

STATE GOVERNMENT CONTROL OVER PRIVATE ENTERPRISE IN INDIA

PARESHNATH CHATTERJEE*

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 that the Union list includes almost everything, that the private sector enterprises are concerned with. The span of control left with the states relates only to a fringe of their activities.¹ These are facts that have to be underlined right at the outset.

The framers of the Indian Constitution anticipated the building up of a strong government at the centre, in terms of what can be termed "concentric federalism." The states were supposed to be acting on the periphery. The changes noticed during the last few years have given this basis quite a serious jolt which does not owe itself to politics alone. The objective side of the entire basis calls for a reconsideration, despite the probe by the *Administrative Reforms Commission*. The peculiarities of the Indian political phenomenon which are becoming more and more manifest everyday 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

*M.A., Ph.D.

1. The following matters are exclusively under the central control :

- (a) "Industries declared by Parliament by law to be necessary for the purpose of defence or for the prosecution of war." (*Entry 7, 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, Union List*);
- (c) Inter-State or commerce, incorporation, regulation and winding up of trading or non-trading corporation, including banking and insurance and other financial corporation;
- (d) Import and export trade; and
- (e) High-yielding, elastic varieties of direct and indirect taxes make their way into the central exchequer. Only a portion of these go back to the coffers of the States via the Finance Commission awards and other grants and payments.

In addition, foreign exchange, its earning regulation and disbursement are matters of exclusive central jurisdiction.

by the switches and shifts that have taken place. In the specific context of control of private enterprise an attempt has been made to take note of some of these changes and to suggest that all this is not discouraging. However, this would require 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 on the basis of conscious loyalty to sovereignty of the nation. The most question is: are these contradictory to each other ?

The Indian federalism has been centred on making the federal government strong that has, as its overall objective of focusing on the need for 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 magnitudes that major part of the attention of 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 this unity through 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 and what formal and informal substitutes are evolved for bringing the states to common platform of understanding and mutual exchange of experience. Private enterprises and their control offer excellent illustration as to what positive role of the states can be, *vis-a-vis* what it has remained all these years. Unfortunately, not much serious thinking has gone into this question.

Private Enterprise

The organised sector of private enterprises in this country has been in the purview of the centre. This relates to their establishment, running and earnings almost in toto. Let us take the case of companies. At present some 27,000 public and private limited companies are functioning. These companies are administered by the Indian Companies Act, 1956 which is a central legislation. The firms and unitary concerns are also subject to various degrees of central control depending on the lines of their 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 enterprises. The extent of state participation in various productive activities is grossly inadequate to create any visible impact. It is from this point of view that the subject is very significant and of some topical interest.

In regard to the exercise of control over 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 capital invested, the role of the states is rather small and insignificant. This would require some detailed explanation, particularly in the context of noticeable indifference to such activities of private sector. The states have remained powerless in some of the crucial questions in this respect. In some important 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 merit. The entrepreneurs coming from other states not only bring their funds with them but also their own trusted personnel to man the key positions and in some cases it extends to the lower levels of hierarchy. The employment benefits from such industrialisation from the point of view of states have been negligible. 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 these 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 Commission's* awards is not doubted here, but the motivation of states towards industrialisation under private sector 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 states on the choice of product and product-mix is not quite adequate. While such choices are generally 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, states have not always been in a position to direct their economic efforts in a way that would reduce their dependence on other

states or ensure fuller utilisation of resources available. Any question related to inter-state activity would involve the centre. In a large measure the private enterprise activity has resulted in augmenting the power exercised by the centre. While the resources available to states for organised exploitation may have been considerable, the benefits accruing to them from such resources have been doubtful.

Size Economics

In the context of size, the trends in this country have been quite interesting. While all the banes of large scale have accrued to private sector, the benefits of large scale have not generally arisen. This is partly because of the fact that the size-economics, 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 production units, even in those cases where the size of the establishment in the sense of controlling unit has been large. Diversification and integration have been generally of the conglomerate type. It is in this situation perhaps that one may look askance at the proposition of there being monopoly power accumulating side by side with 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. Not only are private limited companies an overwhelming majority in number but even public limited companies have small capital in general. In particular industries, however, there has been official direction in favour of formation of public limited companies, such as manufacture of cement. In addition, banking and insurance companies are required to be public limited by law.

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 areas in which such activities have been organised or located. Lack of local motivation has not only made state governments but also the people of the area relatively uninterested, if not totally indifferent. 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 directions and doses of investment under private initiative have been matters in which the states have been asked to help with funds and facilities but their regulatory powers have been generally limited. The incentives and attractions offered by states for larger activities 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

Most states did this by establishing enterprises which were public sector limited companies, so that there could be more and more public participation. This participation has been noticed in many different industries. 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 control of states than that under the centre. The state government companies have not been bound by areas indicated in *Industrial Policy Resolution, 1956*. This is, an important question.

The prices and return on the capital employed have remained issues under sharp public focus. The prices charged by private entrepreneurs have looked more to the question of their own 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 area in question. The profit motive being there, the entrepreneurs have not cared to cater for local consumption, as much as would be desirable in the interest of local development. Outside employment, coupled with higher prices has, however, brought serious repercussions on local markets both directly and indirectly. The pressure on consumption being pushed up, the cost of living in the area has also gone up, so that, paradoxically, industrialisation of this type has adversely affected the existing levels of living, leave aside improvement. In the circumstances, the states desirous of having something done in this respect have found their going very difficult. Any step taken by states to counter this anomalous situation would invoke all kinds of criticism including the pet slogan of parochialism and magnified by a section of the press and the public.

Exports

Similarly, adequate motivations have not been created for 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 in the 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 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 rests with the centre. A better alternative could perhaps have been to allocate foreign exchange to 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 states over the joint stock companies. The *Administrative Reforms Commission* has suggested decentralisation of power among the Regional Directorates with regard to 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 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 with the administrative control developing 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 could be better taken care of. 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, without reference to their genuine needs.

