

## SOME QUESTIONS REGARDING CORPORATE STRUCTURE

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Over a course of time the idea of property has been changing. As Prof. Freund says.

To Locke whom we owe the 'life, liberty and property' of the Constitution, the idea of property was doubtless an extension of human, personality, comprising the fruits of ones labour, the tools of ones trade, and the household goods and lands with which one was surrounded. Property consisted of 'belonging' in an intimate sense. Today property has been largely dehumanised. Much of it by the French '*Société's anonymes*'. The property of the individual has more and more come to consist of relationships to groups to which the individuals belong, whether as investor or as workers. Property still represents 'belonging' but in another sense.<sup>1</sup>

It has also not been defined in any system of law; for a definition of property is related to the political and economic set up accepted by the community. Legal systems abound in illustrations of property, but no definition is attempted. The Transfer of Property Act explains whether particular things are property or not for the purpose of the transfer of property under the Act. But it does not define the term property. The Supreme Court of India discussed the conception of property in a number of cases. In *Commr. H.R.E. v. Lakshmindra*<sup>2</sup> the Supreme Court said:

There is no reason why the word property as used in article 19(1) of the Constitution should not be given liberal and wide connotation and should not be extended to those well recognised types of interest which have the insignia or characteristics of proprietary rights.<sup>3</sup>

In short the court accepted that the term 'property' in article 19(1) includes both abstract as well as concrete rights of property.

The Constitution of India guarantees the fundamental right to property in article 19(1).

It confers right to property only on the citizens of India. A non-citizen has no fundamental right to property. He may be permitted to

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1. Paul Freund *The Supreme Court of the United States* 78 (1961).

2. A.I.R. 1954 S.C. 282.

3. *Id.* at 288.

hold property, but he cannot complain if a law prohibits him from holding property.

Modern legal systems recognise both natural persons and juristic persons. Human beings are natural persons, and a limited company or a statutory corporation is a juristic person. In a number of cases the Supreme Court was called upon to decide the question as to whether a limited company is a citizen under the Constitution and the extent of the right to property of such limited companies. An important question with reference to a limited company arose in the *Chiranjitlal v. Union of India*.<sup>4</sup> The Government of India had taken over the management of the Sholapur Mill by legislation. The Board of Directors elected by the shareholders was dismissed and a new Board was appointed by the Government. The law was challenged by Chiranjitlal who was one of the shareholders. His contention was that he was deprived of his property without compensation with the result that his right under articles (19(1)(f) and article 31(1) was violated. He also urged that in taking over only the Sholapur Mill, the Government denied equality before law. Hence, this action amounted to violation of article 14. The Court negatived both the contentions. It made distinction between the rights of a shareholder and his incidental privileges. The law in that case did not take away the right of shareholder to dispose of his share, to receive dividend and to participate in the surplus in case of winding up. These rights constituted his property. Hence, he was not deprived of his property, other rights of the shareholder such as right to control the management by directors elected by him, the right to pass resolutions giving directions to the directors elected by him and the right to present winding up petitions were merely suspended by the law. These rights were described by the Supreme Court as mere incidental privileges and as the privileges were curtailed in the interest of general public, the curtailment was justified under article 19(5). The Court also made distinction between a company and its shareholders.

Mukherjea J. laid down an important principle of law regarding corporations and the right of the State to interfere in the working of the corporations. He observed as follows:-

We should bear in mind that a corporation which is engaged in production of commodity vitally essential to the community, has a social character of its own and it must not be regarded as the concern primarily or only of those who invest their money in it. If its possibilities are large

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14. (1959) S.C.R. 12, 128.

For a hundred years American judges have been giving meaning to property and one thing which is most apparent is the impossibility of maintaining any hard and fast concept of property.

and it has a prosperous and useful career for a long period of time and is about to collapse not for any economic reason but through sheer perversity of the controlling authority, one cannot say that the legislature has no authority to treat it as a class by itself and make special legislation applicable to it alone in the interest of the community at large.<sup>5</sup>

The Court in *Chiranjitlal's* case did not discuss the question whether a limited company is a citizen under the Constitution of India. The rights guaranteed under article 19 can be enjoyed by a citizen only. The question came before the court in the case of *State Trading Corporation of India Ltd.*<sup>6</sup> and the court laid down that the corporation was not a citizen. The point was discussed again in *Tata, Engineering and Locomotive Co. v. State of Bihar*.<sup>7</sup> An attempt was made in this case to persuade the court to accept that a corporation is not different from the shareholders and if all the shareholders are citizens of India, the corporation should be considered as citizen of India, by lifting the veil of the corporation. Thus if the corporation is considered as a citizen, it would be entitled to the rights guaranteed by article 19. The court did not accept this argument.

It reaffirmed its views in this case and laid down that a corporation is not a citizen of India. Now, this may be considered as the settled law. Therefore a corporation in India has no fundamental right to property. It can however be deprived of its property by the State under article 31. For the words of article 31 are: 'No person shall be deprived of his property ....' A corporation is definitely a juristic person. Hence, it can be deprived of the property under article 31.

The right to carry on any trade or business may be considered as property. But the Constitution provides for carrying on by the State of any trade, business, industry or service to the complete or partial exclusion of citizens or otherwise. Hence, the State may establish statutory corporations for carrying on any trade, business etc. with the result that the citizens right to carry on the same trade will be affected adversely. Quite a large number of statutory corporations have been established in India. Road transport in all States is now practically nationalized. The Indian Airline Corporation has nationalized the air transport: The Life Insurance Corporation has nationalized Life Insurance.

Article 298 which was amended in 1956 specifically lays down that the executive power of the Union and of each State shall extend to the carrying of any trade or business and to the acquisition, holding and dis-

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5. *Id.* at 19.

6. *S.T. Corp. of India v. Commrcl. Tax Officer* A.I.R. 1963 S.C. 1811.

7. A.I.R. 1965 S.C. 40.

posals of property and making of contracts for that purpose etc. It appears that as a result of this amended article a State can carry on trade or business etc. even without a legislative sanction. The combined effect of article 19(6) and article 298 appears to be that the State can carry on any trade or business and for that purpose create a monopoly for itself. The Supreme Court laid down this view in *Akadvasi Padhan v. State of Orissa*.<sup>8</sup>

the effect of the amendment made in article 19(6) is to protect the law relating to the creation of monopoly and that means that it is only the provisions of the law which are integrally and essentially connected with the creation of the monopoly that are protected. The rest of the provisions which may be incidental do not fall under the latter part of article 19(6) and would inevitably have to satisfy the test of the first part of article 19(6).<sup>9</sup>

Thus the attitude of the court was not to give a blank cheque to the legislature which aimed at creating state monopoly in respect of certain trade or business.<sup>10</sup>

Another important question that arises as a result of State monopoly is the effect of such a monopoly on the right to property guaranteed by article 19 clause (1)(f). Any monopoly is bound to affect the right of citizens to acquire, hold and dispose of property. A State monopoly will have far reaching effect on the right to property. The Supreme Court considered this aspect of the question and laid down that a law which affected a citizen's rights under article 19(1) only indirectly such as one creating state monopoly was valid.<sup>11</sup>

The court supported its conclusion by reference to similar views expressed in *Gopalan's*<sup>12</sup> case in *Ramsing v. The State of Delhi*<sup>13</sup> and the *Express Newspapers v. Union of India*<sup>14</sup> cases. No doubt this is the only available test for determining the validity or otherwise of the impugned legislation. However, this test depends to a great extent on the attitude of the judge deciding the case: "the major inarticulate premise" will have a determining effect on such cases. This is no doubt undesirable, but it is inevitable. The court also laid down another limitation on the State

8. II SCJ 1964 37, 43.

9. *Id.* at 44.

10. See also *Parbhani Transport Society v. R.T.A.*, A.I.R. 1960 SC 81 and *Kondalu v. A.P. S.R.T.C.* A.I.R. 1961 S.C. 82

11. *Akadvasi Padhan v. State of Orissa* II S.C.J. 1964 37, 44.

12. (1950) S.C.R. 88, 101.

13. (1951) S.C.R. 451, 456.

14. 1959) S.C.R. 12, 128.

monopoly. If the State takes over any trade or business, it must not appoint agents' for carrying it on except where it is inevitable and works within well recognised limits of agency.<sup>15</sup>

Thus the Supreme Court in upholding State monopoly with respect to certain trade or business laid down certain principles which must be observed by the State in order to sustain constitutionality of such a monopoly.

Can the State create monopoly in favour of individuals? It appears that such a monopoly would not be unconstitutional, but the law creating the monopoly will have to satisfy, certain requirements. First part of clause (6) of article 19 lays down that the right to carry on any trade or business will be subject to any law imposing in the interest of the general public reasonable restrictions on the exercise of the right. Hence, if a monopoly is created by the State in favour of individual or individuals, the law creating the monopoly must be a valid law and the restrictions imposed by the law must be reasonable. It appears that if such a law indirectly, infringes the fundamental right to acquire, hold and dispose of property, it would not be unconstitutional only on that ground. The Supreme Court examined law creating monopoly in favour of individuals in a number of cases. In *Cooverjee v. Excise Commissioner*,<sup>16</sup> *M. B. Cotton Association v. Union of India*,<sup>17</sup> *Narendra v. Union of India*,<sup>18</sup> *Glass Chatons Association v. Union of India*<sup>19</sup> the court considered the law creating monopoly in favour of individuals and came to the conclusion that the restrictions imposed by the law were reasonable restrictions. But in *Rashid Ahmad v. Municipal Board*<sup>20</sup> and *Yasin v. Town Area Committee*,<sup>12</sup> the court held that the restrictions were unreasonable.

Thus the constitution provides for creating monopoly in favour persons other than States. The rapid industrialisation of India during the last two decades has been primarily due to the limited companies established under the company law. The Indian Companies Act 1913 was repealed and Parliament placed on the statue book the Companies Act of 1956. This Act took into account the rapid industrialisation in the country, the establishment of large number of limited companies, the vesting of large property and power in the hands of the managing

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15. *Id.* at 48.

16. 1954 S.C.R. 873.

17. A.I.R. 1964 S.C. 634.

18. A.I.R. 1960 S.C. 1514.

19. A.I.R. 1961 S.C. 1514.

20. (1950) S.C.R. 568.

21. A.I.R. 1952 S.C. 115.

agents and the directors and the ideal kept by the constitution before the nation of social and economic justice and accordingly provided for the control of the companies. India has not accepted the ideal of bringing all industries in public sector. There is considerable scope for private sector. However adequate legal provisions have been made so that the functioning of private sector is not to the detriment to the ideal of social and economic justice. This ideal is clarified in clauses (b) and (c) of article 39.

It was thought that the provisions of the constitution as originally adopted did not vest adequate authority in the Government of India to control the working of the limited companies. Hence, the Constitution was amended in the year 1955 (fourth amendment) in order to enable the State to control limited companies. The statement of objects and reasons *inter alia* made this clear.

This object was achieved by the Companies Act of 1956. The Companies Act has provided many safeguards against the abuse of powers by those in control of corporations.

Prior to the Companies Act of 1956, the Managing Agents had tremendous powers in their hands. Following were the complaints against the managing agents.

- (a) Interlocking of funds of Companies.
- (b) Trafficking in managing agency rights.
- (c) Speculation in the shares of the operating Companies.
- (d) Appropriation of huge sums by way of Commission and office allowances.

Sections 197A & 356, 358, 342 of the Act aims at preventing some of the abuses. Even if a managing agent resigns his office, he will not be absolved from the liabilities of his previous acts. Transfer of managing agency rights are subject to the sanction of the Central Government. No person can be a managing agent of more than ten companies. The recent amendment of the Companies Act abolishes managing agency system in five industries.

There are many other provisions of the Companies Act, relating to the Directors, share-holders and Auditors etc. which enable the state to have greater control over the limited companies. If these provisions are properly enforced, the evil of concentration of property in the hands of a few people would be greatly reduced.

Dr. D. L. Mazumdar has shown that it is for the first time in the history of company law in any country which accepted the Anglo-Saxon

model of Company legislation that the concept of public interest and its policy implications have been formally recognized in the Companies Act. He classifies the provisions of the Companies Act under the following heads.<sup>22</sup>

- (a) Provisions intended to dissipate or prevent concentration of economic power;
- (b) Provisions designed to reduce inequalities of income or wealth in proprietary or decision making classes in the corporate sector;
- (c) Provisions intended to democratise company management to the extent that the model of political democracy is applicable to business management in the corporate sector.

He further points out that the difficulties that appear to exist in the administration of the Company Law are the difficulties of conflicting theories. He observes.

But no systematic legal philosophy or no formal legal system, which takes into account the realities of new economic and social order in the corporate field, has so far been worked out in the western countries. It is this *hitus* between the *de facto* technological and social situation of the present day and the practical logic of the existing institutions of trade and industry on one the hand, and the prevailing basic laws relating to the organization and working of joint stock companies in the western countries, on which our businessmen and professional have been brought up in the past, on the other that accounts for the deep-seated conflict which still subsists between the thinking of the operators of market place and the custodians of the conventional wisdom on the one hand, and the economic and social realities of the present age and the social urges of our times on the other. In the perspective of history, our new company law appears to be an attempt, *albeit* a partial attempt, to reduce the area of this conflict by the canalising the freedom of private enterprise, wherever possible into channels that subserve the public interest.<sup>23</sup>

As a limited company is not a citizen of India, it has no fundamental right to acquire, hold and dispose of property. However, there is no constitutional bar to the acquiring of property. Hence, limited companies in India have the freedom to acquire property. The rapid industrial development in India has been a result of the work of many a limited company. They have huge property with them. The concentration of huge property in the hands of the directors of the companies has created problems both

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22. Dr. D. L. Mazumdar, "The Concept of Public Interest in the Indian Companies Act 1956" Vol. III, No. 3, *The Indian Advocate* 3, 5 (1963).

23. *Id.* at 14.

in the economic sphere as well as political sphere. For, these corporations do not merely result in concentration of property and wealth in the hands of few but they also affect considerably the social outlook of the community. The extent of the influence of powerful corporations on national life will depend upon the magnitude of concentration of wealth in the corporations and the extent of the control the state exercises over such Corporations. In certain countries the phenomenal growth of the giant Corporation has raised the problem of state sovereignty.

Hence, an effective control of such corporation by the State is absolutely assential. In the United States of America, anti-trust legislation was passed in the same year. All these Acts aimed at restricting the power of the giant corporations and preventing monopoly. To what extent they succeeded is a problem of American Constitutional Law. Prof. Friedean however points out that the effective control of bigcorporations would involve many consideration.<sup>24</sup>

The Government of India appointed a commission known as Monopolies Inquiry Commission to consider this aspect of property. The report of the Commission has been most revealing. The Monopolies Inquiry Commission has recommended the passing of a law by Parliament. A draft Bill called 'The Monopolies and Restrictive Trade Practices Bill' is also included in the report. The principles underlying the Bill in the words of the Commission are as follows—

- (1) We need not strike at concentration of economic power as such, but should do so only when it becomes a monace to the best production (in quality and in quantity) or to fair distribution;
- (2) To accomplish this a constant watch must be kept by a body independent of Government — in addition to what is being done by Government and Parliament—that big business does not misuse its power;
- (3) Monopolistic conditions in any industrial sphere are to be discouraged, if this can be done without injury to the interest of the general public;
- (4) Monopolistic and restrictive practices must be curbed except when they conduce to the common good.<sup>25</sup>

Even if these recommendations are implemented all problems arising out of monopolies may not be solved. For monopolies are destructive of economic efficiency and economic progress. In addition they produces undesirable concentration of power.

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24. Friedman, *Law in Changing Society* 291 (1959).

25. Government of India, Report of the Monopolies Inquiry Commission 159 (1965).



Giant Corporations and monopolies create problems—jurisprudential, economic political and social: Prof. Julius Stone has discussed some of these problems, in his latest book 'Social Dimensions of law and justice'. It would be desirable if some of these problems are discussed in the Seminar. I would particularly refer to the following problems for the consideration of the Seminar.<sup>26</sup>

(1) The first problem is the dependence of society for most of its needs upon a limited number of major corporations. These major corporations find finances for their expansion in the internal resources and thus become still bigger. Hence the problem is 'now to ensure that these entities on which society depended for so much did not fail to meet the responsibility involved'.

(2) The second problem is 'how to ensure that these comparatively few individuals (i.e. directors, secretaries etc.) who controlled vast properties by grace of outrun legal rules would always use the power responsible.

(3) The third problem is as follows:—

If those whose capital had gone to make up the assets of the Corporation were concerned only with the maintenance of reasonable dividends, and if society as a whole was deeply concerned with all aspects of corporate activity, in whose interests were these vast aggregations of wealth and the activities of millions of men working in their enterprises, to be controlled?

(4) The problem of monopolies in India is to be considered from the point of view of monopolies both in the private sector and in the public sector. The Monopolies Inquiry Commission did not deal with the public sector as it was not within the terms of the reference of the Commission. But there are problems created by monopoly in the public sector also. A Parliamentary Committee has been set up to examine the performance of Public Sector concerns and the annual reports of those belonging to the Union has to be presented to Parliament.

It is for the consideration of the Seminar whether these measures are adequate to control monopolies in public sector.

The problems created by giant corporations and monopolies in India are really numerous; it is not possible to refer to all of them in this paper. However, it is essential for the Seminar to consider some of these pro-

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26. See Berle Means, *Modern Corporation & Private Property* (1944), quoted by Stone in *Social Dimension of Law and Justice* 427 (1966).

blems and suggest solution if possible, so that the dangers to the freedom of the individual and to the public life in the country are avoided. For, the Preamble of the Constitution emphasises inter alia justice social economic and political and the dignity of the individual'. Any social order where these principles will be in danger must be averted.<sup>27</sup>

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27. See Stone *Id.* at 467-468.