BENEDICT AND OTHERS
v
MONETARY BOARD OF THE CENTRAL BANK OF SRI LANKA AND OTHERS
(PRAMUKA BANK CASE)

COURT OF APPEAL
SRIPAVAN, J.
CA NO.77/2003
MARCH 20, 27, 2003
APRIL 3, 2003
MAY 19, 20, 22, 2003
JUNE 9, 2003

Monetary Law (Amended) S.32 of 2002 – S.8.(2) C- S.9-S.17 – Banking Amendment Act 33 of 1995 – Cancellation of Licence of a Bank – Validity – Exercise of Discretion – Review of Same by Court – The exercise of discretionary powers –Should reasons be given – Was the Monetary Board properly constituted? – Interpretation Ordinance S.6(3)b – Vested rights.

The petitioners are the depositors of the 5th respondent Pramuka Bank. The petitioners alleged that, the 4th respondent (Director of Bank Supervision) initiated an examination into the affairs of the Bank. An Order was issued directing the Bank to cease the unsound and improper financial practice of recovering interest after the balance sheet date and showing this as income. Thereafter it was alleged that the 4th respondent carried out a second statutory examination into the activities of the Bank. The Report was sent to the 1st respondent, who directed the Bank to freeze the deposits and the advances and listed the Bank as a licensed deposit taking institution.

Thereafter several meetings took place between the Senior Management of the Bank and the officials of the Central Bank. The proposals considered by the bank were considered and rejected by the 1st respondent. Thereafter the 4th respondent submitted a Report to the 2nd respondent (Governor of the Central Bank) that she was satisfied that the current financial conditions of the Bank was critical, and the 1st respondent thereafter directed the Bank to suspend its business forthwith. In terms of section 761, the 4th respondent submitted a Report to the 1st respondent on the post supervision examination of the Bank setting out the several options available in terms of section 76N which would enable the 1st respondent to permit the bank to resume business.

The petitioners alleged that the 1st respondent did not consider any of the options, and that the several options, received the attention of the 1st respondent and that no reasons were given as to why the 1st respondent rejected the options suggested by the 4th respondent even if they were considered, before the cancellation of the Banks Licence.

The petitioners also contend that the Monetary Board was not properly constituted when it made the impugned order. One member was appointed by the President for a period of 6 years and he had ceased to be a member in terms of the Amending Act, and had to be re-appointed by the President on the recommendation of the Minister of Finance with the concurrence of the Constitutional Council.

Held :

i) The court does not dispute that the 1st respondent has a discretion in the matter. It is the 1st respondent alone who can take such a decision provided the 1st respondent acts fairly and reasonably within the four corners of its *lawful jurisdiction.* The court however can examine the exercise of the discretionary power in order to see whether it has been used properly, fairly and according to the rules of reason and justice.

ii) There is nothing to show that, the several options contained in the 4th respondent's report received the attention of the 1st respondent and a decision was taken to reject all of them. The petitioners were led to believe that the 1st respondent arrived at a decision to cancel the licence and to wind up its affairs after considering the Report of the 4th respondent.

iii) No reasons were given as to why the 1st respondent rejected the options suggested by the 4th respondent.

iv) In the absence of reasons, it is impossible to determine whether or not the 1st respondent in fact considered the four options.

v) Failure to give adequate reasons amounts to a denial of justice and is itself an error of law. The reasons must not only be intelligible but should deal with the substantial points which have been raised.

vi) In the absence of reasons the person affected may be unable to see whether there has been a justiciable flaw in the decision making process.

vii) If reasons are not given the Court can only draw an inference that the 1st respondent had no rational reasons for its decision and has failed to act with procedural fairness towards the depositors and creditors.

viii) Section 6(3) (b) of the Interpretation Ordinance, protects the vested rights acquired under the repealed Act, in the absence of any compelling language within the four corners of the repealing Act to a deliberate decision on the part of Parliament to impair those rights, the Monetary Board was therefore properly constituted.

An **APPLICATION** for a *Writ of Certiorari* and *Mandamus*.

Cases referred to :

1. *Secretary of State for Education* v *Tameside Metropolitan B.C.* 1977 AC 1064
2. *Associated Provincial Picture Houses Ltd.*, v *Wednesbury Corporation* 1948 1KB 223 at 229.
3. *Premachandra* v *Jayawickrema* – 1994 2 SRI LR 90 at 101 (SC)
4. *R* v *Secretary of State for the Environment ex.p. Nottinghamshire* – 1986 AC 204 at 249
5. *Premachandra* v Jayawickrema – 1993 2 SRI LR 294 at 314
6. *Re Poyser and Mills, Arbitration* – 1964 2 QB 467.
7. *Suranganie Marapana* v *Bank of Ceylon* – 1997 3 SRI LR 156 at 168
8. *Sirisena and others* v *Kobbekaduwa,* Minister of Agriculture and Lands 80 NLR (Vol.1) 1 at 172
9. *Free Lanka Insurance Company Ltd.*, v *Ranasinghe* – 65 NLR 486
10. *Hai Bai* v *Perera* – 55 NLR 443

M.A.Sumanthiran for petitioners.

Saleem Marsoof, P.C. Addl. Solicitor-General with *Nihal Jayawardena* S.S.C., and *Arjuna Obeysekera* S.C., for 1st Respondent.

K. Kanag Isvaran P.C., with Ms. *D.Wijawardena* for 2-4th Respondents.

Cur. adv. vult

July 02, 2003

SRIPAVAN,J.

The petitioners claim that they are the depositors of the fifth respondent bank which commenced business as a licensed specialised bank (hereinafter referred to as the "bank") on or around 21st July 1997. Accordingly, the provisions contained in PART IXA of the Banking (Amendment) Act No.33 of 1995 apply to this bank. The petitioners allege that on or about July 1999 the fourth respondent initiated an examination into the affairs of the bank as provided in terms of Sec.76L of the said Act. The second respondent in his affidavit dated 10th February 2003 states that the following matters came to light during the course of the statutory examination held in 1999/2000 by the fourth respondent:-

a) That the bank was engaged in an unsound and improper financial practice whereby interest recovered by granting fresh loans to convert non-performing loans into performing loans after the balance sheet date had been wrongfully accounted as income for the bank.

b) That the bank had fictitiously inflated its profit for the accounting year 1999 and thereby showed a profit of Rs.8.3 million when in fact the bank has suffered a loss of Rs.16.5 million for that year. 20

c) The bank had been able to avoid making the required provisioning and thereby violated the directions issued by the Central Bank on this matter.

Accordingly, the first respondent after considering the report submitted by the fourth respondent formed an opinion that the bank was engaged in certain irregular transactions so as to distort the true financial condition of the bank, directed the fourth respondent to issue a direction in terms of Sec. 76K of the said Act. Thus, the fourth respondent issued an order on the bank on 9th December 1999 (1R8) directing it to cease the unsound and improper financial 30 practice of recovering interest after the balance sheet date and showing them as income for the bank.

It appears that the fourth respondent carried out a second statutory examination into the activities of the bank as at 30th September 2001. The affidavit of the second respondent shows that the following matters revealed at the said examination.

a) That the bank had continued with the imprudent activities highlighted in the previous examination by resorting to different irregular and complex practices and thereby circumventing the directions given by the first respondent. 40

b) The bank had resorted to other unusual and questionable transactions and violated several prudential requirements.

c) That the financial condition of the bank was further deteriorating.

d) That several provisions of the Banking Act had been violated.

The report containing the findings of the fourth respondent was sent to the first respondent, who having considered the said report directed the bank to freeze the deposits from the public and the advances as at 12th July 2002. The Counsel for the petitioner submitted that having issued the said direction, the first respondent listed the bank as a licensed deposit taking institution by an advertisement published in the Ceylon Daily News dated 12th September 2002 marked P7. It is to be noted that the said advertisement provided, interalia, as follows - "On the other hand, the financial institutions registered and recognised by the Central Bank of Sri Lanka are supervised and regulated by the Central Bank of Sri Lanka. The fact that they are supervised does not mean that your money is guaranteed by the Central Bank of Sri Lanka. By supervision and regulation, the Central Bank of Sri Lanka attempts to ensure that the financial institution acts in a prudential manner, without exposing the deposits of the public to undue risk".

Several meetings were held on 25th March 2002, 2nd May 2002, 21st June 2002 and 3rd July 2002 between the officials of the Senior Management of the bank and the officials of the Central Bank with regard to matters concerning the financial stability and the ongoing viability of the bank. Consequent to the said discussions, the bank was requested to submit a re-structuring proposal to the first respondent. The said proposals submitted by the bank dated 17th July 2002 and 26th July 2002 marked IR16 and IR17 respectively were considered and rejected by the first respondent as the same were not found to be feasible. On two occasions, namely, 6th August 2002 and 4th October 2002 the fourth respondent observed that the deposit level of the bank had been in excess of the limit and called for explanation from the bank while cautioning that any promotional campaign with a view to attract funds from the public could be detrimental to the interests of the depositors and creditors. The said report had an annexure (A16) explaining the critical condition of the bank, to be submitted to the first respondent. The report further indicated that the fourth respondent after examining the matters would make a recommendation to the first respondent. On 21st October 2002 the fourth respondent submitted a report (A17) to the second respondent in terms of Sec.76 M(1) informing that she was satisfied that the current financial condition

of the bank was critical and moved that timely action be taken to prevent the interests of the depositors and creditors of the bank being further jeopardized.

The first respondent having considered the imminent liquidity crisis faced by the bank on 25th October 2002 made order (A18(a)) directing the bank to suspend its business forthwith. It is relevant to mention that the petitioners are not challenging this order made by the first respondent suspending the business of the bank. 90

In terms of Sec.76M(3) of the Act, once a suspension order is made by the first respondent, it ceases to have effect upon the expiration of a period of sixty days from the date on which such an order is made. Thus, the learned Addl S.G submitted that before the expiration of the sixty days from 25th October 2002, the first respondent had the following two options.

a) To make an order permitting the bank to resume business either unconditionally or subject to such conditions as the first respondent may consider; or 100

b) To cancel the licence issued to the bank and to direct the Board of Directors of the bank to apply for winding up.

On 21st November 2002, the fourth respondent submitted a report to the first respondent on the post-suspension examination of the bank, setting out the several options available in terms of Sec. 76 N which would enable the first respondent to permit the bank to resume business. It may be relevant to reproduce certain paragraphs from the said report marked A19.

"13.2 Liquidation of the bank should be resorted to only **if all other options** to revive the bank fail for the following reasons:- 110

> Firstly, from the depositors point of view, liquidation will have serious repercussions on the existing depositors who are likely to suffer losses given the extent to which the assets of PSDB have been impaired and the parlous state of the financial health of PSDB. Based on the fair value of assets arrived at, the depositors and creditors stand to lose heavily and may receive only a part of their deposits viz.46%.

- Secondly, liquidation could have adverse implications on other financial institutions and could precipitate a crisis in the financial system. This is already evident from the fact that certain small banks are not in a position to comply with the minimum statutory liquidity requirement as a result of a decline in deposits after the suspension. 120
- Thirdly, a complete liquidation procedure would be protracted and would take at least five years and depositors may receive even less than the current estimates suggest. Moreover, in a liquidation scenario, even the recovery of performing advances would eventually become difficult which would result in even lesser amounts being available for the depositors. 130
- Finally, the Central Bank would be exposed to considerable criticism if any policy action to deal with the current crisis would have a contagion effect, especially in respect of the smaller institution.

13.3 In view of the foregoing difficulties, the next option that may be considered is whether the Monetary Board could permit resumption of business conditionally and **simultaneously take steps** that are permitted in terms of Sec.76N of the Banking Act.sec 76N (copy annexed) provides for the Board to do one of the following, in relation to PSDB if the bank is permitted to resume business in terms of Sec.76M(3) (a) 140

a) Make arrangements to amalgamate PSDB with another institution which consents to it.

b) Arrange to bring in fresh capital and shareholders to the bank, and re-constitute the Board of Directors.

c) Re-construct PSDB in any manner as would serve the interest of depositors. This includes the closing down of unviable sections of business and re-organizing the management. 150

d) Direct one or more shareholders of PSDB to transfer ownership of their shares to persons nominated by the Monetary board on payment of compensation based on market value in case of quoted shares, or a price deter-

mined by a valuer nominated by the Board in the case of un-quoted shares.

13.4 Thus, there are **several options** available to the Board, if the Board takes a decision in terms of Sec.76 M(3) (a) to permit the resumption of the business subject to conditions.........

13.5 Taking into account all the circumstances relating to this matter, it would seem that of the options provided for in Sec.76 N, **the most preferable course of action** is for the Monetary Board to require the present shareholders in terms of option (d) to transfer their shares to another bank or banks that consent to the arrangement. 160

13.6 Option (d) has the advantage of enabling the removal of present Directors who have been responsible for the mismanagement and misdeeds of PSDB.......

13.7 In the event action cannot be taken in terms of Sec.76N, **the only available option** would be to cancel PSDB's licence and direct liquidation in terms of Sec.76 M(3) (a) despite the difficulties and resistance that may be encountered." 170

This court does not dispute that the first respondent has a discretion in the matter. However, it is a discretion that has to be exercised reasonably, fairly and justly. As Lord Diplock said "the administrative discretion involves a right to choose between more than one possible course of action upon which there is room for reasonable people to hold differing opinions as to which is to be preferred." - *Secretary of State for Education v Tameside Metropolitan B.C*[1]. The valid exercise of a discretion requires a genuine application of the mind and a conscious choice by the first respondent. The effect of the Monetary Law Act is not to set up the court as an arbiter of the correctness of one view over the other. It is the first respondent alone who can take such a decision and, provided the first respondent acts fairly and reasonably within the four corners of its lawful jurisdiction, this court in my opinion cannot interfere. Accordingly, it follows, that the court can examine the exercise of the discretionary power in order to see whether it has been used properly, fairly and according to the rules of reason and justice. 180

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Thus, one has to consider whether the first respondent did in fact take any positive step to amalgamate the bank with another institution and / or make arrangements to bring in fresh capital and / or consider re-constituting the Board of Directors and / or closing down unviable sections of business and re-organizing the management and / or transferring the ownership of shares to persons nominated by the first respondent as suggested by the fourth respondent in clause 13.3. There can be no legal objection to the first respondent obtaining advice and consulting suitable persons but it is vital that it should analyse the options available and come 200 to a correct decision in the public interest. It is the duty of court to strike a suitable balance between executive / administrative efficiency and legal protection of the citizen. Judicial review means, review of the manner in which the decision was made. Lord Green, MR expounded this theory in *Associated Provincial Picture Houses Ltd* v *Wednesbury Corporation* (2) as follows - *"It is true that discretion must be exercised reasonably. Now what does that mean? Lawyers familiar with the phraseology used in relation to exercise of statutory discretions often use the word "unreasonable" in a rather comprehensive sense. It has frequently been used and is* 210 *frequently used as a general description of the things that must be done. For instance, a person entrusted with a discretion must, so to speak, direct himself properly in law.* ***He must call his own attention to the matters which he is bound to consider****. He must exclude from his consideration matters which are irrelevant to what he has to consider. If he does not obey those rules, he may truly be said, and often is said, to be acting unreasonably."*

"There is no absolute and unfettered discretions in public law; discretions are conferred on public functionaries in trust for the public, to be used for the public good, and the propriety of the exercise 220 *of such discretions is to be judged by reference to the purposes for which they were so entrusted." - G.P.S. De Silva C.J. in Premachandra v Jayawickrama.*(3)

Lord Wrenbury dealing with this argument in *R* v *Secretary of State for the Environment ex.p Nottinghamshire* (4) laid down the law as follows - " *A person in whom is vested discretion must exercise his discretion upon reasonable grounds. A discretion does not empower a man to do what he likes merely because he is minded to do so - he must in the exercise of his discretion do not what he*

*likes but what he ought. In other words, he must, by the use of his reason, **ascertain** and **follow** the course which reason directs. **He must act reasonably.**"* 230

If people who have to exercise a public duty by exercising their discretion fail to take into matters which the fourth respondent considers to be proper for the exercise of their discretion, then in the eye of the law they have not exercised their discretion. *"The review of decisions made in the exercise of statutory power, on the basis of reasonableness, taking into consideration proper matters, the exclusion of irrelevant matters and acting on evidence, being basic tenets of Administrative Law, would be rendered illusory, if the authority vested with power is permitted to take refuge in confidentiality and secrecy as to the true basis of his decision."* - (*Premachandra* v *Jayawickrama*)[5]. No substantial evidence has been placed before court to establish that the first respondent considered any of the options. The decision of the first respondent dated 21st November 2002 (1R36) only states that the Board considered the report A19 and discussed the options currently available and directed the Central Bank to update the information on its findings and to consult a lawyer experienced in corporate matters and report further to the first respondent. It only appears that the first respondent invited the members of the Board of Directors of the Bank and gave them an opportunity on 13th December 2002 (1R37) to respond to the findings of the examination conducted by the Central Bank. The response of the Board of Directors was that they did not have a proposal for reviving the bank. How can the first respondent expect any plans/ proposals from the same Board of Directors when the suggestion by the fourth respondent was to re-constitute the Board? As submitted by the learned Counsel for the petitioners, there is not an iota of suggestion in 1R36 that the several options contained in clause 13.3 received the attention of the first respondent and a decision was taken to reject all of them. The petitioners had been led to believe that the first respondent arrived at a decision to cancel the licence of the bank and to wind up its affairs after considering the report A19 submitted by the fourth respondent. No reasons whatsoever were given as to why the first respondent rejected the options suggested by the fourth respondent even if they were considered. In the absence of rea-

sons, it is impossible to determine whether or not the first respondent in fact considered the four options given in clause 13.3. Failure to give adequate reasons therefore amounts to a denial of justice 270 and is itself an error of law. The reasons must not only be intelligible but should deal with the substantial points which have been raised. The courts have treated inadequacy of reasons as an error on the face of record so that inadequately reasoned decision could be quashed, even if the duty to give reasons was not mandatory. [Vide *Re Poyser and Mills' Arbitration.*](6) In the absence of reasons, the person affected may be unable to see whether there has been a justiciable flaw in the decision making process "*If reasons are not disclosed the inference may have to be drawn that it is because in fact there were no reasons – and so also, if reasons are* 280 *suggested, they were in fact not the reasons which actually influenced the decision in the first place.*" – Wijetunga, J in *Suranganie Marapana* v *Bank of Ceylon*(7). Giving reasons introduces clarity and minimises arbitrariness; it give satisfaction to the party against whom the order is made and also enables the supervisory court to keep any tribunal within bounds. If the reasons are not given, the court can only draw an inference that the first respondent had no rational reason for its decision and has failed to act with procedural fairness towards the depositors and creditors.

As Sharvananda J (as he then was) observed in *Sirisena and* 290 *others* v *Kobbekaduwa, Minister of Agriculture and Lands* (8) - "*It is of the utmost importance to uphold the right and indeed the duty of the courts to ensure that powers shall not be exercised unlawfully which have been conferred on a local authority or the executive, or indeed anyone else, when the exercise of such powers affect the basic rights of an individual. The courts should be alert to see that such powers conferred by statute are not exceeded or abused.*"

Learned Counsel for the petitioner also urged that the Monetary Board was not properly constituted when it made the impugned order, sought to be quashed in these proceedings. It is 300 common ground that the Monetary Law (Amendment) Act No.32 of 2002 was certified by the Speaker on 17th December 2002. Sec.3 of the amending Act No.32 of 2002 repealed Sec.8(2)(c) of the Monetary Law Act as follows:-

(c) three members appointed by the President on the recommendation of the Minister of Finance, with the concurrence of the Constitutional Council.

Sec.9 of the amending Act amended Sec.17 and increased the membership of the Monetary Board from three to five and the quorum.of the members was made three. It was not in dispute that Mr.Chanmugam was appointed as a member of the Monetary Board by the President for a period of six years commencing from 17th July 2001. The contention of the learned Counsel for the petitioner was that Mr.Chanmugam ceased to be a member of the said Board in terms of the amending Act and has to be re-appointed by the President on the recommendation of the Minister of Finance with the concurrence of the Constitutional Council. 310

Mr. Marsooof, A.S.G relied on Sec.6 (3) (b) of the Interpretation Ordinance and argued that Mr.Chanmugam acquired a vested right to function as a member of the Monetary Board. Sec.6(3)(b) of the Interpretation Ordinance reads thus:- 320

"Whenever any written law repeals either in whole or part a former written law, such repeal shall not, in the absence of any express provision to that effect, affect or be deemed to have affected.

a) the past operation of or any thing duly done or suffered under the repealed written law;

b) any offence committed, ***any right****, liberty or penalty acquired or incurred under the repealed written law;*

c) any action, proceeding or thing pending or incompleted when the repealing written law comes into operation, but every such action, proceeding, or thing may be carried on and completed as if there had been no such repeal." 330

I agree with the learned A.S.G. that Sec. 6 (3) (b) of the Interpretation Ordinance protects the vested right acquired under the repealed Act, in the absence of any compelling language within the four corners of the repealing Act to a deliberate decision on the part of Parliament to impair those rights. Vide, *Free Lanka Insurance Company Ltd* v *Ranasinghe*[9], *Hai Bai* v *Perera* .[10] In terms of Sec 17 (3) of the Monetary Law Act as amended by Sec.9 340

of Act No. 32 of 2002 the two ex-officio members and Mr.Chanmugam participated at the Board meeting held on 17th December 2002 at 2.00 p.m. and took a decision to wind up the bank and cancel its licence. I hold that the Monetary Board was properly constituted as the amending Act did not purport to abolish the already existing Board and to re-constitute a new Board.

For the reasons stated, a *writ of certiorari* is issued quashing the cancellation of the bank's licence by the first respondent contained in the letter dated 18th December 2002 marked A21. A mandate in the nature of *writ of mandamus* is issued on the first respondent to consider the several options recommended by the fourth respondent in A19 and thereafter to take such appropriate steps as are provided by law. I make no order as to costs. As agreed by all Counsel, the decision in this application will bind the respective parties in C.A.Appl 65/2003;C.A.Appl 78/2003 and C.A.appl 83/2003. 350

Application allowed

Writ of Certiorari issued quashing the cancellation of the Bank's Licence.

Writ of Mandamus issued to consider the several options.