

Chapter

**VIII**

**AN APPRAISAL**

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# EIGHT

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The financial management has assumed special significance in the existing general economic fragility and recession conditions. The problems of credit squeeze, increasing rate of interest and rising inflationary pressures have eroded the capital base of the private corporate sector. Paucity of corporate capital, instability and turbulence of the economy and increasing government regulations have further placed new responsibility on the financial executives while multiplying the challenges for their decision-making.

The basic philosophy for industrial development has been outlined in various Industrial Policy Resolutions from time to time. The legal framework for its implementation is provided in the policy instruments like the Industries (Development and Regulation) Act, the Capital Issues Control Act, the Foreign Exchange Regulation Act, the Monopolies and Restrictive Trade Practices Act. In the light of these, the industrial licensing is only one but a very significant aspect of the comprehensive regulatory system of the government for the private corporate sector industries. The main objectives of most of these measures including industrial licensing have been to curb the so-called evils of private enterprise and to allow it to develop only in conformity with the overall government policies and goals.

The package of economic policies unfolded by the Government during the last two years is designed to reduce drastically state intervention in the working of private enterprises. Attempts have been made to liberalise a number of provisions of the industrial licensing, policy and procedures. More important among them being liberalisation of decision-making at various levels, streamlining of industrial approval

procedures. The latest announcement exempts the MRTP and FERA companies in 22 industries from licensing and reduces the export obligations in the case of units located in backward districts. The scheme of re-endorsement of capacity has been streamlined and the criterion of the scale of production, required for economic production, introduced so that units will be allowed to go up to such a scale in the interest of bringing down the cost of production. The Government has further assured that the duty structure will be rationalised and necessary measures will be taken for infrastructure support and appropriate pricing policy.

• A welcome feature of the policy of liberalisation is the bold step of the Government to raise the asset limit for units or groups requiring registration under Chapter III of the MRTP Act from Rs. 20 crores to Rs. 100 crores. This hike has freed an estimated 40 per cent of companies from MRTP constraints. This was followed up with the extension to a select range of industries of exemption from Sections 21 and 22 of the MRTP Act. This list of such industries, currently numbering 27, is likely to be expanded from time to time. The second feature of liberalisation frees companies belonging to large houses from obtaining clearance for substantial expansion and investment. A third feature of liberalisation relates to the proposal to increase the asset limit of dominant undertakings from Rs. 1 crore to Rs. 3 crores. The dominant undertaking will continue to operate under the prevailing scheme of industrial regulation. An important factor for due consideration may be the extent to which the government must abjure discretionary intervention in public interest if liberalisation is to unleash new growth impulses.

• One dominant feature of the Companies Act, 1956 is that, in a large number of matters, the approval of the Central Government is required as the final authority. Matters relating to capital structure, finance, inter-corporate loans and investments, directors, disclosures, cost audit, convertibility of loans into equity etc. represent a vast extension of the regulatory powers of the government over the activities of the private sector companies. How far have these regulations served public purpose? The experience of last 30 years (Six Five Year Plans) should provide opportunity for an appraisal as to how far these regulations have served the corporate growth. Any such objective appraisal will be an eye opener and will bring to limelight the contribution of the government regulation to the healthy growth of the corporate private sector. However, while living in a complex society with an industrialised economy, it would be futile to expect the company law to be reduced to a few inessential recitations.

• So far as the big companies of the private corporate sector are concerned, they cannot avoid government regulation. It is self-evident

that with thousands of crores of rupees as paid-up-capital, with huge investment of financial institutions, and with millions of employees, the working of the private sector cannot be left in an unregulated manner. The companies are now recognised as socio-economic institution of national significance.

The financial institutions, as sponsored by the government, have filled up the gap in corporate finance and their remarkable contribution is in the form of loans, guarantees and subscriptions to shares of companies. Their objectives determine the sphere of their activity. It is through these institutions that the government is exercising its control over the financial management of the private corporate sector. A review of the financial pattern reveals that the term-lending institutions lay emphasis on conversion of debt into equity. The private sector feels that the financial institutions should have liberal approach in enforcing the convertibility clause. In this respect the government issued Guidelines for convertibility clause in 1984. The loan agreement also empowers the institutions to appoint nominee directors on the management boards of the assisted concerns. The role of the nominee directors is an evolving and challenging one. They constitute a vital link between the financial institutions on the one hand and the assisted concerns on the other. As such their functioning is generally criticised and there appears to be enough scope for further improvement. It will be worthwhile if the government can effectively implement the Guidelines of 1984 regulating the appointment and the functioning of the nominee directors.

The financial institutions should take effective steps to protect their loans and investments in the private corporate sector companies. As and when circumstances so require, they can even introduce major changes at the management board level in the public interest. Subsequently, as a shareholder, they may also convene an extra-ordinary general meeting of the shareholders to get their approval for the same. As the loans and investments are made out of the national wealth, the financial institutions are under a duty to safeguard them and to give proper directions to the financial management of the aided companies.

The financial situation of the money market brings into focus the emerging new trends in the corporate financial management and the changing preferences among the investing public. A noticeable feature of the corporate administration, in the recent years, is that they are aware of the fact that they will still have to depend mostly on the traditional source of finance-funds from the banks. However, there is a growing awareness of the limitations involved in getting bank loans in the light of the credit control and statutory diversion of about 40 per cent

of the funds to the priority sectors. The diversion of banks' funds to the corporate fold through debentures and public deposits has to be examined in the light of the accepted priorities of the Reserve Bank of India and the Central Government. The corporate competition for funds has also eroded bank deposits to a great extent.

"The share markets are zooming and the equity shares, debentures or bonds floated by many companies have been over-subscribed. A new class of investors has emerged and a considerable large amount of investible resources including unaccounted funds are being diverted to share markets. The buoyancy in the stock market has also been sustained to a large extent in the recent years. The government appears to be keen to keep the share market in a happy and gay mood to feed the capital needs of new companies and promote savings and channelise investment in national economy for rapid industrial growth. Investors have entered the year 1986 with high hopes and a cheerful note. The share market has ushered the year 1986 with a note of anxious optimism.

. It is significant to note that there was a 50 per cent rise in the amount of new issues as compared to 1984-85 when the amount of new issues totalled Rs. 2,003 crores. In 1983-84, the new issues totalled Rs. 1,000 crores. There is going to be a big rise, according to capital market sources, in the amount of new share capital issues in 1986-87 and the total amount may very well touch the figure of Rs. 4,500 crores as against more than Rs. 3,000 crores in 1985-86.

· Sources point out that the Finance Minister's latest announcement regarding withdrawal of his budget (1986) proposal envisaging deletion of Section 80M of the Income Tax Act relating to deduction in respect of income by way of inter-corporate dividends has given a new sense of confidence in the industry. Experts maintain that some recent developments in the investment sector, especially the entry of the giant public sector companies with bonds and debenture offers, have added a new dimension to the working and functioning of the capital market. Issues have now become more competitive since the investors have become choosy. There is going to be a qualitative change in the operations of the capital market in the coming years and while the number of issues may be less, the volume per issue will be larger.

· The government has already taken some vital measures to improve the functioning of the Stock Exchanges in the light of the recommendations made by the high-power committee headed by Shri G.S. Patel. The committee has recommended fixation of overall ceiling on the cost of public issues and raising the minimum requirement of paid-up equity

capital for eligibility for listing of a company on a stock exchange to Rs. 50 lakhs from the earlier level of Rs. 10 lakhs. Thus, there is greater emphasis on the need for improving the functioning of the financial system in the context of changing perspectives of the economy and thrust on rapid industrial development.

These questions assume great importance and require proper analysis by the government and the monetary authorities bearing in mind the fact that all the companies are not profit-making companies and the interest of the trade, industry, banking sector and the investors also require adequate protection. The government regulation should evolve working strategies to meet the changing preferences of the investing public. Good financial management depends on evolving the right response to each emerging challenge.

The managerial remuneration gains special significance as the king-pin of corporate performance in the top management. In order to encourage professionalisation of management it is essential that the managers and executives should be rewarded commensurate with their responsibilities in an enterprise. The matter is widely examined by the government, judiciary and management experts at various stages. The societal interest and national objectives call for equitable justice with the executives in the private sector and in other spheres as the corporate sector does not function in isolation. It is well recognised that the managerial remuneration in the private sector cannot be left in the traditional unregulated manner due to changing socio-economic values and compulsions. It is in this connection that one can appreciate government regulation of managerial appointment and remuneration in the private corporate sector. Subject to statutory criteria the government may issue some general guidelines, as the basis for uniform managerial remuneration, and also specifically mention the cases and the extent to which slight deviations can be made to deal with special situations of the enterprise. However, the recommendations of the Bhoothalingam and Sacher Committees, that any revision of managerial remuneration would be justified and effective only as part of an integrated income policy for the entire country, deserve due consideration for any long range decision-making by the government.

¶ The concept of corporate control and corporate power has to be analysed in view of emerging Indian perspectives and trends. The metamorphosis is all the more remarkable when measured against a change in the locus of control that has occurred as big companies have evolved in response to seismic changes in society, economy and technology. For a long time there was no movement to restructure the

corporate financial functioning. Now there is a movement to regulate the working of the financial management of the private corporate sector. The aim is to protect the society's interest and to achieve the planned industrial development targets. Recent liberalisation of industrial policy is also a new experiment in the same direction. A further refinement of the industrial policy is necessary. The restructuring would imply not only emergence of economic capacities for new industries but also rationalisation of the existing ones and production of goods of high quality at low costs. The dynamic units could even expand to globally competitive scales.

◦ A basic question is often discussed in many quarters : Is government regulation and consequent legislation curbing and controlling the corporate sector desirable ? There is no simple answer to this question. If one says "no" the next question will be, should the industries and corporate sector be allowed to function without any relevance to national objectives and priorities ? Should they be permitted to pursue a selfish business policy irrespective of the interests of the consumers, the community and welfare of the society at large ? Obviously, one cannot agree with this.

◦ If the answer is in the affirmative, the industries must be regulated and controlled. In such a situation the leaders of the private corporate sector, who mostly believe in *laissez faire* approach, will protest against such curbs and controls by the government. They emphasise that the steps should be taken to remove or minimise controls on production, prices and distribution, curbs on import of technology, foreign capital and restrictions under the MRTP Act. According to them controls, regulations and curbs on credit had seriously impeded economic growth in the country.

◦ In view of the Directive Principles of the Constitution, pronouncements of the Parliament and successive governments and changed socio-economic conditions, going back to the traditional *laissez-faire* policy seems impossible. However, there may be some justification for rethinking and review of the mechanism on controls and regulations in the light of changing conditions of the society and the objectives of the government. The best strategy should, therefore, be to ensure that the regulatory measures in force do promote and not prevent corporate growth. In other words, such regulatory measures should be constructive without being excessive. They should be capable of promoting incentive, initiative, investment and interest in public weal. As finance is a vital input for industrial growth, it is imperative that financial policies are restructured and regulated in such a manner as to make different sources of finance elastic enough to meet the genuine requirements of productive private corporate sector industries.



The basic objection to government regulation stems from the in-built system of approvals and clearances under various corporate legislations. The object of any regulation must be to see that public interest does not suffer. The purpose cannot obviously be to act as a brake for the normal functioning of the corporate sector.

The corporate financial management has a duty to investors, shareholders, employees and the society. The duty towards investors may be stated within the concept of disclosure which has been a cornerstone of various regulatory provisions of the Companies Act. The aim is to enable the investors to have necessary information regarding company affairs. The duty to shareholders revolves around the directors' responsibilities as a fiduciary custodian of the company's assets. It is the bounden duty of the financial management to see that its employees thrive and prosper as social instrument for the public good. As regards duty towards society, which is rapidly expanding in all directions, it is now well recognised that the companies should be profit-oriented in a socially acceptable manner. It also refers to new awareness in the society which require that the companies should participate in financing various civil endeavours in the interest of the society. Where these duties are ignored or abused by the private corporate sector the society will interpose its veto and the government regulation of the corporate affairs becomes imperative in the social interest.

