2024 INSC 253

REPORTABLE

IN THE SUPREME COURT OF INDIA
ORIGINAL JURISDICTION

Original Suit No. 1 of 2024

State of Kerala …Plaintiff(s)

versus

Union of India …Defendant(s)

with

I.A. No. 6149 of 2024

ORDER

SURYA KANT, J.

1. State of Kerala has instituted this Original Suit under Article 131 of the Constitution of India against the Union of India, challenging, *inter alia*, the following (collectively, the "Impugned Actions"):

(a) Amendment Act No. 13 of 2018 (dated 28.03.2018):

By this Amendment Act, the Parliament has amended Section 4 of the Fiscal Responsibility and Budget Management Act,

2003, whereby the Central Government is obligated to ensure that the aggregate debt of the Central Government and the State Governments does not exceed sixty percent of the gross domestic product by the end of Financial Year (F.Y.) 2024-25;

(b) Letter No. 40(1)/PF-S/2023-24 (dated 27.03.2023):

Through this letter, the Defendant has imposed a 'Net Borrowing Ceiling' on the Plaintiff - State, to restrict the maximum possible borrowing that Plaintiff could make under law. This ceiling was quantified as three percent of the projected Gross State Domestic Product (GSDP) for the F.Y. 2023-24, which came to INR 32,442 crores. This Net Borrowing Ceiling covered all sources of borrowings, including open market borrowings, loans from Financial Institutions, and the liabilities arising out of the Public Account of the Plaintiff. Additionally, to prevent the States from by-passing the Net Borrowing Ceiling by using State-Owned Enterprises, the ceiling has also been applied to certain borrowings by such enterprises; and

(c) Letter No. 40(12)/PF-S/2023-24/OMB-52 (dated 11.08.2023):

In this letter, the Defendant has accorded its consent to the Plaintiff to raise open market borrowing of INR 1,330 crores. It has also noted that the total open market borrowing allowed to the Plaintiff for the F.Y. 2023-24 was INR 21,852 crores.

2. The instant suit has been filed on the premise that by undertaking the Impugned Actions, the Defendant - Union of India has exceeded its power under Article 293 of the Constitution of India, which provides:

> "***293. Borrowing by States.***—
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> *(1) Subject to the provisions of this article, the executive power of a State extends to borrowing within the territory of India upon the security of the Consolidated Fund of the State within such limits, if any, as may from time to time be fixed by the Legislature of such State by law and to the giving of guarantees within such limits, if any, as may be so fixed.*
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> *(2) The Government of India may, subject to such conditions as may be laid down by or under any law made by Parliament, make loans to any State or, so long as any limits fixed under article 292 are not exceeded, give guarantees in respect of loans raised by any State, and any sums required for the purpose of making such loans shall be charged on the Consolidated Fund of India.*
>
> *(3) A State may not without the consent of the Government of India raise any loan if there is still*

outstanding any part of a loan which has been made to the State by the Government of India or by its predecessor Government, or in respect of which a guarantee has been given by the Government of India or by its predecessor Government.

(4) A consent under clause (3) may be granted subject to such conditions, if any, as the Government of India may think fit to impose."

3. Besides the afore-mentioned final relief in the suit, the Plaintiff -State also seeks interim injunction, *inter alia*, to mandate Union of India: *(a)* to restore the position that existed before the Defendant imposed ceiling on all the borrowings of the Plaintiff; and *(b)* to enable the Plaintiff to borrow INR 26,226 crores on an immediate basis.

4. We have heard Mr. Kapil Sibal, Ld. Senior Advocate, for the Plaintiff - State, and Mr. R. Venkataramani, Ld. Attorney General for India and Mr. N. Venkataraman, Ld. Additional Solicitor General of India, on behalf of the Defendant – Union of India at a considerable length, and have perused the Plaint and other documents on record on the issue of maintainability of suit as well as the interim relief sought by the Plaintiff - State.

5. In support of its prayer for the interim injunction, the Plaintiff - State has mainly urged that: *(i)* under Article 293 of the Constitution, the Union of India does not have the power to

regulate all the borrowings of a State and conditions can be imposed only on the loans sought from the Central Government; *(ii)* the liabilities arising out of the Public Account and State-Owned Enterprises cannot be included in the borrowings of the Plaintiff; *(iii)* the Plaintiff – State is in dire need of INR 26,226 crores to pay dues arising out of various budgetary obligations including dearness allowance, pension scheme, subsidies, etc.; *(iv)* there has been under-utilization of permissible borrowing space from previous years, which the Plaintiff should be allowed to use now; *(v)* the over-borrowing from the years before F.Y. 2023-24 cannot be adjusted from the Net Borrowing Ceiling of this F.Y. and must instead be repaid at the date of maturity of such borrowing; and *(vi)* the debt is sustainable because it satisfies the Domar model, such that the GSDP of the Plaintiff – State is rising faster than the effective interest rate.

6. *Per contra*, the Defendant – Union of India controverted the Plaintiff's interim claim and has argued that: *(i)* since management of public finance is a national issue, the Union of India has the power to regulate all the borrowings of the Plaintiff - State to maintain the fiscal health of the country; *(ii)* the liabilities arising out of Public Account and State-Owned enterprises can be

included in the borrowings of the Plaintiff since they may be used to by-pass the borrowing ceiling; *(iii)* the pending dues have arisen on account of the fiscal mismanagement by the State of Kerala and are not a consequence of regulation of borrowing by the Union of India; *(iv)* the Plaintiff's contention regarding under-utilized borrowing space from the previous years is based on erroneous facts; *(v)* the over-borrowing done in a F.Y. has to be adjusted against the borrowing amount of the next F.Ys.; and *(vi)* the fiscal health of the country will be jeopardized if the Plaintiff – State is allowed to undertake more debt.

7. On a critical analysis of the contentions of both the sides, it seems to us that the instant suit raises more than one substantial questions regarding interpretation of the Constitution, including:

(a) What is the true import and interpretation of the following expression contained in Article 131 of the Constitution: "*if and in so far as the dispute involves any question (whether of law or fact) on which the existence or extent of a legal right depends*"?

(b) Does Article 293 of the Constitution vest a State with an enforceable right to raise borrowing from the Union

government and/or other sources? If yes, to what extent such right can be regulated by the Union government?

(c) Can the borrowing by State-Owned Enterprises and liabilities arising out of the Public Account be included under the purview of Article 293(3) of the Constitution?

(d) What is the scope and extent of Judicial Review exercisable by this Court with respect to a fiscal policy, which is purportedly in conflict with the object and spirit of Article 293 of the Constitution?

8. Since Article 293 of the Constitution has not been so far the subject to any authoritative interpretation by this Court, in our considered opinion, the aforesaid questions squarely fall within the ambit of Article 145(3) of the Constitution. We, therefore, deem it appropriate to refer these questions for pronouncement by a Bench comprising five judges.

9. In addition, and as a necessary corollary to these questions, it appears that on merits also, various questions of significant importance impacting the Federal Structure of Governance as embedded in our Constitution, like, the following, arise for consideration*:*

(a) Is fiscal decentralization an aspect of Indian Federalism? If yes, do the Impugned Actions taken by the Defendant purportedly to maintain the fiscal health of the country violate such Principles of Federalism?

(b) Are the Impugned Actions violative of Article 14 of the Constitution on the ground of 'manifest arbitrariness' or on the basis of differential treatment meted out to the Plaintiff vis-à-vis other States?

(c) What has been the past practice regarding regulation of the Plaintiff's borrowing by the Defendant? If such practice has been restrictive of Plaintiff's borrowings, can it estop the Plaintiff from bringing the present suit? Conversely, if such practice has not been restrictive, can it serve as the basis for the Plaintiff's legitimate expectations against the Defendant - Union of India?

(d) Are the restrictions imposed by the Impugned Actions in conflict with the role assigned to the Reserve Bank of India as the public debt manager of the Plaintiff?

(e) Is it mandatory to have prior consultation with States for giving effect to the recommendations of Finance Commission?

10. The Registry is accordingly directed to place this matter before Hon'ble the Chief Justice of India for the constitution of an appropriate Bench to answer the aforementioned questions and/or such other issues as may be identified by the Five-Judge Bench.

11. We may now advert to the issue as to whether, pending the decision on the questions formulated above, the Plaintiff – State can be granted the ad-interim injunction as briefly noticed in paragraph 3 of this Order?

12. The globally acknowledged golden principles, collectively known as the Triple-Test, are followed by the Courts across the jurisdictions as the pre-requisites before a party can be mandatorily injuncted to do or to refrain from doing a particular thing. These three cardinal factors, that are deeply embedded in the Indian jurisprudence as well, are:

(a) A '*Prima facie* case', which necessitates that as per the material placed on record, the plaintiff is likely to succeed in the final determination of the case;

(b) 'Balance of convenience', such that the prejudice likely to be caused to the plaintiff due to rejection of the interim relief will be higher than the inconvenience that the defendant may face if the relief is so granted; and

(c) 'Irreparable injury', which means that if the relief is not granted, the plaintiff will face an irreversible injury that cannot be compensated in monetary terms.

13. At this juncture, it is necessary to distinguish the standard of scrutiny in applying these parameters for 'prohibitory' and 'mandatory' injunctions. Prohibitory injunctions vary from mandatory injunctions in terms of the nature of relief that is sought. While the former seeks to restrain the defendant from doing something, the latter compels the defendant to take a positive step.[1] For instance, hypothetically, in the context of a construction dispute, if a plaintiff seeks to prevent the defendant from demolishing a structure, it would be deemed a prohibitory injunction. Whereas, if a plaintiff wants to compel the defendant to demolish a structure, then this would amount to mandatory injunction.

[1] *State of Haryana v. State of Punjab*, (2004) 12 SCC 673, para 37-38.

14. In that sense, prohibitory injunctions are forward-looking, such that they seek to restrict a future course of action. Conversely, mandatory injunctions are backward-looking, because they require the defendant to take an active step and undo the past action.[2] Since mandatory injunctions require the defendant to take a positive action instead of merely being restrained from performing an act, they carry a graver risk of prejudice for the defendant if the final outcome subsequently turns out to be in its favour. For instance, in the example above, preventing the demolition of a structure for the time being cannot be perceived to be on the same pedestal as mandating the demolition of a construction. While the former may still be undone, i.e., the defendant may still be compelled to demolish the structure should the plaintiff succeeds in his final claim, undoing the latter, i.e., rebuilding the construction, would cause graver injustice. The Courts are, therefore, relatively more cautious in granting mandatory injunction as compared to prohibitory injunction and thus, require the plaintiff to establish a stronger case.[3]

15. Reverting to the facts of the case in hand, the Plaintiff – State has sought mandatory injunction and not a prohibitory one.

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[2] *Shepherd Homes Ltd. v. Sandham*, [1970] 3 WLR 348.
[3] *Id.*, *Dorab Cawasji Warden v. Coomi Sorab Warden*, (1990) 2 SCC 117, para 16.

Instead of arguing that the Defendant – Union of India should refrain from imposing a Net Borrowing Ceiling during the next F.Y., the Plaintiff has applied for a backward-looking injunction, i.e., for an injunction to undo the imposition of the Net Borrowing Ceiling that covered various liabilities and to restore the position that existed before such ceiling. Hence, the Plaintiff is required to meet a higher standard for the triple-test of interim relief as mentioned in paragraph 12 above of this order.

16. Coming to the first factor, i.e., the *prima facie* case, the Plaintiff – State has raised various substantive questions of constitutional interpretation. Generally speaking, the phrase '*prima facie* case' is not a term of art and it simply signifies that at first sight the plaintiff has a strong case. According to Webster's International Dictionary, '*prima facie* case' means a case established by '*prima facie* evidence', which in turn means the evidence that is sufficient in law to raise a presumption of fact unless rebutted.

17. The Plaintiff – State has argued that based on the States Finance Accounts audited by the Comptroller and Auditor General of India and the achievements of the fiscal deficit targets, the Plaintiff – State has under-utilized permissible borrowing space in

the last three F.Ys. (2020-21, 2021-22 and 2022-23) to the extent of INR 24,434 crores. The Plaintiff – State contends that even going by the stand of the Union, the under-utilized space of the Plaintiff for the said period borrowings is INR 10,722 crores, which it should be allowed to borrow.

18. Mr. Kapil Sibal, learned Senior Counsel for the Plaintiff – State, submitted that under the recommendations of the 15th Finance Commission, the State is entitled to borrow up to the maximum permissible fiscal deficit for the year. He relied on paragraphs 12.64 and 12.65 of the Report of the 15th Finance Commission, which read as under:

> ***"12.64 If a State is not able to fully utilise its sanctioned borrowing limit, as specified above, in any particular year during the first four years of our award period (2021-22 to 2024 - 25), it will have the option of availing this unutilised borrowing amount (calculated in rupees) in any of the subsequent years within our award period.***
>
> *12.65 Based on these assumptions, we have worked out the debt path for States, as presented in Table 12.4. Since all estimated revenue deficits are met by equivalent provision of revenue deficit grant, the revenue surpluses run by the States are reflected by the negative numbers on revenue deficit presented in the table. The State debt in aggregate tapers off gradually after 2022-23. This is similar to the pattern in the debt path of the Union shown in Table 12.2. The State-specific indicative debt paths are given in Annex 12.1.*

Table 12.4: Indicative Deficit and Debt Path for State Governments

(% of GSDP)

	2020-21	***2021-22***	***2022-23***	***2023-24***	***2024-25***	***2025-26***
*Revenue deficit**	*-0.1*	*-0.5*	*-0.8*	*-1.2*	*-1.7*	*-2.5*
Fiscal deficit	*4.5*	*4.0*	*3.5*	*3.0*	*3.0*	*3.0*
Total liabilities	*33.1*	*32.6*	*33.3*	*33.1*	*32.8*	*32.5*

**negative values indicate surplus and positive values indicate deficit*

Note: While arriving at the total liabilities of States for the year 2021-22, an aggregate fiscal deficit of 3.5 per cent of GSDP is taken because some States may not avail of the full unconditional net borrowing space of 4 per cent."

19. According to the learned Senior Counsel, since the fiscal deficit for 2023-24 is 3% of GSDP, they should be allowed the full borrowing without any restrictions.

20. Mr. N. Venkataraman, learned ASG, controverted the submission of the Plaintiff – State. According to learned ASG, while the figures as projected by the State are themselves in dispute, the State is not entitled to borrow the amounts as claimed since the over-borrowing by the State of Kerala from F.Ys. 2016-17 to 2019-20 is INR 14,479 crores. According to him, if these over-borrowings are factored in the borrowing space, it will be found that the State has not under-utilized but over-utilized its borrowing capacity by INR 2,941.82 crores till F.Y. 2022-23. The

learned ASG, relying on paragraph 14.64 of the Report of the 14th Finance Commission, contended that if the State is not able to fully utilize its sanctioned borrowings limit of 3% of GSDP in any particular year during the first four years of the award period (2015-16 to 2018-19), the State will have the option of availing this un-utilized borrowing amount (calculated in Rupees) only in the following year within the award period. However, there is a difference between under-utilization of the borrowing limit and over-utilization of the borrowing limit. Learned ASG maintained that over-utilization is dealt with in Annexure 14.2 of Chapter-XIV in the Report of the 14th Finance Commission, which clearly prescribes as under:

> "***Case II. Over-utilizing the borrowing amount****:*
>
> *If a State, in a given year, borrows over and above the sanctioned borrowing limit by x amount, then in the succeeding year, the same x amount of the previous year will be deducted from the States borrowing limit of that year*."

21. According to learned ASG, the Plaintiff – State is wrong in contending that such deduction in the succeeding year can only be made within the award period of the 14th Finance Commission. He explained that over-borrowings of the previous year were adjusted for the F.Ys. 2021-22, 2022-23 and 2023-24 (as on date)

to the tune of INR 9,197.15 crores, INR 13,067.78 crores and INR 4,354.72 crores respectively. According to learned ASG, the State was fully conscious of the correct position in law and had rightly acquiesced in the adjustments of the over-borrowings. Having acquiesced, it does not lie in the mouth of the Plaintiff – State to contend that once the period for the 15th Finance Commission has set in from F.Ys. 2021-22 to 2025-26, the over-borrowings of the previous years have absolutely no relevance. Learned ASG vehemently argued that the Plaintiff is wrong in contending that a reading of the report of the 14th and 15th Finance Commission indicates that for both under-utilization and over-utilization, all adjustments have to be made within the period covered by the Report of the Commission.

22. *Prima facie*, we are inclined to accept the argument of the Union that where there is over-utilization of the borrowing limit in the previous year, to the extent of over-borrowing, deductions are permissible in the succeeding year, even beyond the award period of the 14th Finance Commission. This is, however, a matter which will have to be finally decided in the suit.

23. At this stage, based on the contentions of the Plaintiff – State with which we are not *prima facie* convinced, permitting any

borrowing—whether INR 24,434 crores as claimed in the written note or INR 10,722 crores as alternatively claimed—would not be tenable.

24. In fact, it has been admitted by the Plaintiff – State that there has been over-borrowing/over-utilization of the borrowing limit between the F.Ys. 2017-18 and 2019-20. It is not denied that if, as contended by the Union, such over-borrowings are adjustable in the succeeding years, then the State has already exhausted its borrowing limits for the F.Y. 2023-24.

25. We find, *prima facie*, that there is a difference in the mechanism which operates when there is under-utilization of borrowing and when there is over-utilization of borrowing. The Plaintiff – State has not been able to demonstrate at this stage that even after adjusting the over-borrowings of the previous year, there is fiscal space to borrow.

26. Our attention has also been invited to the Kerala Fiscal Responsibility Act, 2003. The Act is enacted to provide for the responsibility of the government to ensure prudence in fiscal management and fiscal stability by progressive elimination of revenue deficit and sustainable debt management consistent with fiscal stability, greater transparency in fiscal operations of the

government and conduct of fiscal policy in a medium term fiscal framework and for matters connected there with and incidental thereto. The Preamble of the Act also states that it was felt expedient to provide for the responsibility of the government to ensure prudence in fiscal management and fiscal stability by progressive elimination of revenue deficit and sustainable debt management consistent with fiscal stability.

27. In view of above, we find *prima facie* merit in the submission of the Union of India that after inclusion of off budget borrowing for F.Y. 2022-23 and adjustments for over-borrowing of past years, the State has no unutilized fiscal space and that the State has over-utilized its fiscal space. Hence, we are unable to accept the argument of the Plaintiff at the interim stage that there is fiscal space of unutilized borrowing of either INR 10,722 crores as was orally prayed during the hearing or INR 24,434 Crores which was the borrowing claimed in the negotiations with the Union.

28. Therefore, the Plaintiff – State has failed to establish a *prima facie* case regarding its contention on under-utilization of borrowing. Further, with respect to its other contentions, while the Plaintiff has sought to construe Article 293 restrictively to limit the Central government's power only to the loans granted by it, the

Defendant has contended that if Article 293 is read in such a manner, it would render this provision redundant as the Central Government has an inherent power as a lender to impose conditions on such loans even in the absence of any express constitutional provision. Similarly, the Defendant has contested the Plaintiff's narrow reading of the term 'borrowing' and has argued that off-budget borrowings could also be included in the same if they are used to by-pass the conditions imposed under Article 293 of the Constitution.

29. Since this Article has not been the subject of an authoritative pronouncement of this Court so far, we cannot readily accept the Plaintiff's contention over the Defendant's interpretation by taking it on face value. In this regard, we have referred the matter to a larger bench of five judges, as mentioned in paragraph 10 of this order.

30. Hence, on consideration of the limited material available on record so far, the Plaintiff – State has not established a *prima facie* case to the extent required in the instant suit.

31. With respect to the second prong for claiming the interim relief, the Plaintiff – State has argued that if the interim injunction is not granted, it is likely to face extreme financial hardship on

account of its pending dues. As against this, the Defendant – Union of India has highlighted the grave consequences regarding the fiscal health of the country if the Plaintiff is allowed the interim relief. The Union of India has argued that additional borrowing by the State will have spill-over effects and may raise the prices of borrowing in the market, possibly crowding out the borrowing by private investors. This may then have an adverse impact on the production of goods and services in the market, possibly affecting the economic well-being of every citizen. Since the Central government borrows money from outside the country and lends money to the State governments, borrowings of the States are intricately linked to the creditworthiness of the country in the international market. Hence, the Union of India argued that in case such borrowings by State Governments are not regulated, it may negatively impact the macro-economic growth and stability of the entire nation.

32. On a comparative evaluation of the submissions, it seems to us that the mischief that is likely to ensue in the event of granting the interim relief, will be far greater than rejecting the same. If we grant the interim injunction and the suit is eventually dismissed, turning back the adverse effects on the entire nation at such a

large scale would be nearly impossible. *Au contraire*, if the interim relief is declined at this stage and the Plaintiff - State succeeds subsequently in the final outcome of the suit, it can still pay the pending dues, may be with some added burden, which can be suitably passed on the judgment - debtor. The balance of convenience, thus, clearly lies in favour of the Defendant – Union of India.

33. Finally, as regards to the third pre-condition, we find that the Plaintiff – State has sought to equate 'financial hardship' with 'irreparable injury'. It appears *prima facie* that 'monetary damage' is not an irreparable loss, as the Court can always balance the equities in its final outcome by ensuring that pending claims are adjusted along with resultant additional liability on the opposite party.

34. We may hasten to remind ourselves at this stage that according to the Defendant-Union of India, the Plaintiff – State is apparently a highly debt stressed State that has mismanaged its finances. This statement, however, is strongly refuted by the State. According to the Union, the Plaintiff has the highest ratio of Pension to Total Revenue Expenditure among all States and requires urgent measures to reduce its expenditure. Instead of

doing so, the Plaintiff is borrowing more funds to meet its day-to-day expenses such as salaries and pensions. Accordingly, the Defendant has contended that the financial hardship is not attributable to the regulation of Plaintiff's borrowing and is actually a consequence of its own actions. Furthermore, the Defendant maintains that restriction on the borrowing is a step towards the betterment of fiscal health of the State because if such borrowings are not restricted, the Plaintiff's position will become more precarious, leading to a vicious cycle of deteriorating financial health and increased borrowing to repair the same.

35. If the State has essentially created financial hardship because of its own financial mismanagement, such hardship cannot be held to be an irreparable injury that would necessitate an interim relief against Union. There is an arguable point that if we were to issue interim mandatory injunction in such like cases, it might set a bad precedent in law that would enable the States to flout fiscal policies and still successfully claim additional borrowings.

36. In any case, we cannot be oblivious of the fact that in light of the Plaintiff's contention regarding pending financial dues, the Defendant has already made an offer to allow additional borrowing.

In a meeting dated 15.02.2024, the Defendant first offered consent for INR 13,608 crores, out of which INR 11,731 crore was subject to the pre-requisite of withdrawal of the suit, a condition that we disapproved of. Subsequently, in a meeting dated 08.03.2024, the Union offered a consent for INR 5,000 crores. Further, vide circulars dated 08.03.2024 and 19.03.2024, the Union has accorded consent for INR 8,742 crores and INR 4,866 crores respectively, which comes to a sum total of INR 13,608 crores. Even if we assume that the financial hardship of the Plaintiff is partly a result of the Defendant's Regulations, during the course of hearing this interim application, the concern has been assuaged by the Defendant – Union of India to some extent so as to bail out the Plaintiff – State from the current crisis. The Plaintiff thus has secured substantial relief during the pendency of this interim application.

37. To sum up, we are of the view that since the Plaintiff – State has failed to establish the three prongs of proving *prima facie* case, balance of convenience and irreparable injury, State of Kerala is not entitled to the interim injunction, as prayed for.

38. In light of the above observations, I.A. No. 6149 of 2024 is disposed off.

39. It is clarified that the observations made hereinabove are for the limited purpose of deciding the prayer for ad-interim injunction and shall have no bearing on the final outcome of the Original Suit.

40. The main case be placed before Hon'ble the Chief Justice of India for constitution of an appropriate Bench.

..... J.
(SURYA KANT)

..... J.
(K.V. VISWANATHAN)

NEW DELHI

DATED: 01.04.2024