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Demarcation of Power between the Centre and the States- The Indian context

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by

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The Context of Government control over private enterprise in India raises very interesting issues as regards the distribution of power between the Centre and the State, and in some ways, the fundamentals of federalism in this country. Some of the issues that have come into larger focus during the last few years could hardly have been anticipated by the framers of the Indian Constitution. In some other aspects everybody seems to have been caught unawares. To a student, these issues and the debate on them have provided a rich ground for learning. The purpose of this paper is to raise certain points with respect to the position and role of the Centre and the States in exercising control over private interpretation of the provisions in the Indian Constitution.

Features

The characteristic features of Indian federalism with particular respect to the exercise of control over private enterprise, are that as it has evolved over years. The States themselves do not appear to have much say in view of the fact:

- a. "Industries declared by Parliament by law to be necessary for the purpose of defence or for the prosecution of war". (Entry 7 in the Union List);
- b. "Industries, the control of which by the Union is declared by Parliament by law to be expedient in the public interest". (Entry 52 in the Union List);
- c. Inter-State trade or commerce, incorporation, regulation and winding up of trading or non-trading corporations, including banking and insurance and other financial corporations;
- d. Import and export trade;
- e. High-yielding, elastic varieties of direct and indirect taxes only a portion of which go back to the coffers of the States via the Finance Commission awards;

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f. Foreign exchange, its earning, regulation and disbursement are matters of Central jurisdiction and almost everything that the private sector enterprises are concerned with are covered by the list. The activities of the States relate only to be a fringe of their activities.

The framers of the Indian Constitution anticipated the building up of a strong Government at the Centre and the States were supposed to be acting on the periphery. The changes noticed during the last few years have given this base quite a serious jolt. The entire basis calls for reconsideration, despite the probe by the Administrative Reforms Commission. The peculiarities of the Indian political phenomenon require tackling the issues in formal frames of analysis, which have to be developed indigenously in view of there being almost no precedent in any other country exactly comparable to what we have witnessed here. Political observers and commentators have seen in these changes various trends and portents but it seems only a few of them have felt encouraged by the switches and shifts that have taken place. In the specific context of control of private enterprise this paper makes an attempt to take note of some of these changes and to suggest that all this is not discouraging but our ways would have to be mended not only to sponsor and nurture the dispersal of power centres to the States but also to see to their keeping centripetal to the overall national interest.

The Indian federalism has been centred on making the Federal Government strong that has as its overall objective of stressing the unity of the country. This unity has not always been a conscious one resulting from the States' subscribing to a common objective. The local problems of each State have been so many and of such diverse magnitude that the major part of the attention of the States has gone into setting these matters right. The one party Government at the Centre and the States considerably hid some of these problems through the mechanism of the party organisation. With the emergence of non-Congress Governments in some of the States, the informal attempts to forge unity through the party organisation came under severe constraints. As yet no effective alternative to this has been found. On such a finding will, however, depend much as to what shape the Indian federation takes on what formal substitutes are evolved for bringing the States to a common platform of understanding and exchange of experience. Private enterprises and its control offer an illustration as to what the positive role of the States can be, vis-a-vis what it has remained all these years.

Private Enterprise

The organised sector of the private enterprises in this country has been in the purview of the Centre. This relates to establishment, running and earnings almost in toto. Let us take the case of companies. There are at present some 27000 such companies functioning in India, including both private and public limited companies. These companies are administered by the Indian Companies Act which is a Central legislation. The firms and unitary concerns are also subject to various degrees of Central control depending on their lines of activities. Banking and Insurance companies are also matters of exclusive Central control. The States

have almost no motivation in regard to their development and functioning. The benefits that arise to the States out of the functioning of these enterprises are in most cases indirect and marginal if not altogether absent. This has been partially met in cases where the States themselves have established such enterprises or otherwise participated in the share capital of private enterprise. The extent of State participation in the various productive activities is grossly inadequate to create any visible impact. It is from this point of view that the subject chosen for the Seminar is very significant and timely.

In regard to exercise of control over the employment; choice of product and product-mix; size; location; and form of enterprise, whether companies, firms or unitary concerns; and the pattern, doses and size of investment, as also the prices and the return on the capital invested, the role of the States is rather small and unimportant. This would require some detailed explanation, particularly in the context of the noticeable indifference to such activities of the private sector. The States have remained powerless in some of the crucial questions in this respect. In some respects, even the Centre has not been able to do much. It is proposed to deal with the above points in the same serial order.

Employment

In many of the States, the pressure of people migrating from other States has grown into alarming proportions. Desirability of such large scale migration would depend on several factors. In matters of private sector employment, it is in very few cases that recruitments are based purely on what is called merit. The entrepreneurs coming from other States not only bring their funds with them but also their own people whom they can trust and in whom they can confide. In some of the enterprises in some States, not only are the key positions manned by people brought from the entrepreneurs' own loyalty groups but also those at the lower levels of hierarchy, in which cases people from other areas are given preference. The employment benefits from such industrialisation from the point of view of the States have been negligible in many cases. On the other hand, such enterprises have invariably created tremendous pressures on the available infra-structure, housing and consumption. In an essentially non-affluent area, the large income differentials, between these people and the local people, create all kinds of tension a large part of which could be avoided. The States get from such enterprises only such fringe benefits as sales tax and other local taxes from their activities. The States do not in any other way participate in their profits.

The taxes on income of such enterprises are collected by the Centre and the States get only such share of the total collection of these taxes all over the country as are awarded to them by the Finance Commission from time to time. The rationale of the Finance Commissions awards is not doubted here. What is being argued is that the motivation of the States towards industrialisation under private initiative is not adequate in this

respect, particularly because such awards are not exclusively based on collection of such taxes. The corporation tax is, however, a Central jurisdiction exclusively.

The influence of the States on the choice of product and product-mix is not quite adequate. While such choices are based on the availability of the productive factors, the discretion is almost exclusively of the private entrepreneurs, so that the States themselves have not been in a position to regulate overcrowding in particular lines of activities, except to a relatively small extent. Thus the States have not always been in a position to direct their economic efforts in a way that would reduce their dependence on other States. Any question related to inter-State activity would involve the Centre. In a very large measure the private enterprise activity has resulted in augmenting the power exercised by the States. While the resources available to the States for organised exploitation may have been considerable, the benefits accruing to the States themselves from such resources have been doubtful.

Size Economies

In the context of size, the trends in this country have been quite interesting. While all the banes of large scale have accrued to the private sector, the benefits of large scale have not generally arisen. This is partly because of the fact that the size-economies particularly of production are invariably linked up with the individual plants, the size of which has been generally small. On the other hand, the banes of large scale have resulted from the scattered nature of the production units, even in those cases where the size of the establishment in the sense of the controlling unit has been large. It is in this situation perhaps that one may look askance at the proposition of the there being monopoly power accumulating side by side with the small size units. The overall picture is that most Indian private sector enterprises are small scale ones, in the corporate sector as well as outside. The States themselves have not been able to do anything substantial in this respect and the Centre has never taken the problem quite seriously. In particular industries, however, there have been official direction in favour of formation of public limited companies, such as manufacture of cement. Inter-State activity of private enterprises has resulted in extending areas of Central control while it has hardly looked to the interest of proper development of the areas in which such activities have been organised. Lack of local motivation has not only made the State governments but also the people of the area relatively uninterested. These observations are true in cases where the head office is in one State and the plant activity falls in another, the markets are in States other than that in which production takes place; and the employees come from other States. In addition, the direction and doses of investment under the private initiative have been matters in which the States have been asked to help with funds and facilities but their regulatory powers have been limited. The incentives and attractions offered by States for larger activities in

in desired lines have not been accorded the kind of response that the States had in view. In a rather desperate way many States therefore had to start enterprises in those lines in which activities were desired to be organised on a larger scale. This most States did by establishing enterprises which were public limited companies, so that there could be more and more public participation. Incidentally, while most public sector enterprises organised as joint stock companies are private limited companies, of those that are public limited a larger number are under the control of States than that under the Centre.

The prices and the return on capital employed have remained issues under sharp public focus. The prices charged by the private entrepreneurs have looked more to the question of immediate profit than any other question. The States have not so far had much of a say in this matter. The availability of goods in the areas where goods are produced has been subject to the level of prices ruling in them. As such, when the area has been poor and not in a position to absorb all the goods offered, the benefit in the form of supply of goods has not accrued to the local areas. The profit motive being there, the entrepreneurs have not cared to cater for local consumption. Outside employment coupled with higher prices have serious repercussions on the local markets both directly and indirectly. The pressure on consumption being pushed up, the cost of living in the area has also gone up. In the circumstances, the States desirous of having something done in this respect have found their going very difficult.

Exports

Similarly, adequate motivations have not been created for the States to boost up exports, maximise foreign exchange earnings and strengthen themselves financially because all these are matters of Central control. Lack of adequate motivation in these vital matters has resulted in two types of consequences. First, exercise of control over these large and widely scattered areas has resulted in uncalled for expansion in the Central Secretariat and its suburbs as well as control agencies created for the purpose. Secondly, the control actually exercised has not been of the kind necessary. The States have played the role of spectators in this process and have faced criticisms for not doing much in these directions. Many of these States have now started export corporations for getting those very benefits which accrue to the private entrepreneurs on exporting under various export promotion schemes. This is a recent development in this country. Apart from addition to the total export effort put in, this kind of direct participation has augmented the States' discretion to spend foreign exchange in the same way as it does in the case of private exporters. The control of such effort even when the States are participating directly is with the Centre. A better alternative could perhaps have been to allocate foreign exchange to the States on the basis of total foreign exchange earnings of the States. Devolution in this respect would seem to be desirable to allow each State to have an effective economic plan without the Centre having to play the role of arbiter as it has been doing.

Demarcation of power to control the activities of private enterprises between the Centre and the States can hardly be real without extending the power of the States over the joint stock companies. The Administrative Reforms Commission has suggested the decentralisation of power among the Regional Directorates with regard to the functions of inspection and investigation. It is necessary to consider in this respect whether the Central authority should be reorganised as a federative body with effective powers transferred to the States to exercise control over the corporate sector within each State. This would require creation of adequate administrative machinery in each State and the Regional Directorates can in such cases be organised as coordinating agencies. The overall control may rest with the Centre but the administrative control devolving on the States, the unequal distribution of corporate bodies over the States and different areas within each State resulting in indiscriminate concentration of corporate activity in particular areas. Decentralisation of control should also apply to the banks and other corporate bodies to take care of different rather centrifugal tendencies, such as deposits generated in one area being unduly channelised in other areas.

(The issues raised in this paper, it may be submitted here, comprise the other side of the coin on the issue of federalism. It is not necessary that all the alternatives suggested here would be acceptable. But that much serious thinking has not gone into these questions is a fact and that this august gathering should devote some time to a consideration of these issues is a submission that is made with all earnestness.)
