has not expressed itself in any of the three decisions, either directly or indirectly, upholding the proposition that for computing the total periods of detention prescribed in clauses (i) and (ii) of proviso (*a*) to Section 167(2) of the Code, the date of arrest and not the date of production of the accused before the magistrate should be taken as the starting point. In the light of our findings we are clearly of the view that the contentions of the appellants cannot be sustained. The learned Single Judge, it must therefore be held, has acted correctly in allowing the petition filed by the State for cancellation of the bail granted to the appellants. As the Munsif Magistrate has granted bail to the appellants before the expiry of 90 days of remand period allowed under law, the order of the Magistrate will not tantamount to one passed under the provisions of Chapter XXXIII of the Code and hence there is no scope for contending that re-arrest of the appellants can be ordered only in terms of sub-section (5) of Section 437. We, however, make it clear that after the appellants surrender themselves to custody or are taken into custody by re-arrest, they will not stand precluded from seeking enlargement on bail by filing applications under sub-section (1) of Section 437 of the Code and satisfying the court that they deserve to be enlarged on bail.

35. In the result, the judgment of the High Court is upheld and the appeal is dismissed accordingly.

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(BEFORE A. P. SEN AND D. P. MADON, JJ.)

Civil Appeal No. 4412 of 1985

CENTRAL INLAND WATER TRANSPORT CORPORATION LIMITED AND ANOTHER .. Appellants ;

Versus

BROJO NATH GANGULY AND ANOTHER .. Respondents.

And

Civil Appeal No. 4413 of 1985

CENTRAL INLAND WATER TRANSPORT CORPORATION LIMITED AND ANOTHER .. Appellants ;

Versus

TARUN KANTI SENGUPTA AND ANOTHER .. Respondents.

Civil Appeals Nos. 4412 and 4413 of 1985†,
decided on April 6, 1986

Labour and Services — Termination — Unconscionable terms in contract of employment are void — Company wholly owned by Government — Held on facts, covered by the definition of the State under Articles 12 and 36 and therefore

†From the Judgment and Order dated August 9, 1985 of the Calcutta High Court in F. M. A. T. No. 1604 and 649 of 1983.

subject to Part III and IV of the Constitution — Term in contract of employment as also service rules of the company providing for termination of services of permanent employees without assigning reasons on three months' notice or pay in lieu thereof on either side — Held on facts, unconscionable, arbitrary and opposed to public policy — Hence void under Section 23 of Contract Act as also violative of Article 14 — Central Inland Water Transport Corporation Ltd. (Service, Discipline and Appeal) Rules, 1979, Rule 9(i) — Held, void and unconstitutional to the extent it confers such right of termination on the Corporation — Remaining part of the Rule entitling the employees to terminate their services on notice would prevail — Corporation directed to make suitable modifications in the Rule — Termination orders made in terms of appointment letters and under the impugned Rule set aside and reinstatement with full arrears of pay ordered

The appellant-Corporation is a Government company incorporated under the Companies Act. The majority shares of the Corporation are held by the Union of India and the remaining shares are held by the States of W. B. and Assam. Article 51 of the Articles of Association of the Corporation conferred upon the President of India to issue directions or instructions regarding affairs or conduct of the business of the Corporation or of the Directors thereof as also regarding exercise and performance of its functions pertaining to national security and public interest. Article 51-A entitled the President to call for returns, accounts etc. of the Corporation. Articles 14, 15, 16, 17 and 37 conferred on the President power to appoint and remove Chairman and the Board of Directors of the Corporation. Articles 41 and 42 were regarding the President's control over the working of the Corporation. Article 47 provided for appointment and re-appointment of the auditors of the Corporation to be made by the Central Government on the advice of the Comptroller and Auditor-General of India and the nature of control to be exercised by the Comptroller and Auditor-General in the matter of audit and accounts.

Since another company viz. the Rivers Steam Navigation Co. Ltd. was carrying on the same business as the Corporation was doing, a Scheme of Arrangement was entered into between the Corporation and that company for dissolution of the latter and takeover of its business and liabilities by the former. The Scheme inter alia stipulated that the Corporation shall take as many of the existing staff or labour as possible and that those who could not be taken over shall be paid by the transferor company all moneys due to them under the law and all legitimate and legal compensations payable to them either under Industrial Disputes Act or otherwise legally admissible and that such moneys shall be provided by the Government of India to the transferor Company who would pay these dues. The Calcutta High Court approved the Scheme

Each of the respondents in the two appeals were in the service of the said company. Their services were taken over by the Corporation after the High Court's sanction to the Scheme of Arrangement. While the respondent Ganguly was appointed as the Deputy Chief Accounts Officer and was later promoted as Manager (Finance), the respondent Sengupta was appointed as Chief Engineer (River Services) and was later promoted as General Manager (River Services). Their appointment letters were in a stereotype form under which the Corporation could without any previous notice terminate their services, if the Corporation was satisfied that the employee was unfit medically or if he was guilty of any insubordination, intemperance or other misconduct, or of any breach of any rules pertaining to his service or conduct or non-performance of his duties. The letters of appointment further stipulated that they would be

subject to the rules and regulations of the Corporation. Rule 9(*i*) of the Corporation's Service, Discipline and Appeal Rules of 1979 provided that the services of a permanent employee could be terminated on three months' notice on either side or on payment of three months' pay plus DA to the employee or on deduction of a like amount from his salary as the case may be in lieu of the notice.

By a confidential letter the respondent Ganguly was asked to reply within 24 hours to the allegations of negligence made against him. After having his representation and detailed reply, a notice under Rule 9(*i*) was served on him terminating his services with immediate effect by paying three months' pay. Similarly a charge-sheet was issued to the respondent Sengupta intimating him that a disciplinary inquiry was proposed against him under the Rules and calling upon him to file his written statement of defence. Sengupta denied the charges made against him and asked for inspection of documents and copies of statements of witnesses mentioned in the said charge-sheet. But a notice was served on him under Rule 9(*i*) terminating his services with immediate effect by paying three months' salary. Both Ganguly and Sengupta filed writ petitions before High Court and a Division Bench of that court allowed the same.

The Corporation filed appeals before Supreme Court. The main questions for determination were (*i*) whether the appellant-Corporation was an instrumentality of the State so as to be covered by Articles 12 and 36 of the Constitution and (*ii*) whether an unconscionable term in a contract of employment entered into with the Corporation was void under Section 23 of the Contract Act and violative of Article 14 and as such whether Rule 19(*i*) which formed a part of the contract of employment between the Corporation and its employees to whom the said Rules applied, was void ? Supreme Court confirmed the judgment of the High Court with modification in the declaration made by it and dismissed the Corporation's appeals with costs.

I. INSTRUMENTALITY OF THE STATE

A. **Constitution of India — Articles 12 and 36 — 'The State'— Scope of the expression — Compared with expression 'State' in Article 308 — Government company defined Section 617 of Companies Act, 1956, whether falls within "the State" — Test to determine — Central Inland Water Transport Corporation Ltd., a Government company, jointly and wholly owned by the Central Government and two State Governments and managed by Chairman and Board of Directors appointed and removable by Central Government, held on facts, covered by Article 12 and therefore an instrumentality or agency of the State**

Held :

A State must have a relatively permanent legal organization, determining its structure and the relative powers of its major governing bodies or organs That is to be found in its Constitution. (Para 17)

While Article 308 read with other provisions of Part XIV of the Constitution show that the word 'State' applies to the federating units (other than the State of J & K) which altogether constitute the Union of India, Article 12 as also Article 36 define the expression 'the State' so as to extend its meaning by the use of the word 'includes' in Article 12 to include within it also what otherwise may not have been comprehended by that expression when used in its ordinary legal sense. The expression "the State" in Article 12 includes— (1) the Government of India, (2) Parliament of India, (3) the government of each of the states which constitute the Union of India, (4) the legislature of

each of the States which constitute the Union of India, (5) all local authorities within the territory of India, (6) all local authorities under the control of the Government of India, (7) all other authorities within the territory of India, and (8) all other authorities under the control of the Government of India. (Paras 19 and 21)

The State, being an abstract entity, acts through its agencies or instrumentalities. By extending the executive power of the Union and of each of the States to the carrying on of any trade or business, Article 298 does not convert either the Union of India or any of the States which collectively form the Union into a merchant buying and selling goods or carrying on either trading or business activity, for the executive power of the Union and of the States, whether in the field of trade or business or in any other field, is always subject to constitutional limitations and particularly the provisions relating to Fundamental Rights in Part III and is exercisable in accordance with and for the furtherance of the Directive Principles of State Policy. (Para 39)

Sukhdev Singh v. *Bhagatram Sardar Singh Raghuvanshi,* (1975) 1 SCC 421 : 1975 SCC (L & S) 101 : (1975) 3 SCR 619 : AIR 1975 SC 1331, *relied on*

A Comparative Study, W. Friedmann and J. F. Garner : *Government Enterprise,* 507, *referred to*

[*See* editorial note at page 165]

The trading and business activities of the State constitute "public enterprise". The structural forms in which the government operates in the field of public enterprise are many and varied. These may consist of government departments, statutory bodies, statutory corporations, government companies, etc. The immunities and privileges possessed by bodies so set up by the Government under Article 298 are subject to Fundamental Rights and exercisable in accordance with and in furtherance of the Directive Principles of State Policy. (Para 40)

For the purposes of Article 12, Court must necessarily see through the corporate veil to ascertain whether behind that veil is the face of an instrumentality or agency of the State. If there is an instrumentality or agency of the State which has assumed the garb of a government company as defined in Section 617 of the Companies Act, it does not follow that it thereby ceases to be an instrumentality or agency of the State. (Para 67)

Applying the above test to the present case, it is clear that the appellant-Corporation is 'the State' within the meaning of Article 12. It is nothing but the government operating behind a corporate veil, carrying out a governmental activity and governmental functions of vital public importance through the instrumentality of a Government Company. Merely because it has so far not the monopoly of inland water transportation is not sufficient to divest it of its character of an instrumentality or agency of the State. (Para 67)

Sukhdev Singh v. *Bhagatram Sardar Singh Raghuvanshi,* (1975) 1 SCC 421 : 1975 SCC (L & S) 101 : (1975) 3 SCR 619 : AIR 1975 SC 1331 ; *Ramana Dayaram Shetty* v. *International Airport Authority of India,* (1979) 3 SCC 489 : (1979) 3 SCR 1014 : AIR 1979 SC 1628 ; *U. P. Warehousing Corpn.* v. *Vinay Narayan Vajpayee,* (1980) 3 SCC 459 : 1980 SCC (L & S) 453 : (1980) 2 SCR 773 and *Ajay Hasia* v. *Khalid Mujib Sehravardi,* (1981) 1 SCC 722 : 1981 SCC (L & S) 258 : (1981) 2 SCR 79 : AIR 1981 SC 487, *applied*

Rai Sahib Ram Jawaya Kapur v. *State of Punjab,* (1955) 2 SCR 225 : AIR 1955 SC 459 ; *Rajasthan State Electricity Board, Jaipur* v. *Mohan Lal,* (1967) 3 SCR 377 : AIR 1967 SC 1857 : (1968) 1 LLJ 257 ; *Som Prakash Rekhi* v. *Union of India,* (1981) 1 SCC 449 : 1981 SCC (L & S) 200 : (1981) 2 SCR 111 : AIR 1981 SC 212 ; *B. S. Minhas* v. *Indian Statistical Institute,* (1983) 4 SCC 582 : 1984 SCC (L & S) 26 ; *Manmohan Singh Jaitla* v. *Commissioner, Union Territory of Chandigarh,* 1984 Supp SCC 540 : 1984 SCC (L & S) 269 ; *Workmen* v. *Hindustan Steel Ltd.,* 1984 Supp SCC 554 : 1985 SCC (L & S) 269 ; *P. K. Ramachandra Iyer* v. *Union of India,* (1984) 2 SCC 141 : 1984 SCC (L & S) 214 ;

A. L. Kalra v. *Project and Equipment Corpn. of India Ltd.*, (1984) 3 SCC 316 : 1984 SCC (L & S) 497 and *W. B. State Electricity Board* v. *Desh Bandhu Ghosh*, (1985) 3 SCC 116 : 1985 SCC (L & S) 607, *relied on*

Praga Tools Corpn. v. *C. A. Imanual*, (1969) 1 SCC 585 : (1969) 3 SCR 773 : AIR 1969 SC 1306 ; *State of Bihar* v. *Union of India*, (1970) 1 SCC 67 : (1970) 2 SCR 522 : AIR 1970 SC 1446 ; *S. L. Agarwal* v. *General Manager, Hindustan Steel Ltd.*, (1970) 1 SCC 177 : (1970) 3 SCR 363 : AIR 1970 SC 1150 ; *Sabhajit Tewary* v. *Union of India*, (1975) 1 SCC 485 : 1975 SCC (L & S) 99 : (1975) 3 SCR 616 : AIR 1975 SC 1329 and *S. S. Dhanoa* v. *Municipal Corpn.*, (1981) 3 SCC 431 : 1982 SCC (L & S) 6 : 1981 SCC (Cri) 733, *distinguished*

Re the Earldom of Oxford, (1625) W. Jo. 96 : (1626) 82 ER 50 ; *Sankari Prasad Singh Deo* v. *Union of India and State of Bihar*, 1952 SCR 89 : AIR 1951 SC 458; *Gurugobinda Basu* v. *Sankari Prasad Ghosal*, (1964) 4 SCR 311 : AIR 1964 SC 254 : *Rylands* v. *Fletcher*, (1868) LR 3 HL 330 and *Donoghue* v. *Stevenson*, (1932) AC 562, *referred to*

II. UNCONSCIONABLE CONTRACT OF EMPLOYMENT

B. Labour and Services — Termination — Termination of services of permanent employees on three months' notice or pay on either side — Such provisions in the terms of employment, held, void and inoperative under Section 23 of Contract Act — If employer is an instrumentality of the State covered by Articles 12 and 36, snch provision would also be violative of Articles 14, 38, 39 and 41 — Merely entitling employees also to terminate their services on three months' notice or pay does not amonnt to mutnality having regard to their nnequal bargaining power

C. Contract Act, 1872 — Section 23 — Contracts which are unconscionable, unfair, unreasonable and opposed to pnblic policy are void under — Circumstances under which contracts can be held to be void on these grounds — Concepts of nnconscionableness, unfairness, unreasonableness and public policy stated — Contractual terms of employment in stereotyped form on 'take it or leave it' basis detrimental to the employees, even if accepted by the employees, liable to be declared void and inoperative on these grounds — Central Inland Water Transport Corporation Ltd. (Service, Discipline and Appeal) Rules, 1979, Rule 9(i), held, void to that extent — Labour and Services — Termination — Contracts — Standard form contracts

D. Constitution of India — Articles 14 and 12 — Contract with instrumentality of the State — Terms of contract of employment and service rules detrimental to the employees — If found to be unconscionable, unfair, unreasonable, against public policy and pnblic interest and against principle of distributive justice in the context of Parts III and IV of the Constitution, held, would be violative of Article 14 — Central Inland Water Transport Corporation Ltd. (Service, Discipline and Appeal) Rules 1979, Rule 9(i), held, violative of Article 14 on that ground — Words and Phrases — "pnblic policy" — Jurisprudence

E. Constitution of India — Articles 39(a) and 41 — Service rule of the State or its instrumentality providing for termination of service of permanent employees withont reasons merely on three months notice is violative of Article 39(a) and 41 — Expressions 'adequate means of livelihood' in Article 39(a) and 'effective provision for securing the right to work' in Article 41 — Meaning of

F. Constitution of India — Article 14 — Arbitrariness and discrimination — Service rules of Government company covered by Article 12 — Central Inland Water Transport Corporation Ltd. (Service, Discipline and Appeal) Rules,

1979, Rule 9(i) — Held, partly violative of Article 14 being arbitrary, unguided and discriminatory

G. **Constitution of India — Article 14 — Arbitrariness — Presumption in favour of high officers that they would not act arbitrarily or capriciously would not prevail if provisions do not enjoin them to observe principles of natural justice while taking adverse actions — Administrative Law**

H. **Constitution of India — Article 14 — Natural justice principles are implicit in Article 14**

I. **Labour and Services — Termination — Natural justice — Service rules of the State or its instrumentality not providing for observance of audi alteram partem rule while terminating services of permanent employee violative of Article 14 — Mere fact that power of termination is vested in high officers would not save the rule from unconstitutionality — Constitution of India, Article 14 — Administrative Law**

J. **Labour and Services — Registration — Right to resign — Deprivation of, not justified — Resignation should normally be accepted — Circumstances when employer can refuse to accept it — Central Inland Water Transport Corporation Ltd. (Service, Discipline & Appeal) Rules, 1979, Rules 9 & 11**

K. **Constitution of India — Article 226 — Alternative remedy — Illegal termination of service — Remedy under Article 226 would be more efficacious than a civil suit — Hence writ petition under Article 226 maintainable**

L. **Constitution of India — Preamble and Articles 38 & 39 — Held, embody the jurisprudential doctrine of distributive justice — Jurisprudence (Para 82)**

M. **Constitution of India — Article 14 — Unconscionable contract entered into by State while in superior bargaining position, held, covered**

Held :

Clause (*i*) of Rule 9 of the Service, Discipline and Appeal Rules, 1979 of the Central Inland Water Transport Corporation Limited is void under Section 23 of the Contract Act, 1872, as being opposed to public policy and is also ultra vires Article 14 of the Constitution to the extent that it confers upon the Corporation the right to terminate the employment of a permanent employee by giving him three months' notice, or pay in lieu of the notice. Such a condition or provision is unconscionable, unfair, unreasonable and opposed to public policy. (Para 112)

An unconscionable bargain or contract is one which is irreconcilable with what is right or reasonable or the terms of which are so unfair and unreasonable that they shock the conscience of the Court. (Paras 76 and 93)

Shorter Oxford Dictionary, 3rd edn. Vol. II, p. 2288 ; Chitty on Contracts, 25th ed. Vol. I, paras 4, 486 and 516 ; Black's Law Dictionary, 5th edn. p. 38; Reinstatement of the Law —Second, as adopted and promulgated by American Law Institute, Vol. II, S. 208, pp. 107, 112 ; Law of Uniust Contracts, published by Butterworths in 1982, p. 28-29, *relied on*

Accidental Worldwide Investment Corpn. v. *Skibs A/S Avanti,* (1976) 1 Lloyd's Rep 293 ; *North Ocean Shipping Co. Ltd.* v. *Hyundai Construction Co. Ltd.,* (1979) QB 705 ; *Pao On* v. *Lau Yin Long,* (1980) AC 614 and *Universe Tankships Inc. of Monrovia* v. *International Transport Workers Federation,* 1981 ICR 129 : (1982) 2 WLR 803, *referred to*

The doctrine of distributive justice is another jurisprudential concept which has affected the law of contracts. According to this doctrine, distributive fairness and justice in the possession of wealth and property can be achieved not only by taxation but also by regulatory control of private and contractual

transactions even though this might involve some sacrifice of individual liberty. This doctrine has found constitutional recognition through the Preamble and Articles 38 and 39 (Para 82)

Lingappa Pochanna Appelwar v. *State of Maharashtra*, (1985) 1 SCC 479, *relied on*

The test of reasonableness or fairness of a clause in a contract where there is inequality of bargaining power is another theory recognised in the sphere of law of contracts. The courts will not enforce and will, when called upon to do so, strike down an unfair and unreasonable contract, or a clause in a contract, entered into between parties who are not equal in bargaining power. Lord Diplock in *A. Schroeder Music Publishing Co. case* has given the test of fairness thus : "Whether the restrictions are both reasonably necessary for the protection of the legitimate interests of the promisee and commensurate with the benefits secured to the promiser under the contract. For the purpose of this test all the provisions of the contract must be taken into consideration." This is in consonance with right and reason, intended to secure social and economic justice and conforms to the mandate of the great equality clause in Article 14. There can be myriad situations which result in unfair and unreasonable bargains between parties possessing wholly disproportionate and unequal bargaining power. These cases can neither be enumerated nor fully illustrated. The court must judge each case on its own facts and circumstances. The above principle will apply where the inequality of bargaining power is the result of the great disparity in the economic strength of the contracting parties or where the inequality is the result of circumstances, whether of the creation of the parties or not or where the weaker party is in a position in which he can obtain goods or services or means of livelihood only upon the terms imposed by the stronger party or go without them or where a man has no choice, or rather no meaningful choice, but to give his assent to a contract or to sign on the dotted line in a prescribed or standard form or to accept a set of rules as part of the contract, however unfair, unreasonable and unconscionable a clause in that contract or form or rules may be. This principle, however, will not apply where the bargaining power of the contracting parties is equal or almost equal. This principle may not apply where both parties are businessmen and the contract is a commercial transaction. However, these are only illustrations as it is difficult to give an exhaustive list of all bargains of this type. (Paras 83, 84 & 89)

Gillespie Brothers & Co. Ltd. v. *Roy Bowles Transport Ltd.*, (1973) QB 400 ; *Lloyds Bank* v. *Bundy*, (1974) 3 All ER 757 ; *A. Schroeder Music Publishing Co. Ltd.* v. *Macaulay (formerly Instone)*, (1974) 1 WLR 1308 ; *Levison* v. *Patent Steam Carpet Co. Ltd.*, (1978) QB 69 and *Photo Production Ltd.* v. *Securicor Transport Ltd.*, (1980) AC 827, *relied on*

The contracts of the types to which the principle formulated above applies are not contracts which are tainted with illegality but are contracts which contain terms which are so unfair and unreasonable that they shock the conscience of the court. In the vast majority of cases such contracts are entered into by the weaker party under pressure of circumstances, generally economic, which results in inequality of bargaining power. Such contracts will not fall within the four corners of the definition of "undue influence" given in Section 16(1) of the Contract Act, even though at times they are between parties one of whom holds a real or apparent authority over the other. Contracts in prescribed or standard forms or which embody a set of rules as part of the contract are entered into by the party with superior bargaining power with a large number of persons who have far less bargaining power or no bargaining power at all. Such contracts which affect a large number of persons or a group or groups of persons, if they are unconscionable, unfair and unreasonable, are injurious to the public interest. Such a contract or its clause should be

adjudged void under Section 23 of the Contract Act on ground of being opposed to public policy. (Paras 91 & 93)

The case may be different where the purpose of the contract is illegal or immoral. (Para 93)

A. Schroeder Music Publishing Co. Ltd. v. *Macaulay (formerly Instone)*, (1974) 1 WLR 1308 and *Kedar Nath Motani* v. *Prahlad Rai*, (1960) 1 SCR 861 : AIR 1960 SC 213, *approved*

Public policy, is not the policy of a particular government. It connotes some matter which concerns the public good and the public interest. The principles governing public policy must be and are capable, on proper occasion, of expansion or modification. If there is no head of public policy which covers a case, then the court must in consonance with public conscience and in keeping with public good and public interest declare such practice to be opposed to public policy. Above all, in deciding any case which may not be covered by authority, courts should be guided by the Preamble to the Constitution and the principles underlying the Fundamental Rights and the Directive Principles. (Para 92)

Rule 9(*i*) can aptly be called 'the Henry VIII Clause'. It confers an absolute, arbitrary and unguided power upon the Corporation. It does not even state who on behalf of the Corporation is to exercise that power. While the Rules provide for four different modes in which the services of a permanent employee can be terminated earlier than his attaining the age of superannuation, namely, Rules 9(*i*), 9(*ii*), 36(*iv*)(*b*) read with 38 and 37, Rule 9(*i*) is the only rule which does not state in what circumstances the power conferred by that rule is to be exercised. Thus even where the Corporation could proceed under Rule 36 and dismiss an employee on the ground of misconduct after holding a regular disciplinary inquiry, it is free to resort instead to Rule 9(*i*) in order to avoid the hassle of an inquiry. No opportunity of a hearing is at all to be afforded to the permanent employee whose service is being terminated in the exercise of this power. It thus violates audi alteram partem rule of natural justice also which is implicit in Article 14. It is not covered by any of the situations which would justify the total exclusion of the audi alteram partem rule. The view that the Board of Directors would not exercise this power arbitrarily or capriciously as it consists of responsible and highly placed persons ignores the fact that however highly placed a person may be, he must necessarily possess human frailties and "power tends to corrupt, and absolute power corrupts absolutely". (Para 98)

W. B. State Electricity Board v. *Desh Bandhu Ghosh*, (1985) 3 SCC 116 : 1985 SCC (L & S) 607, *followed*

Union of India v. *Tulsiram Patel*, (1985) 3 SCC 398 : 1985 SCC (L & S) 672 and *Swadeshi Cotton Mills* v. *Union of India*, (1981) 1 SCC 664, *relied on*

Lord Acton's : *Historical Essays and Studies*, Appendix, *referred to*

Rule 9(*i*) is also discriminatory for it enables the Corporation to discriminate between employee and employee. It can pick up one employee and apply to him Rule 9(*i*). It can pick up another employee and apply to him Rule 9(*ii*). It can pick up yet another employee and apply to him Rule 36(*iv*)(*b*) read with Rule 38 and to yet another employee it can apply Rule 37. All this the Corporation can do when the same circumstances exist as would justify the Corporation in holding under Rule 38 a regular disciplinary inquiry into the alleged misconduct of the employee. (Para 99)

The Corporation is a large organisation. The said Rules form part of the contract of employment between the Corporation and its employees who are not workmen. These employees have no powerful Union to support them. They had no voice in the framing of the said Rules. They had no choice but to accept the said Rules as part of their contract of employment. There is gross disparity between the Corporation and its employees, whether they be workmen or officers. The Corporation can afford to dispense with the services of an officer and will find many others to take his place but an officer cannot afford to lose his job because if he does so, there are not many jobs waiting for him. A clause such as Rule 9(*i*) is against right and reason. It is wholly unconscionable. It has been entered into between parties between whom there is gross inequality of bargaining power. Rule 9(*i*) is a term of the contract between the Corporation and all its officers. It affects a large number of persons and it squarely falls within the principle stated earlier. The government and its agencies and instrumentalities constitute the largest employer in the country. A clause such as Rule 9(*i*) in a contract of employment affecting large sections of the public is harmful and injurious to the public interest for it tends to create a sense of insecurity in the minds of those to whom it applies and consequently it is against public good. Such a clause, therefore, is opposed to public policy and as such it is void under Section 23 of the Contract Act. (Para 100)

It is not possible to accept the contention that this was a contract entered into by the Corporation like any other contract entered into by it in the course of its trading activities and the court, therefore, ought not to interfere with it. The employees cannot be equated with goods which could be bought and sold ; nor could a contract of employment be equated with a mercantile transaction between two businessmen much less when the contract of employment is between a powerful employer and a weak employee. (Para 101)

[*See* editorial note at page 165]

Although Rule 9(*i*) was supported by mutuality inasmuch as it conferred an equal right upon both the parties but considering the unequal position of the Corporation and its employees, there is no real mutuality. (Para 102)

As the Corporation is "the State" within the meaning of Article 12, it was amenable to the writ jurisdiction of the High Court under Article 226 and as such its actions must be in conformity with Article 14. But Rule 9(*i*) is both arbitrary and unreasonable and it also wholly ignores and sets aside the audi alteram partem rule ; it, therefore, violates Article 14. (Paras 104 and 105)

Sukhdev Singh v. *Bhagatram Sardar Singh Raghuvanshi*, (1975) 1 SCC 421 : 1975 SCC (L & S) 101 : (1975) 3 SCR 619 : AIR 1975 SC 1331; *Ramana Dayaram Shetty* v. *International Airport Authority of India*, (1979) 3 SCC 489 : (1979) 3 SCR 1014 : AIR 1979 SC 1628 and *Ajay Hasia* v. *Khalid Mujib Sehravardi*, (1981) 1 SCC 722 : 1981 SCC (L & S) 258 : (1981) 2 SCR 79, *relied on*

W. B. State Electricity Board v. *Desh Bandhu Ghosh*, (1985) 3 SCC 116 : 1985 SCC (L & S) 607, *affirmed*

S. S. Muley v. *J. R. D. Tata*, 1980 Lab IC 11 : (1979) 2 SLR 438 (Bom), *approved*

Manohar P. Kharkhar v. *Raghuraj*, (1981) 2 LLJ 459 (Bom), *criticised*

Further, the Corporation being covered by Article 12, its actions must also be in accordance with the Directive Principles prescribed by Part IV. An 'adequate means of livelihood' mentioned in Article 39(*a*) cannot be secured to the citizens by taking away without any reason the means of livelihood. The mode of making 'effective provision for securing the right to work' referred to in Article 41 cannot be by giving employment to a person and then without

any reason throwing him out of employment. The action of an instrumentality or agency of the State, if it frames a service rule such as Rule 9(*i*) or a rule analogous thereto would, therefore, also be contrary to Articles 39(*a*) and 41. (Para 110)

The respondents could have filed a civil suit for a declaration that the termination of their services was contrary to law on the ground that Rule 9(*i*) was void. But in such a suit the civil court could not have awarded reinstatement as that would have amounted to granting specific performance of a contract of personal service. As the Corporation is 'the State' it was open to the respondents to adopt the far more efficacious remedy under Article 226. (Para 103)

The High Court was, therefore, right in quashing the impugned orders of termination of services of the respondents and directing the Corporation to reinstate them and to pay them all arrears of salary. The High Court was, however, not right in declaring Rule 9(*i*) in its entirety as ultra vires Article 14 of the Constitution and in striking down as being void the whole of that clause. Rule 9 also confers upon a permanent employee the right to resign from the service of the Corporation. By entering into a contract of employment a person does not sign a bond of slavery and a permanent employee cannot be deprived of his right to resign. A resignation by an employee would, however normally require to be accepted by the employer in order to be effective. It can be that in certain circumstances an employer would be justified in refusing to accept the employee's resignation as, for instance, when an employee wants to leave in the middle of a work which is urgent or important and for the completion of which his presence and participation are necessary. An employer can also refuse to accept the resignation when there is a disciplinary inquiry pending against the employee. In such a case, to permit an employee to resign would be to allow him to go away from the service and escape the consequences of an adverse finding against him in such an inquiry. There can also be other grounds on which an employer would be justified in not accepting the resignation of an employee. The Corporation ought to make suitable provisions in that behalf in the said Rules. Therefore, while the judgment of the High Court requires to be confirmed, the declaration given by it requires to be suitably modified. (Para 111)

[Ed. Recently the Supreme Court in *LIC* v. *Escorts Ltd.*, (1986) 1 SCC 264 (paras 102 and 103) held that when the State or its instrumentality ventures into the corporate world and is engaged in ordinary commercial transactions like purchasing shares of a company it assumes to itself the ordinary role of a shareholder with all the rights available to such a shareholder. In such a situation the actions of the State or its instrumentality cannot be questioned on ground of violation of fundamental rights (Article 14 in that case). But it is worthwhile to read para 39 of the present judgment which shows a diversion of opinion.]

III. MISCELLANEOUS

N. **Contract Act, 1872 — Section 24 — Where several distinct promises made for a single consideration and some of them are unenforceable, the rest of the promises would be enforceable and the entire agreement would not become void — Constitution of India, Article 13 — Severability**

Held :

An agreement is not always void in its entirety. If several distinct promises are made for one and the same lawful consideration, and one or more of them

be such as the law will not enforce, that will not of itself prevent the rest from being enforceable. (Para 75)

Pickering v. *Ilfracombe Ry. Co.*, (1868) LR 3 CP 235, *relied on*

O. **Constitution of India — Article 141 — Ratio decidendi — Applicability to subsequent case — Merely because a point had not been decided in earlier case, court would not be barred to decide the same in the subsequent case by applying the general law laid down by the court earlier**

It is fallacious to assume that merely because a point has not fallen for decision by the court, it should not be decided at any time. The whole process of judicial interpretation lies in extending or applying by analogy the ratio decidendi of an earlier case to a subsequent case which differs from it in certain essentials, so as to make the principle laid down in the earlier case fit in with the new set of circumstances. The sequitur of the above assumption would be that the court should tell the suitor that there is no precedent governing his case and, therefore, it cannot give him any relief. This would be to do gross injustice. (Para 66)

Rylands v. *Fletcher*, (1868) LR 3 HL 330 and *Donoghue* v. *Stevenson*, (1932) AC 562, *referred to*

P. **Jurisprudence — Law — Role of law in society — Law should move forward in tune with the changed ideas and ideologies of the society (Para 26)**

Q. **Contracts — Adhesion contracts — Concept of (Para 79)**

Chitty on Contracts, 25th edn. Vol. I, para 4 and Black's Law Dictionary, 5th edn. p. 38, *referred to*

R. **Judicial activism — Burden on courts to adapt the law to the changing needs of society — Interpretation of Statutes (Para 26)**

S. **Constitution of India — Generally — Is not a written constitution in the strict legal sense — It has an idealistic and philosophical base as indicated by its Preamble and Parts III and IV (Para 32 to 34)**

T. **Contracts — Concepts of conscionableness, fairness, reasonableness and distributive justice affect the law of contracts (Paras 76 to 89)**

U. **Labour and Services — Service rules — 'Henry VIII clause' — Meaning of — Administrative Law — Delegated Legislation — Words and phrases (Paras 97 and 98)**

W. B. State Electricity Board v. *Desh Bandhu Ghosh*, (1985) 3 SCC 116 : 1985 SCC (L & S) 607, *referred to*

R-M/7334/CLA

Advocates who appeared in this case :

Shanti Bhushan, Senior Advocate, (*Subrata Ray* and *A.K. Sil*, Advocates with him) for the Appellants.
Y. S. Chitale, Senior Advocate, (*H. K. Puri*, *G. A. Shah*, *Mrs Anil Katiyal*, *C. V. Subba Rao*, *R. N. Poddar*, Advocates with him) for the Respondents.
Mridul Ray and *K. Swami*, Advocates for the Interveners.

The Judgment of the Court was delivered by

MADON, J.—These appeals by special leave granted by this Court raise two questions of considerable importance to government companies and their

employees including their officers. These questions are :

(1) Whether a government company as defined in Section 617 of the Companies Act, 1956, is "the State" within the meaning of Article 12 of the Constitution ?

(2) Whether an unconscionable term in a contract of employment is void under Section 23 of the Indian Contract Act, 1872, as being opposed to public policy and, when such a term is contained in a contract of employment entered into with a government company, is also void as infringing Article 14 of the Constitution in case a government company is "the State" under Article 12 of the Constitution ?

2. Although the record of these appeals is voluminous, the salient facts lie within a narrow compass. The first appellant in both these appeals, namely, the Central Inland Water Transport Corporation Limited (hereinafter referred to in short as "the Corporation"), was incorporated on February 22, 1967. The majority of the shares of the Corporation were at all times and still are held by the Union of India which is the second respondent in these appeals, and the remaining shares were and are held by the State of West Bengal and the State of Assam. Section 617 of the Companies Act, 1956 (Act 1 of 1956), provides as follows :

> 617. *Definition of 'government company'.*—For the purposes of this Act government company means any company in which not less than fifty-one per cent of the paid-up share capital is held by the Central Government, or by any State Government or governments, or partly by the Central Government and partly by one or more State Governments and includes a company which is a subsidiary of a government company as thus defined.

As all the shares of the Corporation are held by different governments, namely, the Government of India and the Governments of West Bengal and Assam, the Corporation is not only a government company as defined by the said Section 617 but is a company wholly owned by the Central Government and two State Governments.

3. Clause III(A) of the Memorandum of Association of the Corporation lists the main objects of the Corporation and Clause III(B) of the Memorandum of Association lists the objects incidental or ancillary to the main objects. It is unnecessary to reproduce all these objects for according to the petitions filed by the Corporation for obtaining special leave in these appeals, it is currently engaged in carrying out the following activities, namely,

(*i*) maintaining and running river service with ancillary function of maintenance and operation of river-site jetty and terminal ;

(*ii*) constructing vessels of various sizes and descriptions ;

(*iii*) repairing vessels of various sizes and descriptions ; and

(*iv*) undertaking general engineering activities.

4. Article 4 of the Articles of Association of the Corporation provides

that the Corporation is a private company within the meaning of clause (*iii*) of sub-section (1) of Section 3 of the Companies Act and that no invitation is to be issued to the public to subscribe for any shares in, or debentures or debenture stock of, the Corporation. Article 51 of the Articles of Association confers upon the President of India the power to issue from time to time such directions or instructions as he may consider necessary in regard to the affairs or the conduct of the business of the Corporation or of the directors thereof. The said article also confers upon the President the power to issue such directions or instructions to the Corporation as to the exercise and performance of its functions in matters involving national security or public interest. Under the said article, the directors of the Corporation are bound to comply with and give immediate effect to such directions and instructions. Under Article 51-A, the President has the power to call for such returns, accounts and other information with respect to properties and activities of the Corporation as might be required from time to time. Under Article 40, subject to the provisions of the Companies Act and the directions and instructions issued from time to time by the President under Article 51, the business of the Corporation is to be managed by the Board of Directors. Under Article 14(*a*), subject to the provisions of Section 252 of the Companies Act, the President is to determine in writing from time to time the number of directors of the Corporation which, however, is not to be less than two or more than twelve and under Article 14(*b*), at every annual general meeting of the Corporation, every director appointed by the President is to retire but is eligible for re-appointment. Under Article 15(*a*), the President has the power at any time and from time to time to appoint any person as an additional director. Under Article 16, the President has the power to remove any director appointed by him from office at any time in his absolute discretion. Under Article 17, the vacancy in the office of a director appointed by the President caused by retirement, removal, resignation, death or otherwise, is to be filled by the President by fresh appointment. Article 18 provides that the directors are not required to hold any share qualification. Under Article 37, the President may from time to time appoint one of the directors to the office of the Chairman of the Board of Directors or to the office of the Managing Director or to both these offices for such time and at such remuneration as the President may think fit and the President may also from time to time remove the person or persons so appointed from service and appoint another or others in his or their place or places. Under Article 41, the Chairman of the Board has the power, on his own motion, and is bound, when requested by the Managing Director in writing, to reserve for the consideration of the President the matters relating to the working of the Corporation set out in the said article. Article 42 lists the matters in respect of which prior approval of the President is required to be obtained. Under Article 47, the auditor or auditors of the Corporation are to be appointed or re-appointed by the Central Government on the advice of the Comptroller and Auditor-General of India. The said article also confers power upon the Comptroller and Auditor-General of India to direct the manner in which the accounts of

the Corporation are to be audited and to give the auditors instructions in regard to any matter relating to the performance of their function. Under the said article, he has also the power to conduct a supplementary or test audit of the accounts of the Corporation by such person or persons as he may authorise in that behalf and for the purposes of such audit to require such information or additional information to be furnished to such person or persons on such matters by such person or persons as the Comptroller and Auditor-General may, by general or special order, direct.

5. Under clause (*v*) of the Memorandum of Association, the authorised share capital was rupees four crores. It was raised to rupees ten crores by a special resolution passed at the Annual General Meeting of the Corporation held on December 30, 1972, and further raised to rupees twenty crores by a special resolution passed at the Annual General Meeting held on November 5, 1979.

6. The above facts and the provisions aforementioned of the Memorandum of Association and the Articles of Association clearly show that not only is the Corporation a government company of which all the shares were and are owned by the Central Government and two State Governments but is a government company which is under the complete control and management of the Central Government.

7. A company called the "Rivers Steam Navigation Company Limited" was carrying on very much the same business including the maintenance and running of river service as the Corporation is doing. A Scheme of Arrangement was entered into between the said Company and the Corporation. The Calcutta High Court by its order dated May 5, 1967, approved the said Scheme of Arrangement and ordered the closure of the said Company and further directed that upon payment to all the creditors of the said Company, the said Company would stand dissolved without winding up by an order to be obtained from the High Court and accordingly, upon payment to all the creditors, the said Company was ordered to be dissolved. The said Scheme of Arrangement provided that the assets and certain liabilities of the said Company would be taken over by the Corporation. The said Scheme of Arrangement as approved by the High Court also provided as follows :

(*a*) That the new Company shall take as many of the existing staff or labour as possible and as can be reasonably taken over by the said transferee Company subject to any valid objection to any individual employee or employees.

(*b*) That as to exactly how many can be employed it is left to the said transferee Company's bona fide discretion.

(*c*) That those employees who cannot be taken over shall be paid by the transferor Company all moneys due to them under the law and all legitimate and legal compensations payable to them either under Industrial Disputes Act or otherwise legally admissible and that

such moneys shall be provided by the Government of India to the existing transferor Company who will pay these dues.

8. The first respondent in Civil Appeal 4412 of 1985, Brojo Nath Ganguly, was, at the date when the said Scheme of Arrangement became effective, working in the said Company and his services were taken over by the Corporation and he was appointed on September 8, 1967, as a Deputy Chief Accounts Officer. The first respondent in Civil Appeal 4413 of 1985, Tarun Kanti Sengupta, was also working in the said Company and his services were also taken over by the Corporation and he was appointed on September 8, 1967, as Chief Engineer on the ship "River Ganga". It is unnecessary to refer at this stage to the terms and conditions of the letters of appointment issued to these two respondents as they have been subsequently superseded by service rules framed by the Corporation except to state that under the said letters of appointment the age of superannuation was fifty-five years unless the Corporation agreed to retain them beyond this period. The said letters of appointment also provided that these respondents would be subject to the service rules and regulations including the conduct rules. Service rules were framed by the Corporation for the first time in 1970 and were replaced by new rules in 1979.

9. We are concerned in these appeals with the "Central Inland Water Transport Corporation Ltd. Service Discipline and Appeal Rules" of 1979 framed by the Corporation. These rules will hereinafter be referred to in short as "the said Rules". The said Rules apply to all employees in the service of the Corporation in all units in West Bengal, Bihar, Assam or in other State or Union Territory except those employees who are covered by the standing orders under the Industrial Employment (Standing Orders) Act, 1946, or those employees in respect of whom the Board of Directors has issued separate orders. Rule 9 of the said Rules deals with termination of employment for acts other than misdemeanour. The relevant provisions of the said Rule 9 relating to permanent employees are as follows :

> 9. *Termination of employment for Acts other than misdemeanour.*—(*i*) The employment of a permanent employee shall be subject to termination on three months' notice on either side. The notice shall be in writing on either side. The Company may pay the equivalent of three months' basic pay and dearness allowance, if any, in lieu of notice or may deduct a like amount when the employee has failed to give due notice.
>
> (*ii*) The services of a permanent employee can be terminated on the grounds of "services no longer required in the interest of the Company" without assigning any reason. A permanent employee whose services are terminated under this clause shall be paid 15 days' basic pay and dearness allowance for each completed year of continuous service in the Company as compensation. In addition he will be entitled to encashment of leave to his credit.

Under Rule 10, an employee is to retire on completion of the age of fifty-eight years though in exceptional cases and in the interest of the Corporation, an extension may be granted with the prior approval of the Chairman-cum-Managing Director and the Board of Directors. Rule 11 provides as follows :

> 11. *Resignation.*—Employees who wish to leave the Company's

services must give the Company the same notice as the Company is required to give them under Rule 9.

Rule 33 provides for suspension of an employee where a disciplinary proceeding against him is contemplated or is pending or where a case against him in respect of any criminal offence is under investigation or trial. Rule 34 provides for payment of subsistence allowance during the period of suspension. Rule 36 sets out the different penalties which can be imposed on an employee for his misconduct. These penalties are divided into minor and major penalties. Rule 37 is as follows :

> 37. *Acts of misconduct.*—Without prejudice to the general meaning of the term 'misconduct' the Company shall have the right to terminate the services of any employee at any time without any notice if the employee is found guilty of any insubordination, intemperance or other misconduct or of any breach of any rules pertaining to service or conduct or non-performance of his duties.

Rule 38 prescribes the procedure for imposing a major penalty and sets out in detail how a disciplinary inquiry is to be held. Rule 38 provides for action to be taken by the disciplinary authority on the report made by the Inquiring Authority. Rule 40 prescribes the procedure to be followed for imposing minor penalties. Rule 43 provides for a special procedure to be followed in certain cases. This special procedure consists of dispensing with a disciplinary inquiry altogether. The said Rule 43 provides as follows :

> 43. *Special procedure in certain cases.*—Notwithstanding anything contained in Rule 38, 39 or 40, the disciplinary authority may impose any of the penalties specified in Rule 36 in any of the following circumstances :
>
> (*i*) The employee has been convicted on a criminal charge, or on the strength of facts or conclusions arrived at by a judicial trial ; or
>
> (*ii*) where the disciplinary authority is satisfied for reasons to be recorded by it in writing that it is not reasonably practicable to hold an inquiry in the manner provided in these Rules ; or
>
> (*iii*) where the Board is satisfied that in the interest of the security of the Corporation/Company, it is not expedient to hold any inquiry in the manner provided in these Rules.

Rule 45 provides for an appeal against an order imposing penalty to the appropriate authority specified in the schedule to the said Rules and Rule 45-A provides for a review.

10. We are concerned in these appeals with the validity of clause (*i*) of Rule 9 only.

11. So far as Ganguly, the first respondent in Civil Appeal 4412 of 1985, is concerned, he was promoted to the post of Manager (Finance) in October 1980 and also acted as General Manager (Finance) from November 1981 to March 1982. On February 16, 1983, a confidential letter was sent to him by the General Manager (Finance), who is the third appellant in Civil Appeal 4412 of 1985, to reply within twenty-four hours to the allegation of negligence in the maintenance of provident fund accounts. Ganguly made a representation as also gave a detailed reply to the said show cause notice. Thereafter by a letter

dated February 26, 1983, signed by the Chairman-cum-Managing Director of the Corporation, a notice under clause (*i*) of Rule 9 of the said Rules was given to Ganguly terminating his service with the Corporation with immediate effect. Along with the said letter a cheque for three months' basic pay and dearness allowance was enclosed.

12. So far as Sengupta, the first respondent in Civil Appeal 4413 of 1985, is concerned, he was promoted to the post of General Manager (River Services) with effect from January 1, 1980. His name was enrolled by the Bureau of Public Enterprises and he was called for an interview for the post of Chairman-cum-Director of the Corporation by the Public Enterprises Selection Board. According to Sengupta, he could not appear before the Selection Board as he received the letter calling him for the interview after the date fixed in that behalf. According to Sengupta, the new Chairman-cum-Managing Director who was selected at the said interview bore a grudge against him for having competed against him for the said post and on February 1, 1983, he issued a charge-sheet against Sengupta intimating to him that a disciplinary inquiry was proposed to be held against him under the said Rules and calling upon him to file his written statement of defence. By his letter dated February 10, 1983, addressed to the Chairman-cum-Managing Director, Sengupta denied the charge made against him and asked for inspection of documents and copies of statements of witnesses mentioned in the said charge-sheet. By a letter dated February 26, 1983, signed by the Chairman-cum-Managing Director notice was given to Sengupta under clause (*i*) of Rule 9 of the said Rules, terminating his service with the Corporation with immediate effect. Along with the said letter a cheque for three months' basic pay and dearness allowance in lieu of notice was enclosed.

13. Both Ganguly and Sengupta filed writ petitions in the Calcutta High Court under Article 226 of the Constitution challenging the termination of their service as also the validity of the said Rule 9(*i*). In both these writ petitions ***rule nisi*** was issued and an *ex parte* ad interim order staying the operation of the said notice of termination was passed by a learned Single Judge of the High Court. The appellants before us went in letters patent appeal before a Division Bench of the said High Court against the said ad interim orders, the appeal in the case of Ganguly being FMAT No. 1604 of 1983 and in the case of Sengupta being FMAT No. 649 of 1983. On January 28, 1985, the Division Bench ordered in both these appeals that the said writ petitions should stand transferred to and heard by it along with the said appeals. The said appeals and writ petitions were thereupon heard together and by a common judgment delivered on August 9, 1985, the Division Bench held that the Corporation was a State within the meaning of Article 12 of the Constitution and that the said Rule 9(*i*) was ultra vires Article 14 of the Constitution. Consequently the Division Bench struck down the said Rule 9(*i*) as being void. It also quashed the impugned orders of termination dated February 26, 1983. It is against the said judgment and orders of the Calcutta High Court that the present appeals by special leave have been filed.

13-A. The contentions raised on behalf of the Corporation at the hearing of these appeals may be thus summarized :

(1) A government company stands on a wholly different footing from a statutory corporation for while a statutory corporation is established by a statute, a government company is incorporated like any other company by obtaining a certificate of incorporation under the Companies Act and, therefore, a government company cannot come within the scope of the term "the State" as defined in Article 12 of the Constitution.

(2) A statutory corporation is usually established in order to create a monopoly in the State in respect of a particular activity. A government company is, however, not established for this purpose.

(3) The Corporation does not have the monopoly of inland water transport but is only a trading company as is shown by the objects clause in its Memorandum of Association.

(4) Assuming a government company is "the State" within the meaning of Article 12, a contract of employment entered into by it is like any other contract entered into between two parties and a term in that contract cannot be struck down under Article 14 of the Constitution on the ground that it is arbitrary or unreasonable or unconscionable or onesided or unfair.

At the hearing of these appeals the Union of India, which is the second respondent in these appeals, joined in the contentions raised by the Corporation.

14. The arguments advanced on behalf of the contesting respondents in broad outlines were as follows :

(1) The definition of the expression "the State" given in Article 12 is wide enough to include within its scope and reach a government company.

(2) A State is entitled to carry on any activity, even a trading activity, through any of its instrumentalities or agencies, whether such instrumentality or agency be one of the departments of the government, a statutory corporation, a statutory authority or a government company incorporated under the Companies Act.

(3) Merely because a government company carries on a trading activity or is authorised to carry on a trading activity does not mean that it is excluded from the definition of the expression "the State" contained in Article 12.

(4) A government company being "the State"within the meaning of Article 12 is bound to act fairly and reasonably and if it does not do so, its action can be struck down under Article 14 as being arbitrary.

(5) A contract of employment stands on a different footing from other contracts. A term in a contract of employment entered into by a private employer which is unfair, unreasonable and unconscionable

is bad in law. Such a term in a contract of employment entered into by the State is, therefore, also bad in law and can be struck down under Article 14.

15. During the course of the hearing of these appeals the Central Inland Water Transport Corporation Officers' Association made an application for permission to intervene in these appeals and permission to intervene was granted to it by this Court. The said Association supported the stand taken by the contesting respondents.

16. We will now examine the correctness of the rival submissions advanced at the Bar.

17. The word "State" has different meanings depending upon the context in which it is used. In the sense of being a polity, it is defined in the Shorter Oxford English Dictionary, Third Edition, Volume II, page 2005, as :

> a body of people occupying a defined territory and organized under a sovereign government.

The same dictionary defines the expression "the State" as :

> the body politic as organized for supreme civil rule and government ; the political organization which is the basis of civil government ; hence, the supreme civil power and government vested in a country or nation.

According to Black's Law Dictionary, Fifth Edition, page 1262,

> In its largest sense, a 'State' is a body politic or a society of men.

According to Black, the term "State" may refer :

> either to the body politic of a nation (e.g. United States) or to an individual governmental unit of such nation (e.g. California).

In modern international practice, whether a community is deemed a State or not depends upon the general recognition accorded to it by the existing group of other States. A State must have a relatively permanent legal organization, determining its structure and the relative powers of its major governing bodies or organs. This legal organizational permanence of a Stage is to be found in its Constitution. With rare exceptions, such as the United Kingdom, most States now have a written Constitution. The constitutional structure of a State may be either unitary, as when it has a single system of government applicable to all its parts, or federal when it has one system of government operating in certain respects and in certain matters in all its parts and also separate governments operating in other respects in distinct parts of the whole. In such a case the units or sub-divisions having separate governments are variously called 'states' as in India, USA and Australia, 'provinces' as in Canada, 'cantons' as in Switzerland, or designated by other names.

18. Our Constitution is federal in structure. Clause (1) of Article 1 of the Constitution provides that "India, that is Bharat, shall be a Union of States" and clause (2) of that article provides that "The States and the territories thereof shall be as specified in the First Schedule". The word "States" used in Article 1 thus refers to the federating units, India itself being a State consisting of these units. The term "States" is defined variously in some of the other

articles of the Constitution as the context of the particular Part of the Constitution in which it is used requires. Part VI of the Constitution is headed "The States" and provides for the form of the three organs of a State, namely, the Executive, the Legislature and the Judiciary. Article 152,which is the opening Article in Part VI of the Constitution, provides as follows :

> 152. *Definition.*—In this Part, unless the context otherwise requires, the expression 'State' does not include the State of Jammu and Kashmir.

The State of Jammu and Kashmir is excluded because that State, though one of the States which constitute the Union of India, had, in pursuance of the provisions of Article 370 of the Constitution read with the Constitution (Application to Jammu and Kashmir) Order, 1954 (C O 48), set up a Constituent Assembly for the internal Constitution of the State and it had framed the Constitution of Jammu and Kashmir which was adopted and enacted by that Constituent Assembly on November 17, 1965. Article 152 also, therefore, uses the expression "State" as meaning the federating units which constitute the Union of India. Part XIV of the Constitution deals with services under the Union and the States. Article 308 provides as follows :

> 308. *Interpretation.*—In this Part, unless the context otherwise requires, the expression 'State' does not include the State of Jammu and Kashmir.

This definition read with the other provisions of Part XIV shows that the word "State" applies to the federating units (other than the State of Jammu and Kashmir for the reason mentioned above) which together constitute the Union of India because in the other articles of Part XIV wherever the Union of India is referred to, it is described as "the Union". Article 366 of the Constitution defines certain expressions used in the Constitution of India. That article, however, does not contain any definition of the term "State". Under Article 367(1), unless the context otherwise requires, the General Clauses Act, 1897 (Act 10 of 1897), subject to any adaptations and modifications that may be made therein by the President of India under Article 372 to bring that Act into accord with the provisions of the Constitution, applies for the interpretation of the Constitution. Clause (58) of Section 3 of the General Clauses Act defines the term 'State" as follows :

> (58) *'State'.*—(*a*) as respect any period before the commencement of the Constitution (Seventh Amendment) Act, 1956, shall mean a Part A State, a Part B State or a Part C State; and
>
> (*b*) as respects any period after such commencement, shall mean a State specified in the First Schedule to the Constitution and shall include a Union Territory.

This definition, therefore, also confines the term "State" to the federating units which together form the Union of India.

18-A. We are concerned in these appeals with Article 12. Article 12 forms part of Part III of the Cons itution which deals with Fundamental Rights and provides as follows :

> 12. *Definition.*—In this Part, unless the context otherwise requires,

> 'the State' *includes* the Government and Parliament of India and the Government and the Legislature of each of the States and all local or other authorities within the territory of India or under the control of the Government of India. (emphasis supplied)

The same definition applies to the expression "the State" when used in Part IV of the Constitution which provides for the Directive Principles of State Policy, for the opening Article of Part IV, namely, Article 36, provides :

> 36. *Definition.*—In this Part, unless the context otherwise requires, 'the State' has the same meaning as in Part III.

The expression "local authority" is defined in clause (31) of Section 3 of the General Clauses Act as follows :

> (31) 'local authority' shall mean a municipal committee, district board, body of port commissioners or other authority legally entitled to, or entrusted by the government with, the control or management of a municipal or local fund.

19. Thus, the expression "the State" when used in Parts III and IV of the Constitution is not confined to only the federating States or the Union of India or even to both. By the express terms of Article 12 the expression "the State" includes—

(1) the Government of India,
(2) Parliament of India,
(3) the government of each of the States which constitute the Union of India,
(4) the legislature of each of the States which constitute the Union of India,
(5) all local authorities within the territory of India,
(6) all local authorities under the control of the Government of India,
(7) all other authorities within the territory of India, and
(8) all other authorities under the control of the Government of India.

20. There are three aspects of Article 12 which require to be particularly noticed. These aspects are :

(*i*) the definition given in Article 12 is not an explanatory and restrictive definition but an extensive definition,
(*ii*) it is the definition of the expression "the State " and not of the term "State" or "States", and
(*iii*) it is inserted in the Constitution for the purposes of Parts III and IV thereof.

21. As pointed out in Craies on *Statute Law*, Seventh Edition, page 213, where an interpretation clause defines a word to *mean* a particular thing, the definition is explanatory and prima facie restrictive ; and whenever an interpretation clause defines a term to *include* something, the definition is extensive. While an explanatory and restrictive definition confines the meaning of the word defined to what is stated in the interpretation clause, so that wherever the word defined is used in the particular statute in which that interpretation

clause occurs, it will bear only that meaning unless where, as is usually provided, the subject or context otherwise requires, an extensive definition expands or extends the meaning of the word defined to include within it what would otherwise not have been comprehended in it when the word defined is used in its ordinary sense. Article 12 uses the word "includes". It thus extends the meaning of the expression "the State" so as to include within it also what otherwise may not have been comprehended by that expression when used in its ordinary legal sense.

22. Article 12 defines the expression "the State" while the other articles of the Constitution referred to above, such as Article 152 and Article 308, and clause (58) of Section 3 of the General Clauses Act define the term "State". The deliberate use of the expression "the State" in Article 12 as also in Article 36 would have normally shown that this expression was used to denote the State in its ordinary and constitutional sense of an independent or sovereign State and the inclusive clause in Article 12 would have extended this meaning to include within its scope whatever has been expressly set out in Article 12. The definition of the expression "the State" in Article 12 is, however, for the purposes of Parts III and IV of the Constitution. The contents of these two Parts clearly show that the expression "the State" in Article 12 as also in Article 36 is not confined to its ordinary and constitutional sense as extended by the inclusive portion of Article 12 but is used in the concept of the State in relation to the Fundamental Rights guaranteed by Part III of the Constitution and the Directive Principles of State Policy contained in Part IV of the Constitution which principles are declared by Article 37 to be fundamental to the governance of the country and enjoins upon the State to apply in making laws.

23. What then does the expression "the State" in the context of Parts III and IV of the Constitution mean ?

24. Men's concept of the State as a polity or a political unit or entity and what the functions of the State are or should be have changed over the years and particularly in the course of this century. A man cannot obstinately cling to the same ideas and concepts all his life. As Emerson said in his essay on "*Self-Reliance*" : "A foolish consistency is the hobgoblin of little minds". Man is by nature ever restless, ever discontent, ever seeking something new, ever dissatisfied with what he has. This inherent trait in the nature of man is reflected in the society in which he lives for a society is a conglomerate of men who live in it. Just as man by nature is dissatisfied, so is society. Just as man seeks something new, ever hoping that a change will bring about something better, so does society. Old values, old idcologies and old systems are thus replaced by new ideologies, a new set of values and a new system ; they in their turn to be replaced by different ideologies, different values and a different system. The ideas that seem revolutionary become outmoded with the passage of time and the heresies of today become the dogmas of tomorrow. What proves to be adequate and suited to the needs of a society at a given time and

in particular circumstances turns out to be wholly unsuited and inadequate in different times and under different circumstances.

25. The story of mankind is punctuated by progress and retrogression. Empires have risen and crashed into the dust of history. Civilizations have flourished, reached their peak and passed away. In the year 1625, Carew, C.J., while delivering the opinion of the House of Lords in *Re the Earldom of Oxford*[1], in a dispute relating to the descent of that Earldom, said :

> .....and yet time hath his revolution, there must be a period and an end of all temporal things, *finis rerum*, an end of names and dignities, and whatsoever is terrene .....

The cycle of change and experiment, rise and fall, growth and decay, and of progress and retrogression recurs endlessly in the history of man and the history of civilization. T. S. Eliot in the First Chorus from "*The Rock*" said :

> O perpetual revolution of configured stars,
> O perpetual recurrence of determined seasons,
> O world of spring and autumn, birth and dying ;
> The endless cycle of idea and action,
> Endless invention, endless experiment.

26. The law exists to serve the needs of the society which is governed by it. If the law is to play its allotted role of serving the needs of the society, it must reflect the ideas and ideologies of that society. It must keep time with the heartbeats of the society and with the needs and aspirations of the people. As the society changes, the law cannot remain immutable. The early nineteenth century essayist and wit, Sydney Smith, said : "When I hear any man talk of an unalterable law, I am convinced that he is an unalterable fool." The law must, therefore, in a changing society march in tune with the changed ideas and ideologies. Legislatures are, however, not best fitted for the role of adapting the law to the necessities of the time, for the legislative process is too slow and the legislatures often divided by politics, slowed down by periodic elections and overburdened with myriad other legislative activities. A constitutional document is even less suited to this task, for the philosophy and the ideologies underlying it must of necessity be expressed in broad and general terms and the process of amending a Constitution is too cumbersome and time-consuming to meet the immediate needs. This task must, therefore, of necessity fall upon the courts because the courts can by the process of judicial interpretation adapt the law to suit the needs of the society.

27. A large number of authorities were cited before us to show how the courts have interpreted the expression, "the State" in Article 12. As these authorities are decisions of this Court, we must perforce go through the whole gamut of them though we may preface an examination of these authorities with the observation that they only serve to show how the concepts of this Court have changed both with respect to Article 12 and Article 14 to keep pace with

1 (1625) W Jo 96, 101 : (1626) 82 ER 50, 53

changing ideas and altered circumstances. Before embarking upon this task we would, however, like to quote the following passage (which has become a classic) from the opening paragraph of Justice Oliver Wendell Holmes's "*The Common Law*" which contains the lectures delivered by him while teaching law at Harvard and which book was published in 1981 just one year before he was appointed an Associate Justice of the Massachusetts Supreme Judicial Court :

> It is something to show that the consistency of a system requires a particular result, but it is not all. The life of the law has not been logic : it has been experience. The felt necessities of the time, the prevalent moral and political theories, intuitions of public policy, avowed or unconscious, even the prejudices which judges share with their fellow-men, have had a good deal more to do than the syllogism in determining the rules by which men should be governed. The law embodies the story of a nation's development through many centuries, and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics. In order to know what it is, we must know what it has been, and what it tends to become. We must alternately consult history and existing theories of legislation. But the most difficult labour will be to understand the combination of the two into new products at every stage. The substance of the law at any given time pretty nearly corresponds, so far as it goes, with what is then understood to be convenient ; but its form and machinery, and the degree to which it is able to work out desired results, depend very much upon its past.

28. We will, therefore, briefly sketch the temper of the times in which our Constitution was enacted and the purposes for which Parts III and IV inserted in our Constitution.

29. The bombs which had rained down upon the cities of Europe, Africa and Asia and the Islands in the Pacific had changed, and changed dramatically, not only the political but also the sociological, ideological and economic map of the world. A world reeling from the horrors of the Second World War and seeking to recover from the trauma caused by its atrocities sought to band all nations into one Family of Man and for this purpose set up the United Nations Organization in order to save succeeding generations from the scourge of war which had twice in this century brought untold sorrow to mankind and in order to reaffirm faith in fundamental human rights, in the dignity and worth of the human person and in the equal rights of man and woman and of nations large or small, and thus to give concrete shape to the dream of philosophers and poets that the war-drums would throb no longer and the battle-banners would be furled in the Parliament of Man and the Federation of the World. But much had gone before. There was the signing of the Inter-Allied Declaration of June 12, 1941, at St. James' Palace in London by the representatives of the United Kingdom, the Commonwealth, General de Gaulle and the governments in exile of the European countries conquered by Nazi Germany ; there was the Atlantic Charter of August 14, 1941 ; there was the Declaration of the United Nations signed on New Year's Day of 1942 at Washington, D. C., by twenty-six nations who were fighting the Axis ; there

was the Declaration made at the Moscow Conference in October 1943 and at the Teheran Conference on December 1, 1943 ; there was the Dumbarton Oaks Conference held in Washington, DC, in August and September 1944 ; there was the Yalta Conference in February 1945 ; all these culminating in the adoption on June 25, 1945, of the Charter of the United Nations in the Opera House of San Francisco and the affixing of signatures thereon the next day in the auditorium of the Veterans' Memorial Hall. Thereafter, in pursuance of Article 68 of the Charter of the United States, the Economic and Social Council set up the Human Rights Commission in 1946. This Commission began its work in January 1947 under the chairmanship of Mrs Eleanor Roosevelt, the widow of President Franklin D. Roosevelt. The Universal Declaration of Human Rights prepared by the Commission was adopted by the General Assembly on December 10, 1948, at its session held in the Palais de Chaillot in Paris. Of the fifty-eight nations represented at that session, none voted against it, two were absent, and eight abstained from voting.

30. It was thus in an atmosphere surcharged with human suffering and yet a firm resolve not to succumb to it that the Constituent Assembly which was set up to frame the Constitution of India embarked upon its task on December 9, 1946, reassembled after the midnight of August 14, 1947, as the sovereign Constituent Assembly for India. After Partition and fresh elections in the new Provinces of West Bengal and East Punjab, it reassembled on October 31, 1947, and thereafter on November 26, 1949, adopted and enacted the Constitution of India.

31. Before commencing its work, the Constituent Assembly adopted a Resolution laying down its objectives :

> 1. This Constituent Assembly declares its firm and solemn resolve to proclaim India as an Independent Sovereign Republic and to draw up for her future governance a Constitution ; . . .
>
> * * *
>
> 4. Wherein all power and authority of the Sovereign Independent India, its constituent parts and organs of government, are derived from the people ; and
> 5. Wherein shall be guaranteed and secured to all the people of India justice, social, economic and political : equality of status, of opportunity, and before the law ; freedom of thought, expression, belief, faith, worship, vocation, association, and action, subject to law and public morality ; and
> 6. Wherein adequate safeguards shall be provided for minorities, backward and tribal areas, and depressed and other backward classes ; and
> 7. Whereby shall be maintained the integrity of the territory of the Republic and its sovereign rights on land, sea, and air according to justice and the law of civilised nations ; and
> 8. This ancient land attains its rightful and honoured place in the world

and makes its full and willing contribution to the promotion of world peace and the welfare of mankind.

32. In its strict legal sense the written Constitution of a country is a document which defines the regular form or system of its government, containing the rules that directly or indirectly affect the distribution or exercise of the sovereign power of the State and it is thus mainly concerned with the creation of the three orgns of the State—the executive, the legislature and the judiciary, and the distribution of governmental power among them and the definition of their mutual relation (see *Sankari Prasad Singh Deo* v. *Union of India and State of Bihar*[2] ; O. Hood Phillips' "*Constitutional and Administrative Law*", Sixth Edition, page 11 ; Dicey's "*An Introduction to the Study of the Law of the Constitution*", Tenth Edition, page 23 ; and Jowitt's *Dictionary of English Law*, Second Edition, Volume I, page 430).

33. The framers of our Constitution did not, however, want to frame for the Sovereign Democratic Republic which was to emerge from their labours a Constitution in the strict legal sense. They were aware that there were other Constitutions which had given expression to certain ideals as the goal towards which the country should strive and which had defined the principles considered fundamental to the governance of the country. They were aware of the events that had culminated in the Charter of the United Nations. They were aware that the Universal Declaration of Human Rights had been adopted by the General Assembly of the United Nations, for India was a signatory to it. They were aware that the Universal Declaration of Human Rights contained certain basic and fundamental rights appertaining to all men. They were aware that these rights were born of the philosophical speculations of the Greek and Roman Stoics and nurtured by the jurists of ancient Rome. They were aware that these rights had found expression in a limited form in the accords entered into between the rulers and their powerful nobles, as for instance, the accord of 1188 entered into between King Alfonso IX and the Cortes of Leon, the Magna Carta of 1215 wrested from King John of England by his barons on the Meadow of Runnymede and to which he was compelled to affix his Great Seal on a small island in the Thames in Buckinghamshire—still called Magna Carta Island, and the guarantees which King Andrew II of Hungary was forced to give by his Golden Bull of 1822. They were aware of the international treaties of the midseventeenth century for safeguarding the right of religious freedom and the rights of aliens. They were aware of the full blossoming of the concept of Human Rights in the writings of the "philosophes" such as Voltaire, Rousseau, Diderot, Rayal, d'Alembert and others, and of the concrete expression given to it in the various Declarations of Rights of the American Colonies (particularly Virginia) and in the American Declaration of Independence. They were aware that in 1789, during the early years of the French Revolution, the French National Assembly had in "The Declaration of the Rights of Man and

2. 1952 SCR 89, 106 : AIR 1951 SC 458

of the Citizen" proclaimed these rights in lofty words and that Revolutionary France had translated them into practice with bloody deeds. They were aware of the treaties entered into between various States in the nineteenth century providing protection for religious and other minorities. They were aware that these rights had at last found universal recognition in the Universal Declaration of Human Rights. They were aware that the first ten amendments to the Constitution of the United States of America contained certain rights akin to Human Rights. They knew that the Constitution of Eire contained a chapter headed "Fundamental Rights"and another headed "Directive Principles of State Policy". They were aware that the Constitution of Japan also contained a chapter headed "Rights and Duties of the People". They were aware that the major traditional functions of the State have been the defence of its territory and its inhabitants against external aggression, the maintenance of law and order, the administration of justice, the levying of taxes and the collection of revenue. They were also aware that increasingly, and particularly in modern times, several States have assumed numerous and wide-ranging functions, especially in the fields of education, health, social security, control and maintenance of natural resources and natural assets, transport and communication services, and operation of certain industries considered basic to the economy and growth of the nation. They were also aware that Section 8 of Article 1 of the Constitution of the United States of America contained "a welfare clause" empowering the federal government to enact laws for the overall general welfare of the people. They were aware that countries such as the United States, the United Kingdom and Germany had passed social welfare legislation.

34. The framers of our Constitution were men of vision and ideals, and many of them had suffered in the cause of freedom. They wanted an idealistic and philosophic base upon which to raise the administrative superstructure of the Constitution. They, therefore, headed our Constitution with a preamble which declared India's goal and inserted Parts III and IV in the Constitution.

35. The Preamble to the Constitution, as amended by the Constitution (Forty-second Amendment) Act, 1976, proudly proclaims :

> WE, THE PEOPLE OF INDIA, having solemnly resolved to constitute India into a SOVEREIGN SOCIALIST SECULAR DEMOCRATIC REPUBLIC and to secure to all its citizens :
>
> JUSTICE, social, economic and political ;
>
> LIBERTY of thought, expression, belief, faith and worship ,
>
> EQUALITY of status and of opportunity ; and to promote among them all
>
> FRATERNITY assuring the dignity of the individual and the unity and integrity of the Nation ;
>
> IN OUR CONSTITUENT ASSEMBLY this twenty-sixth day of November, 1949, do HEREBY ADOPT, ENACT AND GIVE TO OURSELVES THIS CONSTITUTION.

36. Part III of the Constitution gives a constitutional mandate for certain Human Rights—called Fundamental Rights in the Constitution—adapted to the needs and requirement of a country only recently freed from foreign rule and desirous of forging a strong and powerful nation capable of taking an equal place among the nations of the world. It also provides a constitutional mode of enforcing them. Amongst these Rights is the one contained in Article 14 which provides :

> 14. *Equality before law.*—The State shall not deny to any person equality before the law or the equal protection of the laws within the territory of India.

37. Part IV of the Constitution prescribes the Directive Principles of State Policy. These Directive Principles have not received the same constitutional mandate for their enforcement as the Fundamental Rights have done. In the context of the Welfare State which is the goal of our Constitution, Articles 37 and 38(1) are important. They are as follows :

> 37. *Application of the principles contained in this Part.*—The provisions contained in this Part shall not be enforceable by any court, but the principles therein laid down are nevertheless fundamental in the governance of the country and it shall be the duty of the State to apply these principles in making laws.
>
> 38. *State to secure a social order for the promotion of welfare of the people.*—(1) The State shall strive to promote the welfare of the people by securing and protecting as effectively as it may a social order in which justice, social, economic and political, shall inform all the institutions of the national life.

Under clause (*a*) of Article 39, the State is, in particular, to direct its policy towards securing that the citizens, men and women equally, have the right to an adequate means of livelihood. Article 41 directs that the State shall, within the limits of its economic capacity and development, make effective provision for securing the right to work.

38. The difference between Part III and Part IV is that while Part III prohibits the State from doing certain things (namely, from infringing any of the Fundamental Rights), Part IV enjoins upon the State to do certain things. This duty, however, is not enforceable in law but nonetheless the court cannot ignore what has been enjoined upon the State by Part IV, and though the court may not be able actively to enforce the Directive Principles of State Policy by compelling the State to apply them in the governance of the country or in the making of laws, the court can, if the State commits a breach of its duty by acting contrary to these Directive Principles, prevent it from doing so.

39. In the working of the Constitution it was found that some of the provisions of the Constitution were not adequate for the needs of the country or for ushering in a Welfare State and the constituent body empowered in that behalf amended the Constitution several times. By the very first amendment made in the Constitution, namely, by the Constitution (First Amendment)

Act, 1951, clause (6) of Article 19 was amended with retrospective effect. Under this amendment, sub-clause (*g*) of clause (1) of Article 19 which guarantees to all citizens the right to carry on any occupation, trade or business, was not to prevent the State from making any law relating to the carrying on by the State, or by a corporation owned or controlled by the State, of any trade, business, industry or service, whether to the exclusion, complete or partial, of citizens or otherwise. This amendment also validated the operation of all existing laws insofar as they had made similar provisions. Article 298, as originally enacted, provided that the executive power of the Union and of each State was to extend, subject to any law made by the appropriate legislature, to the grant, sale, disposition or mortgage of any property held for the purposes of the Union or of such State, as the case may be, and to the purchase or acquisition of property for those purposes respectively, and to the making of contracts ; and it further provided that all property acquired for the purposes of the Union or of a State was to vest in the Union or in such State, as the case may be. Article 298 was substituted by the Constitution (Seventh Amendment) Act, 1956. As substituted, it provides as follows :

> 298. *Power to carry on trade, etc.*—The executive power of the Union and of each State shall extend to the carrying on of any trade or business and to the acquisition, holding and disposal of property and the making of contracts for any purpose :
>
> Provided that—
>
> (*a*) the said executive power of the Union shall, insofar as such trade or business or such purpose is not one with respect to which Parliament may make laws, be subject in each State to legislation by the State ; and
>
> (*b*) the said executive power of each State shall, insofar as such trade or business or such purpose is not one with respect to which the State legislature may make laws, be subject to legislation by Parliament.

Article 298, as so substituted, therefore, expands the executive power of the Union of India and of each of the States which collectively constitute the Union to carry on any trade or business. By extending the executive power of the Union and of each of the States to the carrying on of any trade or business, Article 298 does not, however, convert either the Union of India or any of the States which collectively form the Union into a merchant buying and selling goods or carrying on either trading or business activity, for the executive power of the Union and of the States, whether in the field of trade or business or in any other field, is always subject to constitutional limitations and particularly the provisions relating to Fundamental Rights in Part III of the Constitution and is exercisable in accordance with and for the furtherance of the Directive Principles of State Policy prescribed by Part IV of the Constitution.

40. The State is an abstract entity and it can, therefore, only act through its agencies or instrumentalities, whether such agency or instrumentality be human or juristic. The trading and business activities of the State constitute

"public enterprise". The structural forms in which the government operates in the field of public enterprise are many and varied. These may consist of government departments, statutory bodies, statutory corporations, government companies, etc. In this context, we can do no better than cite the following passage from "*Government Enterprise — A Comparative Study*" by W. Friedmann and J. F. Garner, at page 507 :

> The variety of forms in which the various States have, at different times, proceeded to establish public enterprises is almost infinite, but three main types emerge to which almost every public enterprise approximates : (1) departmental administration ; (2) the joint stock company controlled completely or partly by public authority ; and finally (3) the public corporation proper, as a distinct type of corporation different from the private law company. Each of these three types will be briefly analysed in a comparative perspective.
>
> As the tasks of government multiplied, as a result of defence needs, post-war crises, economic depressions and new social demands, the framework of civil service administration became increasingly insufficient for the handling of the new tasks which were often of a specialised and highly technical character. At the same time, 'bureaucracy' came under a cloud. In Great Britain the late Lord Hewart had written of 'the new despotism" and Dr. C. K. Allen of 'bureaucracy triumphant'. In France the *Confederation Generale du Travail* (CGT) had stated in its Programme in 1920 that 'We do not wish to increase the functions of the State itself nor strengthen a system which would subject the basic industry to a civil service regime, with all its lack of responsibility and its basic defects, a process which would subject the forces of production to a fiscal monopoly. . . . ' This distrust of government by civil service, justified or not, was a powerful factor, in the development of a policy of public administration through separate corporations which would operate largely according to business principles and be separately accountable. In the common law countries, where the government still enjoys considerable immunities and privileges in the fields of legal responsibility, taxation, or the binding force of statutes, other considerations played their part. It seemed necessary to create bodies which, if they were to compete on fair terms in the economic field, had to be separated and distinct from the government as regards immunities and privileges.

41. The immunities and privileges possessed by bodies so set up by the Government in India cannot, however, be the same as those possessed by similar bodies established in the private sector because the setting up of such bodies is referable to the executive power of the government under Article 298 to carry on any trade or business. As pointed out by Mathew, J. in *Sukhdev Singh* v. *Bhagatram Sardar Singh Raghuvanshi*[3] (at page 648 of the Reports : SCC p. 452, para 93) : "The governing power wherever located must be subject to the fundamental constitutional limitations." The privileges and immunities of these bodies, therefore, are subject to Fundamental Rights and exercisable in accordance with and in furtherance of the Directive Principles of State Policy.

3. (1975) 3 SCR 619 (1975) 1 SCC 421 : 1975 SCC (L & S) 101 AIR 1975 SC 1331

42. It is in the context of what has been stated above that we will now review the authorities cited at the Bar. When we consider these authorities, we will see how as constitutional thinking developed and the conceptual horizon widened, new vistas, till then shrouded in the mist of conventional legal phraseology and traditional orthodoxy, opened out to the eye of judicial interpretation, and many different facets of several articles of the Constitution, including Articles 12 and 14, hitherto unperceived, became visible. There, however, still remain vistas yet to be opened up, veils beyond which we today cannot see to be lifted, and doors to which we still have found no key to be unlocked.

43. In *Rai Sahib Ram Jawaya Kapur* v. *State of Punjab*[4] the State of Punjab, which used to select books published by private publishers for prescribing them as text-books and for this purpose used to invite offers from publishers and authors, altered that practice and amended the notification in that behalf so that thereafter only authors were asked to submit their books for approval as text-books. The validity of this notification was challenged inter alia on the ground that the executive power of a State under Article 162 extended only to executing the laws passed by the legislature or supervising the enforcement of such law. Under Article 162, subject to the provisions of the Constitution, the executive power of a State extends to the matters with respect to which the legislature of the State has power to make laws, namely, the matters enumerated in the State List (List II) in the Seventh Schedule to the Constitution. Under the proviso to that article, in any matter with respect to which the legislature of a State and Parliament have power to make laws, that is, the matters enumerated in the Concurrent List (List III) in the Seventh Schedule to the Constitution, the executive power of the State is to be subject to, and limited by, the executive power expressly conferred by the Constitution or by any law made by Parliament upon the Union or authorities thereof. Under Article 154(1), the executive power of the State is vested in the Governor and is to be exercised by him either directly or through officers subordinate to him in accordance with the Constitution. The corresponding provisions as regards the executive power of the Union of India are contained in Article 73 and Article 53(1). Repelling the above contention, Mukherjea, C.J., who spoke for the Constitution Bench of the Court observed (at page 230) :

> A modern State is certainly expected to engage in all activities necessary for the promotion of the social and economic welfare of the community.

The following passage (at pages 235-36) from the judgment of the Court in that case with respect to the meaning of the expression "executive function" is instructive and requires to be reproduced :

> It may not be possible to frame an exhaustive definition of what executive function means and implies. Ordinarily the executive power connotes the residue of governmental functions that remain after legislative and judicial functions are taken away. The Indian Constitution has not

4. (1955) 2 SCR 225 . AIR 1955 SC 549

> indeed recognised the doctrine of separation of powers in its absolute rigidity but the functions of the different parts or branches of the government have been sufficiently differentiated and consequently it can very well be said that our Constitution does not contemplate assumption, by one organ or part of the State, of functions that essentially belong to another. The executive indeed can exercise the powers of departmental or subordinate legislation when such powers are delegated to it by the legislature. It can also, when so empowered, exercise judicial functions in a limited way. The executive government, however, can never go against the provisions of the Constitution or of any law. This is clear from the provisions of Article 154 of the Constitution but, as we have already stated, *it does not follow from this that in order to enable the executive to function there must be a law already in existence and that the powers of the executive are limited merely to the carrying out of these laws.* (emphasis supplied.)

44. In *Rajasthan State Electricity Board, Jaipur* v. *Mohan Lal*[5] a Constitution Bench of this Court by a majority held that the Electricity Board of Rajasthan constituted under the Electricity (Supply) Act, 1948 (Act 54 of 1948) was "the State" as defined in Article 12 because it was "other authority" within the meaning of that article. The court held that the expression "other authority" was wide enough to include within it every authority created by a statute, on which powers are conferred to carry out governmental or quasi governmental functions and functioning within the territory of India or under the control of the Government of India and the fact that some of the powers conferred may be for the purpose of carrying on commercial activities is not at all material because under Articles 19(1)(*g*) and 298 even the State is empowerd to carry on any trade or business. The court further held that in interpreting the expression "other authority" the principle of ejusdem generis should not be applied, because, for the application of that rule, there must be distinct genus or category running through the bodies previously named ; and the bodies specially named in Article 12 being the executive government of the Union and the States, the legislatures of the Union and the States and local authorities, there is no common genus running through these named bodies, nor could these bodies be placed in one single category on any rational basis.

45. *Praga Tools Corpn.* v. *C.A. Imanual*[6] was a case heavily relied upon by the appellants. Praga Tools Corporation was a company incorporated under the Companies Act, 1913, and therefore, a company within the meaning of the Companies Act, 1956. At the material time the Union of India held fifty-six per cent of the shares of the company and the Government of Andhra Pradesh held thirty-two per cent of its shares, the balance of twelve per cent shares being held by private individuals. As being the largest shareholder, the Union of India had the power to nominate the company's directors. The company had entered into two settlements with its workmen's union. These

5. (1967) 3 SCR 377 : AIR 1967 SC 1857 : (1968) 1 LLJ 257
6. (1969) 3 SCR 773 : (1969) 1 SCC 585 : AIR 1969 SC 1306

settlements were arrived at and recorded in the presence of the Commissioner of Labour. Subsequently, the company entered into another agreement with the union, the effect of which was to enable the company, notwithstanding the earlier two settlements, to retrench ninety-two of its workmen. Some of the affected workmen thereupon filed a writ petition under Article 226 of the Constitution in the Andhra Pradesh High Court challenging the validity of the subsequent agreement. A learned Single Judge of the High Court dismissed the petition on merits. In appeal, a Division Bench of that High Court held that the company being one registered under the Companies Act and not having any statutory duty or function to perform was not one against which a writ for mandamus or any other writ could lie. The Division Bench, however, held that though the writ petition was not maintainable the High Court could grant a declaration in favour of the petitioners that the impugned agreement was illegal and void and granted the said declaration. In appeal by the company, a two-Judge Bench of this Court held that the company being a non-statutory body and one incorporated under the Companies Act there was neither a statutory nor a public duty imposed on it by a statute in respect of which enforcement could be sought by means of a *mandamus*. So far as declaration given by the Division Bench of the High Court was concerned, the Court held (at page 780) : (SCC pp. 590-91, para 9)

> In our view once the writ petition was held to be misconceived on the ground that it could not lie against a company which was neither a statutory company nor one having public duties or responsibilities imposed on it by a statute, no relief by way of a declaration as to invalidity of an impugned agreement between it and its employees could be granted. The High Court in these circumstances ought to have left the workmen to resort to the remedy available to them under the Industrial Disputes Act by raising an industrial dispute thereunder.

Though this case was strongly relied upon by the appellants, we fail to see how it is relevant to the submissions advanced by the appellants. The subsequent agreement enabling the company to retrench some of its workmen was challenged on the ground that it was in breach of the earlier settlements entered into between the company and the workmen's union. No question of violation of any of the Fundamental Rights was at all raised in that case. The only question which fell for determination was whether a writ of mandamus can issue to compel the performance of the earlier settlements or to restrain the enforcement of the impugned subsequent agreement and the dispute, therefore, was one which fell within the scope of the Industrial Disputes Act, 1947 (Act 14 of 1947).

46. In *State of Bihar* v. *Union of India*[7] the State of Bihar filed nine suits under Article 131 in connection with the delayed delivery of iron and steel materials for the construction work of the Gandak project. In all these suits the first defendant was the Union of India while the second defendant in six of these suits was the Hindustan Steel Ltd. and in the remaining three,

7. (1970) 2 SCR 522 : (1970) 1 SCC 67 : AIR 1970 SC 1446

the Indian Iron and Steel Company Ltd. This Court held that the specification of the parties in Article 131 was not of an extensive kind and excluded the idea of a private citizen, a firm or a corporation figuring as a disputant either alone or even along with a State or with the Government of India in the category of a party to the dispute under Article 131. The Court further held that the enlarged definition of the expression "the State" given in Parts III and IV of the Constitution did not apply to Article 131 and, therefore, a body like the Hindustan Steel Ltd. could not be considered as "a State" for the purpose of Article 131. We fail to see in what way this decision is at all relevent to the point. The question before the court in that case was whether the Hindustan Steel Ltd. or the Indian Iron and Steel Company Ltd. was a State to enable a suit to be filed against it under Article 131 and not whether either of these companies fell within the scope of the definition of the expression "the State" in Article 12.

47. Another authority relied upon by the appellants was *S. L. Agarwal* v. *General Manager, Hindustan Steel Ltd.*[8]. The facts of that case and the contentions raised thereunder show that this authority is equally irrelevant. In that case an employee of the Hindustan Steel Ltd., whose services were terminated, filed a petition under Article 226 claiming that such termination was wrongful as it was really by way of punishment as the provisions of Article 311(2) of the Constitution had not been complied with. This Court held that the protection of clause (2) of Article 311 was available only to the categories of persons mentioned in that clause and that though the appellant held a civil post as opposed to a military post, it was not a civil post under the Union or a State and, therefore, he could not claim the protection of Article 311(2). The contention which was raised on behalf of the appellant was that as Hindustan Steel Ltd. was entirely financed by the government and its management was directly the responsibility of the government, the post was virtually under the Government of India. This contention was rejected by the court holding that the company had its independent existence and by law relating to corporations it was distinct from its members and, therefore, it was not a department of the government nor were its employees servants holding posts under the Union. No question arose in that case whether the company was "the State" within the meaning of Article 12 and all that was sought to be contended was that it was a department of the government.

48. In *Sabhajit Tewary* v. *Union of India*[9] this Court held that the Council of Scientific and Industrial Research which was a society registered under the Societies Registration Act was not an authority within the meaning of Article 12 and, therefore, certain letters written by it to the petitioner with respect to his remuneration could not be challenged as being discriminatory and violative of Article 14. The contention raised in that case was that the

8. (1970) 3 SCR 363 : (1970) 1 SCC 177 : AIR 1970 SC 1150
9. (1975) 3 SCR 616 : (1975) 1 SCC 485 : 1975 SCC (L & S) 99 : AIR 1975 SC 1329

rules governing the said Council showed that it was really an agent of the government. This Court rejected the said contention in these words (at page 617 of the Reports) : (SCC pp. 486-87, para 4)

> This contention is unsound. The society does not have a statutory character like the Oil and Natural Gas Commission, or the Life Insurance Corporation or Industrial Finance Corporation. It is a society incorporated in accordance with the provisions of the Societies Registration Act. The fact that the Prime Minister is the President or that the government appoints nominees to the Governing Body or that the government may terminate the membership will not establish anything more than the fact that the government takes special care that the promotion, guidance and cooperation of scientific and industrial research, the institution and financing of specific research, establishment or development and assistance to special institutions or departments of the existing institutions for scientific study of problems affecting particular industry in a trade, the utilisation of the result of the researches conducted under the auspices of the Council towards the development of industries in the country are carried out in a responsible manner.

49. We now come to a case of considerable importance, namely, *Sukhdev Singh* v. *Bhagatram Sardar Singh Raghuvanshi*[3]. Two questions fell to be determined in this case, namely, (*i*) whether statutory corporations are comprehended within the expression "the State" as defined in Article 12, and (*ii*) whether the regulations framed by a statutory corporation in exercise of the power conferred by the statute creating the corporation have the force of law. The majority of a Constitution Bench of this Court answered both these questions in the affirmative The statutory corporations before the court in that case were the Oil and Natural Gas Commission established under the Oil and Natural Gas Commission Act, 1956, the Life Insurance Corporation established under the Life Insurance Corporation Act, 1956, and the Industrial Finance Corporation established under the Industrial Finance Corporation Act, 1948. Ray, C.J., speaking for himself and Chandrachud and Gupta, JJ., pointed out (at page 634 of the Reports : SCC p. 439, para 35) that : "The State undertakes commercial functions in combination with governmental functions in a welfare State." The majority held that "the State" as defined in Article 12 comprehends bodies created for the purpose of promoting economic interests of the people and the circumstance that statutory bodies are required to carry on some activities of the nature of trade or commerce does not indicate that they must be excluded from the scope of the expression "the State", for a public authority is a body which has public or statutory duties to perform and which performs those duties and carries on its transactions for the benefit of the public and not for private profit and by that fact such an authority is not excluded from making a profit for the public benefit. Mathew, J., in his concurring judgment held that a finding of State financial support plus an unusual degree of control over the management and policies might lead one to characterise an operation as State action. The learned Judge observed (at pages 651-52 of the Reports) : (SCC p. 456, para 102)

> Institutions engaged in matters of high public interest or performing

public functions are by virtue of the nature of the function performed government agencies. Activities which are too fundamental to the society are by definition too important not to be considered government function. This demands the delineation of a theory which requires government to provide all persons with all fundamentals of life and the determinations of aspects which are fundamental. The State today has an affirmative duty of seeing that all essentials of life are made available to all persons. The task of the State today is to make possible the achievement of a good life both by removing obstacles in the path of such achievements and in assisting individual in realising his ideal of self-perfection. Assuming that indispensable functions are government functions, the problem remains of defining the line between fundamentals and non-fundamentals. The analogy of the doctrine of 'business affected with a public interest' immediately comes to mind.

After referring to the relevant provisions of the Acts under which the above statutory bodies were established, Mathew, J., continued (at pages 654-5 of the Reports) : (SCC pp. 458-59, para 109 and 111)

> The fact that these corporations have independent personalities in the eye of law does not mean that they are not subject to the control of government or that they are not instrumentalities of the government. *These corporations are instrumentalities or agencies of the State* for carrying on businesses which otherwise would have been run by the State departmentally. If the State had chosen to carry on these businesses through the medium of government departments, there would have been no question that actions of these departments would be 'State actions'. Why then should actions of these corporations be not State actions ? ....
>
> The ultimate question which is relevant for our purpose is whether such a corporation is an agency or instrumentality of the government for carrying on a business for the benefit of the public. In other words, *the question is, for whose benefit was the corporation carrying on the business* ? When it is seen from the provisions of that Act that on liquidation of the Corporation, its assets should be divided among the shareholders, namely, the Central and State governments and others, if any, the implication is clear that the benefit of the accumulated income would go to the Central and State governments. Nobody will deny that an agent has a legal personality different from that of the principal. The fact that the agent is subject to the direction of the principal does not mean that he has no legal personality of his own. Likewise, *merely because a corporation has legal personality of its own, it does not follow that the corporation cannot be an agent or instrumentality of the State,* if it is subject to control of government in all important matters of policy. No doubt, there might be some distinction between the nature of control exercised by principal over agent and the control exercised by government over public corporation. That, I think is only a distinction in degree. The *crux of the matter is that public corporation is a new type of institution which has sprung from the new social and economic functions of government and that it therefore does not neatly fit into old legal categories. Instead of forcing it into them, the later should be adapted to the needs of changing times and conditions.* (emphasis supplied.)

50. Various aspects of the question which we have to decide were exhaustively considered by this Court in *Ramana Dayaram Shetty* v. *International*

Airport Authority of India[10]. In that case the Court observed (at p. 1032 of the Reports : SCC p. 504, para 11) : "Today the *government*, as a welfare State, *is the* regulator and *dispenser* of special services and *provider of a large number of benefits, including jobs,* contracts, licences, quotas, mineral rights, etc." The question in that case was whether the International Airport Authority constituted under the International Airports Authority Act, 1971, came within the meaning of the expression "the State" in Article 12. Under the said Act, the Authority was a body corporate having perpetual succession and a common seal and was to consist of a Chairman and certain other members appointed by the Central Government. The Central Government had the power to terminate the appointment of or remove any member from the Board. Although the Authority had no share capital of its own, capital needed by it for carrying out its functions was to be provided only by the Central Government. While considering the question whether such a body corporate was included within the expression "the State" this Court said (at page 1036 of the Reports) : (SCC p. 507, para 14)

> *A corporation may be created in one of two ways. It may be either established by statute or incorporated under a law such as the Companies Act,* 1956 *or the Societies Registration Act,* 1860. Where a corporation is wholly controlled by government not only in its policy-making but also in carrying out the functions entrusted to it by the law establishing it or by the charter of its incorporation, there can be no doubt that it would be an instrumentality or agency of government. But ordinarily where a corporation is established by statute, it is autonomous in its working, subject only to a provision, oftentimes made, that it shall be bound by any directions that may be issued from time to time by government in respect of policy matters. So also a corporation incorporated under law is managed by a board of directors or committee of management in accordance with the provisions of the statute under which it is incorporated. *When does such a corporation become an instrumentality or agency of government* ? (emphasis supplied.)

After considering various factors and the case law on the subject, the court thus summed up the position : (SCC pp. 510-11, para 19)

> It will thus be seen that there are several factors which may have to be considered in determining whether a corporation is an agency or instrumentality of government. We have referred to some of these factors and they may be summarised as under : whether there is any financial assistance given by the State, and if so, what is the magnitude of such assistance whether there is any other form of assistance, given by the State, and if so, whether it is of the usual kind or it is extraordinary, whether there is any control of the management and policies of the corporation by the State and what is the nature and extent of such control, whether the corporation enjoys State conferred or State protected monopoly status and whether the functions carried out by the corporation are public functions closely related to governmental functions. This particularisation of relevant factors is however not exhaustive and by its very nature it cannot be, because with increasing assumption of new tasks, growing complexities of management and administration and the necessity of

10. (1979) 3 SCR 1014 : (1979) 3 SCC 489 · AIR 1979 SC 1628

> continuing adjustment in relations between the corporation and government calling for flexibility, adaptability and innovative skills, it is not possible to make an exhaustive enumeration of the tests which would invariably and in all cases provide an unfailing answer to the question whether a corporation is governmental instrumentality or agency. Moreover even amongst these factors which we have described, no one single factor will yield a satisfactory answer to the question and the court will have to consider the cumulative effect of these various factors and arrive at its decision on the basis of a particularised inquiry into the facts and circumstances of each case.

In the course of its judgment, the court distinguished the case of *Praga Tools Corporation*[8] as also the decision in *S. L. Agarwal* v. *General Manager, Hindustan Steel Ltd.*[8] in very much the same manner as we have done. So far as the case of *Sabhajit Tewary* v. *Union of India*[9] is concerned, the court said as follows : (SCC p. 519, para 31)

> Lastly, we must refer to the decision in *Sabhajit Tewary* v. *Union of India*[9] where the question was whether the Council of Scientific and Industrial Research was an 'authority' within the meaning of Article 12. The court no doubt took the view on the basis of facts relevant to the constitution and functioning of the Council that it was not an 'authority', but we do not find any discussion in this case as to what are the features which must be present before a corporation can be regarded as an 'authority' within the meaning of Article 12. This decision does not lay down any principle or test for the purpose of determining when a corporation can be said to be an 'authority'. If at all any test can be gleaned from the decision, it is whether the corporation is "really an agency of the government". The court seemed to hold on the facts that the Council was not an agency of the government and was, therefore, not an 'authority'.

51. In *U.P. Warehousing Corpn.* v. *Vinay Narayan Vajpayee*[11] an employee of the corporation successfully challenged his dismissal from service. The appellant corporation was established under the Agricultural Produce (Development and Warehousing) Corporation Act, 1956, and was deemed to be a Warehousing Corporation for a State under the Warehousing Corporation Act, 1962. In his concurring judgment, Chinnappa Reddy, J., said (at page 784 of the Reports) : (SCC pp. 468-69, para 22)

> *I find it very hard indeed to discover any distinction, on principle between* a person directly under the employment of the government and a person under the employment of an agency or instrumentality of the government or *a corporation, set up under a statute or incorporated but wholly owned by the government.* It is self-evident and trite to say that the function of the State has long since ceased to be confined to the preservation of the public peace, the exaction of taxes and the defence of its frontiers. It is now the function of the State to secure 'social, economic and political justice', to preserve 'liberty of thought, expression, belief, faith and worship', and to ensure 'equality of status and of opportunity'. (emphasis supplied)

52. In *Ajay Hasia* v. *Khalid Mujib Sehravardi*[12] the Regional Engineering

11 (1980) 2 SCR 773 : (1980) 3 SCC 459 : 1980 SCC (L & S) 453 : AIR 1980 SC 840
12. (1981) 2 SCR 79 : (1981) 1 SCC 722 · 1981 SCC (L & S) 258 : AIR 1981 SC 487

College which was established and administered and managed by a society registered under the Jammu and Kashmir Registration of Societies Act, 1898, was held to be "the State" within the meaning of Article 12. In that case the Court said (at page 91 of the Reports) : (SCC p. 732, para 7)

> It is undoubtedly true that the corporation is a distinct juristic entity with a corporate structure of its own and it carries on its functions on business principles with a certain amount of autonomy which is necessary as well as useful from the point of view of effective business management, but behind the formal ownership which is cast in the corporate mould, the reality is very much the deeply pervasive presence of the government. It is really the government which acts through the instrumentality or agency of the corporation and the juristic veil of corporate personality worn for the purpose of convenience of management and administration cannot be allowed to obliterate the true nature of the reality behind which is the government. *Now it is obvious that if a corporation is an instrumentality or agency of the government, it must be subject to the same limitations in the field of constitutional law as the government itself, though in the eye of the law it would be a distinct and independent legal entity.* If the government acting through its officers is subject to certain constitutional limitations, it must follow *a fortiori* that the government acting through the instrumentality or agency of a corporation should equally be subject to the same limitations. (emphasis supplied.)

After referring to various authorities, the court summarized the relevant tests which are to be gathered from the *International Airport Authority of India case*[19] as follows (at pages 96-7 of the Reports) : (SCC p. 737, para 9)

> (1) One thing is clear that if the entire share capital of the corporation is held by government, it would go a long way towards indicating that the corporation is an instrumentality or agency of government.
>
> (2) Where the financial assistance of the State is so much as to meet almost entire expenditure of the corporation, it would afford some indication of the corporation being impregnated with governmental character.
>
> (3) It may also be a relevant factor.....whether the corporation enjoys monopoly status which is the State conferred or State protected.
>
> (4) Existence of deep and pervasive State control may afford an indication that the corporation is a State agency or instrumentality.
>
> (5) If the functions of the corporation are of public importance and closely related to governmental functions, it would be a relevant factor in classifying the corporation as an instrumentality or agency of government.
>
> (6) "Specifically, if a department of Government is transferred to a corporation, it would be a strong factor supportive of this inference" of the corporation being an instrumentality or agency of Government.

53. The right, title and interest of the Burmah Shell Oil Storage and Distributing Company of India Limited in relation to its undertakings in India were transferred to and vested in the Central Government under Section 3 of the Burmah Shell (Acquisition of Undertakings in India) Act, 1976. Thereafter, under Section 7 of the said Act, the right, title, interest and liabilities of the said company which had become vested in the Central Government, instead of continuing so to vest in it, were directed to be vested in a government company, as defined by Section 617 of the Companies Act, 1956, namely, Bharat

Petroleum. In *Som Prakash Rekhi* v. *Union of India*[13] this Court held that Bharat Petroleum fell within the meaning of the expression "the State" used in Article 12. The following passage (at pages 124-5 of the Reports) from the judgment in that case is instructive and requires to be reproduced : (SCC pp. 461-62, para 26)

> For purposes of the Companies Act, 1956, a government company has a distinct personality which cannot be confused with the State. Likewise, a statutory corporation constituted to carry on a commercial or other activity is for many purposes a distinct juristic entity not drowned in the sea of State, although, in substance, its existence may be but a projection of the State. What we wish to emphasise is that *merely because a company or other legal person has functional and jural individuality for certain purposes and in certain areas of law, it does not necessarily follow that for the effective enforcement of fundamental rights* under our constitutional scheme, we should not scan the real character of that entity ; and if it is found to be a mere agent or surrogate of the State, in fact owned by the State, in truth controlled by the State and in effect an incarnation of the State, constitutional lawyers must not blink at these facts and *frustrate the enforcement of fundamental rights despite the inclusive definition of Article* 12. that any authority controlled by the Government of India is itself State. Law has many dimensions and fundamental facts must govern the applicability of fundamental rights in a given situation. (emphasis supplied.)

54. At the first blush it may appear that the case of *S. S. Dhanoa* v. *Municipal Corporation*[14], runs counter to the trend set in the authorities cited above but on a closer scrutiny it turns out not to be so. The facts in that case were that the Cooperative Store Limited, which was a society registered under the Bombay Cooperative Societies Act, 1925, had established and was managing Super Bazars at different places including at Connaught Place in New Delhi. Under Section 23 of the said Act, the society was a body corporate by the name under which it was registered, with perpetual succession and a common seal. The Super Bazars were not owned by the Central Government but were owned and managed by the said society, though pursuant to an agreement executed between the said society and the Union of India, the Central Government had advanced a loan of rupees forty lakhs to the said society for establishing and managing Super Bazars and it also held more than ninety-seven per cent of the shares of the said society. The appellant who was a member of the Indian Administrative Service was sent on deputation as the General Manager of the Super Bazar at Connaught Place. He along with other officials of the Super Bazar were prosecuted under the Prevention of Food Adulteration Act, 1954. He raised a preliminary objection before the Metropolitan Magistrate, Delhi, before whom he was summoned to appear that no cognizance of the alleged offence could be taken by him for want of sanction under Section 197 of the Code of Criminal Procedure, 1973. On his contention being rejected, he appealed to this Court. Under the said Sec-

13. (1981) 2 SCR 111 : (1981) 1 SCC 449 : 1981 SCC (L & S) 200 : AIR 1981 SC 212
14. (1981) 3 SCC 431 : 1982 SCC (L & S) 6 : 1981 SCC (Cri) 733

tion 197, when any person who is or was inter alia a public servant not removable from his office save by or with the sanction of the government is accused of any offence alleged to have been committed by him while acting or purporting to act in the discharge of his official duty, no court is to take cognizance of such offence except with the previous sanction in the case of a person who is employed or, as the case may be, was at the time of commission of the alleged offence employed, in connection with the affairs of the Union or of the Central Government. As stated in the opening paragraph of the judgment in the said case, the question before the court was whether the appellant was a public servant within the meaning of clause twelfth of Section 21 of the Indian Penal Code for purposes of Section 197 of the Code of Criminal Procedure. The relevant provisions of clause twelfth of Section 21 are as follows :

> 21. *Public servant.—The words 'public servant' denote* a person falling under any of the descriptions hereinafter following, namely :
>
> * * *
>
> *Twelfth.—Every person—*
>
> (*a*) in the service or pay of the government or remunerated by fees or commission for the performance of any public duty by the government ;
>
> (*b*) *in the service or pay of* a local authority, a *corporation established by or under a Central, Provincial or State Act or a government company as defined in Section* 617 *of the Companies Act,* 1956.
>
> (emphasis supplied)

The court pointed out that clause twelfth did not use the words "body corporate" and, therefore, the question was whether the expression "corporation" contained therein taken in collocation of the words "established by or under a Central or Provincial or State Act" would bring within its sweep a cooperative society. The Court said (SCC p. 437, para 7) :

> In our opinion, the expression 'corporation' must, in the context, mean a corporation created by the legislature and not a body or society brought into existence by an act of a group of individuals. A cooperative society is, therefore, not a corporation established by or under an Act of the Central or State legislature.

The court then proceeded to point out that a corporation is an artificial being created by law, having a legal entity entirely separate and distinct from the individuals who compose it, with the capacity of continuous existence and succession. The court held that corporations established by or under an Act of legislature can only mean a body corporate which owes its existence, and not merely its corporate status, to the Act. An association of persons constituting themselves into a company under the Companies Act or a society under the Societies Registration Act owes its existence not to the Act of legislature but to acts of parties, though it may owe its status as a body corporate to an Act of legislature. The observation of the court in that case with respect to companies were not intended by it to apply to government companies as defined in Section 617 of the Companies Act, 1956, for by the express terms of subclause (*b*) of clause twelfth of Section 21 of the Indian Penal Code every person

in the service or pay of a government company as defined in Section 617 of the Companies Act, 1956, is a public servant. The second part of the question which the court was called upon to decide in that case was whether the appellant can be said to be a person who was employed in connection with the affairs of the Union. The court held that the Super Bazar was not an instrumentality of the State and, therefore, it could not be said that the appellant was employed in connection with the affairs of the Union within the meaning of the Section 197 of the Code of Criminal Procedure. This observation was again made with reference to the argument that the appellant was employed in connection with the affairs of the Union. He undoubtedly was not employed in connection with the affairs of the Union just as a person employed in a corporation is not and cannot be said to be holding a civil post under the Union or a State as held by this Court in *S. L. Agarwal* v. *General Manager, Hindustan Steel Ltd.*[8]. In *S. S. Dhanoa case*[14] the court was not called upon to decide and did not decide whether a government company was an instrumentality or agency of the State for the purposes of Parts III and IV of the Constitution and thus, "the State" within the meaning of that expression as used in Article 12 of the Constitution.

55. The Indian Statistical Institute is a society registered under the Societies Registration Act, 1860, and is governed by the Indian Statistical Institute Act, 1959, under which its control completely vests in the Union of India. The society is also wholly financed by the Union of India. In *B. S. Minhas* v. *Indian Statistical Institute*[15] this Court, following *Ajay Hasia case*[12], held that the said society was an "authority" within the meaning of Article 12 and hence a writ petition under Article 32 filed against it was competent and maintainable. In *Manmohan Singh Jaitla* v. *Commissioner, Union Territory of Chandigarh*[16] this Court once again following *Ajay Hasia case*[12] held that an aided school which received a government grant of ninety-five per cent was an "authority" within the meaning of Article 12 and, therefore, amenable to the writ jurisdiction both of this Court and the High Court.

56. In *Workmen* v. *Hindustan Steel Ltd.*[17] the court held that the Hindustan Steel Ltd. was a public sector undertaking and, therefore, was "other authority" within the meaning of that expression in Article 12.

57. In *P.K. Ramachandra Iyer* v. *Union of India*[18] once again following *Ajay Hasia case*[12], the court held that the Indian Council of Agricultural Research which was a society registered under the Societies Registration Act was an instrumentality of the State falling under the expression "other authority" within the meaning of Article 12. The said Council was wholly financed by the government. Its budget was voted upon as part of the expenses incurred

15. (1983) 4 SCC 582 : 1984 SCC (L & S) 26
16. 1984 Supp SCC 540 : 1984 SCC (L & S) 269
17. 1984 Supp SCC 554, 560 : 1985 SCC (L & S) 260
18. (1984) 2 SCC 141 : 1984 SCC (L & S) 214

in the Ministry of Agriculture. The control of the Government of India permeated through all its activities. Since its inception, it was set up to carry out the recommendations of the Royal Commission on Agriculture. According to this Court, these facts were sufficient to make the said Council an instrumentality of the State.

58. In *A. L. Kalra* v. *Project and Equipment Corpn. of India Ltd.*[19], the said Corporation was held to be an instrumentality of the Central Government and hence falling within Article 12. The Project and Equipment Corporation of India Ltd. was a wholly owned subsidiary company of the State Trading Corporation but was separated in 1976 and thereafter functioned as a Government of India undertaking. The finding that it was an instrumentality of the Central Government was, however, based upon concession made by the said Corporation.

59. In *W. B. State Electricity Board* v. *Desh Bandhu Ghosh*[20] the West Bengal State Electricity Board was held to be an instrumentality of the State.

60. As pointed out earlier, the Corporation which is the first appellant in these appeals is not only a government company as defined in Section 617 of the Companies Act, 1956, but is wholly owned by three governments jointly. It is financed entirely by these three governments and is completely under the control of the Central Government, and is managed by the Chairman and Board of Directors appointed by the Central Government and removable by it. In every respect it is thus a veil behind which the Central Government operates through the instrumentality of a government company. The activities carried on by the Corporation are of vital national importance. The Fifth Five Year Plan 1974-79 states that the "outlay of Rs 14·73 crores for the next two years includes development of Rajabagan Dockyard and operation of the Central Inland Water Transport Corporation and operation of river services on the Ganga". According to the Sixth Five Year Plan, 1980-85, inland water transport is recognised as the cheapest mode of transport for certain kinds of commodities provided the points of origin and destination are both located on the water front ; that it is one of the most energy efficient modes of transport and has considerable potential in limited areas which have a network of waterways. This Plan further emphasises that in the North-Eastern Region where other transport infrastructure is severely lacking and more expensive, inland water transport has an additional importance as an instrument of development. The said Plan goes on to state : "In the Central Sector, an outlay of Rs 45 crores has been made for IWT. The most important programme relates to the investment proposal of Central Inland Water Transport Corporation (CIWTC)". The Annual Plan 1984-85 of the Government of India Planning Commission states as follows in paragraph 10.33 :

Inland Water Transport

Against the approved outlay of Rs 12 crores in 1983-84, the revised

19. (1984) 3 SCC 316, 319, 325 : 1984 SCC (L & S) 497
20 (1985) 3 SCC 116 : 1985 SCC (L & S) 607

expenditure in the Central Sector is estimated at Rs 10·40 crores. Bulk of the allocation was for the scheme of Central Inland Water Transport Corporation (CIWTC) for acquisition of vessels, development of Rajabagan Dockyard, creation of infrastructural facilities etc.

The Annual Report 1984-85 of the Government of India, Ministry of Shipping and Transport, states in paragraph 6.1.2. as follows :

> *The Inland Water Transport Directorate is an attached office of this Ministry* headed by a Chief Engineer-cum-Administrator. It has a complement of technical officers who are charged with the responsibility for planning of techno-economic studies on waterways and conducting hydrographic surveys. The Directorate has a Regional Office at Patna. Two sub-offices of this Regional Office have also been sanctioned. One of the sub-offices has been set up at Gauhati and arrangements are under way to set up the other at Varanasi. *The Ministry has also under its control a public sector undertaking, namely, the Central Inland Water Transport Corporation which is the only major company in inland water transport in the country.* (emphasis supplied)

As shown by the Statement of Objects and Reasons to the Legislative Bill, which when enacted became the National Waterway (Allahabad-Haldia Stretch of the Ganga-Bhagirathi-Hooghly River) Act, 1982 (Act 49 of 1982), published in the Gazette of India Extraordinary, Part II, Section 2, dated May 6, 1982, at page 15, the Central Government had set up various committees in view of the advantages in the mode of inland water transport such as its low cost of transport, energy efficiency, generation of employment among weaker sections of the community and less pollution. These committees had recommended that the Central Government should declare certain waterways as national waterways and assume responsibility for their development. A beginning in respect of this matter was thus made by the enactment of the said Act 49 of 1982. Under the said Act, the said stretch was declared to be a national waterway and it was the responsibility of the Central Government to regulate and develop this national waterway and to secure its efficient utilization for shipping and navigation. In the Demands for Grant of the Ministry of Shipping and Transport 1985-86 additional provision was made for an overall increase in Budget Estimates 1985-86 mainly for equity participation/investment in the Corporation. The activities carried on by the Corporation were thus described in the said Demands for Grant :

> *Central Inland Water Transport Corporation.*—CIWTC runs river services between Calcutta and Assam and Calcutta and Bangladesh. It undertakes movement of oil from Haldia to Budge-Budge/Paharpur for the Indian Oil Corporation. It also undertakes lighterage, stevedoring operations, ship building, ship repairing and other engineering services. To meet cash losses over riverine and engineering operations, construction of vessels and for purchase of machinery/equipment etc., budget estimates 1985-86 provide Rs 13·50 crores for loan and Rs 15·41 crores for equity investment in the Corporation.

Last year Parliament passed the Inland Waterways Authority of India Act, 1985. This Act received the assent of the President on December 30, 1985.

Under this Act, an authority called the Inland Waterways Authority of India is to be constituted and it is to be a body corporate by the name aforesaid, having perpetual succession and a common seal, with power, subject to the provisions of the said Act, to acquire, hold and dispose of property, both movable and immovable, and to contract and to sue and be sued by the said name. It is to consist of a Chairman, a Vice-Chairman and other persons not exceeding five. The Chairman, Vice-Chairman and the other persons are to be appointed by the Central Government. The term of office and other conditions of service of the members of the Authority are to be prescribed by the rules. The Central Government has also the power to remove any member of the Authority or to suspend him pending inquiry against him. Under the said Act, the Authority is, in the discharge of its functions and duties, to be bound by such directions on questions of policy as the Central Government may give in writing to it from time to time.

61. It may be mentioned that neither the said Act nor Act 49 of 1982 appears to have been yet brought into force.

62. There can thus be no doubt that the Corporation is a government undertaking in the public sector. The Corporation itself has considered that it is a Government of India undertaking. The complete heading of the said Rules is "Central Inland Water Transport Corporation Limited (A Government of India Undertaking)—Service, Discipline & Appeal Rules, 1979".

63. In the face of so much evidence it is ridiculous to describe the Corporation as a trading company as the appellants have attempted to do. What has been set out above is more than sufficient to show that the activities of the Corporation are of great importance to public interest, concern and welfare, and are activities of the nature carried on by a modern State and particularly a modern Welfare State.

64. It was, however, submitted on behalf of the appellants that even though the cases, out of those referred to above, upon which the appellants had relied upon were either distinguishable or inapplicable for determining the question whether a government company was "the State" or not, the case of *A. L. Kalra* v. *Project and Equipment Corpn. of India Ltd.*[19] relied upon by the respondents was based upon a concession and there was thus no direct authority on the point in issue. It was further submitted that all the other cases in which various bodies were held to be "the State" under Article 12 were those which concerned either a statutory authority or a corporation established by a statute.

65. It is true that the decision in *A. L. Kalra* v. *Project and Equipment Corpn. of India Ltd.*[19] was based upon a concession made by the respondent corporation but the case of *Workmen* v. *Hindustan Steel Ltd.*[17] was that of a government company for Hindustan Steel Limited is a government company as defined by Section 617 of the Companies Act as pointed out in *Gurugobinda*

Basu v. *Sankari Prasad Ghosal*[21]. The case of the *Workmen* v. *Hindustan Steel Ltd.*[17] related to a question whether a disciplinary inquiry was validly dispensed with under Standing Order 32 of the Hindustan Steel Limited. Under that standing order, where a workman had been convicted for a criminal offence in a court of law or where the General Manager was satisfied, for reasons to be recorded in writing, that it was inexpedient or against the interest of security to continue to employ the workman, the workman may be removed or dismissed from service without following the procedure for holding a disciplinary inquiry laid down in Standing Order 31. The order of removal from service of the concerned workman did not set out any reason for the satisfaction arrived at by the disciplinary authority but merely stated that such authority was satisfied that it was no longer expedient to employ the particular workman any further and the order then proceeded to remove him from the service of the company. In these circumstances, this Court held that the order of removal from service was bad in law. In the course of its judgment, this Court observed as follows (at SCC p. 560, para 5) :

> It is time for such a public sector undertaking as Hindustan Steel Ltd. to recast SO 32 and to bring it in tune with the philosophy of the Constitution failing which it being other authority and therefore a State under Article 12 in an appropriate proceeding, the vires of SO 32 will have to be examined. It is not necessary to do so in the present case because even on the terms of SO 32 the order made by the General Manager is unsustainable.

The only reason given by the court for holding that Hindustan Steel Limited was "other authority" and, therefore, "the State" under Article 12 was the fact that it was a public sector undertaking. In the entire judgment, there is no other discussion on this point except what is stated in the passage quoted above. Thus, to the extent that there is no authority of this Court in which the question, namely, whether a Government company is "the State" within the meaning of Article 12 has been discussed and decided, the above submission is correct.

66. Does this, therefore, make any difference ? There is a basic fallacy vitiating the above submission. That fallacy lies in the assumption which that submission makes that merely because a point has not fallen for decision by the court, it should, therefore, not be decided at any time. Were this assumption true, the law would have remained static and would have never advanced. The whole process of judicial interpretation lies in extending or applying by analogy the *ratio decidendi* of an earlier case to a subsequent case which differs from it in certain essentials, so as to make the principle laid down in the earlier case fit in with the new set of circumstances. The *sequitur* of the above assumption would be that the court should tell the suitor that there is no precedent governing his case and, therefore, it cannot give him any relief. This would be to do gross injustice. Had this not been done, the law would have never

21. (1964) 4 SCR 311, 315 : AIR 1964 SC 254

advanced. For instance, had *Rylands* v. *Fletcher*[22] not been decided in the way in which it was, an owner or occupier of land could with impunity have brought and kept on his land anything likely to do mischief if it escaped and would have himself escaped all liability for the damage caused by such escape if he had not been negligent. Similarly, but for *Donoghue* v. *Stevenson*[23] manufacturers would have been immune from liability to the ultimate consumers and users of their products.

67. What is the position before us ? It is only one case decided on a concession and another based upon an assumption that a government company is "the State" under Article 12 ? That is the position in fact but not in substance. As we have seen, authorities constituted under, and corporations established by, statutes have been held to be instrumentalities and agencies of the government in a long catena of decisions of this Court. The observations in several of these decisions, which have been emphasised by us in the passages extracted from the judgments in those cases, are general in their nature and take in their sweep all instrumentalities and agencies of the State, whatever be the form which such instrumentality or agency may have assumed. Particularly relevant in this connection are the observations of Mathew, J., in *Sukhdev Singh* v. *Bhagatram Sardar Singh Raghuvanshi*[3], of Bhagwati, J. (as he then was), in the *International Airport Authority case*[10] and *Ajay Hasia case*[12], and of Chinnappa Reddy, J., in *U. P. Warehousing Corpn. case*.[11] If there is an instrumentality or agency of the State which has assumed the garb of a government company as defined in Section 617 of the Companies Act, it does not follow that it thereby ceases to be an instrumentality or agency of the State. For the purposes of Article 12 one must necessarily see through the corporate veil to ascertain whether behind that veil is the face of an instrumentality or agency of the State. The Corporation, which is the appellant in these two appeals before us, squarely falls within these observations and it also satisfies the various tests which have been laid down. Merely because it has so far not the monopoly of inland water transportation is not sufficient to divest it of its character of an instrumentality or agency of the State. It is nothing but the government operating behind a corporate veil, carrying out a governmental activity and governmental functions of vital public importance. There can thus be no doubt that the Corporation is "the State" within the meaning of Article 12 of the Constitution.

68. We now turn to the second question which falls for determination in these appeals, namely, whether an unconscionable term in a contract of employment entered into with the Corporation, which is "the State" within the meaning of the expression in Article 12, is void as being violative of Article 14. What is challenged under this head is clause (*i*) of Rule 9 of the said Rules. This challenge levelled by the respondent in each of these two appeals succeeded in the High Court.

22. (1868) LR 3 HL 330
23. (1932) AC 562

69. The first point which falls for consideration on this part of the case is whether Rule 9(*i*) is unconscionable. In order to ascertain this, we must first examine the facts leading to the making of the said Rules and then the setting in which Rule 9(*i*) occurs. To recapitulate briefly, each of the contesting respondents was in the service of the Rivers Steam Navigation Company Limited. Their services were taken over by the Corporation after the Scheme of Arrangement was sanctioned by the Calcutta High Court. Under the said Scheme of Arrangement if their services had not been taken over, they would have been entitled to compensation payable to them, either under the Industrial Disputes Act, 1947, or otherwise legally admissible, by the said company, and the Government of India was to provide to the said company the amount of such compensation. Under the letters of appointment issued to these respondents, the age of superannuation was fifty-five. Thereafter, Service Rules were framed by the Corporation in 1970 which were replaced in 1979 by new rules namely, the said Rules. The said Rules did not apply to employees covered by the Industrial Employment (Standing Orders) Act, 1946, that is, to workmen, or to those in respect of whom the Board of Directors had issued separate orders. At all relevant times, these respondents were employed mainly in a managerial capacity. No separate orders were issued by the Board of Directors in their case. These respondents were, therefore, admittedly governed by the said Rules. Under Rule 10 of the said Rules, they were to retire from the service of the Corporation on completion of the age of fifty-eight years though in exceptional cases and in the interest of the Corporation an extension might have been granted to them with the prior approval of the Chairman-cum-Managing Director and the Board of Directors of the Corporation. The said Rules, however, provide four different modes in which the services of the respondents could have been terminated earlier than the age of superannuation, namely, the completion of the age of fifty-eight years. These modes are those provided in Rule 9(*i*), Rule 9(*ii*), sub-clause (*iv*) of clause (*b*) of Rule 36 read with Rule 38, and Rule 37. Of these four modes, the first two apply to permanent employees and the other two apply to all employees. Rule 6 classifies employees as either Permanent or Probationary or Temporary or Casual or Trainee. Clause (*i*) of Rule 6 defines the expression "Permanent employee' as meaning "an employee whose services have been confirmed in writing according to the Recruitment and Promotion Rules". Under Rule 9(*i*) which has been extracted above, the employment of a permanent employee is to be subject to termination on three months' notice in writing on either side. If the Corporation gives such a notice of termination, it may pay to the employee the equivalent of three months' basic pay and dearness allowance, if any, in lieu of notice, and where a permanent employee terminates the employment without giving due notice, the Corporation may deduct a like amount from the amount due or payable to the employee. Under Rule 11, an employee who wishes to leave the service of the Corporation by resigning therefrom, is to give to the Corporation the same notice as the Corporation is required to give to him under Rule 9, that is, a three months' notice in writing.

Under Rule 9(*ii*), the services of a permanent employee can be terminated on the ground of "Services no longer required in the interest of the Company" (that is, the Corporation). In such a case, a permanent employee whose service is terminated under this clause is to be paid fifteen days' basic pay and dearness allowance for each completed year of continuous service in the Corporation and he is also to be entitled to encashment of leave to his credit. Rule 36 prescribes the penalties which can be imposed, "for good and sufficient reasons and as hereinafter provided" in the said Rules, on an employee for his misconduct. Clause (*a*) of Rule 36 sets out the minor penalties and clause (*b*) of Rule 36 sets out the major penalties. Under sub-clause (*iv*) of clause (*b*) of Rule 36, dismissal from service is a major penalty. None of the major penalties including the penalty of dismissal is to be imposed except after holding an inquiry in accordance with the provisions of Rule 38 and until after the inquiring authority, where it is not itself the disciplinary authority, has forwarded to the disciplinary authority the records of the inquiry together with its report, and the disciplinary authority has taken its decision as provided in Rule 39. Rule 40 prescribes the procedure to be followed in imposing minor penalties. Under Rule 43, notwithstanding anything contained in Rules 38, 39 or 40, the disciplinary authority may dispense with the disciplinary inquiry in the three cases set out in Rule 43 and impose upon an employee either a major or minor penalty. We have reproduced Rule 43 earlier. Rule 45 provides for an appeal against an order imposing any of the penalties specified in Rule 36. Under Rule 37, the Corporation has the right to terminate the service of any employee at any time without any notice if the employee is found guilty of any insubordination, intemperance or other misconduct or of any breach of any rules pertaining to service or conduct or non-performance of his duties. The said Rules do not require that any disciplinary inquiry should be held before terminating an employee's service under Rule 37.

70. Each of the contesting respondents in these appeals was asked to submit his written explanation to the various allegations made against him. Ganguly, the first respondent in Civil Appeal 4412 of 1985, gave a detailed reply to the said show cause notice. Sengupta, the first respondent in Civil Appeal 4413 of 1985, denied the charges made against him and asked for inspection of the documents and copies of statements of witnesses mentioned in the charge-sheet served upon him to enable him to file his written statement. Without holding any inquiry into the allegations made against them, the services of each of them were terminated by the said letter dated February 26, 1983, under Rule 9(*i*). The action was not taken either under Rule 36 or Rule 37 nor was either of them dismissed after applying to his case Rule 43 and dispensing with the disciplinary inquiry.

71. It was submitted on behalf of the appellants that there was nothing unconscionable about Rule 9(*i*), that Rule 9(*i*) was not a *nudum pactum* for it was supported by mutuality inasmuch as it conferred an equal right upon both parties to terminate the contract of employment, that the grounds which

render an agreement void and unenforceable are set out in the Indian Contract Act, 1872 (Act 9 of 1872), that unconscionability was not mentioned in the Indian Contract Act as one of the grounds which invalidates an agreement, that the power conferred by Rule 9(*i*) was necessary for the proper functioning of the administration of the Corporation, that in the case of the respondents this power was exercised by the Chairman-cum-Managing Director of the Corporation, and that a person holding the highest office in the Corporation was not likely to abuse the power conferred by Rule 9(*i*).

72. The submissions of the contesting respondents, on the other hand, were that the parties did not stand on an equal footing and did not enjoy the same bargaining power, that the contract contained in the service rules was one imposed upon these respondents, that the power conferred by Rule 9(*i*) was arbitrary and uncanalized as it did not set out any guidelines for the exercise of that power and that even assuming it may not be void as a contract, in any event it offended Article 14 as it conferred an absolute and arbitrary power upon the Corporation.

73. As the question before us is of the validity of clause (*i*) of Rule 9, we will refrain from expressing any opinion with respect to the validity of clause (*ii*) of Rule 9 or Rule 37 or 40 but will confine ourselves only to Rule 9(*i*).

74. The said Rules constitute a part of the contract of employment between the Corporation and its employees to whom the said Rules apply, and they thus form a part of the contract of employment between the Corporation and each of the two contesting respondents. The validity of Rule 9(*i*) would, therefore, first fall to be tested by the principles of the law of contracts.

75. Under Section 19 of the Indian Contract Act, when consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused. It is not the case of either of the contesting respondents that there was any coercion brought to bear upon him or that any fraud or misrepresentation had been practised upon him. Under Section 19-A, when consent to an agreement is caused by undue influence, the agreement is a contract voidable at the option of the party whose consent was so caused and the court may set aside any such contract either absolutely or if the party who was entitled to avoid it has received any benefit thereunder, upon such terms and conditions as to the court may seem just. Sub-section (1) of Section 16 defines "Undue influence" as follows :

> 16. *'Undue influence' defined.*—(1) A contract is said to be induced by 'undue influence' where the relations subsisting between the parties are such that one of the parties is in a position to dominate the will of the other and uses that position to obtain an unfair advantage over the other.

The material provisions of sub-section (2) of Section 16 are as follows :

> (2) In particular and without prejudice to the generality of the foregoing

principle, a person is deemed to be in a position to dominate the will of another—

(*a*) where he holds a real or apparent authority over the other....

We need not trouble ourselves with the other sections of the Indian Contract Act except Sections 23 and 24. Section 23 states that the consideration or object of an agreement is lawful unless inter alia the court regards it as opposed to public policy. This section further provides that every agreement of which the object or consideration is unlawful is void. Under Section 24, if any part of a single consideration for one or more objects, or any one or any part of any one of several considerations for a single object is unlawful, the agreement is void. The agreement is, however, not always void in its entirety for it is well settled that if several distinct promises are made for one and the same lawful consideration, and one or more of them be such as the law will not enforce, that will not of itself prevent the rest from being enforceable. The general rule was stated by Willes, J., in *Pickering* v. *Ilfracombe Ry. Co.*[24] (at page 250) as follows :

> The general rule is that, where you cannot sever the illegal from the legal part of a covenant, the contract is altogether void ; but where you can sever them, whether the illegality be created by statute or by the common law, you may reject the bad part and retain the good.

76. Under which head would an unconscionable bargain fall ? If it falls under the head of undue influence, it would be voidable but if it falls under the head of being opposed to public policy, it would be void. No case of the type before us appears to have fallen for decision under the law of contracts before any court in India nor has any case on all fours of a court in any other country been pointed out to us. The word "unconscionable" is defined in the *Shorter Oxford English Dictionary,* Third Edition, Volume II, page 2288, when used with reference to actions etc. as "showing no regard for conscience; irreconcilable with what is right or reasonable". An unconscionable bargain would, therefore, be one which is irreconcilable with what is right or reasonable.

77. Although certain types of contracts were illegal or void, as the case may be, at Common Law, for instance, those contrary to public policy or to commit a legal wrong such as a crime or a tort, the general rule was of freedom of contract. This rule was given full play in the nineteenth century on the ground that the parties were the best judges of their own interests, and if they freely and voluntarily entered into a contract, the only function of the court was to enforce it. It was considered immaterial that one party was economically in a stronger bargaining position than the other ; and if such a party introduced qualifications and exceptions to his liability in clauses which are today known as "exemption clauses" and the other party accepted them, then full effect would be given to what the parties agreed. Equity, however, interfered in many cases of harsh or unconscionable bargains, such as, in the law

24. (1868) LR 3 CP 235

relating to penalties, forfeitures and mortgages. It also interfered to set aside harsh or unconscionable contracts for salvage services rendered to a vessel in distress, or unconscionable contracts with expectant heirs in which a person, usually a money-lender, gave ready cash to the heir in return for the property which he expects to inherit and thus to get such property at a gross undervalue. It also interfered with harsh or unconscionable contracts entered into with poor and ignorant persons who had not received independent advice (See *Chitty on Contracts,* Twenty-fifth Edition, Volume I, paragraphs 4 and 516).

78. Legislation has also interfered in many cases to prevent one party to a contract from taking undue or unfair advantage of the other. Instances of this type of legislation are usury laws, debt relief laws and laws regulating the hours of work and conditions of service of workmen and their unfair discharge from service, and control orders directing a party to sell a particular essential commodity to another.

79. In this connection, it is useful to note what Chitty has to say about the old ideas of freedom of contract in modern times. The relevant passages are to be found in *Chitty on Contracts,* Twenty-fifth Edition, Volume I, in paragraph 4, and are as follows :

> These ideas have to a large extent lost their appeal today. "Freedom of contract", it has been said, "is a reasonable social ideal only to the extent that equality of bargaining power between contracting parties can be assumed, and no injury is done to the economic interests of the community at large". Freedom of contract is of little value when one party has no alternative between accepting a set of terms proposed by the other or doing without the goods or services offered. Many contracts entered into by public utility undertakings and others take the form of a set of terms fixed in advance by one party and not open to discussion by the other. These are called "*contrats d'adhesion*" by French lawyers. Traders frequently contract, not on individually negotiated terms, but on those contained in a standard form of contract settled by a trade association. And the terms of an employee's contract of employment may be determined by agreement between his trade union and his employer, or by a statutory scheme of employment. Such transactions are nevertheless contracts notwithstanding that freedom of contract is to a great extent lacking.
>
> Where freedom of contract is absent, the disadvantages to consumers or members of the public have to some extent been offset by administrative procedures for consultation, and by legislation. Many statutes introduce terms into contracts which the parties are forbidden to exclude, or declare that certain provisions in a contract shall be void. And the courts have developed a number of devices for refusing to implement exemption clauses imposed by the economically stronger party on the weaker, although they have not recognised in themselves any general power (except by statute) to declare broadly that an exemption clause will not be enforced unless it is reasonable. Again, more recently, certain of the judges appear to have recognised the possibility of relief from contractual obligations on the ground of "inequality of bargaining power". What the French call "*contracts d'adhesion*", the American call "adhesion

contracts" or "contracts of adhesion". An "adhesion contract" is defined in *Black's Law Dictionary*, Fifth Edition, at page 38, as follows :

> *Adhesion contract.*—Standardized contract form offered to consumers of goods and services on essentially 'take it or leave it' basis without affording consumer realistic opportunity to bargain and under such conditions that consumer cannot obtain desired product or services except by acquiescing in form contract. Distinctive feature of adhesion contract is that weaker party has no realistic choice as to its terms. Not every such contract is unconscionable.

80. The position under the American Law is stated in *Reinstatement of the Law—Second* as adopted and promulgated by the American Law Institute, Volume II which deals with the law of contracts, in Section 208 at page 107, as follows :

> § 208. *Unconscionable Contract or Term*
>
> If a contract or term thereof is unconscionable at the time the contract is made a court may refuse to enforce the contract, or may enforce the remainder of the contract without the unconscionable term, or may so limit the application of any unconscionable term as to avoid any unconscionable result.

In the Comments given under that section it is stated at page 107 :

> Like the obligation of good faith and fair dealing (§ 205), *the policy against unconscionable contracts or terms applies to a wide variety of types of conduct*. The determination that a contract or term is or is not unconscionable is made in the light of its setting, purpose and effect. Relevant factors include weaknesses in the contracting process like those involved in more specific rules as to contractual capacity, fraud and other invalidating causes ; the policy also overlaps with rules which render particular bargains or terms unenforceable on grounds of public policy. *Policing against unconscionable contracts or terms has sometimes been accomplished* by adverse construction of language, by manipulation of the rules of offer and acceptance or *by determinations that the clause is contrary to public policy* or to the dominant purpose of the contract'. Uniform Commercial Code § 2-302 Comment 1....A bargain is not unconscionable merely because the parties to it are unequal in bargaining position, nor even because the inequality results in an allocation of risks to the weaker party. *But gross inequality of bargaining power, together with terms unreasonably favourable to the stronger party,* may confirm indications that the transaction involved elements of deception or compulsion, or may show that the weaker party had no meaningful choice, no real alternative, or did not in fact assent or appear to assent to the unfair terms. (emphasis supplied)

There is a statute in the United States called the Universal Commercial Code which is applicable to contracts relating to sales of goods. Though this statute is inapplicable to contracts not involving sales of goods, it has proved very influential in, what are called in the United States, "non-sales" cases. It has many times been used either by analogy or because it was felt to embody a general accepted social attitude of fairness going beyond its statutory application to sales of goods. In the Reporter's Note to the said Section 208, it is stated at page 112 :

> It is to be emphasised that a contract of adhesion is not unconscionable

per se, and that all unconscionable contracts are not contracts of adhesion. Nonetheless, *the more standardised the agreement and the less a party may bargain meaningfully, the more susceptible the contract or a term will be to a claim of unconscionability.* (emphasis supplied)

The position has been thus summed up by John R. Peden in *"The Law of Unjust Contracts"* published by Butterworths in 1982, at pages 28-29 :

> ....Unconscionability represents the end of a cycle commencing with the Aristotelian concept of justice and the Roman law *laesio enormis,* which in turn formed the basis for the medieval church's concept of a just price and condemnation of usury. These philosophies permeated the exercise, during the seventeenth and eighteenth centuries, of the Chancery court's discretionary powers under which it upset all kinds of unfair transactions. Subsequently the movement towards economic individualism in the nineteenth century hardened the exercise of these powers by emphasising the freedom of the parties to make their own contract. While the principle of *pacta sunt servanda* held dominance, the consensual theory still recognised exceptions where one party was overborne by a fiduciary, or entered a contract under duress or as the result of fraud. However, these exceptions were limited and had to be strictly proved.
>
> It is suggested that the judicial and legislative trend duing the last 30 years in both civil and common law jurisdictions has almost brought the wheel full circle. Both courts and parliaments have provided greater protection for weaker parties from harsh contracts. In several jurisdictions this included a general power to grant relief from unconscionable contracts, thereby providing a launching point from which the courts have the opportunity to develop a modern doctrine of unconscionability. American decisions on Article 2.302 of the UCC have already gone some distance into this new arena....."

The expression *"laesio enormis"* used in the above passage refers to *"laesio ultra dimidium vel enormis"* which in Roman law meant the injury sustained by one of the parties to an onerous contract when he had been overreached by the other to the extent of more than one-half of the value of the subject-matter, as for example, when a vendor had not received half the value of property sold, or the purchaser had paid more than double value. The maxim *"pacta sunt servanda"* referred to in the above passage means "contracts are to be kept".

81. It would appear from certain recent English cases that the courts in that country have also begun to recognise the possibility of an unconscionable bargain which could be brought about by economic duress even between parties who may not in economic terms be situate differently (see, for instance, *Occidental Worldwide Investment Corpn.* v. *Skibs A/S Avanti*[25], *North Ocean Shipping Co. Ltd.* v. *Hyundai Construction Co. Ltd.*[26], *Pao On* v. *Lau Yin Long*[27] and *Universe Tankships Inc. of Monrovia* v. *International Transport Workers*

25. (1976) 1 Lloyd's Rep 293
26. (1979) QB 705
27. (1980) AC 614

Federation[28], and the commentary on these cases in Chitty on *Contracts*, Twenty-fifth Edition, Volume I, paragraph 486).

82. Another jurisprudential concept of comparatively modern origin which has affected the law of contracts is the theory of "distributive justice". According to this doctrine, distributive fairness and justice in the possession of wealth and property can be achieved not only by taxation but also by regulatory control of private and contractual transactions even though this might involve some sacrifice of individual liberty. In *Lingappa Pochanna Appelwar* v. *State of Maharashtra*[29], this Court, while upholding the constitutionality of the Maharashtra Restoration of Lands to Scheduled Tribes Act, 1974, said (at SCC p. 493, para 16) :

> The present legislation is a typical illustration of the concept of distributive justice, as modern jurisprudence know it. Legislators, judges and administrators are now familiar with the concept of distributive justice. Our Constitution permits and even directs the State to administer what may be termed 'distributive justice'. The concept of distributive justice in the sphere of law-making connotes, inter alia, the removal of economic inequalities and rectifying the injustice resulting from dealings or transactions between unequals in society. Law should be used as an instrument of distributive justice to achieve a fair division of wealth among the members of society based upon the principle : 'From each according to his capacity, to each according to his needs'. *Distributive justice comprehends* more than achieving lessening of inequalities by differential taxation, giving debt relief or distribution of property owned by one to many who have none by imposing ceiling on holdings, both agricultural and urban, or by *direct regulation of contractual transactions by forbidding certain transactions and, perhaps, by requiring others. It also means that* those who have been deprived of their properties by unconscionable bargains should be restored their property. All such laws may take the form of forced redistribution of wealth as a means of achieving a fair division of material resources among the members of society or *there may be legislative control of unfair agreements.* (emphasis supplied.)

When our Constitution states that it is being enacted in order to give to all the citizens of India "JUSTICE, social, economic and political", when clause (1) of Article 38 of the Constitution directs the State to strive to promote the welfare of the people by securing and protecting as effectively as it may a social order in which social, economic and political justice shall inform all the institutions of the national life, when clause (2) of Article 38 directs the State, in particular, to minimize the inequalities in income, not only amongst individuals but also amongst groups of people residing in different areas or engaged in different vocations, and when Article 39 directs the State that it shall, in particular, direct its policy towards securing that the citizens, men and women equally, have the right to an adequate means of livelihood and that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment and that there should be equal pay for equal work for both men and women, it is the doctrine of distributive justice which is speaking through these words of the Constitution.

28. (1981) ICR 129 : (1982) 2 WLR 803
29. (1985) 1 SCC 479

83. Yet another theory which has made its emergence in recent years in the sphere of the law of contracts is the test of reasonableness or fairness of a clause in a contract where there is inequality of bargaining power. Lord Denning, MR, appears to have been the propounder, and perhaps the originator —at least in England, of this theory. In *Gillespie Brothers & Co. Ltd.* v. *Roy Bowles Transport Ltd.*[30] where the question was whether an indemnity clause in a contract, on its true construction, relieved the indemnifier from liability arising to the indemnified from his own negligence, Lord Denning said (at pages 415-416) :

> The time may come when this process of 'construing' the contract can be pursued no further. The words are too clear to permit of it. *Are the courts* then powerless ? Are they *to permit the party to enforce his unreasonable clause, even when it is so unreasonable, or applied so unreasonably, as to be unconscionable* ? When it gets to this point, I would say, as I said many years ago :
>
> > 'there is the vigilance of the common law which, while allowing freedom of contract, watches to see that it is not abused' : *John Lee & Son (Grantham) Ltd.* v. *Railway Executive*[31]
>
> It will not allow a party to exempt himself from his liability at common law when it would be quite unconscionable for him to do so. (emphasis supplied.)

In the above case the Court of Appeal negatived the defence of the indemnifier that the indemnity clause did not cover the negligence of the indemnified. It was in *Lloyds Bank Ltd.* v. *Bundy*[32] that Lord Denning first clearly enunciated his theory of "inequality of bargaining power". He began his discussion on this part of the case by stating (at page 763) :

> There are cases in our books in which *the courts will set aside a contract,* or a transfer of property, *when the parties have not met on equal terms, when the one is so strong in bargaining power and the other so weak that, as a matter of common fairness, it is not right that the strong should be allowed to push the weak to the wall.* Hitherto those exceptional cases have been treated each as a separate category in itself. But I think the time has come when we should seek to find a principle to unite them. I put on one side contracts or transactions which are voidable for fraud or misrepresentation or mistake. All those are governed by settled principles. I go only to those where there has been inequality of bargaining power, such as to merit the intervention of the court. (emphasis supplied)

He then referred to various categories of cases and ultimately deduced therefrom a general principle in these words (at page 765) :

> Gathering all together, I would suggest that *through all these instances there runs a single thread.* They rest on '*inequality* of bargaining power'. By virtue of it, the English law gives relief to one who, without independent advice, enters into a contract on terms which are very unfair or transfers property for a consideration which is grossly inadequate, when his bargain-

30. (1973) QB 400, 416
31. (1949) 2 All ER 581, 584
32. (1974) 3 All ER 757

ing power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influences or pressures brought to bear on him by or for the benefit of the other. When I use the word 'undue' I do not mean to suggest that the principle depends on proof of any wrongdoing. The one who stipulates for an unfair advantage may be moved solely by his own self-interest, unconscious of the distress he is bringing to the other. I have also avoided any reference to the will of the one being 'dominated' or 'overcome' by the other. *One who is in extreme need may knowingly consent to a most improvident bargain, solely to relieve the straits in which he finds himself.* Again, I do not mean to suggest that every transaction is saved by independent advice. But the absence of it may be fatal. With these explanations, I hope this principle will be found to reconcile the cases. (emphasis supplied)

84. Though the House of Lords does not yet appear to have unanimously accepted this theory, the observations of Lord Diplock in *A. Schroeder Music Publishing Co. Ltd.* v. *Macaulay (formerly Instone)*[33] are a clear pointer towards this direction. In that case a song writer had entered into an agreement with a music publisher in the standard form whereby the publishers engaged the song writer's exclusive services during the term of the agreement, which was five years. Under the said agreement, the song writer assigned to the publisher the full copyright for the whole world in his musical compositions during the said term. By another term of the said agreement, if the total royalties during the term of the agreement exceeded £ 5,000 the agreement was to stand automatically extended by a further period of five years. Under the said agreement, the publisher could determine the agreement at any time by one month's written notice but no corresponding right was given to the song writer. Further, while the publisher had the right to assign the agreement, the song writer agreed not to assign his rights without the publisher's prior written consent. The song writer brought an action claiming, inter alia, a declaration that the agreement was contrary to public policy and void. Plowman, J., who heard the action granted the declaration which was sought and the Court of Appeal affirmed his judgment. An appeal filed by the publishers against the judgment of the Court of Appeal was dismissed by the House of Lords. The Law Lords held that the said agreement was void as it was in restraint of trade and thus contrary to public policy. In his speech Lord Diplock, however, outlined the theory of reasonableness or fairness of a bargain. The following observations of his on this part of the case require to be reproduced *in extenso* (at pages 1315-16) :

My Lords, the contract under consideration in this appeal is one whereby the respondent accepted restrictions upon the way in which he would exploit his earning power as a song writer for the next ten years. Because this can be classified as a contract in restraint of trade the restrictions that the respondent accepted fell within one of those limited categories of contractual promises in respect of which the courts still retain the power to relieve the promisor of his legal duty to fulfil them. In order to determine whether this case is one in which that power ought to be exercised, what your Lordships have in fact been doing has been to assess

33. (1974) 1 WLR 1308

the relative bargaining power of the publisher and the song writer at the time the contract was made and to decide whether the publisher had used his superior bargaining power to exact from the song writer promises that were unfairly onerous to him. Your Lordships have not been concerned to inquire whether the public have in fact been deprived of the fruit of the song writer's talents by reason of the restrictions, nor to assess the likelihood that they would be so deprived in the future if the contract were permitted to run its full course.

It is, in my view, salutary to acknowledge that in refusing to enforce provisions of a contract whereby one party agrees for the benefit of the other party to exploit or to refrain from exploiting his own earning power, the public policy which the court is implementing is not some 19th-century economic theory about the benefit to the general public of freedom of trade, but the protection of those whose bargaining power is weak against being forced by those whose bargaining power is stronger to enter into bargains that are unconscionable. Under the influence of Bentham and of *laiseez faire* the courts in the 19th century abandoned the practice of applying the public policy against unconscionable bargains to contracts generally, as they had formerly done to any contract considered to be usurious ; but the policy survived in its application to penalty clauses and to relief against forfeiture and also to the special category of contracts in restraint of trade. If one looks at the reasoning of 19th-century judges in cases about contracts in restraint of trade one finds lip service paid to current economic theories, but if one looks at what they said in the light of what they did, one finds that they struck down a bargain if they thought it was unconscionable as between the parties to it and upheld it if they thought that it was not.

So I would hold that the question to be answered as respects a contract in restraint of trade of the kind with which this appeal is concerned is : "*Was the bargain fair* ?" *The test of fairness is, no doubt, whether the restrictions are both reasonably necessary for the protection of the legitimate interests of the promisee and commensurate with the benefits secured to the promisor under the contract. For the purpose of this test all the provisions of the contract must be taken into consideration.* (emphasis supplied)

Lord Diplock then proceeded to point out that there are two kinds of standard forms of contracts. The first is of contracts which contain standard clauses which "have been settled over the years by negotiation by representatives of the commercial interests involved and have been widely adopted because experience has shown that they facilitate the conduct of trade". He then proceeded to state : "If fairness or reasonableness were relevant to their enforceability the fact that they are widely used by parties whose bargaining power is fairly matched would raise a strong presumption that their terms are fair and reasonable". Referring to the other kind of standard form of contract Lord Diplock said (at page 1316) :

The same presumption, however, does not apply to *the other kind of standard form of contract.* This is of comparatively modern origin. It is *the result of the concentration of particular kinds of business in relatively few hands.* The ticket cases in the 19th century provide what are probably the first examples. *The terms of this kind of standard form of contract have not been the subject of negotiation* between the parties to it, or approved

by any organisation representing the interests of the weaker party. *They have been dictated by that party whose bargaining power,* either exercised alone or in conjunction with others providing similar goods or services, *enables him to say* : 'If you want these goods or services at all, these are the only terms on which they are obtainable. *Take it or leave it'.*

To be in a position to adopt this attitude towards a party desirous of entering into a contract to obtain goods or services provides a classic instance of superior bargaining power. (emphasis supplied.)

85. The observations of Lord Denning, MR, in *Levison* v. *Patent Steam Carpet Co. Ltd.*[31] are also useful and require to be quoted. These observations are as follows (at page 79) :

In such circumstances as here the Law Commission in 1975 recommended that a term which exempts the stronger party from his ordinary common law liability should not be given effect except when it is reasonable : see The Law Commission and the Scottish Law Commission Report, Exemption Clauses, Second Report (1975) (August 5, 1975), Law Com. No. 69 (H. C. 605), pp. 62, 174 ; and there is a Bill now before Parliament which gives effect to the test of reasonableness. This is a gratifying piece of law reform : but I do not think we need wait for that Bill to be passed into law. You never know what may happen to a Bill. Meanwhile the common law has its own principles ready to hand. In *Gillespie Bros. & Co. Ltd.* v. *Roy Bowles Transport Ltd.*[30] I suggested that an exemption or limitation clause should not be given effect if it was unreasonable, or if it would be unreasonable to apply it in the circumstances of the case. I see no reason why this should not be applied today, at any rate in contracts in standard forms where there is inequality of bargaining power.

86. The Bill referred to by Lord Denning in the above passage, when enacted, became the Unfair Contract Terms Act, 1977. This statute does not apply to all contracts but only to certain classes of them. It also does not apply to contracts entered into before the date on which it came into force, namely, February 1, 1978 ; but subject to this it applies to liability for any loss or damage which is suffered on or after that date. It strikes at clauses excluding or restricting liability in certain classes of contracts and torts and introduces in respect of clauses of this type the test of reasonableness and prescribes the guidelines for determining their reasonableness. The detailed provisions of this statute do not concern us but they are worth a study.

87. In *Photo Production Ltd.* v. *Securicor Transport Ltd.*[35], a case before the Unfair Contract Terms Act, 1977, was enacted, the House of Lords upheld an exemption clause in a contract on the defendants' printed form containing standard conditions. The decision appears to proceed on the ground that the parties were businessmen and did not possess unequal bargaining power. The House of Lords did not in that case reject the test of reasonableness or fairness of a clause in a contract where the parties are not equal in bargaining position. On the contrary, the speeches of Lord Wilberforce, Lord Diplock and Lord Scarman would seem to show that the House of Lords in a fit case would accept

34. (1978) QB 69
35. (1980) AC 827

that test. Lord Wilberforce in his speech, after referring to the Unfair Contract Terms Act, 1977, said (at page 843) :

> This Act applies to consumer contracts and those based on standard terms and enables exception clauses to be applied with regard to what is just and reasonable. It is significant that Parliament refrained from legislating over the whole field of contract. After this Act, *in commercial matters generally, when the parties are not of unequal bargaining power,* and when risks are normally borne by insurance, not only is the case for judicial intervention undemonstrated, but there is everything to be said, and this seems to have been Parliament's intention, for leaving the parties free to apportion the risks as they think fit and for respecting their decisions. (emphasis supplied)

Lord Diplock said (at page 850-51) :

> Since the obligations implied by law in a commercial contract are those which, by judicial consensus over the years or by Parliament in passing a statute, have been regarded as *obligations which a reasonable businessman would realise that he was accepting when he entered into a contract of a particular kind,* the court's view of the reasonableness of any departure from the implied obligations which would be involved in construing the express words of an exclusion clause in one sense that they are capable of bearing rather than another, is a relevant consideration in deciding what meaning the words were intended by the parties to bear. (emphasis supplied)

Lord Scarman, while agreeing with Lord Wilberforce, described (at page 853) the action out of which the appeal before the House had arisen as "*a commercial dispute between parties well able to look after themselves*" and then added : "*In such a situation* what the parties agreed (expressly or impliedly) is what matters ; and the duty of the courts is to construe their contract according to its tenor".

88. As seen above, apart from judicial decisions, the United States and the United Kingdom have statutorily recognised, at least in certain areas of the law of contracts, that there can be unreasonableness (or lack of fairness, if one prefers that phrase) in a contract or a clause in a contract where there is inequality of bargaining power between the parties although arising out of circumstances not within their control or as a result of situations not of their creation. Other legal systems also permit judicial review of a contractual transaction entered into in similar circumstances. For example, Section 138(2) of the German Civil Code provides that a transaction is void "when a person" exploits "the distressed situation, inexperience, lack of judgmental ability, or grave weakness of will of another to obtain the grant or promise of pecuniary advantages . . . which are obviously disproportionate to the performance given in return". The position according to the French law is very much the same.

89. Should then our courts not advance with the times ? Should they still continue to cling to outmoded concepts and outworn ideologies ? Should we not adjust our thinking caps to match the fashion of the day ? Should

all jurisprudential development pass us by, leaving us floundering in the sloughs of 19th century theories ? Should the strong be permitted to push the weak to the wall ? Should they be allowed to ride roughshod over the weak ? Should the courts sit back and watch supinely while the strong trample underfoot the rights of the weak ? We have a Constitution for our country. Our judges are bound by their oath to "uphold the Constitution and the laws". The Constitution was enacted to secure to all the citizens of this country social and economic justice. Article 14 of the Constitution guarantees to all persons equality before the law and the equal protection of the laws. The principle deducible from the above discussions on this part of the case is in consonance with right and reason, intended to secure social and economic justice and conforms to the mandate of the great equality clause in Article 14. This principle is that the courts will not enforce and will, when called upon to do so, strike down an unfair and unreasonable contract, or an unfair and unreasonable clause in a contract, entered into between parties who are not equal in bargaining power. It is difficult to give an exhaustive list of all bargains of this type. No court can visualize the different situations which can arise in the affairs of men. One can only attempt to give some illustrations. For instance, the above principle will apply where the inequality of bargaining power is the result of the great disparity in the economic strength of the contracting parties. It will apply where the inequality is the result of circumstances, whether of the creation of the parties or not. It will apply to situations in which the weaker party is in a position in which he can obtain goods or services or means of livelihood only upon the terms imposed by the stronger party or go without them. It will also apply where a man has no choice, or rather no meaningful choice, but to give his assent to a contract or to sign on the dotted line in a prescribed or standard form or to accept a set of rules as part of the contract, however unfair, unreasonable and unconscionable a clause in that contract or form or rules may be. This principle, however, will not apply where the bargaining power of the contracting parties is equal or almost equal. This principle may not apply where both parties are businessmen and the contract is a commercial transaction. In today's complex world of giant corporations with their vast infra-structural organizations and with the State through its instrumentalities and agencies entering into almost every branch of industry and commerce, there can be myriad situations which result in unfair and unreasonable bargains between parties possessing wholly disproportionate and unequal bargaining power. These cases can neither be enumerated nor fully illustrated. The court must judge each case on its own facts and circumstances.

90. It is not as if our civil courts have no power under the existing law. Under Section 31(1) of the Specific Relief Act, 1963 (Act 47 of 1963), any person against whom an instrument is void or voidable, and who has reasonable apprehension that such instrument, if left outstanding, may cause him serious injury, may sue to have it adjudged void or voidable, and the court may, in its discretion, so adjudge it and order it to be delivered up and cancelled.

91. Is a contract of the type mentioned above to be adjudged voidable

or void ? If it was induced by undue influence, then under Section 19-A of the Indian Contract Act, it would be voidable. It is, however, rarely that contracts of the types to which the principle formulated by us above applies are induced by undue influence as defined by Section 16(1) of the Indian Contract Act, even though at times they are between parties one of whom holds a real or apparent authority over the other. In the vast majority of cases, however, such contracts are entered into by the weaker party under pressure of circumstances, generally economic, which results in inequality of bargaining power. Such contracts wil not fall within the four corners of the definition of "undue influence" given in Section 16(1). Further, the majority of such contracts are in a standard or prescribed form or consist of a set of rules. They are not contracts between individuals containing terms meant for those individuals alone. Contracts in prescribed or standard forms or which embody a set of rules as part of the contract are entered into by the party with superior bargaining power with a large number of persons who have far less bargaining power or no bargaining power at all. Such contracts which affect a large number of persons or a group or groups of persons, if they are unconscionable, unfair and unreasonable, are injurious to the public interest. To say that such a contract is only voidable would be to compel each person with whom the party with superior bargaining power had contracted to go to court to have the contract adjudged voidable. This would only result in multiplicity of litigation which no court should encourage and would also not be in the public interest. Such a contract or such a clause in a contract ought, therefore, to be adjudged void. While the law of contracts in England is mostly judge-made, the law of contracts in India is enacted in a statute, namely, the Indian Contract Act, 1872. In order that such a contract should be void, it must fall under one of the relevant sections of the Indian Contract Act. The only relevant provision in the Indian Contract Act which can apply is Section 23 when it states that "The consideration or object of an agreement is lawful, unless . . . the court regards it as . . . opposed to public policy."

92. The Indian Contract Act does not define the expression "public policy" or "opposed to public policy". From the very nature of things, the expressions "public policy", "opposed to public policy", or "contrary to public policy" are incapable of precise definition. Public policy, however, is not the policy of a particular government. It connotes some matter which concerns the public good and the public interest. The concept of what is for the public good or in the public interest or what would be injurious or harmful to the public good or the public interest has varied from time to time. As new concepts take the place of old, transactions which were once considered against public policy are now being upheld by the courts and similarly where there has been a well recognized head of public policy, the courts have not shirked from extending it to new transactions and changed circumstances and have at times not even flinched from inventing a new head of public policy. There are two schools of thought- "the narrow view" school and "the broad view" school.

According to the former, courts cannot create new heads of public policy whereas the latter countenances judicial law-making in this area. The adherents of "the narrow view" school would not invalidate a contract on the ground of public policy unless that particular ground had been well-established by authorities. Hardly ever has the voice of the timorous spoken more clearly and loudly than in these words of Lord Davey in *Janson* v. *Driefontein Consolidated Gold Mines Ltd.*[36] : "Public policy is always an unsafe and treacherous ground for legal decision". That was in the year 1902. Seventy-eight years earlier, Burrough, J., in *Richardson* v. *Mellish*[37] described public policy as "a very unruly horse, and when once you get astride it you never know where it will carry you". The Master of the Rolls, Lord Denning, however, was not a man to shy away from unmanageable horses and in words which conjure up before our eyes the picture of the young Alexander the Great taming Bucephalus, he said in *Enderby Town Football Club Ltd.* v. *Football Assn. Ltd.*[38] ; "With a good man in the saddle, the unruly horse can be kept in control. It can jump over obstacles". Had the timorous always held the field, not only the doctrine of public policy but even the Common Law or the principles of Equity would never have evolved. Sir William Holdsworth in his "*History of English Law*", Volume III, page 55, has said :

> In fact, a body of law like the common law, which has grown up gradually with the growth of the nation, necessarily acquires some fixed principles, and if it is to maintain these principles it must be able, on the ground of public policy or some other like ground, to suppress practices which, under ever new disguises, seek to weaken or negative them.

It is thus clear that the principles governing public policy must be and are capable, on proper occasion, of expansion or modification. Practices which were considered perfectly normal at one time have today become obnoxious and oppressive to public conscience. If there is no head of public policy which covers a case, then the court must in consonance with public conscience and in keeping with public good and public interest declare such practice to be opposed to public policy. Above all, in deciding any case which may not be covered by authority our courts have before them the beacon light of the Preamble to the Constitution. Lacking precedent, the court can always be guided by that light and the principles underlying the Fundamental Rights and the Directive Principles enshrined in our Constitution.

93. The normal rule of Common Law has been that a party who seeks to enforce an agreement which is opposed to public policy will be non-suited. The case of *A. Schroeder Music Publishing Co. Ltd.* v. *Macaulay*[39], however, establishes that where a contract is vitiated as being contrary to public policy, the party adversely affected by it can sue to have it declared void. The case may be different where the purpose of the contract is illegal or immoral. In

36. (1902) AC 484, 500
37. (1824) 2 Bing 229, 252 : 130 ER 294, 303 and (1824-34) All ER 258, 266
38. (1971) Ch 591, 606

Kedar Nath Motani v. *Prahlad Rai*[39], reversing the High Court and restoring the decree passed by the trial court declaring the appellants' title to the lands in suit and directing the respondents who were the appellants' benamidars to restore possession, this Court, after discussing the English and Indian law on the subject, said (at page 873) :

> The correct position in law, in our opinion, is that what one has to see is whether the illegality goes so much to the root of the matter that the plaintiff cannot bring his action without relying upon the illegal transaction into which he had entered. If the illegality be trivial or venial, as stated by Williston and the plaintiff is not required to rest his case upon that illegality, then public policy demands that the defendant should not be allowed to take advantage of the position. A strict view, of course, must be taken of the plaintiff's conduct, and he should not be allowed to circumvent the illegality by resorting to some subterfuge or by misstating the facts. If, however, the matter is clear and the illegality is not required to be pleaded or proved as part of the cause of action and the plaintiff recanted before the illegal purpose was achieved, then, unless it be of such a gross nature as to outrage the conscience of the court, the plea of the defendant should not prevail.

The types of contracts to which the principle formulated by us above applies are not contracts which are tainted with illegality but are contracts which contain terms which are so unfair and unreasonable that they shock the conscience of the court. They are opposed to public policy and require to be adjudged void.

94. We will now test the validity of Rule 9(*i*) by applying to it the principle formulated above. Each of the contesting respondents was in the service of the Rivers Steam Navigation Company Limited and on the said Scheme of Arrangement being sanctioned by the Calcutta High Court, he was offered employment in the Corporation which he had accepted. Even had these respondents not liked to work for the Corporation, they had not much of a choice because all that they would have got was "all legitimate and legal compensation payable to them either under the Industrial Disputes Act or otherwise legally admissible". These respondents were not covered by the Industrial Disputes Act for they were not workmen but were officers of the said company. It is, therefore, difficult to visualize what compensation they would have been entitled to get unless their contract of employment with their previous employers contained any provision in that behalf. So far as the original terms of employment with the Corporation are concerned, they are contained in the letters of appointment issued to the contesting respondents. These letters of appointment are in a stereotype form. Under these letters of appointment, the Corporation could without any previous notice terminate their service, if the Corporation was satisfied on medical evidence that the employee was unfit and was likely for a considerable time to continue to be unfit for the discharge of his duties. The Corporation could also without any previous notice dismiss either

39. (1960) 1 SCR 861 : AIR 1960 SC 213

of them, if he was guilty of any insubordination, intemperance or other misconduct, or of any breach of any rules pertaining to his service or conduct or non-performance of his duties. The above terms are followed by a set of terms under the heading "Other Conditions". One of these terms stated that : "You shall be subject to the service rules and regulations including the conduct rules". Undoubtedly, the contesting respondents accepted appointment with the Corporation upon these terms. They had, however, no real choice before them. Had they not accepted the appointments, they would have at the highest received some compensation which would have been probably meagre and would certainly have exposed themselves to the hazard of finding another job.

95. It was argued before us on behalf of the contesting respondents that the term that these respondents would be subject to the service rules and regulations including the conduct rules, since it came under the heading "Other Conditions" which followed the clauses which related to the termination of service, referred only to service rules and regulations other than those providing for termination of service and, therefore, Rule 9(*i*) did not apply to them. It is unnecessary to decide this question in the view which we are inclined to take with respect to the validity of Rule 9(*i*).

96. The said Rules as also the earlier rules of 1970 were accepted by the contesting respondents without demur. Here again they had no real choice before them. They had risen higher in the hierarchy of the Corporation. If they had refused to accept the said Rules, it would have resulted in termination of their service and the consequent anxiety, harassment and uncertainty of finding alternative employment.

97. Rule 9(*i*) confers upon the Corporation the power to terminate the service of a permanent employee by giving him three months' notice in writing or in lieu thereof to pay him the equivalent of three months' basic pay and dearness allowance. A similar regulation framed by the West Bengal State Electricity Board was described by this Court in *W. B. State Electricity Board* v. *Desh Bandhu Ghosh*[20] (at SCC p. 118, para 4) as :

> . . . a naked 'hire and fire' rule, the time for banishing which altogether from employer-employee relationship is fast approaching. Its only parallel is to be found in the Henry VIII clause so familiar to administrative lawyers.

As all lawyers may not be familiar with administrative law, we may as well explain that "the Henry VIII clause" is a provision occasionally found in legislation conferring delegated legislative power, giving the delegate the power to amend the delegating Act in order to bring that Act into full operation or otherwise by order to remove any difficulty, and at times giving power to modify the provisions of other Acts also. The Committee on Ministers' Powers in its report submitted in 1932 (Cmd. 4060) pointed out that such a provision had been nicknamed "the Henry VIII clause" because "that King is regarded popularly as the impersonation of executive autocracy" The Committee's

Report (at page 61) criticised these clauses as a temptation to slipshod work in the preparation of bills and recommended that such provisions should be used only where they were justified before Parliament on compelling grounds. Legislation enacted by Parliament in the United Kingdom after 1932 does not show that this recommendation had any particular effect.

98. No apter description of Rule 9(*i*) can be given than to call it "the Henry VIII clause". It confers absolute and arbitrary power upon the Corporation. It does not even state who on behalf of the Corporation is to exercise that power. It was submitted on behalf of the appellants that it would be the Board of Directors. The impugned letters of termination, however, do not refer to any resolution or decision of the Board and even if they did, it would be irrelevant to the validity of Rule 9(*i*). There are no guidelines whatever laid down to indicate in what circumstances the power given by Rule 9(*i*) is to be exercised by the Corporation. No opportunity whatever of a hearing is at all to be afforded to the permanent employee whose service is being terminated in the exercise of this power. It was urged that the Board of Directors would not exercise this power arbitrarily or capriciously as it consists of responsible and highly placed persons. This submission ignores the fact that however highly placed a person may be, he must necessarily possess human frailties. It also overlooks the well-known saying of Lord Acton, which has now almost become a maxim, in the appendix to his "*Historical Essays and Studies*", that "Power tends to corrupt, and absolute power corrupts absolutely". As we have pointed out earlier, the said Rules provide for four different modes in which the services of a permanent employee can be terminated earlier than his attaining the age of superannuation, namely, Rule 9(*i*), Rule 9(*ii*), sub-clause (*iv*) of clause (*b*) of Rule 36 read with Rule 38 and Rule 37. Under Rule 9(*ii*) the termination of service is to be on the ground of "Services no longer required in the interest of the Company". Sub-clause (*iv*) of clause (*b*) of Rule 36 read with Rule 38 provides for dismissal on the ground of misconduct. Rule 37 provides for termination of service at any time without any notice if the employee is found guilty of any of the acts mentioned in that rule. Rule 9(*i*) is the only rule which does not state in what circumstances the power conferred by that rule is to be exercised. Thus, even where the Corporation could proceed under Rule 36 and dismiss an employee on the ground of misconduct after holding a regular disciplinary inquiry, it is free to resort instead to Rule 9(*i*) in order to avoid the hassle of an inquiry. Rule 9(*i*) thus confers an absolute, arbitrary and unguided power upon the Corporation. It violates one of the two great rules of natural justice—the *audi alteram partem* rule. It is not only in cases to which Article 14 applies that the rules of natural justice come into play. As pointed out in *Union of India* v. *Tulsiram Patel*[40] (at SCC page 463, para 72) : "The principles of natural justice are not the creation of Article 14. Article 14 is not their begetter but their constitutional guardian". That case has traced in some detail the origin and development of the concept of principles of natural justice and of the *audi alteram partem*

40. (1985) 3 SCC 398 : 1985 SCC (L & S) 672

rule (at pages 463-480). They apply in diverse situations and not only to cases of State action. As pointed out by O. Chinnappa Reddy, J., in *Swadeshi Cotton Mills* v. *Union of India*[41] they are implicit in every decision-making function, whether judicial or quasi-judicial or administrative. Undoubtedly, in certain circumstances the principles of natural justice can be modified and, in exceptional cases, can even be excluded as pointed out in *Tulsiram Patel case*[40]. Rule 9(*i*), however, is not covered by any of the situations which would justify the total exclusion of the *audi alteram partem* rule.

99. The power conferred by Rule 9(*i*) is not only arbitrary but is also discriminatory for it enables the Corporation to discriminate between employee and employee. It can pick up one employee and apply to him clause (*i*) of Rule 9. It can pick up another employee and apply to him clause (*ii*) of Rule 9. It can pick up yet another employee and apply to him sub-clause (*iv*) of clause (*b*) of Rule 36 read with Rule 38 and to yet another employee it can apply Rule 37. All this the Corporation can do when the same circumstances exist as would justify the Corporation in holding under Rule 38 a regular disciplinary inquiry into the alleged misconduct of the employee. Both the contesting respondents had, in fact, been asked to submit their explanation to the charges made against them. Sengupta had been informed that a disciplinary inquiry was proposed to be held in his case. The charges made against both the respondents were such that a disciplinary inquiry could easily have been held. It was, however, not held but instead resort was had to Rule 9(*i*).

100. The Corporation is a large organization. It has offices in various parts of West Bengal, Bihar and Assam, as shown by the said Rules, and possibly in other States also. The said Rules form part of the contract of employment between the Corporation and its employees who are not workmen. These employees had no powerful workmen's Union to support them. They had no voice in the framing of the said Rules. They had no choice but to accept the said Rules as part of their contract of employment. There is gross disparity between the Corporation and its employees, whether they be workmen or officers. The Corporation can afford to dispense with the services of an officer. It will find hundreds of others to take his place but an officer cannot afford to lose his job because if he does so, there are not hundreds of jobs waiting for him. A clause such as clause (*i*) of Rule 9 is against right and reason. It is wholly unconscionable. It has been entered into between parties between whom there is gross inequality of bargaining power. Rule 9(*i*) is a term of the contract between the Corporation and all its officers. It affects a large number of persons and it squarely falls within the principle formulated by us above. Several statutory authorities have a clause similar to Rule 9(*i*) in their contracts of employment. As appears from the decided cases, the West Bengal State Electricity Board and Air India International have it. Several government companies apart from the Corporation (which is the first appellant before us) must be having it. There are 970 government companies with paid-

41. (1981) 1 SCC 664

up capital of Rs. 16,414.9 crores as stated in the written arguments submitted on behalf of the Union of India. The government and its agencies and instrumentalities constitute the largest employer in the country. A clause such as Rule 9(*i*) in a contract of employment affecting large sections of the public is harmful and injurious to the public interest for it tends to create a sense of insecurity in the minds of those to whom it applies and consequently it is against public good. Such a clause, therefore, is opposed to public policy and being opposed to public policy, it is void under Section 23 of the Indian Contract Act.

101. It was, however, submitted on behalf of the appellants that this was a contract entered into by the Corporation like any other contract entered into by it in the course of its trading activities and the court, therefore, ought not to interfere with it. It is not possible for us to equate employees with goods which can be bought and sold. It is equally not possible for us to equate a contract of employment with a mercantile transaction between two businessmen and much less to do so when the contract of employment is between a powerful employer and a weak employee.

102. It was also submitted on behalf of the appellants that Rule 9(*i*) was supported by mutuality inasmuch as it conferred an equal right upon both the parties, for under it just as the employer could terminate the employee's service by giving him three months' notice or by paying him three months' basic pay and dearness allowance in lieu thereof, the employee could leave the service by giving three months' notice and when he failed to give such notice, the Corporation could deduct an equivalent amount from whatever may be payable to him. It is true that there is mutuality in Rule 9(*i*)—the same mutuality as in a contract between the lion and the lamb that both will be free to roam about in the jungle and each will be at liberty to devour the other. When one considers the unequal position of the Corporation and its employees, the argument of mutuality becomes laughable.

103. The contesting respondents could, therefore, have filed a civil suit for a declaration that the termination of their service was contrary to law on the ground that the said Rule 9(*i*) was void. In such a suit, however, they would have got a declaration and possibly damages for wrongful termination of service but the civil court could not have ordered reinstatement as it would have amounted to granting specific performance of a contract of personal service. As the Corporation is "the State", they, therefore, adopted the far more efficacious remedy of filing a writ petition under Article 226 of the Constitution.

104. As the Corporation is "the State" within the meaning of Article 12, it was amenable to the writ jurisdiction of the High Court under Article 226. It is now well established that an instrumentality or agency of the State being "the State" under Article 12 of the Constitution is subject to the constitutional limitations, and its actions are State actions and must be judged in the light of the Fundamental Rights guaranteed by Part III of the Constitution (see,

for instance, *Sukhdev Singh* v. *Bhagatram Sardar Singh Raghuvanshi*[3], *International Airport Authority case*[10] and *Ajay Hasia case*[3]). The actions of an instrumentality or agency of the State must, therefore, be in conformity with Article 14 of the Constitution. The progression of the judicial concept of Article 14 from a prohibition against discriminatory class legislation to an invalidating factor for any discriminatory or arbitrary State action has been traced in *Tulsiram Patel case*[10] (at pages 473-476). The principles of natural justice have now come to be recognized as being a part of the constitutional guarantee contained in Article 14. In *Tulsiram Patel case*[10] this Court said (at page 476, para 95) :

> The principles of natural justice have thus come to be recognized as being a part of the guarantee contained in Article 14 because of the new and dynamic interpretation given by this Court to the concept of equality which is the subject-matter of that article. Shortly put, the syllogism runs thus : violation of a rule of natural justice results in arbitrariness which is the same as discrimination ; where discrimination is the result of State action, it is violation of Article 14 ; therefore, a violation of a principle of natural justice by a State action is a violation of Article 14. Article 14, however, is not the sole repository of the principles of natural justice. What it does is to guarantee that any law or State action violating them will be struck down. The principles of natural justice, however, apply not only to legislation and State action but also where any tribunal, authority or body of men, not coming within the definition of 'State' in Article 12, is charged with the duty of deciding a matter.

105. As pointed out above, Rule 9(*i*) is both arbitrary and unreasonable and it also wholly ignores and sets aside the *audi alteram partem* rule. It, therefore, violates Article 14 of the Constitution.

106. On behalf of the appellants reliance was placed upon the case of *Radhakrishna Agarwal* v. *State of Bihar*[42]. The facts in that case were that a contract, called a "lease", to collect and exploit *sal* seeds from a forest area was entered into between the State of Bihar and the appellants in that case. Under one of the clauses of the said contract, the rate of royalty could be revised at the expiry of every three years in consultation with the lessee and was to be binding on the lessee. The State unilaterally revised the rate of royalty payable by the appellants and thereafter cancelled the lease. The Patna High Court dismissed the writ petition filed by the appellants and the appellants' appeal to this Court was also dismissed. In that case it was held that when a State acts purely in its executive capacity, it is bound by the obligations which dealings of the State with individual citizens import into every transaction entered into in exercise of its constitutional powers, but this is only at the time of entry into the field of consideration of persons with whom the government could contract, and after the State or its agents have entered into the field of ordinary contract the relations are no longer governed by the constitutional provisions but by the legally valid contract which determines rights and obligations of the parties *inter se*. The court then added (at p. 255): (SCC pp. 462-63, para 10)

> No question arises of violation of Article 14 or of any other consti-

42. (1977) 3 SCR 249 : (1977) 3 SCC 457 : AIR 1977 SC 1496

tutional provision when the State or its agents, purporting to act within this field, perform any act. In this sphere, they can only claim rights conferred upon them by contract and are bound by the terms of the contract only unless some statute steps in and confers some special statutory power or obligation on the State in the contractual field which is apart from contract.

107. We fail to see what relevance that decision has to the case before us. Employees of a large organization form a separate and distinct class and we are unable to equate a contract of employment in a stereotype form entered into by "the State" with each of such employees with the "lease" executed in *Radhakrishna Agarwal case*[42]. Further, the contract or the lease between the parties in that case was a legally valid contract. In that case what the appellants were doing was to complain of a breach of contract committed by the State of Bihar acting through its officers. The contesting respondents are not complaining of any breach of contract but their contention is that Rule 9(*i*) which is a term of their contract of employment is void. They are not complaining that the action of termination of their service is in breach of Rule 9(*i*). Their complaint is not merely with respect to the State action taken under Rule 9(*i*) but also with respect to the action of the State in entering into a contract of employment with them which contains such a clause or rather forcing upon them a contract of employment containing such a clause. As we have held earlier, Rule 9(*i*) is void even under the ordinary law of contracts.

108. We must now turn to two decisions of the Bombay High Court as each party has relied strongly upon one of them, namely, *S. S. Muley* v. *J.R.D. Tata*[43] and *Manohar P. Kharkhar* v. *Raghuraj*[44], commonly known as the "*Makalu case*" as it related to certain cables which were damaged in an aircraft named 'Makalu' belonging to Air India International. The decision in *Muley case*[43] was relied upon by the respondents while the decision in *Makalu case*[44] was relied upon by the appellants. Both the cases related to Regulation 48 of the Air India Employees' Service Regulations framed by Air India International. Air India International is a corporation established under the Air Corporations Act, 1953 (Act 27 of 1953) and it is indisputably "the State" within the meaning of Article 12 of the Constitution. Under clause (*a*) of the said Regulation 48, the services of a permanent employee can be terminated "without assigning any reason" by giving him thirty days' notice in writing or pay in lieu of notice. In both these cases, the services of the concerned employees were terminated under Regulation 48(*a*). The said Regulations also provided for dismissal of an employee who was found guilty of misconduct in a disciplinary inquiry held according to the procedure prescribed in the said Regulations. In *Muley case*[43] a learned Single Judge of the Bombay High Court, Sawant, J., held the said Regulation 48(*a*) to be void as infringing Article 14 of the Constitution. In *West Bengal State Electricity Board case*[20] this Court stated (at SCC page 119, para 4) : "The learned Judge

43. 1980 Lab IC 11 : (1979) 2 SLR 438 (Bom)
44. (1981) 2 LLJ 459 (Bom)

struck down Regulation 48(*a*) and we agree with his reasoning and conclusion". The reasoning upon which Sawant, J., reached his conclusion was that there was no guidance given anywhere in the impugned regulation for the exercise of the power conferred by it, that it placed untrammelled power in the hands of the authorities, that it was an arbitrary power which was conferred and it did not make any difference that it was to be exercised by high ranking officials. In the *Makalu case*[44] a contrary view was taken by a Division Bench of the Bombay High Court. The Division Bench rightly held that the employees of a statutory corporation did not enjoy the protection conferred by Article 311(2). It, however, further held that the phrase "without assigning any reason" used in the said Regulation 48 only meant a disclosure of the reasons to the employee concerned. After going into the facts which had been pleaded by Air India International to justify the termination of the service of the petitioners in that case, the Division Bench held that the impugned orders were justified. It further held that Regulation 48 was not a one-sided regulation since under Regulation 49 the employee was also permitted to resign without assigning any reason by giving the notice prescribed therein. The Division Bench applied to the said Regulation 48 the analogy of the ordinary law of master and servant under which no servant can claim any security of tenure. It also brought in the analogy of the right to compulsorily retire an employee where a provision in that behalf is made in the Service Rules. The Division Bench further held that it was difficult to conceive of any authority, which was "the State" under Article 12 of the Constitution and bound by the constitutional guarantees contained in Part III of the Constitution, terminating the services of its employees without reason or arbitrarily. It further held that the existence of relevant reasons was a *sine qua non* for exercising the power under Regulation 48. It went on to state that because of the complexity of modern administration and the unpredictable exigencies which may arise in the course thereof, it was necessary for an employer to be vested with powers such as those conferred by Regulation 48. The Division Bench took great pains to discern in some of the sections of the Air Corporations Act guidelines for the exercise of the power conferred by Regulation 48. According to the Division Bench, the choice of Air India International to proceed under Regulation 48 would have to be dictated for the purpose of the needs and exigencies of its administration and if that power was exercised arbitrarily, the court would strike down the action taken under Regulation 48.

109. We were invited by learned counsel for the appellants to peruse the judgment in that case and we did so with increasing astonishment. Though the said judgment bears the date September 18, 1981, we were unable to make out whether it was a judgment given in the year 1981 or in the year 1881 or even earlier. We find ourselves wholly unable to agree with the view taken by the Division Bench. Apart from the factual aspects of the case, as to which we say nothing, we find every single conclusion reached by the Division Bench and the reasons given in support thereof to be wholly erroneous. The Division Bench overlooked that it was not dealing with a case of a non-speaking order but with the validity of a regulation. The meaning given by it to the expression

"without assigning any reason" was wrong and untenable. Starting with this wrong premise, it has gone from one wrong premise to another. In the light of what we have said earlier about the principles of public policy evolved, and tested by the principle which we have formulated, the said Regulation 48(*a*) could never have been sustained. In *W. B. State Electricity Board case*[20], a three-Judge Bench of this Court said as follows (at SCC page 119, para 5) :

> The learned counsel for the appellant relied upon *Manohar P. Kharkhar* v. *Raghuraj*[41] to contend that Regulation 48 of the Air India Employees' Service Regulations was valid. It is difficult to agree with the reasoning of the Delhi High Court that because of the complexities of modern administration and the unpredictable exigencies arising in the course of such administration it is necessary for an employer to be vested with such powers as those under Regulation 48. We prefer the reasoning of Sawant, J. of the Bombay High Court and that of the Calcutta High Court in the judgment under appeal to the reasoning of the Delhi High Court.

The mention of the Delhi High Court in the above passage is a slip of the pen, for it was the Bombay High Court which decided the case. We are in respectful agreement with what has been stated in the above passage. The *Makalu case*[14] was wrongly decided and requires to be overruled. We are, however, informed that an appeal against that judgment is pending in this Court and rather than overrule it here, we leave it to the Bench which hears that appeal to reverse it.

110. We would like to observe here that as the definition of "the State" in Article 12 is for the purposes of both Part III and Part IV of the Constitution, State actions, including actions of the instrumentalities and agencies of the State, must not only be in conformity with the Fundamental Rights guaranteed by Part III but must also be in accordance with the Directive Principles of State Policy prescribed by Part IV. Clause (*a*) of Article 39 provides that the State shall, in particular, direct its policy towards "securing that the citizens, men and women, equally have the right to adequate means of livelihood". Article 41 requires the State, within the limits of its economic capacity and development, to "make effective provision for securing the right to work". An adequate means of livelihood cannot be secured to the citizens by taking away without any reason the means of livelihood. The mode of making "effective provision for securing the right to work" cannot be by giving employment to a person and then without any reason throwing him out of employment. The action of an instrumentality or agency of the State, if it frames a service rule such as clause (*i*) of Rule 9 or a rule analogous thereto would, therefore, not only be violative of Article 14 but would also be contrary to the Directive Principles of State Policy contained in clause (*a*) of Article 39 and in Article 41.

111. The Calcutta High Court was, therefore, right in quashing the impugned orders dated February 26, 1983, terminating the services of the contesting respondents and directing the Corporation to reinstate them and to pay them all arrears of salary. The High Court was, however, not right in declaring clause (*i*) of Rule 9 in its entirety as ultra vires Article 14 of the Consti-

tution and in striking down as being void the whole of that clause. What the Calcutta High Court overlooked was that Rule 9 also confers upon a permanent employee the right to resign from the service of the Corporation. By entering into a contract of employment a person does not sign a bond of slavery and a permanent employee cannot be deprived of his right to resign. A resignation by an employee would, however, normally require to be accepted by the employer in order to be effective. It can be that in certain circumstances an employer would be justified in refusing to accept the employee's resignation as, for instance, when an employee wants to leave in the middle of a work which is urgent or important and for the completion of which his presence and participation are necessary. An employer can also refuse to accept the resignation when there is a disciplinary inquiry pending against the employee. In such a case, to permit an employee to resign would be to allow him to go away from the service and escape the consequences of an adverse finding against him in such an inquiry. There can also be other grounds on which an employer would be justified in not accepting the resignation of an employee. The Corporation ought to make suitable provisions in that behalf in the said Rules. Therefore, while the judgment of the High Court requires to be confirmed, the declaration given by it requires to be suitably modified.

112. In the result, both these appeals fail and are dismissed but the order passed by the Calcutta High Court is modified by substituting for the declaration given by it a declaration that clause (*i*) of Rule 9 of the "Service, Discipline and Appeal Rules, 1979" of the Central Inland Water Transport Corporation Limited is void under Section 23 of the Indian Contract Act, 1872, as being opposed to public policy and is also ultra vires Article 14 of the Constitution to the extent that it confers upon the Corporation the right to terminate the employment of a permanent employee by giving him three months' notice in writing or by paying him the equivalent of three months' basic pay and dearness allowance in lieu of such notice.

113. By interim orders passed in the petitions for special leave to appeal filed by the Corporation, we had granted pending the disposal of these petitions a stay of the order of the Calcutta High Court insofar as it directed the reinstatement of the contesting respondents. At that stage the Corporation had undertaken to pay to the said respondents all arrears of salary and had also undertaken to pay thereafter their salary from month to month before the tenth day of each succeeding month until the disposal of the said petitions. We hereby vacate the stay order of reinstatement passed by us and direct the Corporation forthwith to reinstate the first respondent in each of these appeals and to pay to him within six weeks from today all arrears of salary and allowances payable to him, if any still remain unpaid.

114. The first appellant in both these appeals, namely, the Central Inland Water Transport Corporation Limited, will pay to the first respondent in each of these appeals the costs of the respective appeals. The other parties to these appeals and the intervener will bear and pay their own costs of the appeals.