THE CAPITAL ISSUES CONTROL ACT, 1947

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A little more than twenty-five years have passed since the control over the issue of capital by joint stock companies was first introduced in 1943 as a war measure. This meant an exercise of the check on the non-essential uses of the scarce resources and their diversion and employment to the more essential, that is, defence purposes. After the war, however, the necessity of capital issues control continued to be felt. There was serious inflation. With the pent-up demand for consumer goods due to their scarce availability during the war there was the possibility of investment flowing into less priority sector of industry at the cost of much needed goods and services for the common man. To prevent such an eventuality, the control was first put on the statute book in 1947, as a temporary measure being continued from time to time. Then began the era of planning after the independence of India. The *Industrial Policy Resolution* was adopted by Government in 1948. The Industries (Development and Regulation) Act was passed in 1951. But because of its utility, the Capital Issues (Continuance of Control) Act was retained and continued from year to year.

The year 1956 is important from more than one point of view as far as the corporate sector is concerned. It was in that year that the Companies Act 1956 was enacted and the Securities Contracts (Regulation) Act was also put on the statute book. The Capital Issue Control Act was also permanently put on the statute book immediately thereafter. Thus, the capital issues control became part and parcel of planned industrial development of the country promoting investment interest in the corporate sector, with due safeguards for the common investor and also ensuring broad-based shareholdings in the maximum possible number of public limited companies.

The main object of the Capital Issues Control Act, as of the Industries (Development and Regulation) Act, was the regulation of balanced investment in all sectors of the economy in accordance with the priorities laid down in the *Five Year Plans*. But while the licensing of various industries in accordance with *Plan* targets laid down in the *Five Year Plans* is being cared for by the Industries (Development & Regulation) Act, the financial

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aspects of the concerned projects have been the area of capital issues control. This has involved two things primarily, one, the regulation of the financial structure of joint-stock companies and the other, the protection of the interests of the investing public. Thus the control has attempted to foster a healthy and rational growth of the corporate sector in the country.

As a measure of this healthy and rational growth, the control has evolved, during the course of the last two decades, some sound principles for the healthy financial structure of joint stock companies. For example, the control has been guiding the companies to conform to a capital structure with an equity-preference raito of 3:1 so as to ensure that the capital structure is not loaded with a preponderance of fixed interest bearing securities to the chargin of the equity investors, Another principle which has been evolved is that the total long-term borrowings of a company should normally not be more than double the amount of share capital and reserves. Or, where the securities are issues by a company for taking over an existing business or asset, the take-over should be effected at book value or a proper valuation certificate must be produced. This is with a view to avoiding giving undue advantage to the seller. Similarly, either the securities may be issued at par or at premium; but in case of the latter, it has been laid down that the amount of premium shall be fixed only with the approval of the *Controller of Capital Issues*. Whenever the public are first asked to subscribe to the share capital, the initial promoters, directors and their friends are required to put in a part of the capital in the enterprise to share the risk. These principles are mainly to protect the interests of the ordinary investors who part with their money for purposes of a profitable investment but do not, or are unable to take part in the practical management of the company.

It might appear that the government have arbitrarily laid-down these principles and are forcing the companies to fall in line with their wisnes. But it is not so at all. Whatever principles for the financial soundness of the corporate sector have been laid, and are being followed, have been evolved by the willing help and support of the private corporate sector. This type of cooperation of the private sector is secured by government through a statutory committee formed by the government under the Capital Issues Control Act, known as the *Capital Issues Control Advisory Committee*. The *Committee* has, as its members, a representative of the *Federation of the Indian Chambers of Commerce and Industry* of India, a nominee of the *Associated Chambers of Commerce and Industry*, possibly a well-known Chartered Accountant, a member of Parliament and some other know ledgeable person in the capital market. The chairman of the *Committee* nominated by Government, is a person of great standing in the financial and commercial circles. It is easy to imagine the close collaboration of the private secured by the government in the formulation of principles

being followed by the control when an Advisory Committee is composed of such eminent personages as enumerated above. The result is a complete satisfaction to the private sector with the working of this control.

It would be interesting to know how capital issues control has adopted itself so usefully with the evolution of certain financial institutions as part of the capital market during the course of its existence for the last two decades. The *Industrial Finance Corporation of India* was established in 1948, the *Industrial Credit and Investment Corporation of India* in 1955 and the *State Financial Corporation* in the fifties in general. It is acknowledged that the contribution made by these financial institutions (and the recently established *Industrial Development Bank of India*) in the industrial Development of the country is immense. There would hardly be a big project or a big company which would go in production without securing some help from these institutions. As these institutions were themselves new, at least in the initial stages, they looked forward to the government for some guidance. Herein the Capital Issues Control came in handy to them. The financial institutions have looked upon the financing schemes approved by Capital Issues Control of government as adequately satisfactory in examining viability of projects. It has already been indicated that when the Capital Issues Control was placed on the statute book permanently, the Securities Contracts (Regulation) Act, 1956 and the Companies Act 1956 were also enacted. In the administration of these enactments, the Capital Issues Control is a living companion looking after the economic aspect of the investments in the corporate sector.

Besides, there are certain allied matters also with which this control has been associated. For example, it has been able to persuade a number of 100% foreign-owned companies to associate Indian capital, for instance, Hindustan Lever, Guest Keen Williams, Indian Oxygen, Glaxo, Pfizer, Goodyear, Brook Bond. The Gramophone Company, Avery of India, Associated Electrical Industries etc. The premia determined by the Capital Issues Control, in consultation with the foreign companies have been considered fair and reasonable in evey case not only in protecting the equity interest of the foreign shareholders of these companies but also by the common investor in India who found investments in these companies as a sound and attractive investment. Another method through which the Control may be said to have protected the interests of the ordinary investors has been the regulation *inter se* ratios of the valuation of the shares of the merging companies. When application for issue of capital for such mergers are received, the Control sees to it that the ratio of exchange of the merging company's shares for the merged company's share is a reasonable one.

The policy of the Capital Issues Control is under constant review of

the government. One such instrument, already mentioned, is the *Capital Issues Control Advisory Committee* whose meetings are generally held every quarter. Whatever problems crop up, or doubt arise or suggestions made from outside responsible quarters, all these are referred to the Committee for advice. The recommendations of the Committee are seriously considered by government and such modifications, as are considered necessary, are made in the policy. A number of relaxations in the control have been made in the past. A comparatively more important of the relaxations was the Capital Issues (Exemption) Order 1966, which gave a number of relaxations to the different parts of the corporate sector. The latest one, however, the Capital Issues (Exemption) Order 1969, recently notified, would top it. It would be seen therefrom that except retaining the core of the control at the strategic points, all the frills have been now done away with, while at the same time ensuring that the companies follow sound financial rules of the corporate sector.

It can also be said that this control has never been rigid or dogmatic in its approach to the financial problems of a company. That is why, although the principles have been evolved, individual cases of difficulty have been sympathetically considered and flexibility observed in the grant of consent if the merits of the case permitted so. Similarly, the exemption limit of the control has been often revised upwards as the economy of the country, mainly the climate for capital market, demanded.

Looking back over two decades of this Control's working, one can easily feel a sense of satisfaction that the control has amply achieved what it was intended to achieve. Some sound financial principles, wholly workable, for the corporate sector, have been evolved and gladly accepted by the joint stock companies in practice. The financial institution such as the *IDBI, IFC, ICICI, Unit Trust of India* and *Life Insurance Corporation of India* which now play a major part in financing the corporate sector ensure that by and large all the principles followed by Capital Issues Control are generally observed by the companies. Thus, there is an indentity of ideas between the Capital Issues Control, the financial institutions and the joint stock companies. It has prevented to exploitation of ordinary investor, a commonly expressed apprehension, by regulating share prices (at premium etc.) bonus issues, take-over and merger, rates, share valuation cases etc. Considerable indianisation of foreign-owned companies in a reasonable manner has been effected. The control has also provided an important help to the administration of the financial aspects of the company law, and has served as a useful guide to the newly emerging financial institutions of the country as part of the capital market. Similarly, figures of the capital issue consents serve as a useful indicator of the investment intentions in the country, an index of the capital market conditions ; and statistics collected

and kept by the control are being reliably and widely used by various agencies for purposes of economic analysis.

The control, as it exists to-day, may be now said to be providing a sort of adjunct to the working of the *Foreign Investments Board.* With control over the issues of capital by Indian companies retained only on the most essential aspects, it is felt that some guidance and regulation of the new companies in which foreign participation is important, is still needed. The *Foreign Investments Board* which is the approving agency for such cases often needs the collaboration of this control and it would appear that the current area of the control mainly confines itself to this.