depend on the text and the context. They are the bases of interpretation. One may well say if the text is the texture , context is what gives the colour. Neither can be ignored. Both are important. That interpretation is best which makes the textual interpretation match the contextual. A statute is best interpreted when we know why it was enacted. With this knowledge, the statute must be read, first as a whole and then section by section, clause by clause, phrase by phrase and word by word. If a statue is looked at, in the context of its enactment, with the glasses of the statute-maker, provided by such context, its scheme, the sections, clauses, phrases and words may take colour and appear different than when the statute is looked at without the glasses provided by the context. With those glasses we must look at the Act as a whole and discover what each section, each clause, each phrase and each word is meant and designed to say as to fit into the scheme of the entire Act. No part of a statute and no word of a statute can be construed in isolation. Statutes have to be construed so that every word has a place and everything is in its place."

Caution

9. The duty of the courts to find the legislative intent and to give effect to it could take it much beyond the task entrusted to it under the Constitution. Its function is to interpret the legislation and not to legislate. Justice K. Jagannath Shetty of the Supreme Court [9] cautioned in these words.

> "232. Let me here add a word of caution. This adventure, no doubt, enlarges our discretion as to interpretation. But it does not imply power to us to substitute our own notions of legislative intention. It implies only a power of choice where differing constructions are possible and different meanings are available."

Golden Rule for Drafting

10. The observations of the Supreme Court extracted above lay down the golden rule of interpretation of statutes. While they help us in interpreting the statutes administered by the Bank, they offer a tremendous insight on how the rules, regulations, circulars, notifications etc., issued by the Bank may be interpreted. The draftsman's golden rule is stated by Justice Krishna Iyer [10] as under.

"In drafting it is not enough to gain a degree of precision which a person reading in good faith can understand, but it is necessary to attain if possible to a degree of precision which a person reading in good faith can understand, but it is necessary to attain if possible to a degree of precision which a person reading in bad faith cannot misunderstand."

I have a high opinion of lawyers. With all their faults, they stack up well against those in every other occupation or profession. They are better to work with or play with or fight with or drink with, than most other varieties of mankind.

— TWEED, Harrison, accepting the presidency of the association of the Bar of the City of New York, May 10, 1945.

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[1] Maxwell on Interpretation of Statutes 12th edition page 1.
[2] A.R.Antulay v. R.S.Nayak and Others, (1988) 2 SCC 602 (paragraph 71). Per Sabyasachi Mukharji J.
[3] M/s Giridhari Lal & Sons V/s B.N. Mathur & Ors. (1986) 2 SCC 237 (paragraph 12).
[4] M/s Giridhari Lal & Sons V/s B.N. Mathur & Ors. (1986) 2 SCC 237 (paragraph 6).
[5] Punjab Land Development and Reclamation Corporation Ltd. V. Presiding Officer Labour Court and Others, (1990) 3 SCC 682 (paragraph 67).
[6] M/s Giridhari Lal & Sons V/s B.N. Mathur & Ors. (1986) 2 SCC 237 (paragraph 7).
[7] Kehar Singh and Others v. State (Delhi Administration) (1988) 3 SCC 609 (paragraph 231, 233)
[8] RBI V/s Peerless, AIR 1987 SC 1023 (paragraph 33) =(1987)1 SCC 424
[9] Kehar Singh and Others v. State (Delhi Administration) (1988) 3 SCC 609
[10] Moti Ram and Others v. State of Madhya Pradesh, (1978) 4 SCC 47 (paragraph 29)