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GOVERNMENT CONTROL OF COMPANIES

by

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The Companies Act, 1956 abounds in Government control. They are there for various reasons which could of course be explained; but at the outset one would be amazed by the number, variety and extent of them. There are about 296 provisions in the Companies Act vesting the Government with several sorts of powers. If sub-divided, there are 42 cases where the company management has to approach the Government for approval or permission, such as, for change of company's name, for appointment and remuneration of managerial personnel, for loans, investments, for issue of share warrants payable to bearer, for conversion of a public company into a private one and so on. There are 47 things which the Government can order, require, enquire or authorise for, for example, power to order special audit, cost audit, investigation, inspection, search, enquiry and what not. There are then 9 cases in which the Government can declare or notify a certain thing for example, declaring an unit to be a branch, to notify which are recognised stock-exchanges, to notify what are the qualifications for the professional services rendred by a director and so on. There are 23 provisions under which the Government has power to grant exemptions or affect modifications. In 5 cases the Government has been empowered to grant extensions for various purposes; under 12 provisions it has power to frame and prescribe rules and forms; in 6 cases it has power to make appointments; in yet another 6 cases it has right to be heard by Court or receive notices etc. and under 3 sections it has power to delegate. The list is not yet over. There are about 85 other provisions in the Act empowering Registrar of Companies to exercise all sorts of powers over companies. Lastly, there are about 58 kinds of returns, documents, forms or notices which are required to be filed with the Registrar. These controls total upto two hundred and ninety six. (Details given in a Separate Appendix).

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On these premises the first question-and anybody would naturally ask that- would be- why so many controls ? Do the corresponding laws in other countries have them as well ? Does our country wish to control the companies more than the others ? I would try to give my answer to these questions in the following words.

It is a universally acknowledged fact that the harbinger of company legislation in the world was the famous Bubble Act of 1720, which was passed by the British Parliament to arrest speculative and fraudulent company formations. If that be the strating point of company legislation, one may feel that the need for public protection came first than the protection of the shareholder himself. The fact that the shareholder has limited liability in loss and unlimited scope of sharing in profits led further to the need of public protection. But when the size of the companies grew and a wide gap between the management and the shareholders developed, the question of protection of the interest of the shareholder himself came up. Then the further growth of corporations and their increasing dependence on outside agencies for their finance brought in the question of protection of creditors' interests. In course of time, the companies wielded so much influence and power over the market and the community, that the questions of protection of interests of consumers and the community came in. Next came the question of protecting the interest of employees, State and what not. To-day it is universally accepted that a company is not only responsible to its shareholders but is also towards its employees, creditors, consumers, community and State. According to the Declaration adopted at the International Seminar on Social Responsibilities of Business, held in 1965 in Delhi, a corporation is a citizen. "Like a citizen, it is esteemed and judged by its actions in relation to the community of which it is a member as well as by its economic performance".

This burgeoning responsibility of a company really called for certain safeguards for all those factions to whom the company owes its responsibility. Thus came the Government Control. It must however be remembered here that Government control is not the only agency to provide these safeguards; it is only the last one to step in. I/aforesaid interests over the agency of Government Control. These are:

(1) Self-control, viz., voluntary assumption to social responsibility.

(2) Inner Controls, viz., some built-in-safeguards in the Company Law itself.

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I shall give ~~priority to the~~ following three agencies to safeguard the

3. Outer Controls, viz., the pressures of outside agencies like the like the press, consumers' stock exchanges and so on;

In case all these three agencies of safeguards are absent or inadequate or ineffective the fourth agency, namely, the State control is allowed to play its role. Now, I shall explain in brief the role being played by the earlier three agencies of safeguards in international corporate scenes with reference to the increasing inroad of the fourth agency in our own country.

(1) <u>Self-Control:</u>

The best example of self-control and discharge of social responsibilities by companies is that of the U.S.A.

A recent survey by the National Industrial Conference Board of America provides confirming evidence of a trend that has been evident for some time: The nation's leading corporations consider public affairs to be an important responsibility of management. Over 80 per cent of the more than 1,000 firms surveyed had a public affairs function, embracing such activities as relations with legislators, political and economic education, community relations, and corporate philanthropy. The top issues that the companies regarded as 'urgent' were inflation, taxation, and labour relations; near the top came a host of socio-economic problems, including air and water pollution, poverty, civil rights, and urban renewal. Only a small minority of the companies said it was not their business to solve the nation's problems but simply to produce and sell goods.

The other example in this regard may be given of Dutch companies. They fix prices of their products in Government consultation and make voluntary extra annual payments to their employees if the business has gone well, since they feel it right and proper that the employees should have some share in the results. The employees are also encouraged to participate in companies' share capital.

(2) <u>Inner Controls:</u>

The best examples of inner controls, according to me, are the company laws of Germany and Italy. Under the German company law system, there are dual Boards-one executive and the other supervisory. This supervisory Board largely consists of representatives of employees, consumers and the

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community which decide on broad policy matters of the company, Furthermore, the German banks have been very generally successful in carrying out their task of acting as shareholders' proxies in such a way as to achieve a satisfactory balance of interests. The shareholders enjoy a right of appropriating 50% of the profits made by the company in any manner they think fit without depending on the directors' recommendation.

In Italy, the shareholders have the right with 1/5th minority only to apply to the Court against irregular management as opposed to "mismanagement and oppression" in India which is very difficult to prove. The same percentage of shareholders who are for all purposes nothing but a minority can also ask the directors to discuss their liability to the company in the general meeting. Any single shareholder in Italy/right to appeal against the decision of the company and so on.

(3) Outer Controls:

Examples of outer controls are available almost in every developed country. In the U.S.A. the Securities Stock Exchange and Stockholders Associations exercise a great amount of influence over companies. In the U.K. particularly, the influence of press and consumers' associations is well known. In France, the public consciousness plays a big role in dissuading company managements from resorting to malpractices.

(4) Government Control and India:

In our country, although we do have something of each of the aforesaid three agencies, they are not in adequate measure; whereas the fourth agency, viz., the Government Control, which has come since the other three are lacking, is in excessive measure. In a way, I would liken our system of company law to a kind of brew, where every thing of the world is present. Unfortunately this brew is not tasteful. Too much of Government control has acted like an extra dose of salt. The nutritive contents of self control, inner control, and outer control is disproportionately less. This, perhaps, is not the fault of the cook who prepared it since he had to manage with the materials made available to him. He did not find the nutritive ingredients of self control, inner and outer controls available in the market in the desired quantities; he however prepared the prescribed quantity which had to be kept up by

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making up the deficiency by putting in excessive salty doses of Government control, which was available in abundant supply.

Joke apart, a stage has now come when the Government itself is seeking ways to reduce the quantum of Government control over companies provided the real safeguards for those sections of society which are concerned with the working of companies are provided by other agencies. (For some detailed suggestions in this regard, reference may be made to the author's article in the Annual Special Number of Capital published this year). Some broad suggestions are being made here for consideration in this respect.

For self-control and voluntary discharge of social responsibilities by companies, I would suggest that the recommendations made by the Study Group on Social Responsibilities of Business set up in Calcutta under the Chairmanship of Hon'ble Mr. Justice P.B. Mukharjee should receive close consideration by trade and industry. The said Report is being published by Oxford & IBH publishing Co. and will be available shortly.

For inner controls, my foremost suggestion would be the participation of greater and greater number of shareholders in company management. This could be achieved in more than one ways. The first is by providing for proportional representation of the shareholders on the company's Board so that at least a minority of 10%, if it so decides, can appoint a director on the Board. The second alternate, is based on the feeling as expressed by Mr. Folkert Wilken, in his small book "New Forms of Ownership in Industry", that the power of 51% to exclusively control the destiny of the company is too great a power. I would suggest that the majority decisions of a company taken in its general meetings should be considered to have been taken only if they have been taken by 70% majority in place of only 51% as at present, and special resolution should require 90% majority in place of 75% as at present.

<u>Companies Appellate Tribunal:</u>

I would also venture to suggest the formation of Companies Appellate Tribunal, not of the type which has recently been buried. The previous Tribunal was meant for exercising certain powers formerly being exercised by the Court. This Appellate Tribunal which I am suggesting is for completely different purpose. This is for prefering

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appeal by a company on any decision of the Government on the application made to it for approval, which according to the company might have been wrongly rejected. This Tribunal should also enable a given minority, say 10%, to appeal against any decision made by a company in its general meeting by majority.

Outer Controls:

For the outer controls, I would suggest the building up of a healthy independent press, formation of uninfluenceable shareholders associations, formation of consumer resistance committees and strengthening of the independence of the stock exchanges in the country.

Till these agencies begin to work, Government controls seem inevitable. But in exercising these controls, the Government Officials have to act in a very responsible manner. By saying so I do not mean that they are not doing so at present but what I mean to say is to stress the point that on the one hand, they have to effectively enforce the control; while on the other, they have not to onstruct the working freedom of companies without any purpose being served.

APPENDIX

Government powers under various Sections of the Companies Act, 1956.

1. Power to approve, permit: (1) 21, (2) 31, (3) 43A(4) (4) 79, (5) 81(1A), (6) 81(3), (7) 114(1), (8) 149(2B), (9) 198, (10) 204, (11) 208, (12) 259, (13) 268, (14) 269, (15) 2 ∠ (17) 295, (18) 309(3), (19) 309(4), (20) 309(5B), (21) 310, (22) 311, (23) 316, (24) 326, (25) 328, (26) 343, (27) 345, (28) 346, (29) 352, (30) 360(1), (31) 363, (32) 370(1) & (2), (33) 372, (34) 373, (35) 386, (36) 387, (37) 388E(3), (38) 388E(5), (39) 396A, (40) 549, (41) 572, (42) 637A.

2. Power to order, require, enquire or authorise for: (1) 22, (2) 81(4), (3) 167, (4) 209(1), (5) 209(4), (6) 227(4A), (7) 233A, (8) 233B, (9) 235, (10) 236, (11) 237, (12) 239, (13) 240(1A), (14) 246(2), (15) 241, (16) 242, (17) 243, (18) 244, (19) 245, (20) 247, (21) 248, (22) 249, (23) 250, (24) 276, (25) 294(5), (26) 307(6), (27) 332, (28) 347, (29) 388B, (30) 388C, (31) 388E(1), (32) 396, (33) 399, (34) 400, (35) 401, (36) 408, (37) 409, (38) 439, (39) 439(5E), (40) 463(1) & (2), (41) 534, (42) 545 (3), (43) 550, (44) 610, (45) 615(1), (46) 621(1), (47) 624B.

3. Power to declare or notify: (1) 2(9), (2) 2(39), (3) 10, (4) 20, (5) 309(1), (6) 324, (7) 349(1) & (4), (8) 369, (9) 410.

4. Power to exempt, rectify or modify: (1) 25, (2) 43A, (3) 89, (4) 108(1C), (5) 158 (3)(a), (6) 166, (7) 205, (8) 211(4), (9) 212, (10) 228, (11) 274, (12) 283, (13) 285, (14) 300, (15) 385(1), (16) 551, (17) 578, (18) 594, (19) 613, (20) 620A, (21) 620B, (22) 637B, (23) 641.

5. Power to extend: (1) 108(1D), (2) 213, (3) 370A, (4) 496, (5) 508(1).

6. Power to frame and prescribe rules & forms: (1) 108(1A), (2) 130, (3) 131, (4) 163, (5) 170, (6) 226, (7) 503(5), (8) 553(1), (9) 635B(3), (10) 640B, (11) 642(1), (12) 647.

7. Power to make appointments: (1) 153A, (2) 224, (3) 408, (4) 448(1A), (5) 609, (6) 624A.

8. Power to be heard, to receive etc.: (1) 394A, (2) 407, (3) 451(2), (4) 530(1), (5) 555, (6) 612.

9. Power to delegate: (1) 10E, (2) 10E(4A), (3) 637(1).

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∠ (16) 293B,

10. Registrar's power, rights etc.: (1) 17(4), (2) 18(1)
3. 18(3), (4) 23(1), (5) 23(2), (6) 24(1), (7) 25(7),
(8) 32(2), (9) 33(2), (10) 34(1), (11) 43A(1), (12) 43A(2),
(13) 52, (14) 60(3), (15) 75, (16) 627, (17) 95(2), (18) 9
(19) 103(1), (20) 103(4), (21) 125(1), (22) 130(1), (23) 1
(2), (24) 131, (25) 132, (26) 134(1), (27) 137(1), (28) 13
(29) 138(2), (30) 138(3), ∠(37) 150(1), (38) 166(1), (39) 19
(1), (40) 209(1), (41) 209(4)(b), (42) 209(4)(c)(1)& (2),
(43) 209(4)(d)(i) & (ii), (44) 210(4), (45) 220, (46) 224(1
(47) 234(1), (48) 234(3A), (49) 234(6), (50) 234(7), (51) 2
(52) 264(1), (53) 276, (54) 306, (55) 307(5)(6), (56) 394(1
(57) 395(4A)(a)(iv), (58) 439(5), (59) 444, (60) 445(2),
(61) 431(2), (62) 497(5)/509(5), (63) 515(3), (64) 516(1),
(65) 524(4), (66) 545(3), (67) 545(4), (68) 545(6), (69) 515
(70) 553(2)(a), (71) 556, (72) 559(2), (73) 560(1), (74) 570
(75) 574, (76) 579(2), (77) 597(1)(2), (78) 597(3), (79) 610
(80) 611, (81) 614, (82) 621(1),

11. Filing of returns, documents forms or notices etc. with the Registerer: (1) 18(1) & (3), (2) 31(2A), (3) 33(1) & (2),
(4) 43A(2), (5) 43A(8), (6) 44(1), (7) 60(1), (8) 70(1),
(9) 75(1), (10) 76(1), (11) 76(1)(v), (12) 95(1), (13) 97,
(14) 103(1), (15) 107(5), (16) 125(1), (17) 127(1), (18) 128,
(19) 129, (20) 135, (21) 137(1), (22) 137(2), (23) 138(1),
(24) 146(2), (25) 149(1), (26) 149(2), (27) 149(2A), (28) 156
(29) 157(2), (30) 159,160, & 161, (31) 165(5), (32) 192(1),
(33) 209(1), (34) 220(1), (35) 264(1), (36) 266, (37) 267(1),
(38) 303(2), (39) 391(3), (40) 394(3), (41) 395(4A)(iii),
(42) 404(3), (43) 421, (44) 445(1), (45) 462(4), (46) 466(3),
(47) 481(2), (48) 488(2), (49) 499: (50) 497(3)and 509(3),
(51) 501(1), (52) 516(1), (53) 518(5), (54) 551(1) & 551(2),
(55) 555(6), (56) 559(2), (57) 567, (58) 568.

∠(31) 138(4), (32) 138(1), (33) 139, (34) 140, (35) 146, (36) 149(3)