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Semester-I

Programme Coordinator

Dr. Mukesh Singh Tomar
Associate Professor, Department of Management Studies
Center for Distance and Online Education,
Teerthanker Mahaveer University, Moradabad

Units Written by	Unit No.
Dr. Mukesh singh Tomar	

Editor

Professor Vipin Jain
Director,
Center for Distance and Online Education,
Teerthanker Mahaveer University, Moradabad

Dr. Amit Kansal
Assistant Director,
Center for Distance and Online Education,
Teerthanker Mahaveer University, Moradabad

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SYLLABUS

Course Name: Environmental Economics

Course Code: MAESP203

Course objective: This course develops managerial perspective to economic fundamentals as aids to decision making under given environmental constraints.

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Unit I Meaning of Environment of Business and Economic Environment

Unit II Elements of Economic Environment, Socio-Cultural Environment,

Unit III Inter-relationship between ecology and development

Unit III Environmental movement in India, New Economic Policy

Block II Theory of Consumer Choice

Unit IV Cardinal utility approach, indifference approach, revealed preference and

Unit V Theory of consumer choice under risk

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Block III Pricing practices

Unit VII Methods of price determination;

Unit VIII Pricing of multiple products; price discrimination

Unit IX International price discrimination and dumping

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Unit XII Theories of business cycles-psychological,

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Unit 1 ❑ Business Environment – An Overview

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1.0 Objectives

Business may be identified as the act of combining the resources or factors of production for pursuing a particular economic or commercial activity with the objective of making profit. The ultimate purpose of a business is to maximize owner's value over the long term by selling goods and services. But as an institution in society catering to the needs of people and drawing resources or factors of production from society, every business entity has to take into consideration the circumstances around it, the sum total of which is business environment. Thus,business environment refers to all the external forces that have a bearing on the functioning of business. Some external forces help and some hinder business. Just as the life and success of an individual depends on his innate capability, including psychological factors, traits and skills, to cope with the environment, so also the survival and success of a business entity depends on (1) its innate strength- the resources at its command, including physical resources, skill and organization- and
(2) its adaptability to the environment. The total business system thus operates with two sets of factors-the internal factors and the external factors.

The internal factors, corning from within the firm, are the factors over which thefirm has control. It can more or less alter or modify such factors as its personnel, physical facilities, organization and functional means (such as the marketing mix) to suit a specific situation. These factors are therefore generally regarded as controllablevariables. They are variables in the sense that in accordance with the needs of a particular situation, some changes may be introduced to their quantity or quality. Theinternal factors are varied by business from time to time to suit the requirements of business. These internal factors are sometimes regarded as constituting a micro environment, while the external factors are said to constitute a macro environment. Adaptability with the environment is one of the secrets of business success. The external factors, coming from outside the firm, are the factors more or less beyond thecontrol of the firm, for example, **the economic environment, political environment, legal environment, socio-cultural environment, demographic environment, competitive environment, technological environment, global environment and natural environment.** These environmental factors are largely regarded as uncontrollablevariables for business.

As the environmental factors are, by and large, uncontrollable, the success of a business depends to a very large extent on its adaptability to the environment, thatis, its ability to properly design and adjust the internal controllable factors to cope with the business environment. The external factors are not static. They change through time as the state of the economy or the polity or the society or as the international economy changes. Hence, business organizations have to remain alert about the changes taking place in the environment around them and adjust their internal factors to cope with the changing environment, so that they might surviveand succeed.

1.1 Introduction

1.1.1 Characteristics of Modern Business

Modern business has certain characteristics. The characteristics are partly the outcome of the changes in environment that are taking place through time. The characteristics are :

Change : Change is the basic character! stic-of business. If there is any single word that can best describe today's business, it is change. Business was always dynamic because the society is dynamic, human wants are dynamic. But modern business is more dynamic than the businesses of the yesterdays, as the pace of scientific and technological change in modem times has become faster. New technologies herald the arri val of new products leaving behind the old ones. "Today's growth product", aptly remarked Theodore Levitt, "may be tomorrow's earthen pot". The ever-changing market place has become a 'battle ground[1] for different companies surviving on consumers' loyatly and preferences. For developingnew products to suit the customer's demand and survive in competition the companiesare spending more and more on Research and Development.

Large-Scale Operation : Mass production and mass marketing are the norms followed by modem business enterprises. Machines are fast replacing manual labour in the manufacturing process. With machines operating machines, production in bulkhas become possible. Marketing activities are being stepped up to match massive production. New channels of distribution, super markets, discount houses and trade fairs have sprung up to meet the challenges of mass production and ultimately they cater to the demands of consumers.

Mass production and mass marketing have ensured economies of scale to the manufacturers, and the benefits of increasing scale of operation also accrue to the consumers in the form of reduced price, per unit of product. But large-scale production has also brought problems of management in every sphere of production and distribution. Hence, survival in business has become very tough.

Diversification : Today's business is characterized by diversification. The product portfolio of any medium or large business house is widely diversified,because business today do not like to keep their investments tied to any single lineof manufacturing or service for fear of losing every thing if the particular venturefails or does not perform well. Risk diversification ensures risk reduction through product diversification. Moreover, diversification through product differentiation enables well established companies to caterto the multidimensional needs of the consumers and thereby enjoy their continued patronage, so that they may expandtheir consumer base. Well-known Indian companies, like the Tatas and the Birlas, have diversified into wide variety of products and services for the purpose of extending their operation to a large number of customers spread over wider areas.

Companies also follow the merger and acquisition route to diversification. The nineties witnessed a surge in mergers and acquisitions across the globe. The valueof cross border mergers and acquisitions has risen more than seven times between 1987 and 1999. "The value of completed cross-border mergers and acquisitions rose from little less than $100 billion in 1987 to $720 billion in 1999". The developed countries accounted for more than 65 per cent of the mergers and acquisitions in terms of value, and the balance went in favour of the developing nations and Central and Eastern European Countries. With the repeal of the provisions relating to the regulation of monopolies in the MRTP Act, 1969, many Indian successful companieshave started acquiring smaller companies for expanding their share of the market anddiversifying production and distribution of goods and services in recent times. The high-tech IT industries of Indian origin are also acquiring foreign companies in developed countries.

Globalisation : Since end of the World War-II and particularly since the cominginto existence of the Bretton Woods system, the countries of the world have come closer to each other every day. The process has been further accelerated by the WorldTrade Organisation. Today the world has become virtually boundaryless. Goods and services produced in one country can be sold to other countries across the world

without much difficulty. Production facilities are being set up in different countries and products are being sold through a global network. Gradually, business houses are exposed to global competition which augers well for consumers, requiring quality goods at reasonable prices.

Infact, intern ationalisation orglobaJisation is fast becoming imperative for modern business due to technological innovations; crumbling trade barriers, freer flow of capital and technology, information explosion, intensity of market competition,changing life styles and the demand for new products. Internationalisation of business is a means of sustaining a strong domestic base in terms of technology, product, market and capital over a long period.

Science : Science and scientific ideas also occupy a major role in the global economic scenario. Infact, since the beginning of production for market, man has tried to improve upon the tools and techniques of production-to reduce the cost of production and develop new products and services for gaining greater share ofmarkets. The development, first of electricity and then atomic power, advances in metallurgy and allied fields, accomplishments relating to the space-age programmes, application of mathematics in managerial decision-making have made business processes more rational and precise than before.

Information : Another characteristic of contemporary business is the growing importance of information. Businessmen, having better information about markets, products, customer profile and the strategies of their competitors, always gain over others in the field. With the development of informantion technology it is now possible to collect, store, analyse, manipulate and transfer data and information from one place to another at a lightening speed. Hence, business information system andits management have assumed additional importance in modem business. Businessmenare now free from the drudgery of much detailed paper work. They can progress further by feeding right people with right information at the right time.

Government Regulation : In the 17th, 1 8th and 19th centuries government's role in business was the minimum. Adam Smith was the apostle of free trade within as well as between nations. But unrestricted competition did achieve neither full employment nor maximum wellbeing everywhere. The Great Depression, which started in the USA and spread to many other countries in the 30s of the last century, led to the arrival of the welfare state concept whose economic advocate was Keynes.

Keynes' plea for government participation in the economy for offsetting the shortfall of private investment was accepted by most economists. Subsequently, government regulations for controlling the abuses of unrestricted private business became a featureof policy throughout the world. These persist in India even in the post-reform era.

1.1.2 Objectives of Business

Before we discuss business objectives, it is desirable to be clear about themeaning of two other relevant concepts, viz., vision and mission of business. Vision refers to the goals that are broad, most general, and all-inclusive. A vision describes aspirations for the future, without specifying the means necessary to achieve those aspirations. A vision becomes tangible as a mission statement. Objectives render mission statements more concrete. In other words, mission statements seek to makea vision more specific, and objectives are attempts to make mission statements more concrete. Objectives, therefore, represent the operational side of an organization.

It may be stated that a typical business unit seeks to achieve more than one objective and there are always constraints on the attainment of some objectives. Objectives vary with the passage of time, as people's requirement change, so also change the technological and other variables. However, objectives common to most business are the following :

Profit : Making profit is the primary goal of any business enterprise. Profit is simply the excess of income over expense. Profit is the main incentive, motivator, strong sustainer, and judicious allocator of resources, objective indicator of productivityand a solid basis for growth, expansion and survival. Profit enables a businessmanto realize his other objectives too.

But some enterprises are not primarily and exclusively interested in making profits. For example, hospitals, schools, charitable institutions and government agencies are not basically concerned with the making of profit only. The non-profit enterprises customarily rely on gifts, endowments, receipts from money-raising projects, subsidies or taxes for sustenance. The basic objectives of these establishmentsare the provision of services that are socially desirable and useful.

In profit-making enterprises profit should not be the end in itself. Profit should be the beginning-the prime motivator for further developments in all other respects. Profit should promote the well being of all concerned. All the stakeholders should

share the profit according to their respective stakes in the business, so that they remain contended with the functioning of the business.

Growth : Growth is the next most important objective of business. Just as a living being .cannot remain static, it either grows or declines and ultimately dies; a business can also hardly remain static for long. The strategies adopted to achieve growth are the following.

(a) Production of more goods and services and expansion of the horizon of operation by extending to new markets;

(b) Diversification into new geographical areas of production and distribution of goods and services;

(c) Forward and backward integration for expansion in operation;

(d) Increasing the share of the market;

(e) Reduction in the cost of production and-increase in productivity.

Power : Business houses have vast resources at their command. These resources confer enormous economic and political power on the owners and managers. Several enlightened businessmen, like J . N Tata, G. D. Birla, and Dhirubhai Ambani have used their power for the good of society by providing the government with novel ideas for economic development of the country. Examples of successful businessmenplaying important role in providing political and even academic leadership, particularlyin the field of development of management science, are many. Hence, successful businessmen can make their experience available to society for the good of mankind.

Employee Satisfaction and Development : Success of a business depends, amongst others, on a contended and competent workforce. Hence, employee satisfaction and development is a very important objective of business. Successful business houses everywhere in the world care most for their employees. After all, is the employees who work and the result of their work is reflected in the growth ofthe business in terms of profit and expansion. Human resource development is a concern of every business organisation nowadays

Quality Product and Service : Providing quality product and service is yet another objective of business. For a a short period of time a company can survive through aggressive marketing strategy without bothering for quality. But in the long run companies who bother about quality and customer satisfaction only survive.

Quality earns brand loyalty and brand loyalty ensures expansion of the business through diversification. Side by side with production of quality products, the business should provide prompt quality service to its customers. Defects remain inthe products even in spite of strict quality control. So the producer must be ready to entertain customers' complaint. Thus, even the new products coming from the housesof -Tata, Godrej, Hindustan Liver, etc. get easier access to the market because oftheir quality consciousness and customer care. Hence, one objective of a business house has to be providing customer satisfaction through quality products and services.

Market Leadership : Market leadership is the ultimate objective of every business. However, in order to achieve the position business houses encourage innovation. Schumpeter pinpointed innovation as crucial for business growth. Innovation may take place in the development of a newproduct, improvement in thequality of existing products, advertising, distribution, finance or any other relevantfield. Market leadership means rising above others in the market. This cannot be achieved without being ahead of others.

More Joy and Pleasure for People : Economic development in may countries has now reached a stage where men's demand for services is increasing faster than that for basic necessities. The basic reason behind this increase in demand for services is growing demand for joy and pleasure. After all, the driving factor behind human civilization is quest for pleasure and comfort. From the day of f abri cationof tool s for hunting to the development of computer and information technology the motive that drove mankind is more benefit and pleasure at lesser effort. In thedeveloped countries today around 70 per cent of the working people find employmentin the service sector and the percentage of national income derived from the service sector is higher. In the context of the above, business houses should strive to give people more joy and pleasure by designing their products and services accordingly.

Good Corporate Citizenship: A business organization has a separate entity distinct from the members composing it. As an entity it has to work within the framework of different rules and laws enacted by the State. Good corporate citizenshipimplies that a business unit obeys the laws of the land, pays taxes, and honours all commitments like every good citizen. Bending rules to its favour, not abiding by the different laws of the land by adopting all dubious means might help earning high profit and enable a company to keep its shareholders in good humour. But, it cannot

earn respectability. Further, business organizations indulging in malpractices may land in trouble any time. It has been found that many otherwise successful business houses find it difficult to come out of the inglorious situation once they are found indulging in such activities. Hence, every business house should strive to be a good corporate citizen.

1.2 Business Environment

Business environment is the environment within which business operates, determined by political, economic, social, legal and technological factors originating at home and abroad.

1.2.1 Economic Environment

Economic health of the country, economic policies and economic systems are the important external factors that constitute the economic environment of business.

The economic conditions of a country-for example, the state of health of economy, the stage of development of the economy, economic resources, the levelsof income and prices, the pattern of distribution of income, and assets, etc. are amongthe important determinants of business strategies.

In a developing country, the low per capita income of people is one of the reasons for very low demand for products of luxurisus consumption and high demandfor essential commodities. However, in such countries the market for products for which the demand is income-elastic expands with increase in income. As the business houses are unable to increase the purchasing power of the people to generate a higher demand for its costlier products, they may have to reduce the price and concentrate on the production of essential commodities. It may even be necessary to develop new low-cost products to suit the low-income market. On the other hand, business prospects are generally bright in countries where investment andincomes are high and rising.

The economic policy of the government, needless to say, has a very great impacton business. For example, a restrictive import policy, or a policy of protection, may greatly help the import-competing industries, while a liberalization of imports may put such industries in a difficult position. In every country such changes in policy occur from time to time and the business houses are required to be alert about it.

In India, the government's concern about the concentration of economic power had restricted the role of the large business houses andforeign concerns to the core sector, the heavy investment sector, the export sector and the backward regions. But with the liberalization of Indian economy through new economic policy in 1991,most of those restrictions having been withdrawn, the Indian and foreign corporates are investing in all the sectors except the defence and strategic industries.

The monetary and fiscal policies of a government can provide incentives and disincentives to economic development in a country. In India, cheap money (low interest) policy combined with budgetary (fiscal) tax and other concessions have brought about a revival of India's corporate sector after 2001 (which sector was depressed since 1994 for all sorts of reasons). These policy-measures of the government provide the environment under which business houses operate in the country.

The scope of private business in a country 1 argely depends upon the economic system of the country. At the one end there are the free market economies orcapitalist economies and at the other end there are the centrally planned economies, with a large number of countries in between the two extremes. However, with the disintegration of the East European communist countries the importance of state command and control in economic development has declined since late eighties. But the developing countries of Asia, Africa and Latin America largely follow a policyof mixed economy. The freedom of private enterprise is maximum in the free market economies, whereas in the developing counties the extent of State intervention being greater, the degree of freedom of operation of business houses-is less. So the business houses operating in a country have to take into consideration the nature of the prevailing economic system and its constraints.

1.2.2 Political and Legal Environment

Political environment refers to the condition created by the political factors operating within the country. Important among such factors are the nature of the government and the character of the party system. The government may be dictatorial or democratic. In a dictatorship policy making is a one-man or one-party show. Ina democracy policy making is in the hands of the majority party (in power) elected through a process of free vote by all adult citizens for a specific period of time. Ina multiple party regime the citizens, including business houses, have greater

opportunities to ventilate and redress their grievances and fight for their interests than in a single-party system. The majority party (forming the government) is checkedand balanced by the opposition. The level and rate of business growth have been generally higher in democratic than in dictatorial countries.

The legal environment is created by the legal enactments, conventions and practices prevailing in the country. If it is not helpful, business would stumble and suffer. In Indi a we have a framework of helpful industrial and commercial laws, supported by an independent judiciary, which is conducive to good business.

1.2.3 Socio-Cultural Environment

The socio-cultural fabric is an important environmental factor that should be analysed while formulating business strategies. The socio-cultural environment is thesum total of the customs, traditions, beliefs, tastes and preferences, and values of people. The customs and traditions of people reflect basic tenets of their ci vilization. They general ly change very slowly with economic development and changes in the social relations. Hence, any thing that apparently goes against the customs and beliefs of people will not get approval of the people of the society. Marketingstrategy has to take note of this. Thus, for a business to be successful, its strategy should be the one that is appropriate in the prevailing socio-cultural environment.The marketing mix shall have to be designed as best to suit the environmentalcharacteristics of the market. In the competition for expanding their markets in the developing and the least developed countries, many multinational companies ofEurope and America had to change the character! sties of their products and marketing mix to suit the beliefs, customs, traditions, etc. of people of those countries. For example, Helene Curtis had to switch to black shampoo in Thailandto satisfy popular local demand; Nestle today brews more than forty varieties of instant coffee to satisfy different national tastes. But tastes and beliefs can also be changed by aggressive marketing, as has been the case with women's wear in Indiain the last two decades (an illustration of western cultural imperialism)

Social inertia and associated factors come in the way of the promotion of certainproducts, services or ideas. We come across such social stigmas in marketing of family planning ideas, use of bio-gas for cooking, etc. In such circumstances, the success of marketing depends, to a very large extent, on the success of coping with social attitudes or value systems of the country concerned.

1.2.4 Demographic Environment

The demographic environment (really apart of the economic environment) is created by the different characteristics of the population. A high-population countryis a country with a high market potential.

A rapidly increasing population indicates a growing demand for many products. High population growth rate also indicates an increase in labour supply. As labouris cheap relatively to capital, countries with huge population generally use labour- intensive technology unlike in countries with low-population (Europe and America).

Similarly, the age composition and sex ratio determines what are to be produced and how they are to be produced. In countries with higher longevity of people and lower birth and death rates, there will be plenty of senior people. Thus, goods and services used by the senior people will be very much on demand. On the other hand, with decline in the number of middle aged and younger people, there will be dearthof skilled and energetic people, to man the factories and workshops. Today there isa growing demand in the developed countries of West for technically ski lied manpower from the developing countries like India and China. Side by side, most of the high-tech industries of those countries are also out-sourcing their jobs to these countries to discourage immigration from these countries and also having the work done at a lower cost with the skilled workers working in their own countries and thereby having a greater margin of profit. This has led to the growth of "call-centres"around the world to do specialists job with the help of information technology systemstationing oneself anywhere in the world.

Lastly, the occupational mobility of people also influences the pattern of business development of a country. Higher mobility of people ensures dispersal of industries for the purpose of getting maximum advantage in the form of economicsof localization of industries and scale of operation.

1.2.5 Competitive Environment

Competition is another very important external factor that influences sustainability and growth of business entities in a country. Business strategy of a firm is highly influenced by the nature and degree of competition prevailing in acountry. Since the dawn of civilization, mankind thrived and enriched themselves in all spheres of life through competition. Business, being apart of human society, cannot succeed and

reach perfection without healthy competition. Cost-effectiveness and product quality cannot be ensured in a non-competitive environment.

In countries with absolute State control over all forms of economic activities development could not proceed beyond certain levels and this actually led to the disintegration of the erstwhile East European communist countries and subsequent opening up of the economies of China and some other countries like Vietnam,Albania, etc.

In India, on the other hand, there existed strict control over big business houses for a pretty long time under the Monopolies and Restrictive Trade Practices Act1969. But in course of time it was realized that restrictions on growth in the scaleof operation of business houses actually discourage efficiency in operation andeconomics of scale. Hence, with the adoption of the New Economic Policy in 1991, the operation of the Act has come to be limited to only the restrictive trade practices, pre-entry scrutiny of investment decisions by the big business houses has beendispensed with. The Act has been repealed and in its place the Competition Act, 2002 has been brought to ensure competition among business houses. Moreover, no discrimination is now made among the Indian and foreign enterprises with respect to the operation of the policy on monopolies and restrictive trade practices in thecountry. This change in policy has led to an increase in foreign investment in the country through equity participation (portfolio investment) and direct investment (foreign direct investment). As a result of these investments, foreign technologies arealso flowing into the country, paving the way for opening up of the new horizons in development.

1.2.6 Technological Environment

Technological environment refers to the situation in respect of the state oftechnology in the country. With respect to the state cf technological development, countries differ widely. In this / difference lies the advantage of certain nations in the specialization of production and distribution. Hence, the technologies are patented. The countries possessing the patents and trademarks do not like to share them with others unless the terms and conditions of sharing the technology are favourable to thesupplier of technology. Naturally, even as some technologies are shared, all the technologies are not shared, and the countries have to depend largely on their own technological capabilities.

Thus, business houses setting up their working facilities in a country have totake into consideration the state of technology available in the country. The principal purpose of a business entity being making of profit, it has to ensure itself about the best way of doing the work so that the cost of production and the quality of products can be acceptable to people of the country.

Again, a firm that cannot cope with the technological changes taking place inthe country may not survive. Further, the different technological environments of different markets or countries may call for product modifications. Because, people will not accept a technology with which they are not familiar or not convinced about the desirability of the use of technology. The application of a particular technologyin a country also requires trained manpower capable of working with the technology. So all these factors are required to be taken into consideration before deciding upon the use of a technology in production or distribution of goods and services in the country.

1.2.7 Global Environment

The global environment is the totality offerees, originating from outside the country and having impact, good or bad, upon domestic businesses. In the circumstances, global environment is very important from the point of view ofcertain categories of business. It is particularly important for industries directlydepending on imports or exports and also for import competing industries. Forexample, a recession in foreign markets, or the adoption of protectionist policies in foreign nations, may create difficulties for export industries. On the other hand, a boom in the export market or a relaxation of the protectionist policies abroad may help the export-oriented industries. A liberalization of imports may help some industries that use imported items in the manufacturing of sofne final products, but may adversely affect import-competing industries.

It has been observed that major international developments have their spread effects on countries across the world. The Great Depression in the United States inthe 1930s sent its shock waves to a number of other countries. Oil price hikes by OPEC had adversely affected a number of economies. These hikes increased the cost of production and the prices of certain products, such as fertilizers, synthetic fibers, etc. in India. The situation also created demand for automobile models that economiseenergy consumption.

A good export market also enables a firm to develop a profitable product mix and to consolidate its position in the domestic market. Export market facilitates the attainment of optimum capacity utilization; a company may be able to mitigate the effects of domestic recession by exporting. However, a company, which depends too much on the export market has also to face the impact of adverse developments in foreign markets. Exports add to national income.

1.2.8 Natural Environment

This is given by the state of country's natural resources, including air and water and climate and topography and access to the sea. Differences in geographical conditions between markets may sometimes call for changes in the marketing mix. Geographical and ecological factors also influence the location of certain industries. For example, industries with high material index tend to be located near the sources of raw materials. Climate and weather conditions influence the location of certain industries like the cotton textile industry, tea and coffee industries. Temperate climate promotes labour efficiency. Business activities have effects upon the natural environment. Hence, business has a responsibility to see to it that its practices do not lead to an excessive depletion of a scarce natural resource and /or a degradation ofthe natural environment around it (through, for example, pollution or ecological destruction). Legislation has been passed in many countries, including India, for preventing environmental destruction by individuals or institutions. The environmentfactor is considered in social audit of many firms.

1.3 Knowing the environment

Business being a product of different environmental factors, there develops a , relationships between business and its environment. First, there is symbiotic relationship betweu business and its environment and among the environmentalfactors. Business both influences and is influenced by its natural environment. Secondly, these environmental factors are dynamic; they keep on changing as-years roll by. Lastly, a particular business firm, by it self, may not be in a position tochange its environment. But along with other firms, business will be in a position to mould the environment into their favour to a large extent.

The environment, as described above, provides a mass of information some of which may be ambiguous or not necessary. It is the task of a business house to select the information relevant to it and adjust its operations to conform to the requirement of the environment. Three different steps seek to address this problem. They are :
(i) the enacted environment, (ii) the domain and domain consensus, and (iii) the task environment.

Enacted environment- an organization seeks to create its own environment outof the total external environment. The environment that the organization creates is called enactment. Enactment implies that the organization creates a relevant environment for itself by aggressively scooping, narrowing and scanning the externalenvironment. In effect, the organization creates the envioinment to which it reacts.It does not react to the entire environment because every thing there is not relevantto it.

Domain and domain consensus- the domain is that part of the enacted environment, which the organization carves out foritself. The firm delineates its own territory out of the environment. The delineated territory comprises the range of products offered, population served and services rendered. The organization focuses its efforts on these three areas while paying less attention to other areas.

As is well known, an organization has many stake holders-owners, employees, customers, government, public, suppliers and lenders. Domain consensus is formed when all the stakeholders agree upon the domain of the organization.

When domain consensus is not reached, conflicts may arise regarding which part of the environment should be monitored. This conflict causes confusion and backbiting,when the company is blind- sided by an unexpected occurrence from a poorlymonitored sector. Hence, in order to reach domain consensus the enterprise should identify the domain for itself that is accepted by the concerned stakeholders.

The task environment-this specifies the range of products to be offered, the technology to be employed and the production strategies to be.used to counter competition. The task environment being the final stage from where the result emerges requires constant and careful surveillance. At the same time the other elements are also not to be ignored or paid less attention.

1.4 Importance of environment analysis

Environment analysis has three basic goals. First, the analysis provides an understanding of the current environment and the changes likely to take place in the task environment. It is important that one must be aware of the existing environment.At the same time, one must also have the vision to see far into the future. After all, every business should have a long-term projection (or forecast).

Secondly, environmental analysis provides inputs for strategic decision-making. Mere . collection of data and information about the different constituents of the environment is not enough. The information collected should be used in strategic decision-making to gain maxi mum advantage out of them.

'Thirdly, environmental analysis should facilitate and foster strategic thinking i n organizations-typically a rich source of ideas and understanding of the context within which a firm operates. It should challenge the current wisdom by bringing fresh viewpoints into the organization. To be specific, the benefits of environmental study are as follows:

1. Development of broad strategies and long-term policies of the firm.
2. Development of action plans to deal with technological changes.
3. To foresee the impact of socio-economic changes at the national and international levels on the firm's stability (future).
4. To analyse competitors' strategies and formulate effective counter-strategies.
5. To keep the business on the dynamic path to development.

Management has to take decisions quickly and correctly to cope with the changing scenario. Hence, business decisions taken under the pressure without proper analysis of the environment is likely to be incorrect or misleading. It is true that in an ever-changing situation every decision taken may not be correct, but every effort should be made to make it appropriate to the particular situation. "Environmentalanalysis and diagnosis give strategists time to anticipate opportunities and to plan to take optimal responses to these opportunities. It also helps strategists to develop an early warning system to prevent threats or to develop strategies, which can turn a threat to the firm's advantage". When conducted properly, environmental analysis

leads to the enhanced capacity and commitment to understanding, anticipating and responding to external changes on the part of the firm's key strategic managers. Responsiveness is achieved by inducing managers to think beyond their task or industry environments, often forcing them to relfect upon their cognitive biases. In short, at the process level, environmental analysis offers one basis for organizational learning. In the real world of business, firms that systematically analyse and diagnosethe environment succeed more than those who do not.

1.5 Process of environmental analysis

Environment analysis is a challenging, time-consuming and expensive affair.The analysis proceeds through four distinct sequential steps; (i) scanning, (ii) monitoring, (iii) forecasting, and (iv) assessment.

Scanning: Being the first step in the process of environmental analysis, it involves general surveillance of all environmental factors and their interactions in order to (a) identify early signals of possible environmental change, and (b) detect environmental changes already under way,

Scanning is not a structured analysis. It is a general analysis of the relevant variables. The potentially relevant data for scanning are unlimited, but are sometimes scattered, vague and imprecise. The fundamental purpose of the analysis in scanning is, therefore, to make the data and information precise, relevant and purposefulthrough proper selection, arrangement and study.

Monitoring: Monitoring involves tracking the environmental trends, sequences of events, or streams of activities. It frequently involvesfollowing the relevant signalsor indicators identified during scanning. The purpose of monitoring is to assemble sufficient data to discern whether certain trends and patterns are emerging. Thus, as monitoring progresses, the data frequently turn precise and purposeful. Three outcomesemerge from monitoring: (a) a specific descripti on of environmental trends and patterns to be forecast; (b) the identification of trends for further monitoring, and (c) the identification of areas for further scanning. The outputs of this stage become the input of the subsequent stage, that is, forecasting. They may also require further scanning and monitoring, if necessary.

Forecasting: Scanning and monitoring provide a picture of the trend of what hastaken place- the relationship between cause and effect. Strategic decision-making for

the future, however, requires understanding of the possible future path of events. Naturally, forecasting calls for rigorous analysis of the essential elements of the environment and linking them with the prospects of the firm.

Forecasting is concerned with developing plausible projections of the direction, scope, and intensity of environmental changes. It tries to layout the evolutionary pathof anticipated changes. Unlike two earlier steps (scanning and monitoring), forecastingis well-focused and is a much more deductive and complex activity. This is so because the focus, scope and goals of forecasting are more specific than the earlier two stages of environmental analysis.

Assessment: Scanning, monitoring and forecasting are not the ends in themselves.Unless their outputs can be assessed to determine their implications for the organisation's current and potential strategies, scanning, monitoring and forecasting would simply provide 'nice-to-know' information. Assessment involves identifying and evaluating how and why current and projected environmental changes affect or will affect strategic management of the organization.

In assessment, the frame of reference moves from understanding the environment-the focus of scanning, monitoring and forecasting-to identifying what the understanding means for the organization. Assessment, therefore, tries to answer questions such as what are the key issues in the environment, and what the implications of such issues for the organization are.

Linkages among the four steps

Though conceptually scanning, monitoring, forecasting and assessment are separate activities, they are very much linked with each other. For example, upon unearthing an emerging trend in the consumers' demand through scanning, one mightquickly start analyzing the potential implications of the trend.for the organization by implicitly forecasting the future path of the trend. If warranted by the potentialimpact, one may then continue scanning and monitoring. Also, forecasting often proves difficult, if not impossible, because of insufficient knowledge and data about the topic or trends being forecast, thus forcing a return to scanning and monitoring efforts. The resulting implications often require the organisation to conduct further scanning, monitoring and forecasting. Thus, environmental analysis is not as easy as moving from scanning to monitoring and the other two earlier steps.

1.6 Limitations of environmental analysis

Environmental analysis, as with any other analysis, has certain limitations. These limitations are :

1. Environmental analysis does not foretell the future, nor does it eliminate uncertainty for any organization. It helps fight uncertainty. Thus, organizations that practice environmental analysis sometimes confront unexpected events-events not anticipated during environmental analysis. Environmental analysis, however, should reduce the frequency and extent of surprises that may confront a company.

2. Environmental analysis itself is not a sufficient guarantor of organization effectiveness. It is only one of the inputs in strategy development and testing.

3. The potential or environmental analysis is often not realised. It is some times used for comparing results and at ti mes managers place uncritical faith in the data without thinking about the data's verifiability or accuracy.

4. Too much reliance is often placed on the information collected through environmental scanning. When there is overloading of information, one is likely to get lost in the mass of information and become purposeless. So, effort must be given to collect only the data and information necessary for the organisation, and they should be analysed with due care in accordance with the steps suggested.

Success lies in adventure and strategic risk-taking. It eludes those who hesitateto venture" forward. Environmental analysis often makes an individual too cautious in his approach, and he is likely to be overtaken by events.

1.7 Summary

Business organisations operate in a particular socio-economic-geographical- political-natural environment. The factors of the environment are external to business.Hence, they are more or less uncontrollable andeven unmanipulable by business. Further, these external factors change from time to time in accordance with changes

in peoples' need, belief and use. But, the factors internal to business, particularly its resources and other operational advantages, are controllable and manipulable. In order to cope with the external environment, business organisations use their internal factors and resources. But, the purposeful use of internal resources by business for strategic decision-making cannot be made without an analysis of the environment around it.

The analysis of the environment is required to be done by top executives of business for decision making. To be specific, top executives in marketing, financeand human resource, who make important decisions in business about fixing oftargets of production and sale are the persons who undertake environmental analysis. With the rapid improvement in information technology the task has become easier. The business organisations now maintain Management Information System to handlethe job of analysing the environment. In a competitive world every organisation tries to be ahead of others, and for this they have to commit more time, resource and energy to environmental analysis. Ultimately the success of a business depends on how perfectly strategic decisions are taken and how efficiently they are executed.

1.8 Exercises

Long answer type :

1. What is business ? What do you understand by internal and external factors of business ? Examine their relevant importance in business operations.
2. Examine the principal characteristics of modern business.
3. State and explain the principal characteristics of modern business. Show how they influence business activities.
4. What do you understand by vision, mission and objectives of business ? Explain the principal objectives of business.
5. What do you understand by business environment ? Give a brief account of the different constituents of business environment.
6. State the importance of environment analysis in business. Give an account of the process of environment analysis.

7. State how different steps of environment analysis are linked with each other. Mention the limitations of environment analysis.

Short answer type :

1. Mention the major types of environment in which businesses operate.
2. State the role of internal factors in business.
3. State the characteristics of modern business.
4. What is meant by domain and domain consensus?
5. Define and explain task environment.
6. Mention the external factors in business.
7. State what is meant by environment analysis.
8. Mention how four steps of environment analysis are linked with each other.
9. State how environment scanning is made.

Objective type :

Find the correct answer :

1. Broad'goal of business is set by –
   - (a) vision
   - (b) mission
   - (c) objectives
   - (d) none of the above.
2. Political environment refers to –
   - (a) influence exerted by political system,
   - (b) influence exerted by strikes,
   - (c) influence exerted by legislature, executive and judiciary,.
   - (d) influence exerted by the President of India.

3. Process of environmental analysis begins with—
   (a) forecasting
   (b) scanning
   (c) monitoring
   (d) information management
4. New economic policy was announced in—
   (a) 1987
   (b) 1990
   (c) 1991
   (d) 1995

Answers of objective type question : 1. (a), 2. (a), 3. (b) and 4. (c).

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Unit 2 ❑ Business and Society

Structure

2.0 Objectives

2.1 Introduction

2.2 The Macro Environment of Business

2.3 Business Ethics

  2.3.1 Ethics and Decision Making in Business

2.4 Role of the State in the Business Scenario

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  2.5.3 Unique Role of Mutual Fund in Corporate Governance

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2.6 Summary

2.7 Exercises

2.8 References

2.0 Objectives

By society we understand a collection of human beings, generally within some identifiable geographical limits. These human beings have common ways of living, thinking, aspirations, beliefs and faith that are again the products of the environment they live in and the institutions they create and depend upon for their sustenance. These people, with their hopes, aspirations, beliefs and faiths, have material needs forsatisfying which they depend upon some institutions and practices known as business. Thus, the relationship between business and society is very close. In fact

business is an integral part of the society it has to cater to. Business is organized for satisfying wants of people. Profit is the principal motivating force behind business. Business, canied on by some members of society, is a pan of society. Being a partof society, meeting needs and wants of society for profit, business influences society,which, in turn influences business. The types of products to be manufactured, the marketing strategies to be employed, the way business should be organized, are all influenced by the social structure and culture of society. The social system, on the other hand, is influenced by the way business functions. The organization of business, the way business functions, innovations, transmission and diffusion ofinformation and new ideas, etc., may influence society. Business activities can greatly influence social attitudes, tastes, values, outlooks, customs, traits, etc. However, it is very difficult and in some cases-, almost impossible, to change many elements of the social environment in the short period.

The relation between business and society is very close, but at the same time the basis of relationship being supply of goods and services for profit, there existspotential scope of conflict between business and society. Businesses may have practices which harm society. Hence, over the centuries, there have emerged certain codes and conventions to be followed by both business organizations and society for their mutual benefit. The objective of the study extends to examining the changing relationship between the two parties having sometimes opposing interests but at the same time dependent upon each other for their sustenance and growth. Adam Smith was sure that if conducted in the right way, business would maximize both its own profit and benefit for society, for the two need each other.

2.1 Introduction

The first step in understanding business is to recognize that business is something very specific and limited. Despite widespread belief to the contrary, business is not the whole of economic life, far less the whole of life. In highlighting
the fact that business has boundaries, and that it specifies something panicular and distinctive, the classic business pronouncement that 'Business is business' expressesa fundamental truth (Elaine Sternberg 1994). Business is about the provision of quality goods and services within a community in a way that provides long-term financial benefit to the owners. If a business fails in respect of quality, or concentrates

too much on short-term profits, it will not survive for long, and owners will ultimately be the losers. But business must both survive and thrive. On the micro level it must focus on owners[1] profit, but on the macro level it has to address to the wider demands of social justice. It may survive, but it will not flourish unless it attends to the demands of ethics and morality within society.

Social responsibility of business and business ethics have to be understood with reference to the purpose of business cited above. Through economic or commercial activities businessmen satisfy material human wants and .other social needs. On the other hand, business depends for its survival and prosperity on society who provide the resources, raw materials, services and infrastructure that it needs for converting the factors of .production into profitable goods and services. Again, in order to be able to create and enjoy the fruits of enterprise, business needs protection from society. As such, when we speak of business-society relationships, we may in fact mean business and the local community, a country as a whole, or business and a specific group of people (consumers, stock holders, employees etc.)- But, when we refer to business and entire society, we think of society as being composed of numerous interest groups, more or less formalized organizations and a variety of institutions. Each of these groups, organizations and .institutions is a purposeful aggregation of people who have banded together because they represent a common cause or share a set of common beliefs and interest in a particular issue. Thus, business must attend to the legitimate demands and interests of all stakeholders. Ithas obligations not just to shareholders, but also to employees, suppliers, customers, creditors, the wider community and the natural environment, which it may harm through pollution.

2.2 The Macro Environment of Business

Business environment is divided into macro-environment and micro-environment. The micro-environment is created by forces arising from within business units. The macro environment of business includes the conditions that exist around business. Accordingly, environment influences business activities and is also the key concept in understanding business-society relationship and formulation of business ethics.The macro environment has four principal segments: social, economic, political and technological.

The social segment of the environment focuses on demographics, lifestyles of people, social values, beliefs, and institutions. The economic segment comprises the economic policy of state- the direction of development, monetary and fiscal policies, balance of payment position of the country and the level of employment and income of people. The political segment of the environment includes primarily the processby which legislations are passed and administered in the country. The businesshouses also take keen interest in the regulatory processes and the changes that occur over time in business regulations and policy towards different industries. Finally, the technological segment represents the total state of technology-based advancements or progress made by the country and also the policy of the country towards research and development for technological development.

● Social Responsibility of Business

In the most simple and traditional way, the social responsibility of business can be interpreted as the responsibility of business in respect of the impact of theiractions on society. As business operates within society, it cannot disown responsibilityto society. It has to see to it that the harmful effects of its modes and operations upon society are minimized and beneficial effects maximised.

Naturally the idea of social responsibility requires business to consider its activities in terms of the social system and hold itself responsible for the effects ofits acts anywhere in that system.

The social responsibility idea is not entirely new. The classical view is that society could determine its needs and wants through the marketplace and business could fix the terms of trade depending upon the market forces (the forces of demand and supply). Adam Smith found the role of "invisible hand" of the market in transforming self-interest into societal interest. For ensuring rational development through individual effort, Smith suggested a system consisting of six institutions - economic motivation, private property, free enterprise, free markets, competition andlimited liability. The role of government should be very small. That government isthe best which governs the least, confines the government to political functions only.

Towards the end of the nineteenth century it was realized that industrial development with scant regard for social responsibility and near-absence of any role of State create innumerable social-economic problems. In the circumstances, what followed was proliferation of laws regulating business behavior. The legal restrictions

gradually came to influence the attitude and activities of the corporate sector. A new era of social responsibility of business dawned in the wake of the arrival of the welfare state. Social responsibility of business is a late twentieth century concept so far as management science is concerned. Of course, in the days of the classical economists the business community used to volunteer in philanthropic activities like helping the distressed during earthquakes, floods and famines. They had an idea, though vague, of their moral responsibility towards people within as well as outside their work places.

During the economic crisis of the 30s in the 20th century there was a transition from the laissez faire to the Welfare State with mixed economy in certain countries. By the 1950s social responsibility of business came to include employee welfare, decent wages, work place safety measures, retirement benefits, enforced upon business by legislation (e.g. Factories Act) in many countries.

Thus, the period from 1950s may be considered the modern era in which the horizon of the concept of social responsibility of business considerably expanded and gained popular acceptance. During this period, the emphasis moved from little more than a general awareness of social and moral concerns to specific issues, such as product quality and safety, honesty in advertising, employee's rights, affirmative action, environment protection and transparency in accounting. Under the changed scenario, social responsibility came to f be identified as more specific responsibility of the corporate sector, and different scholars defined social responsibility of business in different ways keeping in view the multidimensional impact of corporate activities on society. One definition carne from Joseph McGuire who laid down,"The idea of social responsibility supposes that the corporation has not only economic and legal obligations, but also certain responsibilities to society which extended beyond these obligations".

The above definition reflects the extent of consciousness of society about the positive role of the corporate sector in protecting and furthering the interest of peoplearound them. Thus the relation between society and business came to be recognized as a two-way one: both are dependent on each other for their survival and growth. 'There exists an implicit or explicit contract between business and the community in which it operates. Business is expected to create wealth, supply markets, generate employment, innovate and produce a sufficient surplus to sustain its activities and

improve its competitiveness while contributing to the maintenance of the community in which it operates".

It would now be pertinent to provide here the four types of responsibilities businesses owe and are supposed to discharge in fulfillment of their duties to society. The four responsibilities are economic, legal, ethical and voluntary / discretionary (philanthropic).

- **Economic Responsibility**

First and foremost, business is an economic entity whose job is to produce goods and services that society wants and to sell them at fair prices. Profiteering is distinguished from normal profit making. Businesses should not do anything that harms the legitimate interests of other players in the economy.

- **Legal Responsibility**

Second, there are legal responsibilities of business. There are many laws relating to businesses which ought to be obeyed by businesses. If this does not happen many interest-groups in society may suffer. Just as there exists almost in every country a'legislative framework to protect business, so also there exists a responsibility onthe part of business to respect the legislative framework for the protection of the non-business sector.

- **Ethical Responsibility**

Ethical responsibilities of business include those activities and practices that are based upon the values that bind society and are respected by its members. Thus, ethical responsibilities embody the range of norms, standards and expectations that reflect the concern for what consumers, employees, stakeholders and the community regard as fair and just.

Ethical values and beliefs of people of a society also change from time to time along with changes in literacy, living standards and technological developments followed by consumer-movements, and aggressive journalism. Ethical responsibilitiesin this sense continually are under scrutiny and debate by the interested sections of the society as to their legitimacy.

- **Philanthropic Responsibilities**

Society also expects from business some voluntary/discretionary or philanthropic responsibilities. Strictly speaking, these responsibilities are not legally enforceable. But, the demand for philanthropic services from business actually originate from the common belief of people everywhere that those who own wealth should do somethingfor the weaker sections of the community. Such activities include provision of health and educational facilities for the poor, creation of recreational facilities, undertaking programmes against drug abuse and other social evils.

2.3 Business Ethics

The discipline that has come to be known as "business ethics" is hardly new. Since ancient times philosophers and social thinkers all over the world have dwelt upon the connection between business and morality. Study on ethics-business relationship has a long history that can be traced at least to the days of Aristotle, who had equated profit with usury. Kautilya, the chief adviser, philosopher and guide of Chandragupta, the founder of the Maurya dynasty, who ruled between 317-293 B. C, in his masterpiece, Arthasasthra, not only dealt with the science of economics but also provided directives for consumer protection, employer-employee relationship and even trading practices. Again, the inscription of Bible that 'it is easier for acamel to pass through the eye of a needle than a rich man to pass through the gatesof heaven" signifies the social belief that acquisition of material wealth through business was never seen as a virtue.

Commerce depends upon the participation of the majority of a society. Thus, forits very existence it depends upon some common understanding among vast majority of the participants. The common grounds of understanding are bas.ed upon ethical values. Ethics is about right and wrong in human conduct. Ethics is about values, choices, dilemmas and character. All these elements assist us to make fundamental decisions. Values are core beliefs about what is intrinsically desirable. They underlie the choices made in work decisions just as they underlie the choices made in one's private life. They give rise to ideals that are called ethics or morals. The two termsare sometimes confused, though they are synonymous. While ethics is derived from Greek with its root being 'Ethikas', moral is derived from Latin. They are interchangeable terms referring to ideals of character or conduct, for distinguishing between right and wrong.

The actual decisions we reach will be the result of how our values can be best realized in a particular situation. But once we start talking about values, we have to face the fact that in a present day society there is practically no essential agreementon values. We live in a multi-cultural and pluralistic society. In the past, people lived in more cohesive communities. There was a general agreement on values, often reinforced by shared culture and religion. Nowadays that form of cohesion hasdisappeared making room for differences on most issues. Thus, the decision-makers are left with the hard task of prioritizing the issues involved and enquiring about their importance on different sections of society. Such ethical enquiries require the decision maker to consider the facts in the light of important values. Values shapethe way the problems are perceived. They are crucial to our notion that there is a problem to be examined rather than blindly accepted.

When ethical analysis of a problem precedes decision-making, the decision is said to be ethically evaluated. In order to reach an ethical decision, one must define the problem and determine the desired result. The value to be maximized must be identified and all aspects of the problem must be analysed with reference to thevalues involved. After this, alternatives to each dimension of the problem have to be identified and assessed for knowing which values to accept and which values to reject. Thus, ethical decisions are decisions that result from a reasoned choice from value alternatives.

● Foundations of Ethical Decision-Making

That the concept of principles or ethics in business is not new has already been shown. But, before the arrival of the nineteenth century and particularly before the great depression of the 1930's, ethics in business decision-making did not attract serious consideration. Traditionally, there have been two broad schools of thought in ethics, which have developed over the years. The two main groups or schools are teleological ethics and deontological ethics.

● Teleological Ethics

Teleology is that branch of knowledge which deals with ends or purposes. In its purest sense teleological ethics primarily focuses on the 'ends', the results of the decision rather than the method of getting that result. A typical teleological view is that the 'ends justify the means'. It implies, the decision maker, before taking decision about the ways or means of doing something has to have the end result or

the target to be achieved before him. The end result (the target to be achieved) will justify the means adopted.

Deontological Ethics

Deontology means the science of duty or moral obligation. In its purest sense deontology focuses on the means of getting the result. It takes the view that how you get there is as important as to where you get. A deontological view would be more along the lines that there are certain things that one should simply not do, forexample killing people or causing mass destruction for reaching the target or goal. Thus, the means is as important as the end.

Forms of Teleological Ethics

In order to deal with different situations, there exist a number of different forms of teleological ethics that have been developed over the years. These include ethical egoism, utilitarianism and Machiavellianism.

The foundation of ethical egoism is based on the principle that "All people are selfish at heart". Ethical egoism suggests that a person should act in a way that maximizes his or her own long-term interests. Writers, such as Hobbes, suggestedthat ultimately we are all genetically programmed to do what is right for us. Under ethical egoism morality means nothing. It would also suggest that we always put our own interest first.

Utilitarianism is based on the idea that a person should act in a way thatmaximizes the good of the greatest number of people. The eighteenth-century philosopher Jeremy Bentham had originally put forward the idea of utilitarianism.But the nineteenth-century philosopher John Stuart Mill popularized the concept as the basis of economic thinking that ensures greatest good for the greatest number.

Machiavellianism is the most extreme version of ideological thinking. Essentiallyit involves doing what one has to do for getting the job done. Another term that is often used to denote Machiavellianism is expediency. This view virtually negates theexistence of morals.

Deontological Theories

The word 'deontology' comes from the Greek word for duty. And this type of thinking represents a very different approach from the teleological approach. Deontologists believe that what is crucial are the rules and principles that guide

reasoning. Essentially, the means are just as important as the ends. Over the years different writers have put forward different .variations of this view. The most notable one is that put forward by Immanuel Kant. Kant's key belief was that one ought only to act such that the pri nciples of one's act could become a universal law of human action in a world in which one would hope to live. Kant's second point was that you should respect everybody as rational and free. In other words, all your decision- making should be made on the basis of respect. Other writers, notably Locke, argued that every body is born with certain natural rights-they cannot be taken away. This should therefore be a fundamental grounding for any ethical decision. Whichever of the above views we take in understanding deontological theories, deontology can be summarized thus :

1. There should be rules and morals in society that should be fair to everyone during a period.
2. These rules should hold good universally even over the passage of time. A decision made today should not have a predictable adverse effect in the future.
3. All members of society under deontology should be treated with equal respect.

Perhaps the biggest problem with decntological thinking is that it does not take into account exceptions, that is. the issues that fall outside the normal set of rules.

2.3.1 Ethics and Decision Making in Business

With the foundations of ethical decision-making before us the problem now is how to make business decisions. The approach should essentially be a careful combination of the best aspects of the teleological and deontological views. Decision-making in a work situation is a complex task because of the number of influencesthat effect the decision calculus. It is neither fighting a war nor indulging in pure and simple philanthropic work. Hence, neither teleological approach nor deontological approach can lead business to the right position. Here the problem itself presents the central issue, but consideration is moderated by a number of factors, including the wishes of those who are affected by the problem, the opportunities and costs associated with solving the problem, the knowledge and interests of the persons who ultimately make the decision, and the likelihood of being able to implement the decision as it is intended.

Further, most problems involve two or more values, and a comparison between them is inevitable, such that a greater return to one can be obtained with a loss to

the other. Not everything is known about the situation and anticipated consequences cannot be predicted with certainty. Moreover, power to make decision is dispersed over a multitude of people and/or departments. Ideally, the decision maker willdetermine the fundamental values to be maximized and then weigh the probable impact of each alternative. This is why it is incumbent upon organization to clearly communicate those values that are most important, so that at least the most importantone can be ultimately considered.

Most work-related decisions have an ethical component. With few exceptions, problems that involve people also involve ethical issues. Decisions that involve conflicts of commitment or obligation have an ethical component. Similarly, decisionsthat involve. basic freedom and civic responsibilities have an ethical component.Only the simplest, most mechanical of decisions are spared of ethical analysis.

Thus, ethical decision-making is the process of identifying a problem, generatingalternatives and choosing from among them so that the alternatives selected maximizethe major ethical values while also achieving the goal of maximising owners' value over the long term in production or distribution of goods and services.

2.4 Role of the State in the Business Scenario

In the early days of industrial revolution it was believed that the State has norole to play in guiding and regulating the activities of business. But subsequent developments proved that, most of the post industrial revolution socio-economic problems owed their origin to the conflict of interest between business and society. This led to large-scale State intervention in different countries of Europe in the activities of business through rules and 'legislations pertaining to different aspects of business activities and also provision for social security of workers and other weaker sections of society. The depression of the 1930s induced the US government to introduce several legislations affecting different aspects of business in the interest of both business and society.

The period that followed war and the depression witnessed gradual removal of barriers to free flow of trade, business and investments across the globe, Globalisation is identified as increasing interdependence and interconnectedness of national economies characterized by increasing movement of goods, services, capital and people across the national boundaries. But rise in the power of corporate sector and

free mobility of finance capital led to the erosion of political power of States. With efficiency becoming the universal goal of corporate houses, capital has become free to move across the national boundaries for investment in places that provide the possibility of better returns.

Under the situation, the State is withdrawing itself from its role as the guardian of the society making social responsibility and ethics the orphans. "In this dramatic sea change what is being lost is any viable notion of social responsibility-the institutional capacity for the achievement of a more equitable society".

In terms of industrial relations, the new production system is steadily replacing the rule-based relation by flexible work contracts without any scope for bargaining. To ensure highly competitive labour markets, the govern mention the other hand, are removing much of the protections accorded to the unions so long.

With the governments of States withdrawing themselves from the role of guardians, the activities of powerful business corporations of developed countries are also creating socio-economic and environmental problems in developing countries particularly. The giant multinational corporations are relocating plants in the developingcountries not only for getting the benefits of cheap labour, but also for producing hazardous materials there and keeping their respective countries of origin freer from environmental pollution and health hazards.

Another dangerous aspect of their operation is that, they are now in the look out for sites for dumping toxic industrial wastes. The obvious choice for the purpose has been the least developed or the developing countries of the world.

Now who bears the responsibility of protecting the rights to safety of the inhabitants and the workers of these poor and technologically backward countries, that do neither have the guts to reject such financially lucrative offers nor possess thetechnical competence to judge the long-term evil effects of dumping toxic and even nuclear wastes? The extreme inequalities that are likely to follow the process of strengthening the market forces might ultimately hurt the prospect of acceptance of the principles of market economy. Hence, for the purpose of making the operationof market forces socially acceptable, their ethics and values must be made to conformto the social requirements and factor endowments of.the countries concerned. The governments of both the developed and the developing countries must co-operate in evolving norms of operation by the business corporations whose operations extend

beyond national boundaries. The corporations on their part should play more responsible role in sustaining confidence of the society to the new system by striving to ensure social justice and equity. "The new paradigm will need to reflect a new relationship between the means to generate wealth and the strategies to distribute wealth. It will be founded on an understanding of ethics and values in the contemporaryworld with recognition of the limits and risks of executive action. If the past teaches anything about corporate social responsibility, it is that the risk of doing nothing far outweigh the risk of doing something".

2.5 Corporate Governance

• The Concept and the structure

Business corporations being very important.economic agents for change and development, it is expected that they will function in a manner that protects the interests of both stakeholders and society. That means they must be socially responsive. The mechanism which is looked upon for ensuring business housesoperate in a socially responsive manner is known as corporate governance.

Corporate governance is the overall management of activities of a corporation. It is concerned with the formulation of long-term objectives and plans and the proper management structure to achieve them. At the same time, it involves making surethat the structure functions to maintain the corporation's responsibility to its various constituencies of stakeholders and society.

The mechanism to ensure corporate governance is provided by four factors, namely, (i) the ownership structure of a corporation, (ii) the financial structure of the corporation, (iii) the functioning of the board of directors of the corporation, and
(iv) the institutional environment within which the corporation operates. .

The **ownership structure** of a corporation determines, to a considerable extent, how a corporation is managed and controlled. The ownership structure can be either dispersed among individuals and institutions or can be concentrated in the hands ofa few large shareholders.

Large shareholders tend to be active in corporate governance either through their representatives on boards or through their active participation in annual general

meetings. Large share holding exemplifies the success of Tata, Birla and Reliance.On the other hand, dispersed shareholding gives the board and the top managers wider latitude in decision-making. Our corporate sector is characterized by the co- existence of state-owned, private and multinational enterprises, The shares of these enterprises are (other than the public sector) held by institutional as well as small investors, In UK and USA share holding is dispersed among individuals and institutional investors, whereas in Japan and Germany shareholding is concentratedin a few hands.

Financial structure, that is, proportion between debt and equity, influences the quality of governance of a corporation. The lenders (the suppliers of debt capital) being interested in short term gains remain very much alert about present functioningand tries to influence decision making to their advantage. Whereas the equity holderscan sacrifice short-term gains for long-term accretion in value of their holdings. Hence, for the shake of better governance,, it is very necessary to maintain a balance between the two different interest groups through an appropriate capital structure.

The board of directors is responsible for setting strategies and styles in selecting top executives of a corporation. The boards are permitted to vary in'size, composition and structure so as to best serve the interest of the corporation and the shareholders, Board members may include both inside and outside directors, specialistsfrom different walks of life. But what is necessary for the sake of good governanceis their commitment to the mission and vision of the corporation.

The institutional environment, provided by legal, regulatory and political forces significantly influences the quality of corporate governance. Because, upon it depends, the welfare of all the interest groups. Hence, the interested parties can charge the board for non-performance and mis-performance.

● The Context

Corporate governance has become a special aspect of political and economic debate in the present era. In recent years American managers, consultants and academics were asking themselves why Japan was overtaking them in global competition. The situation alerted company owners in developed countries about the desirability of effective corporate governance as the most important tool for competitiveness and success in the long run. In fact, the importance of corporate governance has been highlighted by international agencies like the OECD and the World Bank.

The Circumstance-problem

Other than getting return from investment, another important reason that motivates the investors to provide ownership capital to business corporations is the right to votein the genera! meetings of the shareholders on important issues that affect their interest. Creditors (the suppliers of fixed earning capital) also enjoy rights and legal protection that include the right to seize assets that serve as collateral for loans and the right to liquidate the firm when it does not repay debt, amongst others. However the rights given to both the shareholders and creditors are very difficult to enforcefor a variety of reasons. Shareholders, for instance, are spread over a wide area and hence they cannot always assemble in the meetings to exercise their rights. Moreover,generally such rights cannot be exercised by mail; they are required to show up at the meeting and vote. Thus, it is the minority shareholders, who fulfill the quorum, vote and determine policy - changes of the organization. Further, even when shareholders elect the board, the directors do not always represent their interests and passively go by the briefing given in advance by the managers. Again, it is also very difficult on the part of the creditors to vindicate their legal position effectively, as bankruptcy proceedings generally take very longtime to complete. The problem of unpaid bad loans (non-performing assests) has been the headache of banks and other financial institutions in India.

As a social entity a corporation derives its legitimacy from its ability to fulfill social needs. It is, therefore, accountable to society. No institution, however mighty it is, can ignore its responsibility towards society from which it derives its ultimate strength and sustenance. Thus the importance of governance continued to assume growing importance in the business. Corporate governance encompasses the structuraland behavioral issues of the corporate board as to how it should respond to its shareholders, financiers, government and employees. In a wider sense, it means how the corporate board should respond to regulatory and environmental aspects. Inpractice there is no clear-cut definition of corporate governance. According to Milton Friedman "Corporate governance is to conduct the business in accordance with owners' or shareholders' desire, which generally will be to make as much money as possible, while conforming to the basic rules of society embodied in law and social customs". Apparently, in the present day concept, Friedman's definition is too narrow in scope. Over the period of time the definition of corporate governance has been widened. It now encompasses the interest of not only the shareholders but also

other stakeholders. According to Sir Adrian Cadbury (1992) corporate governance is the system by which companies are directed and controlled. There is considerable debate on what actually constitutes corporate governance. But its key elements concern the progress of corporate performance via supervision or monitoring ofmanagement performance and the accountability of management to shareholders and other stakeholders.

2.5.1 Institutional Investors and Corporate Governance

Highly concentrated ownership of corporate securities can be observed in the countries where the legal protection system does not adequately protect the rights of individual shareholders. *In* these countries the highly concentrated ownership ofcorporate securities is looked upon as the only way to protect the interest of institutional investors through greater bargaining power. With the rights concentratedin the hands of a small number of large investors, concerted action for protection and vindication of rights becomes easier than when the rights remain widely dispersed. Thus, the practice of heavily concentrated shareholding for dominant control gained popularity through out the world. In the countries where large shareholdings was less common, such as in UK and USA, hostile takeovers have taken place for consolidation of ownership and acquisition of controlling interest. Jensen takes the view that the takeovers of 1980s in US were caused by a failure in the internal governance mechanism of corporations. Ever since the 1930s, management incentives had become weaker as corporations had become larger and shareholding became more widespread. Boards, which were supposed to be the guardians of shareholder rights, mostly sided with management and were ineffective in carrying out their duties. At the end of the 1980s, the takeover and merger wave ended, and the corporate governance system became more assertive and sensitive to stock market reactions. The underlying substance of this transformation has been that US managers have become much more focused on stock prices. The corporate governance mechanism that had driven this focus has evolved overtime from the leveraged hostile takeovers and buyouts of the 1980s to the incentive-based activist boards of directors and the shareholders in the 1990s.

Other than large shareholding and concentration of ownership through acquisition and takeover, large creditors such as banks and financial institutions have also come to dominate corporate decision making in a big way all over the world. The business

houses look upon the banks and financial institutions as the ultimate source of liquid cash for meeting all eventualities. The dependence of corporate houses on banks and financial institutions has reached a stage where it is very common to find representatives of such institutions as directors in the boards of corporate houses. This is the case for instance in the USA where one-third of large firms have bankers on the board. In the bank-based financial systems, such as in Germany and Japan,the percentage is much higher. In Japan over 50 per cent of large firms have a bankeron the board, an'd in Germany the figure is 75 per cent. With bankers on the board the business houses get easier access to liquidity from time to time and at the same time have the careful surveillance of the financier over the management of financeof the business houses. However, as creditors, the interest of banks and financial institutions may clash with the interest of the shareholders. For example, an increase in return to creditors would mean a corresponding decrease in return to the shareholders. The clash in the interest of creditors and shareholders can be moderatedand even avoided if the banks and financial institutions can be persuaded to take equity stakes in the firm side by side with the supply of credit. In this context, the mutual funds may be the most appropriate alternative in the countries like India.

In the last two decades, various stakeholders in the industrially developed countries have agitated for more active, independent and accountable boards. The common demand in all these agitations is more voice for institutional investors. The rise of institutional investors in these countries have augured well for shareholdersof these countries irrespective of the system of corporate governance they have. The Cadbury Report also noted that, 'Because of their collective stake, we look to the institutions in particular, with the backing of the Institutional Shareholders' Committee,to use their influence as owners to ensure that the companies in'which they have invested comply with the Code'. By virtue of the size of their holdings, the institutional investors have the potential to exercise considerable 'control over the actions of boards of directors, which the small investors do not have.

Over the last few decades, the share markets all-over the world have witnesseda shift-towards increased institutional ownership of corporate securities. This has resulted from a ' growth in public and private pension funds in developed countries and development finance institutions and mutual funds in the developing countries. These institutions generally invest in companies or sectors that are offering higher than the general market rate of return and have under-priced stock. If the company where the institutional investor has invested does not perform well, the institutional

investor can exert pressure through its large shareholdings for actions to be taken thatare likely to improve earnings. Moreover, with big investments, the institutional investors find it inconvenient to sell large blocks of shares without depressing share prices. Thus, their possible retention of holdings acts as threat against under- performance of the board. Institutional investors also believe that the, composition of the boards is an important factor affecting performance of companies. As a result, they seek increased outside representation on boards. This, they believe, improvesthe board's effectiveness in being more responsive to shareholders and improves overall performance.

2.5.2 Corporate Governance in India

An Overview on Various Initiatives towards Corporate Governance Movements in India :

At the time of Independence India bears the legacy of British-derived conventionof corporate governance based on the Anglo-Saxon Model. However, from 1947 through 1991, the Indian government pursued mixed economic policies when the state nationalized banks primarily became the principal provider of both debt and equity capital for private firms, the Public Sector Undertakings were evaluated based on the amount of capital invested rather than on their return on investment, competition, especially the foreign competition, was suppressed. In that time perioda little emphasis on corporate governance mechanisms was given in India. Public listed companies in India were only required to comply with limited governance and disclosure standards enumerated in the Companies Act of 1956, the Listing Norms, and the accounting standards set forth by the Institute of Chartered Accountants of India (ICAI). Faced with a fiscal crisis in 1991, the Indian Government respondedby enacting a series of reforms aimed at general economic liberalization, privatizationand globalization (LPG) movements. The Securities and Exchange Board of India (SEBI) — India's securities market regulator - was formed in 1992 and by the mid- 1990s, the Indian economy was growing steadily, and Indian firms began to seek equity capital especially from abroad to finance expansion into the market spaces created by LPG movement. Ever since its financial liberalization began in 1991,India has undergone significant Corporate Governance reforms. The need for capital especially that of coveted Foreign Institutional Investments (FIIs) amongst other things, led to Corporate Governance reform and many major Corporate Governance initiatives have been launched in India since the mid-1990s; most of these initiatives were focused on improving the governance climate in corporate India which was far

from satisfactory and truly an international standards. A glimpse of such Corporate Governance initiatives taken in India is presented here-

(a) Confederation of Indian Industry (CIl) Desirable Corporate Governance : A Code, 1998

The first major initiative was taken by the Confederation of Indian Industry (CII), India's largest industry and business association, which came up with the first voluntary code of corporate governance in 1998. More than a year before the onsetof the East Asian crisis, CII had set up a committee under the able leadership of Sri Rahul Bajaj to examine corporate governance issues, and recommend a voluntary code of best practices. Drawing heavily from the Anglo-Saxon Model of Corporate Governance, CII drew up a voluntary Corporate Governance Code. The first draft of the code was prepared by April 1997, and the final document, Desirable Corporate Governance: A Code, was publicly released in April 1998. The code was voluntary, contained detailed provisions, and focused on listed companies. However, the CII Code's voluntary nature did not result in a broad overhaul of governance norms and practices by Indian companies. Although the CII Code was welcomed with much fanfare and even adopted by a few progressive companies, it was felt that under Indian conditions a statutory rather than a voluntary code would be far more purposive and meaningful. Consequently, the second major corporate governance initiative in the country was undertaken by SEBI.

(b) Clause 49 of the Listing Agreement of SEBI evolved from the Recommendation of Kumar Manglam Birla Committee, 1999

In early 1999, SEBI had set up a committee under Kumar Mangalam Birla to promote and raise the standards of good corporate governance. The Birla Committee specifically placed an emphasis on independent directors in discussing board recommendations and made specific recommendations regarding board representation and independence. The Committee also recognized the importance of audit committees and made many specific recommendations regarding the function and constitution of board audit committees. Further more, the Committee made several recommendationsregarding disclosure and transparency issues, in particular with respect to information to be provided to shareholders. Among other recommendations, the Birla Committee stated that a company's annual report to shareholders should contain a Management Discussion and Analysis (MD&A) section, modelled after annual reports issued by

companies in the United States, and that companies should transmit certain information,such as quarterly reports and analyst presentations, to shareholders. Furthermore,with respect to shareholder complaints, the Committee recommended that a board committee known as the Investors Grievance Committee, chaired by a nonexecutive director, be formed to address grievances. In early 2000, the SEBI board had accepted and ratified key recommendations of this committee, and these were incorporated into Clause 49 of the Listing Agreement of the Stock Exchanges which is mandatory for almost every listed firm to comply with and report in proper way.

(c) Committee on Corporate Audit & Governance (Naresh Chandra Committee), 2002

The Naresh Chandra committee was appointed in August 2002 by the Departmentof Company Affairs (DCA) under the Ministry of Finance and Company Affairs to examine various corporate governance issues. The Committee submitted its report in December 2002. It made recommendations in two key aspects of corporate governance: financial and non-financial disclosures and independent auditing and board oversight of management and made a series of recommendations regarding, among othermatters, the grounds for disqualifying auditors from assignments, the type of non- audit services that auditors should be prohibited from performing, and the need for compulsory rotation of audit partners.

(d) Narayana Murthy Committee on Corporate Governance, 2003

The fourth initiative on corporate governance in India is in the form of the recommendations of the Narayana Murthy committee. The committee was set up by SEBI, under the chairmanship of Mr. N. R. Narayana Murthy, to review Clause 49, and suggest measures to improve corporate governance standards. Some of the majorrecommendations of the committee primarily related to audit committees, audit reports, independent directors, related party transactions, risk management, directorships and director compensation, codes of conduct and financial disclosures. The Murthy Committee, like the Birla Committee, described the international developments as a factor that motivated reform and stated that recent failures of corporate governance, particularly in the United States, combined with the observations of India's stock exchanges that compliance with Clause 49 up to that point had been uneven, recommended further reform. The Murthy Committee examined a range of corporate governance issues relating to corporate boards and audit committees, as

well as disclosure to shareholders. The Murthy Committee focused heavily on therole and structure of corporate boards and strengthened the director independence definition in the then-existing Clause 49, particularly to address the role of insiderson Indian boards like the director cannot be related to promoters or management at the board level, or one below the board; an executive of the company in the preceding three years; be a supplier, service provider, or customer of the company;or a shareholder owning two percent or more of the company. The Murthy Committee also recommended that nominee directors (i.e., directors nominated by financial institutions particularly, with relationships with the company) be excluded from the definition of independent director, and be subject to the same responsibilities and liabilities applicable to any other director. In order to improve the function of boards, the Murthy Committee recommended that they should also receive trainingin the company's business model and quarterly reports on business risk and risk management strategies. The Murthy Committee also paid particular attention to the role and responsibilities of audit committees. It recommended that audit committees be composed of "financially literate" members, with at least one member having accounting or related financial management expertise. It provided a greater role for the audit committee as well. For example, the Murthy Committee recommendations promoted disclosure and approval of related party transactions by the audit committee.In addition, the committee stated that whistle-blowers must have access to the audit committee without first having to inform their supervisors, and that companies should annually affirm that they have not denied access to the audit committee or unfairly treated whistle-blowers generally. SEBI had initiated certain changes inListing Agreement in line with the Murthy Report covering the areas of governance requirements with respect to corporate boards, audit committees, shareholder disclosure and CEO/CFO certification of internal controls which led transformation of the governance and disclosure standards of Indian public companies.

(e) J. J. Irani Committee on Company Law, 2004

India's corporate governance reform efforts did not cease after adoption ofClause 49. In parallel, the review and redrafting of the Companies Act, 1956 was taken up by the Ministry of Corporate Affairs (MCA) on the basis of a detailed consultative process and the Government constituted an Expert Committee on Company Law under the Chairmanship of Dr. J.J. Irani on 2nd December 2004 to advise on new Companies Bill. There were significant differences between the

proposals contained in the Irani report and the requirements of Clause 49, particularly with respect to the board of directors. First, the requirements for independent directors were different in several respects. Clause 49 required that no independent director should have been an executive of the company in the preceding three financial years, while the Irani Committee's recommendations weaken that requirement so that independent directors, along with their relatives, should not have been an employee of the company in any capacity only in the past single year. Similarly, while clause 49 prohibited an independent director from having served in any executive capacity in a statutory or internal auditing firm that has a material association with the company for the past three years, the Irani report recommended the same requirement for a period of one year only for independent directors andtheir relatives. The Irani Committee also recommended that a third of company directors be independent.

Corporate Governance Reform, in Post Satyam Saga : Biggest Corporate Scam in India :

In the meanwhile in January 2009, the Indian corporate community was rocked by a massive accounting scandal involving Satyam Computer Services (Satyam), one of India's largest information technology companies. The Satyam scandal prompted quick action by the Indian government, including the arrest of several Satyam insiders and auditors, investigations by the MCA and SEBI, and substitution of the company's directors with government nominees.

Satyam's failures were many and systemic—from a weak auditing process to ineffective board oversight to a leader intent on committing fraud. Similar to their role in the first phase of corporate governance reforms, in the post-Satyam period, Indian corporate groups have once again advocated for reconsideration of India's corporate governance rules and advocated for reforms. Shortly after news of the scandal broke, the CII began examining the corporate governance issues arising outof the Satyam scandal and in late 2009, the CII Task Force put out recommendations on corporate governance reform. In addition to the CII, a number of other corporate groups have joined the corporate governance dialogue. The National Association of Software and Services Companies (NASSCOM) also formed a Corporate Governanceand Ethics Committee chaired by Mr. N. R. Narayana Murthy, one of the foundersof Infosys and a leading figure in Indian corporate governance reforms. The Committee issued its recommendations in mid-2010, focusing on stakeholders in the

company. The report emphasized recommendations relating to the audit committee and a whistleblower policy. The report also addressed improving shareholder rights. Additionally, the Institute of Company Secretaries of India (ICSI) has also put forth a series of corporate governance recommendations. In 2009, SEBI made several announcements regarding disclosure and accounting reforms that could result inchanges to the Listing Agreement and in September 2009, the SEBI Committee on Disclosure and Accounting Standards published a discussion paper seeking public comment on several governance issues for reviewing Clause 49 of Listing Rules. Later the Clause 49 of Listing Agreement of SEBI was revised thoroughly in lightof provisions of new Companies Act, 2013.

A Brief Review of] Reforms in Corporate Governance Mechanisms in India under the regime of the New Companies Act, 2013 :

The Companies Act, 2013 has tried to make a paradigm shift in corporategovernance mechanism in India by promulgating various timely and relevant provisions. Here a brief review of such type of provisions for prevailing good governance mechanisms in corporate India has been furnished here vis-a-vis the old Companies Act, 1956 along with the relevant provisions of Clause 49 and Revised Clause 49 of the Listing Agreement -

(a) Composition of Board of Directors :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
Section 252 (1) Every public company (other than a public company which has become such by virtue of section 43(A) shall have at least three directors. (2) Every other company shall have at least two directors. There are no explicit provisions for independent directors under Companies Act, 1956	Section 149 : Every company shall have a Board of Directors consisting of individuals as directors and shall have— (a) a minimum number of three directors in the case of a public company, two directors in the case of a private company, and one director in the case of a One Person Company; and (b) a maximum of fifteen directors	49(1) (A) The Board of directors of the company shall have an optimum combination of executive and non-executive directors with not less than fifty percent of the board of directors comprising of non-executive directors.	No Change

(b) Advocating the independence in board :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
There are no explicit provisions for independent directors.	Section 149 (4) read with Rule 4 ofC o m p a n i e s (Appointment and Qualification of Director) The listed Public Company should have at least one-thirdof the total number of Directors and the Public Companies having paid up share capital of locrore (rupees or more or turnover of loocrore rupees or more or aggregate outstanding loans, debentures and deposits, exceeding 5ocrore rupees must have at least 2 Directors.	Clause 49(I) (ii) : Where the Chairman of the Board is a non-executive director, at least one-third of the Board should comprise of independent directors and in case he is an executive director, at least half of the Board should comprise of independent directors.	Same as Cl.49

(c) Exclusion of Nominee Director from Independent Directors (IDs):

The nominee directors are a special form of directorship which has been appointed by the lending institutions to the borrower's board primarily to safeguard the interests of the lenders. This form of directorship is the regular feature of Indian corporate sector which may find a close resemblance with the Japanese Model of Corporate Governance. Regarding the status of such type of directorship the understanding of our regulatory mechanisms are bifurcated. While the Listing Agreement stated that the nominee directors appointed by an institution that has invested in or lent to the company are deemed to be independent directors, but onthe other hand New Companies Act, 2013 states that a nominee director cannot bean independent director. However, the SEBI Circular in line with the provisions of

Companies Act, 2013 has excluded nominee directors from being considered as independent directors.

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
There are no explicit provisions	Section 149(6) : An independent director in relation to a company, means a director other than a MD or a WTD or a nominee director.	Clause 49(I)(A) Explanation (d): Nominee directors appointed by an institution which has invested in or lent to the company shall be deemed to be independent directors.	Clause 49(II)(B) Nominee director is excluded from the definition of IDs.

(d) Tenure of Independent Director :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec 149(10) : An ID shall hold office upto 5 consecutive years on the Board of a company, but shall be eligible for re-appointment on passing a special resolution by the company and disclosure of such appointment in Board's report. Moreover, it was mentioned in Sec 149(11) that no independent director should hold office for more than two consecutive terms with a cooling off period of 3 years	No such provision	49(II)(B)(3)(a): The maximum tenure of Independent Directors shall be in accordance with the Companies Act, 2013 and clarifications/ circulars issued by the Ministry of Corporate Affairs, in this regard, from time to time.

(e) Qualification of Independent Directors :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec I49(6)(f) read with Rule 5 of Companies (Appointment and Qualification of Directors) Rules, 2014 : An independent director shall possess appropriate skills, experience and knowledge in one or more fields of finance, law, management, sales, marketing, administration, research, corporate governance, technical operations or other disciplines related to the company's business.	No such provision	The qualifications of IDS are not specified in the amended clause 49 of the listing agreement.

(f) Limit on number of directorship :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec 165(1) : No person, after the commencement of this Act, shall hold office as a director, including any alternate directorship, in more than 20 companies at same time provided that the maximum number of public companies in which a person can be appointed as a directors shall not exceed 10.	Clause 49 (I)(C)(i) : A director shall not be a member in more than 10 committees or act as Chairman of more than five committees across all companies in which he is a director.	A person shall not serve as an independent director in more than 7 listed companies. Further, any person who is serving as a whole time director in any listed company shall serve as an independent director in not more than 3 listed companies.

(g) Separate meeting of Independent Directors :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Section 149 read with Schedule IV: IDs of the company shall hold at least one meeting in a year, without the attendance of non-independent directors and members of management. All the independent directors of the company shall strive to be present at such meeting.	No such provision	Clause49(II)(B)(6): The IDs of the company shall hold at least one meeting in a year, without the attendance of non-independent directors and members of management. All the independent directors of the company shall strive to be present at such meeting.

(h) Performance evaluation of IDs :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Section 178(2) read with Schedule IV : The Nomination and Remuneration Committee shall identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the criteria laid down, recommend to the Board their appointment and removal and shall carry out evaluation of every director's performance. The performance evaluation of independent directors shall be done by the entire Board of Directors, excluding the director being evaluated. On the basis of the report of performance evaluation, it shall be determined whether to extend or continue the term of appointment of the independent director.	No such provision	Clause 49(II)B)(5) The Nomination Committee shall lay down the evaluation criteria for performance evaluation of independent directors. The company shall disclose the criteria for performance evaluation, as laid down by the Nomination Committee, in its Annual Report. The performance evaluation of independent directors shall be done by the entire Board of Directors (excluding the director being evaluated). On the basis of the report of performance evaluation, it shall be determined whether to extend or continue the term of appointment of the independent director.

(i) Code for Independent Directors :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Introduced through inclusion of provisions specified in Schedule IV covering areas like guidelines of professional conduct, role and functions are laid down, duties of IDs, manner of appointment and re-appointments, separate .meetings, evaluation mechanisms etc.	No such provision	No separate schedule. Requirements to comply with provisions of Companies Act, 2013 included.

(j) Promoting Gender Diversity in Board :

In line of worldwide trend towards promoting gender diversity in board for inculcating the spirit of a role model (Catalyst, 2007), introducing fresh perspectives (Hudson, 2007), promoting effective leadership (McKinsey & Company, 2008), bringing a competitive edge (Independent Financial Review, 2008), boosting investors confidence etc., the Sec. 149 (i) of Companies Act, 2013 make a revolutionary changes by making it mandatory for every listed company to appoint, at least one woman director within one year as per the second proviso to the Section 149 (i). Moreover, every public company, having paid-up capital of INR100 crore or more, and turnover of INR 300 crore or more, have to compulsorily appoint, at least, one woman director within three years as per the Act.

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec 149(1) and Rule 3 of Companies (Appointment of Directors)Rule, 2014 : The following class of companies shall appoint at least one woman director-(i) every listed company, (ii) Every other public company having-(a) paid-up share capital of 100 cr rupees or more or (b) turnover of three hundred cr rupees or more	No such provision	Clause 49 The provisions regarding appointment of woman director as provided in shall be applicable with effect from April 01, 2015

(k) Introduction of New Form of Directorship-Resident Director :

The Companies Act, 2013 has taken a revolutionary approach by introducing new nomenclature in Corporate India like One Person Company, Limited Liability Firms etc. Likewise, the Companies Act, 2013 introduces the requirement of appointing a resident director, i.e., a person who has stayed in India for a total period of not less than 182 days in the previous calendar year. This provision will prevent the practice of the boards of Indian companies do not comprise entirely of non- resident directors.

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec 149(3): Every company shall have at least one director who has stayed in India for a total period of not less than 182 days in the previous calendar year	No such provision	No such provision

(l) Introduction of New Form of Directorship-Resident Director :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec151 A Listed company may have one director elected by such small shareholders in such manner and with such terms and conditions as may be prescribed	No such provision	No such provision

(m) Frequency of Board Meeting :

The key changes introduced by the Companies Act 2013 with respect to board meetings and processes are like the first board meeting of a company to be held within 30 (thirty) days of incorporation, notice of minimum 7 (seven) days must be given for each board meeting, notice for board meetings may be given by electronic means. However, board meetings may be called at shorter notice to transact "urgent business" provided such meetings are either attended by at least i (one) independent director or decisions taken at such meetings on subsequent circulation are ratified by at least 1 (one) independent director. Moreover, the Companies Act 2013 has permitted directors to participate in board meetings through video conferencing or other audio visual means which are capable of recording and recognising the participation of directors. Participation of directors by audio visual means would alsobe counted towards quorum.

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
Section 285 : Board to meet at least once in every three calendar months. In the case of every company, a meeting of its Board of directors shall be held at least once in every three months and at least four such meetings shall be held in every year	Sec 173 (i) : Every company shall hold the first meeting of the Board within 30 days of the date of incorporation and thereafter holda minimum number of 4 meetingsof its Board every year in such a manner that no more than 182 days shall intervene between two consecutive meetings of the boards.	49(l)(C) : The Board shall meet at least 4 times a year, with a maximum gap of 3 months between any 2 meetings.	No Change

(n) Reorganization of Board Committees-a step towards better governance :

The Companies Act, 2013 envisages 4 (four) types of board committees to be consti- tuted for upholding the spirit of good governance like Audit Committee, Nomination and Remuneration Committee, Stakeholders Relationship Committee and Corporate Social Responsibility Committee.

(i) Audit Committee :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
Sec 292A - Audit Committee (l) Every Public Company having paid-up capital of not less than five crores of rupees shall constitute a committee of the Board known as "Audit Committee" which shall consist of not less than three directors and such number of other directors as the Board may determine of which two-thirds of the total number of members shall be directors, other than managing or whole time directors.	Sec 177 : The Board of Directors of all public companies with paid up capital of ten cr rupees or more or having turnover with one hundred crore rupees or more or aggregate outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more shall constitute an Audit Committee with a minimum of three directors with independent directors forming a majority provided that majority members of Audit Committee including Chairperson shall be persons with ability to read and understand the financial statement	Cl. 49(11) : A qualified and independent audit committee shall be set up, giving the terms of reference subject to the following : (i) The audit committee shall have minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors. (ii) All members of audit committee shall be financially literate and at least one member shall have accounting or related financial management expertise.	Unchanged

(ii) Nomination and Remuneration Committee :

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec 178 : The Board of Directors of all public companies with paid up capital of ten cr rupees or more or having turnover with one hundred crore rupees or more or aggregate outstanding loans or borrowings or debentures or deposits exceeding fifty crore rupees or more shall constitute a Nomination and Remuneration Committee consisting of three or more nonexecutive directors out of which not less than one half shall be independent directors.	Non mandatory committee	Clause 49 has the following provisions regarding Nomination and Remuneration Committee : Members : Atleast three members, all non-executive directors and atleast half to be IDs Chairman : Chairman to be an ID

(iii) Stakeholders Relationship Committee :

This Board Committee is the new inception of the Companies Act, 2013. The CompaniesAct 2013 requires every company having more than 1000 (one thousand) shareholders,debenture holders, deposit holders and any other security holders at any time during afinancial year to constitute a stakeholders relationship committee to resolve the grievances of security holders of the company. The main responsibility of this board committee is tolook after the grievances of the stakeholders of the company in general and shareholdersin particular. However, Clause 49 of the Listing Agreement in line with the recommendation of K.M. Birla Committee required listed companies to set up a shareholders / investorsgrievance committee to examine complaints and issues of shareholders.

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec 178(6): The Board of Directors of a company which consists of more than one thousand shareholders, debenture-holders, deposit-holders and any other security holders at any time during a financial year shall constitute a Stakeholders Relationship Committee consisting of a chairperson who shall be a non-executive director and such other members as may be decided by the board to consider and resolve the grievances of security holders of the company.	Clause 49 (IV) (G): A Board committee under the chairmanship of a non-executive directors shall be formed to specifically look into the redressal of shareholder and investors complaints like transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends etc. The board committee shall be designated as "Shareholders/Investors Grievances Committee"	Introduced now to align with the Act.

(iv) Corporate Social Responsibility Committee :

This is another introduction of the New Companies Act, 2013. New Companies Act 2013 formally makes it mandatory for certain group of major companies to constitute a CSR Committee, which would be responsible to devise, recommend and monitor CSR initiatives of the company. The committee is also required to preparea report detailing the CSR activities undertaken and if not, the reasons for failure to comply.

Companies Act, 1956	Companies Act, 2013	Clause 49	Revised Clause 49
No such provision	Sec 135: Every Company having net worth of rupees five hundred crore or more or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which one director shall be an independent director. The Board should ensure that the company spends in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance ofits CSR policy as specified in Schedule VII	No such provision	Introduced now to align with the Act

2.5.3 Unique Role of Mutual Funds in Corporate Governance

The small investors can exert little influence over the corporate boards : naturally they look upon the mutual funds as their only authorized activist. On the other hand, as the protectors of interest of small savers, the mutual funds evince keen interest in the efficient governance of corporations they invest in. Being the trustees of the funds, they are also expected to act more independently in protecting the interest of small suppliers' funds than the other investment institutions. Hence therole of mutual funds in corporate governance has.to be specially mentioned.

The mutual funds in India are governed by various provisions of the Indian Companies Act,1956, the Indian Trusts Act, 1882, the SEBI Mutual Funds Regulation1996 and the Indian Registration Actl908. Separate authorities, such as Sponsor Company, Asset Management Company, Trustees and Custodian deal with every function of the organization from the formulation of schemes for collection of funds to the ultimate investment of funds and distribution of certificates, leaving little chance for development of vested interest at any stage. Hence, the mutual funds, withtheir unique organizational and management practices as well as immense trust of small investors in them, can provide leasership in promoting ideal corporate governance practice in a country like India in a number of ways. In the first place, as the trustees of investors'money, the mutual funds can try to maximize the value of their investments by encouraging better management through changes in the board of directors of the company in which they have invested. Secondly, instead of consideringthemselves as the mere onlookers, the mutual should consider themselves as responsible investors of funds. Thirdly, they can also popularize the view that 'compliance of law is necessary, but not a sufficient, condition for good corporate governance. It demands compliance of Jaw for maximization of the value of investors' wealth. Fourthly, mutual funds can devise a set of guidelines for their nominees on the corporate boards. In case of merger, inter-corporate investments, joint ventures, appointment of Chairman/Managing Director etc., information from third parties may be of immense importance. Sixthly, mutual funds can take active interest in strategic planning of companies. The purpose of good corporate governancebeing maximization of shareholders' wealth, the board must always be on the lookout for opportunities to take advantage of the emerging developments through strategic planning and corporate restructuring. Lastly, because of their unique position in the governance of companies, the mutual funds can try to convince others on the board as well as the shareholders of the concerned company about the desirability of implementing the Code of Best Practices listed by the Cadbury Committee for good governance. But the mutual fund industry has not been free fromscandals in countries like India.

- **The Cadbury Committee**

The committee appointed in UK in 1991 under the Chairmanship of Sir Adrian Cadbury (Cadbury Committee 1992), to study and report on the accountability aspect of corporate governance, stressed upon improved information to shareholders,

continued self-regulation and strengthening of the independence of the auditors. In brief, the Code of Best Practices of Cadbury Committee included the following : (1) all listed companies should establish an audit committee comprising of at least three non-executive directors. The primary brief of audit committees is to review thefinancial statements and the findings of the external auditors. Thus, non-execuiive directors have been looked upon as the best authority for examining account related matters. (2) In the second place, there should be a remuneration committee for determining executives' pay. (3) In the third place, directors should not be appointed for more than three years without shareholders' approval, the roles of chairman and highest paid executive officers should be disclosed and the computation of performancerelated pay fully explained. (4) Further, to emphasize the importance of independent directors in setting executive directors' remuneration, the Committee suggested appointment of a remuneration committee consisting wholly or mainly of non- executive directors. (5) Finally, in order to address accountability issues relating to internal links between parents and subsidiaries, recommendations were also made concerning the need to produce statements on the effectiveness of internal financial control and the business as a going concern. Thus, the Cadbury Committee assigned vital role to the outside nonexecutive directors in ensuring effective functioning ofthe board for achieving highest standard of governance. It would not be out of place to mention here that by the insertion of section 293A in the Indian Companies Actby the amendment of the Act in 2000, provision has been made for constitution of Audit Committee by the board for examining accounts related matters in everycompany with paid-up capital of rupees fivecrorc and above in the lines suggestedby the Cadbury Committee.

2.5.4 Corporate Governance and Globalisation

Globalisation forced governments to confront conflicting policies. One set of market forces presses for reduced government intervention in economic affairs. Yet, political and economic demands grow for increased state oversight of economic institutions and processes as globalisation gives rise to an environment which exposes domestic firms to greater risks and competition. For several years the corporate sector was not sure about whether the benefits of globalisation would exceed its disadvantages. In the reform era, initially there was crisis, What has been striking as the fallout of the crisis is the absence of a clear, systematic pattern of

structural changes and outcomes at the national and international levels. First, despite the extraordinary conditions favouring reforms and Hbaralisation in the Asian economies, no consistent trend of liberalization has emerged. Japan, Korea, Taiwan, Thailand and Malaysia have been struck by the crisis in different ways and have adopted different policy measures to stabilize their political and economic systems. But it is now felt by many in the Asian countries that gobalisation has been good for corporate governance on the whole.

A succession of bankruptcies (some in the USA and some in Europe) around 2002 has been attributed to bad corporate governance. Can just good audit andaccounting standards ensure good governance ?

2.6 Summary

Business, being a part of society, has to take care of the social values that evolved over time. In many cases the values have been codified and represented inthe political system. Business thrives and develops on the support of society, while society depends on business for meeting its material needs. So business has todevelop its objectives, policies and strategies keeping the values, needs as well as theinstitutional structure of society before it. Corporate governance is corporate management for the attainment of corporate goals which do not contradict with wider social interests in the country. Society looks upon the quality of governance ofcorporations for the fulfillment of its hopes, aspirations and needs. The basic policy tool of corporate governance is the board of directors. Once a board has put its policycriteria in place, evaluation of CEO's performance becomes a matter of systematic reporting of company performance against those criteria.

2.7 Exercises

Essay type questions :

1. State what do you understand by business ethics, and examine the importance of ethics in business.
2. What do you understand by social responsibility of business? Trace the process of the evolution of the concept of social responsibility of business.

3. Explain teleological and deontological concepts of ethics. State how ethical decisions are made in business.
4. State what do you visualize about the role of the state in decision-making in business in the context of globalisation.
5. Write an essay on corporate governance in India.
6. Examine the role of institutional investors in ensuring efficient governance of corporations.
7. Examine the principal recommendations of the Cadbury Committee on corporate governance.

Short answer type questions :

1. Law is 'codified ethics'. Explain.
2. Mention the four different types of ethical responsibilities of business.
3. State briefly the different forms of teleological ethics.
4. Mention what do you understand by deontological ethics.
5. Explain the relation between business ethics and corporate governance.
6. State the role of mutual funds in ensuring good corporate governance.
7. Write a note on corporate governance and globalisation.
8. Is society a stakeholder in business? Give reasons for your answer.

Objective type questions :

Select the correct answer-

1. Social responsibility of business followed
   (a) Technological development
   (b) Political development
   (c) Production of goods and services for exchange
   (d) The ideas of Adam Smith.

2. Utilitarism means
   (a) Maximum good to minimum people
   (b) Minimum good to all people
   (c) Utility for self only
   (d) Maximum good for the greatest number of people.
3. In the present boundaryless world
   (a) State has no role to play in ensuring social justice
   (b) Each State independently has greater role in ensuring social justice
   (c) States have a greater role to play jointly in ensuring social justice to all
   (d) None of the above is correct.
4. Securing good corporate governance is easier
   (a) When there is concentrated ownership of securities
   (b) Where ownership is widely dispersed
   (c) Where full ownership is in the hands of government
   (d) Where ownership is in the hands of creditors, that is, suppliers of loan capital.
5. Large institutional holding of shares emerged in different countries because of
   (a) Failure of individual srnal! investors to protect their interest
   (b) Governments of different countries encouraged shareholding by institutional investors
   (c) The companies preferred larger institutional holdings
   (d) None of the above is correct
6. Recent accounting frauds and failures of giant companies are the results of
   (a) Liberalisation
   (b) Absence of good corporate governance
   (c) Failure of accounting system
   (d) Concentration of share holding in few hands.

Answers of objective type questions- Nos. 1 (c), 2 (d), 3 (c), 4 (a), 5 (a), 6 (b).

2.8 References

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Unit 3 ❑ Political Environment

Structure

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3.5 Summary

3.6 Exercises

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3.0 Introduction

In primitive societies there was barter system – goods exchanged for goods.Then society came to possess some of the characteristics of modern economy - private property, division of labour, market, money and enterprise. But in those days there was no well-defined political philosophy nor any political institution except monarchy to guide and protect the interest of business. Good monarchic gave protection and encouragement to business.

With gradual perfection in the technique of production, the organization ofproduction increased in size and complexity. Division of labour developed to the point at which it involved the establishment of private exchange and the extensionof private property from consumable to productive goods. The economic system became more and more impersonal. Production and exchange came to be guided by the invisible forces of demand and supply.

Plato and then his disciple Aristotle dreamt of an ideal State designed to ensure 'good life' for the free citizens only within a 'city state'. While both Plato and Aristotle justified slavery, Aristotle, the first analytical economist, held that 'incentive' is the prime inducement behind development of new ideas and business ventures. He was also ethical at the same time. While appreciating the role of money as a medium of exchange only; he. was vehemently opposed to the idea'of amassing wealth and earning usurious income.

Christ claimed to speak to, and for, all men. Universal brotherhood in Christianityand human dignity for all led people look upon the institution, that is, Church as the unifying force in society. Thus, with the advent of Christianity came a total changein the attitude towards business that ultimately influenced the growth of merchant capitalism. However, gradually there developed rule of aristocracy around the institution of the Church. Marcantilism demanded a State strong enough to protectthe trading interest and break down of the medieval barriers to commercial expansion.Yet they also sought proteclion of monopolies as an essential basis of State power.

The forces that added prominence to commerce freed men's mind from the fetters of accepted belief. The need for expanded commerce and new empiricalrationalism led to the development of new ideas for tackling with scientific experimentsand solutions of every problem, business and society were facing. Freedom of thought, acquisition of property by industry and reason came to be recognized with utmost respect. The development of new scientific ideas and their application in industry for large scale production to meet the growing need of the expanded market led to the emergence of industrial capitalism in the middle of the seventeenth century.

In the development of industrial capitalism, restrictive regulations of the Monarchic State developed around the Church appeared as the main hurdle. However, under the socio-economic pressure and development of political philosophy

many of the restrictive regulations of domestic industry were abolished in England after the middle of the seventeenth century. Thus, the decline of State intervention went hand in hand with the decline of monopoly power. It may be mentioned here that monopoly power had developed with State patronage during the mercantilist era in England, the examples of which are Merchant Adventurers like the East India Company. Ultimately Adam Smith, through two of his books. Wealth of Nations and Theory of Moral Sentiments, dealt the final blow to overriding authority of State by pleading for least State intervention. Human conduct according to Smith, was naturally actuated by six motives: self love, sympathy, the desire to be free, a senseof propriety, a habit of labour, and the propensity to truck, barter, and exchange one thing for another. Given these springs of conduct, each man is naturally the bestjudge of his own interest and should therefore be left free to pursue it in his own way.

Adam Smith provided the philosophical foundation of laissez-fare capitalismthat paved the way for industrial revolution in England. But by the end of thenineteenth century, in the wake of socio-political problems created by industrial development without any regulatory role-of State, economic philosophers came to look upon the State for playing some role in regulating and supplementing the activities of private business. This was followed by nationalization of industries and the emergence of State regulation over business in England and other countries of Europe (and after the Great Depression of the 1930s in USA). The developing countries opted for more active role of State following the success of economic totalitarianism in East Europe. Keynes's General Theory also helped the process, for he strongly advocated for State participation in the economy. Even in the globalised environment of today the State is looked upon to play its role according to the needs of the countries concerned.

3.1 Nature of Political Environment

Political environment of a country is the political atmosphere generated by the factors emanating from the political system. This system includes the party in power and its political

philosophy, the opposition (if any) and its philosophy, degree of stability of the government, and the relationship between the three agents of the government (the legislature, the executive and the judiciary), The political environmentshould be such as helps and not hinders business growth. What is important is thatthe political system of the country should be efficient and dynamic, besides being

stable. However, stability, though an important requirement by itself will not guarantee economic prosperity. Dynamism and efficiency of the political system ensures the system's alertness to the needs and aspirations of the people. Frequent changes of government create political instability, not liked by foreign investors.

Economically developed countries of today owe their development to the existence of a responsive, stable and honest government in their respective countries. In all the countries of Western Europe and North America as well as in Japan the early emphasis was on the development of a responsible and stable government that created the atmosphere of innovation and investment in these countries. People's desire to innovate and invest depend upon the sense of security and appreciation of the society for those activities, the atmosphere for which is provided by the stability and quality of governance.

It is difficult to say which type of government promotes business most, the dictatorial or the democratic. Although there is one-party rule (party dictatorship) in China, it has registered the highest rate of economic growth in the 1990s and attracted more foreign capital than many democratic countries in the early 21stcentury.

As between democracy and totalitarianism the choice is apparently difficult because there are examples where countries under both the system did well. But, under totalitarian system the tempo of development becomes slow after a certain stage as in the former Soviet Union. Authoritarian ism may ensure stability for a certain period. Democracies, in contrast, guarantee peoples' participation and thus ensure perpetuity of the system with stability, security, dynamism and purposefulness.Public opinion is a guiding factor in democracy, but not much in a totalitarianregime, where not free market but State dictates and determines what goods and services would be produced and how.

3.2 Political Institutions

The political system in India is based upon three vital institutions - parliamentarydemocracy, multiple party system and public opinion. The sovereignty of a State isin the government. The government has three organs - the legislature, the executive and the judiciary.

3.2.1 Legislature

The legislature is the primary and the most important pillar of democracy, for elected representatives of people constitute legislatures. The elected representatives acting as mirrors of public opinion formulate economic and business policies for the country, make laws for their implementation and prescribe penalties for their violation. Laws are enacted in legislature through majority vote.

The influence of legislature on business is considerable, It decides such vital aspects as the types of business activities the country should have, who and how theyshould be owned, and their modes of operation. The majority party controls the legislature. If, their laws are not liked by people, people may vote a different partyto power in the next election.

3.2.2 Executive

The term 'government' in a narrow sense means the executive, comprising the ministry, assisted by appointed civil servants of different grades. The chief function of the executive is to enforce/implement the laws passed by the legislature. Business laws regulate business activities in social interest.

The Constitution of India provided for a federal set-up, with jurisdiction divided between the center and the constituent States. Certain subjects were Central subjects, certain were State Subjects, and the rest formed Concurrent Subjects on which both the Centre and the States could pass laws. Both sets of government have laws, some promoting and some regulating business activity. The sources of revenue also are different for the two levels of government.

Relationship between the government and business: Government-business relationship is a two-way phenomenon. On the one hand business has some responsibilities to the government and on the other hand government too has some responsibilities to business.

Business firms should obey the Jaws of the land. Such laws and regulations maypervade the entire gamut of a business enterprise. By obeying the laws and regulations a business unit like a good citizen serves society and at the same time looks to government for support, sustenance, and guidance. Business also plays a vital role in helping the government to rule the country. Important responsibilities of business towards government are given below :

(a) **Tax payment :** taxes paid by the business enterprises constitute a major source of revenue for a government. Firms are required to pay regular taxes on their sales, income and also deduct tax on incomes received by employees and remit the collection to the government.

(b) **Voluntary programmes :** business firms cooperate with government by providing voluntary services to society, such as, setting up educational institutions and hospitals, providing recreational facilities, encouraging and helping sports and cultural activities.

(c) **Political activities :** experienced business leaders or their associations (Chambers of Commerce) can help and guide the government in the formulation of economic policies for the development of the country. Participation of successful businessmen in politics can be found in different countries of the world, including India.

Responsibilities of government to business: Governments, representing people, have the power and resources to decide, shape, guide and control business activities for the benefit of society. Being democratically elected and having accepted the mixed economy, the government of India is clear about the role it has to play andthe responsibilities it has to discharge towards business. Specifically, the government'sresponsibilities towards business are the following:

(a) **Enactment and enforcement of iaws :** Government establishes and enforces laws and regulations under which business functions. The government enacts laws and regulations covering many aspects of business (e.g. the Companies Act). Government is responsible for providing the 'rules of the game', which make the business system function smoothly and help maintaincompetition, or if monopolies develop, regulate them or supplement them bygovernment operations.

(b) **Maintaining law and order :** It is the prime responsibility of the government to maintain law and order-for protecting life and property. No business of any kind can survive and prosper without security. This duty of the ruler hasbeen recognized since early times. The police maintain internal order, whilstthe military give protection against foreign aggression.

(c) **Money and credit :** With the trasition from barter to a money economy at present the government provides a system of money and credit by means of

which transactions are done. It is also the responsibility of the governmentto regulate money and credit by means of an appropriate monetary policy. Notes and coins are everywhere issued by the government.

(d) **Economic Development :** In both socialist and non-socialist countries governments have the ultimate responsibility for helping the attainment of a high level of economic development with minimum unemployment and environment destruction, and small inequality of income and wealth distribution between individuals, regions and classes. In low-income countries the government should ensure a minimum level of education, healthcare and food security for every citizen, as emphasized by Am arty a Sen, the Nobel Prize winner. In a socialist State practically all aspects of development are taken up by the government on the principles chalked out by .a planning commission (as in the erstwhile Soviet Union). In a mixed economy like India development has been led by the public sector with the private sector playing the second fiddle. Since 1991 the development initiative has been placed upon private enterprise.

(e) **Transfer of technology :** Governments in many countries, as in India, own and finance institutions engaged in research. Products of these researches, particularly those related to industry and business, are made available to interested business houses for raising their competitive power. Apart from this, the government of India also encourages research by business houses by providing substantial relief in Income Tax on expenditures incurred by them on industry-related research.

(f) **Tariffs and quotas :** To protect business from foreign competition the government uses tariffs and quotas. Similarly, to encourage the development of domestic industries the government grants incentives and subsidies. In India much of the industrial development since independence has takenplace behind protective tariff. But since 1991 protection is being withdrawn from many industries of India in a regime of globalisation.

3.2.3 Judiciary

The third organ of the government is the Judiciary, Judiciary is the finalauthority that reviews and examines the way in which the laws have been implemented.

Any body aggrieved by any action of the Executive can appeal to the appropriate level of the judiciary for review and redressal of his grievances. Executive sees to it that the exercise of authority conforms to the general rules laid down by the legislature and also that it is in conformity with the customs and traditions of the country. Judiciary may declare any action/order of the Executive ultra vires. In fact, judiciary is the authority to which people look upon for enforcement of their rightsin the democracy. In enforcing the rule of law, Judiciary exercises two types of functions :

(i) Judicial review-the authority of the courts to rule on the constitutionality of laws and

(ii) The power of the courts to settle legal disputes through proper interpretation of laws.

In the case of judicial review, the Judiciary gets activated when the legislature passes laws that are repugnant to the Constitution and when the executive implements the enactment approved by the legislature in a manner opposed to the requirementsof the legislation. In other words, the court of justice protects the citizens from unlawful Acts passed by the legislature and arbitrary acts indulged in by the Executive.

It is this power of the Judiciary to settle legal disputes that affects business and Citizens for good or ill. All disputes between employer and employee, the business and the public, the customers, the government or any other business and the vise- versa are often referred to courts for settlement.

The judicial pronouncements have far-reaching consequences on business. The consequences may be intense and severe because (i) judicial errors do occur sometimes (ii) possibility of wrong assessment of penalty, (iii) Judges pronounce conflicting verdicts on the same or similar disputes and (iv) there is a lot of confusionand ambiguity in laws relating to industries.

In spite of some criticisms, it may be stated that the Indian Judiciary is impartial and competent. Judiciary, along with other players of the Indian political system, has today reached a stage where they are discharging their designated functions in a manner that enshrines the fundamental values of democracy. It protects the constitutional rights of citizens in countries like India and the USA.

3.3 Role of State in Economic Development

The doctrine of laissez-faire, which was developed in the late seventeenth and early eighteenth centuries, held that the government should limit itself to the maintenance of law and order and that State interference in industry and commerce should be kept to the minimum. It was argued in favour of laissez-faire policy thatit would promote individual freedom, the best use of economic resources and high economic-growth and emlployment. The doctrine reached its zenith in the late nineteenth century, but lost its influence thereafter, particularly in the depressed 1930s.

Towards the beginning of twentieth century, there emerged a strong movement of the working class in the East European countries and gradually the concept ofState capitalism of totalitarian regime in some of those countries. But, in general, State capitalism was not considered an effective solution to the drawbacks of the freeenterprise economy. With neither laissez-faire nor State capitalism considered conducive to optimum economic growth, there gradually came to emerge a general opinion in favour of a system that combines the advantages of both the systems. In fact, there has been a tendency in the free enterprise economies to increase government regulation of the market. Thus, since the early days of twentieth century large scale nationalization of industries and State intervention in the provision of social security to workers started in England and some other countries of Europe.

The Great Depression of nineteen thirties proved beyond doubt that businessmen,left free without any State control over them cannot save themselves or workers orthe economy. Further, it became proved that the "invisible hand" of the market, as visualized by Adam Smith, could not always keep the economy in a state of full- employment equilibrium. The New Deal programme, initiated in USA for stimulatingeconomic recovery after the Great Depression, for the first time paved the way for extensive government participation in economic activity in America.

J.M Keynes of England strongly advocated in favour of the stabilizing role of government in predominantly market economies through variation in the cost and availability of credit, progressive taxation, government investment through public works and other means of pump-priming. Keynesian support for compensatory fiscal policy where public investment would fill up the short fall in private investment for

maintaining income and employment at high levels was based on the concept of the welfare state, not socialism.

The disintegration of colonial rule after the Second World War led to theemergence of independent nations in Asia, Africa and Latin America. Most of these'countries were impressed by the success of socialist central planning in East Europe (e.g. erswhile USSR). Many of them adopted planning for developing their economies. Thus, India initiated an era of planning after Independence in 1951 with her first 5-year Plan. The public or govemmerit sector has all along played theleading role in India until 1991 when, a new Economic Policy was adopted for reducing government role and increasing the role of private enterprise.

Thus, in the post World War II scenario there emerged three distinct economic system in the world. In the first place, the capitalist system with some role for the State. Secondly, the totalitarian system based upon socialism, and thirdly, the mixed economies with large State control and investment under parliamentary democracy. The socialist systems crumbled down in East Europe. In China, a communist country, the political system is one-party dictatorship, but the economic system is semi-capitalistic with increasing exposure to globalisation and private enterprise. Butthere is no country now where the State performs only police functions. The State controls the economy, the degree of control varying from country to country. Without State initiative economic development would not have been possible in the less developed countries, including India.

3.3.1 Roles of Government in the Economy

The roles the governments play in the economies of countries under different political philosophies can be studied under the following three distinct heads :

(i) the role as regulator

(ii) the role as promoter

(iii) the role as entrepreneur.

- **The role of regulator :**

The government regulates a large part of the economy of even most of the non- centrally planned economies. As Marshall Dimock remarks, taken together, the activities of the government cut across all the broad categories of economic

activities, namely, entry into business, conduct of business, business results and relationships.

First, the government may determine the conditions under which persons or associations may enter into certain lines of business (through granting of charter, franchise or license, or permitting any entity to use public facilities or resources).This the government does in accordance with laws relating to partnerships, companiesand cooperatives.

Second, the government may regulate or assist the conduct of economic venturesin many ways. These include controls that lay down general standards and prohibitionsthat are necessary for fulfillment of" the objectives of the government with respectto economic development. Similarly, the government may also assist some industriesto develop by providing different inducements and relief.

Third, public control may extend to the results of business operation as in the limitation of public-utility profits, ceiling on dividends and the imposition of excess- profits taxes on business generally.

Finally, the government may also control the relationship between the various classes in the economy, the purpose being to settle conflicts of interests or of rights and to prevent an undue concentration of economic power in few hands or regions. Examples include prohibition of interlocking of directors among companies, abolitionof certain kinds of holding companies, and the regulation of industrial relations.

The role of regulator of the economy is discharged in two different ways :

(i) Through Direct controls; and

(ii) Through Indirect controls.

The direct administrative or physical controls are drastic in nature. The distinguishing characteristic of direct controls is their discretionary nature. They can be applied selectively from firm to firm and industry-to-industry, at the discretion of the State. Till the adoption of the policy of liberalization of the Indian economy thereexisted direct State control over industries through licensing and price controls.

The indirect controls are usually exercised through various fiscal and monetary incentives and disincentives (penalties). Certain activities may be encouraged ordiscouraged through monetary and fiscal disincentives. For instance, a high import

duty may discourage imports, while fiscal and monetary incentives may encourage the development of export-oriented industries (as in India).

Planning is also a part of regulation, for, as in India, it has determined how muchof the total investment during a particular plan period would be shared between the public and the private sectors;

- **The role of promoter :**

The promotional role played by the government is very important in underdeveloped countries. In these countries, where the infrastractural facilities for development are very inadequate and entrepreneurial risk-taking is scarce, the promotional role of the government assumes special significance. The State in such situations assume direct responsibility for building up and strengthening the necessaryinfrastructure for economic development, such as, power, transport, finance andmarketing facilities.

In many developing countries, including India, the.State has played a veryimportant role in the development of infrastructure for industrial and agricultural development. The State has also promoted economic growth by encouraging and promoting research (e.g. the Green Revolution).

- **The role of entrepreneur :**

As an entrepreneur the State has played a participative role in many countries. The State has started ventures of its own, which, after their success, have beenhanded over to private hands. Some enterprises have been retained by the State, asin India. The State has set up, financial institutions to fill up the gaps in the financial system. Only in England the State had no part to play in the industrial revolution which laid the foundation of development in the 18th and 19th centuries.

In the former Soviet Union, practically all resources (factors of production) except labour were under State ownership and control. So the State was virtually the only entrepreneur. It decided, through its Planning Commission, which goods and services would be produced and how. Accordingly resources used to be allocated between different sectors. How many units of a good would be produced was determined not by any market demand but by the State. The market mechanism virtually did not exist.

A perfectly socialist system is virtually a single entrepreneur system. As there was no question of sustaining loss through market sale, the risk element was absent. The question of risk would arise only when goods of such a country would have tobe sold in foreign markets for importing such goods as could not be produced at home.

In India a system of mixed economy has been adopted where State determines the priorities and aims to realize them through five-year plans jointly with the privatesector. Thus in India, as in many other developing countries, both the State and the private sector have important roles to play in economic growth according to the objectives and priori ties outlined by the State.

3.4 Economic implications of the Constitution of India

Business environment in modern India is largely an outcome of the activities of the government as regulator, promoter and entrepreneur.

The constitution of India provided the basic guidelines for direction of economic development and business activities in the country. The Constitution incorporated a number of matters that are immensely significant for economic and business activities. The socio-economic and political objectives of the Indian republic and the basic guiding principles of functioning of State have been clearly laid down in the Preamble to the Constitution, the Fundamental Rights and the Directive Principles of State Policy. The Constitution also earmarked the economic powers and responsibilitiesof the union government and the state governments.

The economic responsibility bestowed upon the State by the Constitution of India is so enormous that it called for massive government participation in thefunctioning of the economy. In order to ensure the discharge of the functions properly, a number of amendments had to be introduced to the Constitution fromtime to time.

Further, a number of economic laws were passed concerning each and every aspect of economic and business activities of people for realizing the socio-economic and political objectives enshrined in the constitution of India.

3.4.1 The Preamble

WE, THE PEOPLE OF INDIA, having solemnly resolved to constitute India into a SOVEREIGN DEMOCRATIC REPUBLIC to secure to all its citizens :

JUSTICE, social, economic and political;

LIBERTY of thought, expression, belief, faith and worship;

EQUALITY of status and of opportunity;

and to promote among all

FRATERNITY, assuring the dignity of the individual and the unity and integrityof the Nation.

IN OUR CONSTITUENT ASSEMBLY this twentieth day of November 1949,do HEREBY ADOPT, ENACT AND GIVE TO OURSELVES THIS
CONSTITUTION. Thus the Preamble to the Constitution of India lays down that attainment of social, economic and political justice; and equality of status and opportunity should be among the most important basic guiding principles of the functioning of the State. The insertion of the words socialist and secular in 1976 byan amendment of the Constitution further signifies the resolve of the State to ensure to all its citizens economic, social and political equality irrespective of caste, religionetc. Preamble itself is not legislation, but it guides the State in enacting and interpreting laws, traditions and customs and resolving al] ambiguities. At present India is a sovereign socialistic secular democratic republic. The governmental move towards privatization since 1991 perhaps necessitates deletion of the term 'socialistic'.

3.4.2 The Fundamental Rights

It can be claimed that the Constitution of India offers to all its citizens, individually and collectively, the best fruits of democracy and those basic freedoms and conditions of life that alone make life significant, forward looking and productive.Without certain basic rights, humans cannot think and act independently for developingtheir body and soul.

The incorporation of fundamental rights implies constrained government. It aims at preventing the government and the legislature from becoming totalitarian. These rights are similar to the rights included in the American Constitution.

The Fundamental Rights enumerated in the Constitution of India are:

1. Right to Equality;
2. Right to freedom;

3. Right against Exploitation;
4. Right to Freedom of Religion;
5. Cultural and Educational Rights; and
6. Right to Constitutional Remedies.

The Fundamental Rights have immense economic significance. The Right to Equality, signifying equality of opportunity, prohibits discrimination against anycitizen on the grounds of religion, race, caste, sex or place of birth in providing or making available economic and other benefits.

The Right to Freedom guarantees the citizens the right to practice any profession,carry on any occupation, trade or business. This provides unique opportunity to citizens to set up business and pursue economic activities of his choice.

The Right against Exploitation gives people the right of a free citizen. It prohibits traffic in human beings and begging and other forms of forced labour. Any contravention of this provision shall be an offence punishable in accordance withlaw. This right provides scope to people for becoming more productive through the use of his own labour for work of his own choice.

Right to Freedom of Religion is very conducive to the economic progress of a country like India where people of different religions live from ancient times. No economic progress can take place in a country where people are divided into fighting religious and ethnic groups.

Cultural and Educational Rights give people the opportunity of self-developmentthrough the acquisition of skill and competence. Every country requires skilledmanpower for economic progress. In fact, in the era of global competition therequirement of skill and competence is increasing day by day. Hence, the Right to Culture and Education to every citizen is a fundamental requirement of economic progress with human capital development.

Right to Constitutional Remedies is the ultimate right of every citizen to redressal of all grievances in accordance with the provisions of the Constitution of India. Every law of the country has to be in conformity with the rights provided tothe citizens by the Constitution of the country. Hence any alleged violation of anyone of these rights has to be judged with reference to the Constitution. The Supreme Court is the ultimate sentinel of these rights.

3.4.3 The Directive Principles of State Policy

The Directive Principles of State policy is a unique feature of the Constitutionof India, not to be found in any country's constitution. The Directive Principles arein the nature of directions to the legislature and the executive that they shouldexercise their authority in such a manner as to ensure due respect for and observance of these principles. Although these directives are not justifiable in courts, the Courts cannot altogether avoid taking cognizance of them. They are the imperative basis of State policy and the Constitution directs the State to apply these principles in making laws.

The Directive Principles that are economically very significant are mentioned below :

1. The State shall try to promote the welfare of people by securing and protecting as effectively as it may a social order in which justice {social, economic and political) shall form a part in all the institutions of economic life.
2. The State shall, in particular, strive to minimize the inequalities in income and endeavour to eliminate inequalities in status, facilities and opportunities not only among individuals but also amongst groups of people residing in different areas or engaged in different vocations.
3. The State shall, in particular, direct its policy towards securing
   (i) that the citizens, men and women equally, have the right to an adequate means of livelihood;
   (ii) that the ownership and control of material resources of the community are so distributed as best to subserve the common good;
   (iii) that the operation of the economic system does, not result in the concentration of wealth and means of production to the common detriment;
   (iv) that there is equal pay for equal work for men and women;
   (v) that the health and strength of workers, men and women, and the tender age of children are not abused, and that citizens are not forced by economic necessity to enter a vocation unsuited to their age and strength;
   (vi) that children are given opportunities and facilities to develop in a healthy manner and in condition of freedom and dignity, and that childhood and youth are protected against exploitation and against moral and material abandonment.

4. The State shall secure that the operation of the legal system promotes justice, on a basis of equal opportunity, and shall, in particular, provide for legal aid, by suitable legislation or in any other way, to ensure that opportunities for securing justice are not denied to any citizen by reason of economic or other disabilities. (The right to employment was a basic right in the constitution of the erstwhile USSR.)

5. The State shall, within the limits of its economic capacity and development, make effective provision for securing the right to work, to education and to public assistance in cases of unemployment, old age, sickness and disablement, and in other cases of undeserved want.

6. The State shall make provision for securing just and humane conditions of work and for maternity relief.

7. The State shall endeavour to secure, by suitable legislation or in any other way, to all workers – a living wage, conditions of work ensuring a decent standard of life – the State shall endeavour to promote cottage industries on individual or co-operative basis in rural areas.

8. The State shall take steps, by suitable legislation or in any other way, to secure participation of workers in the management of undertakings, establishments or other organizations engaged in industry.

9. The State shall endeavour to organize agriculture and animal husbandry onmodern and scientific lines and shall, in particular, take steps for preserving and improving the breeds, and prohibiting slaughter of cows and calves and other milch and draught cattle.

10. The State shall endeavour to protect and improve the natural environment and protect forest and wild life of the country.

These Directive Principles make quite clear how important is the economic responsibility bestowed on the State by the Constitution of India. Through Constitutional amendments, new directives have been added to provide greater socialist orientation to development.

There have been many occasions when the Directive Principles and FundamentalRights came in conflict with each other. In the early days, the Supreme Court held that the Fundamental Rights were sacrosanct part of the Constitution and nothing,

including the Directive Principles, could override them. But the view that the Fundamental Rights should be subordinate to the Directive Principles gained ground in later years. The Directive Principles .of State Policy enunciated in the Constitution of India, thus, provide governmenl responsibility in functioning of the economy. If they were all implemented, India would have been virtually a socialist State by now.

3.4.4 Division of Power

The Constitution of India distributes the items for legislation among three lists: (1) the Union List, (2) the State List and (3) the Concurrent List. The respective jurisdictions of the Union and the States and their mutual relations are clearly defined. Both the Union and the States can legislate on items in the Concurrent List. Enactment made by Union on any item in the Concurrent List gets priority over that of enacted by the State. This clear division of power between the Union and theStates gave authority to governments at both the levels to legislate on matters of national and regional interests respectively.

3.4.5 Rise and Fall of State Control over Economy in India

The brief account of the economic significance of the Constitution and theDirective Principles given above makes it abundantly clear that the State has to shoulder a heavy responsibility for development with social justice. The government has been very active in playing all the three important economic roles in the interest of the country. But any responsibility has to be supported by appropriate authority. The authority was derived by the State from different legislations passed from timeto time affecting different aspects of economic and social life of people of thecountry. The regulatory framework has undergone changes after 1991 in the economicregime era.

The major legislations include the Industries (Development & Regulation) Act 1951, the Companies Act 1956. (Now Companies Act 2013), the now repealedCapital Issue Control Act 1949, the Securities Contracts (Regulation) Act 1956, erstwhile Monopolies and Restrictive Trade Practices Act, 1969 (replaced now by theCompetition Act), The Essential Commodities Act, 1955, the now repealed Foreign Exchange Regulation Act, 1973, the Consumer Protection Act, 1986, the Sick Industrial Companies Act, 1985, the Securities Exchange Board of India Act, 1992 the Foreign Exchange Maintenance Act, the Information Technology Act 2000, the Securitisation Act 2002, Competition Act 2002 etc.

There are also quite a good number of labour laws to regulate the employer- employee relations, working conditions, wages, bonus, labour welfare and social security.

The banking sector of the country has been brought under the effective controlof the Reserve Bank of India by the Banking Companies Act 1949 and subsequent amendments of the Act. Further, to serve the objectives of the New Economic Policy 1991, the government introduced the Policy of Liberalisation of the Financial Sector of the country on the basis of the Report of the Narsimham Committee and other committees such as – Chelliah Committee, Kelkar Committee etc.

Indirect controls have also been playing their part to serve the national development goals. The various quantitative and qualitative monetary weapons have been deployed from time to time to regulate the monetary conditions mainly to control prices. A number of fiscal and monetary incentives have been offered to encourage the growth of priority sectors like the export-oriented industries and small industries and agriculture. The Industrial Policy announced by the government in 1956 and 1991 provided the basis and direction of economic development of the country. The first four decades of independence were years of State control, import substitution and protectionism. But in 1991 India decided to move away from State control and ownership and to re-enter the global economy.

3.5 Summary

The political environment of country, created by the interplay of political institutions, political ideas and the policies and operations of government influences business policies and operations and thereby economic growth. This influence of the political environment upon the economy has been felt since early times. People eulogised good monarchs like Solomon and Haroon-el-Rashid.

In fact, in India the State plays all the three roles the State can play in the economic development of a country within the bounds of democracy. For dischargingthe responsibilities the State drew authority from wide range of laws passed fromtime to time touching each and every aspect of social, economic and political life of the people.

3.6 Exercises

Essay type Questions :

1. What do you understand by the political environment of a country? Discuss the nature of political environment.
2. Give an account of the evolution of political thoughts about the state's economic role since the ancient days.
3. Discuss the role of the State in economic development.
4. State and explain the different roles the government can play in the economic development of nations.
5. State and explain the economic implication of Fundamental Rights in the Constitution of India.
6. Mention the Directive Principles of State Policy of the Constitution of India that influence the economic and business activities of the citizens.

Short answer type questions :

1. State the principal functions of three organs of government.
2. Are the Directive Principles superior to the Fundamental Rights?
3. Explain the role played by the government of .India in the economic development of the country.
4. Mention the Preamble to the Constitution of India.
5. State the Division of Power in the Indian federation.

Objective type questions :

Select correct answer :

1. Political stability of a country
   (a) is essential for innovations to take place
   (b) is not essential for innovations to take place
   (c) discourages innovations
   (d) none of the above.

2. Economically developed countries of today owe their development to
   (a) totalitarian governments
   (b) responsive governments
   (c) democratic governments
   (d) no governance.
3. Aristotle was in favour of
   (a) using money for usury
   (b) as a medium of exchange in business
   (c) for storing as wealth
   (d) none of the above.
4. Government exercises the role of regulator in economic development
   (a) through direct control
   (b) through indirect control
   (c) through both direct and indirect control
   (d) none of the above.
5. In India the government performs
   (a) only the role of regulator
   (b) only the role of promoter
   (c) only the role of entrepreneur
   (d) all the three roles.
6. Directive Principles of State policy in the Constitution of India are
   (a) legally enforceable
   (b) equal to Fundamental Rights
   (c) legislatures and executives are bound to obey Directive Principles
   (d) in no way relevant to executive actions.

Answer : l(a), 2(b), 3(b), 4(c), 5(d) 6(d).

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Unit 4 ❑ Economic Environment

Structure

4.0 Introduction

4.1 Nature

4.2 Economic System

4.3 Industrial Policy of 1948

4.4 Industrial Policy of 1956

4.5 The Industrial Policy of 1991

4.5.1 Privatisation and Disinvestments

4.5.2 Financial Sector in India

4.5.3 Conclusion on Reforms

4.6 Summary

4.7 Exercises

4.8 References

4.0 Introduction

Business enterprise is essentially an economic institution. It conducts its activities in the market system with the objective of profit maximization. The behaviour of an enterprise being economic in nature it is guided by business plans and targets that are formulated taking into consideration the demand and supply conditions which are influenced by the economic environment. However, when we think about economic environment of business, we commonly refer to the'broad characteristics of theeconomic system in which the firm carries out its business activities. Thus, in the study of economic environment of business we generally put emphasis on the macroeconomic environment that influences activities in a broad and general way.

In modern economy, there are broadly three sectors, namely, the business sector, the household sector of individuals and the government. The basic economic

activities are production and consumption. The business sector is concerned with production whilst the other sectors are chiefly concerned with consumers. But in our times the government is also a part of the business sector in many countries, including India. Among the 'others' the capital market and the external sector has profound influence on business. The business sector being the most dynamic, is dependent upon all the three other sectors. In fact, all the sectors together condition the structure of the economy. However, all the activities that keep on going in these sectors create both jointly and separately the economic environment in which the business houses operate.

Independently, business houses can do little to change their economic environment. However, in countries where state control over the economy is not veryrigid, the business firms can collectively do lots to make economic environment conducive to their activities. Business firms can organize their associations through which they can even influence the policy of governments.

4.1 Nature

The environment has its economic dimensions. The economic environment of business is the economic atmosphere within which business operates, and which both influences and is influenced by the policies and modes of business, for the business- environment relationship is a two-way traffic. The'economic atmosphere is the resultof the operation of innumerable economic variables, the major ones being : the economic policy of the home government, the economic policy of foreign governmentswith whom the home government has trade connections (through exports and imports), the budget with its pro or anti-business stance reflected in its tax / subsidy policy, monetary policy (high or low interest), the movements of commodity and security prices, the attitudes and modes of labour unions, employment and income levels, availability of basic infrastructure (both financial and physical) and technology. Individual business units in any industry have practically no control over the above variables. But if the industry decides to work through their associations, they can influence government policy in a democratic country like India (e.g. strikes forrealizing demands). Some economic forces, working from within business, create a kind of environment over which business units have some control. Thus, business is free to determine its organization pattern, size of man power and output, product quality, internal control system and marketing mix. But in a welfare State this

internal freedom is also considerably curtailed by various laws so that the profit- maximisation motive cannot override wider interests of consumers, workers, small shareholders and creditors.

4.2 Economic System

Each country has its own economic system. Economists define an economic system "as the sum total of the devices by which the preference among alternative purposes of economic activity is determined and by which individual activities are coordinated for the achievement of these purposes. The central problem of economic system is the allocation of resources". These economic devices are not the same everywhere. They differ from country to country according to customs, traditions andsocio-economic and political compulsions.

The scope of private business and the extent of government regulation-of economic activities depend to a large extent on the nature of the economic system, which is an important part of the business environment. However, without denying the existence of national differences we can classify the economic systems as socialism, capitalism and mixed economy. Socialism is a state where all resources other than labour are owned and used by the government along with labour for producing goods and services. The allocation of resources for producing these goods and services is made not by the market forces of demand and supply, but by a planning authority according to their estimate of demand for each good and availability of resources to satisfy that demand, Labourers get their rewards accordingto the principle of each according to his needs instead of each according to his capacity (In the erstwhile USSR the economic system was very much like this). Moreresources are allocated for most useful and less resources for less useful products.

Capitalism, in the true sense, is a system of private property in both consumer and producer goods, freedom of enterprise, freedom of choice of occupation, and purchase in a free market, with very limited or no government intervention in economic activities. In capitalist economies the three central problems of the economy, namely, what to produce, how to produce and for whom to produce are solved by the operation of free market forces of demand and supply. In other words, the operation of the forces of demand and supply solve the problem of allocation of

resources and distribution of goods. Such an economy is therefore naturally characterized by inequality of income and wealth.

In between the two there is a system, called the mixed economy, where the market operates but considerably under State surveillance, so that weaker sections donot suffer, and where some businesses are State-owned, some are privately owned, and the rest are owned jointly by the State and private enterprise (as for instance in India).

Those countries that were poor but wanted to avoid rigors of state control and provide private entrepreneurs a role to play in the production of goods and services for overall development, with economic and social justice to every citizen, adopted the mixed economic systems. In mixed economies the governments discharge, the role of planner and keep in its hand the basic and strategic industries. In mixed economies the government functions as the mediator between the conflicting economicgroups as well as the consumers of end products.

However, in today's world none of the extremes, capitalism and socialism canbe found. The laissez-fare capitalism of Adam Smith's visualization had to be adjusted to be compatible with ground reality; that is possibility of revolution of the poor, particularly of the working class. Thus, since the beginning of the last century and particularly since the Great Depression of USA and after the World War II came adjustments in the capitalist system through the recognition of role of state in regulating the business activities for the better functioning of the economic system,

Similarly, adjustments also came to socialism with limited role for marketmechanism in the allocation of resources for generating entrepreneurship, a basic requirement of economic development. In fact, in the socialist countries it wasobserved that after the standard of living of the people registered some improvement,people's initiative and seriousness for further economic progress started diminishing due to lack of sufficient incentives. Hence, these countries had to provide scope for operation of market forces for encouraging people to take initiative for achieving higher levels in economic development.

4.3 Industrial Policy of 1948

The industrial policy of a country reflects the direction and pattern of industrial development it desires to have to help release the economic, social and political

inputs for national development by means of industrialization. In fact, the industrial development of a country is guided and fostered by the industrial policy of the government.

Immediately after attainment of independence, the government of India felt it necessary to make clear its policy on industrialization of the country. Accordingly,a Resolution on Industrial Policy was announced on April 6, 1948.

The Industrial Policy Resolution of 1948, which envisaged that "the State must play a progressively active role in the development of industries," established exclusive monopoly of the Central Government in the manufacture of arms and ammunitions; the production and control of atomic energy; and ownership and management of railway transport. The establishment of new undertakings in six othermajor industries (1) coal, (2) iron and steel, (3) aircraft manufacture, (4) ship-building, (5) manufacture of telephone, telegraph and wireless apparatus, excluding radio receiving sets, and (6) mineral oils was made the exclusive responsibility of theState. But, in the national interest the State itself can secure the cooperation ofprivate enterprises, subject to such control and regulation as it may deem fit. The restof the industrial field was generally left open to private enterprise, individuals as wellas cooperatives, but the State retained the right to participate in any of these industries.

The Industrial policy Resolution of 1948, thus visualised a mixed economy and emphasized the participative, promotional, and regulatory roles of State in industrialization of India.

4.4 Industrial Policy of 1956

When the Industrial Policy Resolution of 1948 was announced, the Constitution of India had not taken the final shape, the Planning Commission was not there andthe First Five Year Plan was to come after three years. Moreover, "socialistic pattern of society" had not yet been officially adopted as the national objective. As the Industrial Policy of 1948 could not foresee all these things, with the launching of the First Five Year Plan it became clear that the industrial policy of the government needed appropriate change for accommodating the new vision of the planners and policy makers. A new Industrial Policy Resolution was, therefore, announced on

April 30, 1956 coinciding with the launching of the Second Five Year Plan from April 1956.

The Industrial Policy Resolution of 1956 was socialist oriented and widened the horizon of the public sector. In order to realize the aims specified in the Preambleto the Constitution of India and to give effect to the Directive Principles of State Policy as well as to achieve the objective of a socialistic pattern of society it was decided that "the State will progressively assume a predominant and direct responsibility for setting up new industrial undertakings and for developing transport facilities. It will also undertake State trading on an increasing scale. At the same time, as an agency for planned development, in the context of the country's expanding economy, the private sector will have the opportunity to develop and expand. The principle of cooperation should be applied wherever possible, and a steadily increasing proportion of the activities of the private sector to be developed along cooperative lines." It was, thus, clear that the adoption of the principle of socialist pattern of society did not mean the end of the private sector. Instead, the private sector was assigned and expected to play an important role in the nation's economy. The Industrial Policy Resolution of 1956, thus, reiterated the resolve to foster national development through a mixed economy.

The Resolution classified industries into three categories having regard to the role the State would play in each of them.

(i) The first category contained industries "the future development of which will be the exclusive responsibility of the State." Industries in this category were listed in Schedule A of the Resolution. It contained arms and ammunitions, atomic energy, iron and steel, heavy casting and forgings of iron and steel, heavy plant and machinery, heavy electrical plants, coal and lignite, mineral oils, mining, mining and processing of copper, lead, zinc, tin, molybdenum andwolfram, minerals in the schedule of atomic energy, aircraft, air transport, railway transport, ship building, telephone, telegraph and wireless apparatusand generation and distribution of electricity. It was also laid down that railways and air transport, arms and ammunitions and atomic energy are to be developed as central government monopolies.

(ii) In the second category were included industries "which will be progressively State-owned and in which the State will, therefore generally take initiative in

establishing new undertakings, but in which private enterprises will also be expected to supplement the effort of the State.” With a view to accelerating their future development, the State will increasingly establish new undertakingsin these enterprises. At the same time, private enterprise will have the opportunity to develop in this field, either on its own or with State participation.The industries listed in the second category were included in Schedule B of the Resolution. It contained all minerals except “minor minerals”, aluminium and other non-ferrous metals not included in Schedule A, machine tools, Ferro alloys and tool steels, basic and intermediate products required by chemical industries, antibiotics, fertilizers, synthetic rubber, carbonization of coal, chemicalpulp, road transport, and sea transport.

(iii) The third category contained all the remaining industries. “Their development will be undertaken ordinarily through the initiative and enterprise of the private sector, though it will be open to the State to start any industry even in this category. It will be the policy of the State to facilitate and encourage the development of these industries in the private sector, in accordance with the programmes formulated in successive Five Year Plans, by ensuring the development of transport, power and other services and by appropriate fiscal and other measures.”

It was also made clear that division of industries into separate categories doesnot imply that they are being placed in watertight compartments. Inevitably, therewill not be an area of overlapping but also a great deal of dovetailing between industries in the private and public sectors. It will be open to the State to start any industry not included in Schedule A and Schedule B when the need of planning so requires or there are other important reasons for it. In appropriate cases, privately owned units may be permitted to produce an item falling within Schedule A for meeting their own requirements or as by-product. Further, it was mentioned thatthere will ordinarily be no bar on small privately-owned units undertaking production,such as the making of launches and other light craft generation of power for local needs and small scale mining. Again, heavy industries in the public sector mayobtain some of their requirements from private sector.

The Industrial Policy Resolution of 1956 reiterated the government’s determination to provide ali sorts of possible assistance for accelerated development of small and cottage industries in view of their distinct role in a capital-scarce economy with abundant supply of manpower.

Another important objective spelt out by the resolution was the removal of regional disparities ;n development through the accelerated development of the regions lagging industrially. The need to develop proper infrastructural facilities for industrial development in the backward regions was emphasized in the Resolution.

The Industrial Policy Resolution of 1956 was announced after implementationof the Constitution of India, formulation of the Planning Commission and adoptionof the policy for economic development through Five Year Plans. Hence, it was morepragmatic and objective-oriented than the 1948 Resolution. Instead of containing threat of nationalization of privately owned industries, the Resolution provided a definite area for the operation of the private sector. The Policy of 1956 was designed to enable the government in due course to gain a dominant position in the industrial sector of the country. In fact, in terms of this resolution, the task of raising the pillars of economic infrastructure in the country was entrusted to the public sector for reasons of its greater reliability, the very large investment required and the longer gestation periods of the projects crucial for economic development. The PolicyResolution of 1956 therefore provided in very clear terms the basis for future industrial development of the country.

4.5 The Industrial Policy of 1991

The economic reform process started here in 1991, while in China it.began in 1979. The Industrial Policy of 1956 underwent changes in 1973, 1977 and 1980 to accommodate the changing requirements of the Indian economy. But gradually it wasfelt that the Policy of 1956, that reserved a dominant position for the public sectorin the economic development, had yielded some results initially but in course of timebureaucratic decision making and lack of initiative for modernization made many of them unable to cope with the requirement of development. At the same time behind the licensing policy there had developed a web of Bureaucratic control that was time-consuming and corruption-prone. Moreover, behind a tariff-protected market, most Indian industries have not been able to be internationally competitive. Restrictions onthe size of business through the Monopolies and Restrictive Trade Practices Act had put a brake on reaching sufficient economy of scale in operation. Similarly, restrictions put on the inflow of foreign investment and technology through theForeign Exchange Regulation Act 1973 also hindered the technological up-gradation

of Indian industries and foreign investment in high-tech industries, which werenecessary for accelerated development of Indian industries. Thus, a time came when the country was not in a position to pay for its imports. The situation necessitateda change in the industrial policy of the country for making Indian industries competitive, its public sector vibrant and creating a congenial environment for inflowof foreign investment and foreign technology for accelerating the pace of industrial development of the country. A big loan had to be taken from the IMF.

The Industrial Policy of July 24, 1991 introduced significant changes in the policy of industrial development of the country by incorporating the following features of reform:

Industrial Licensing Policy: In the first place the Policy of 19911aid down that the Industrial Licensing will be abolished except for a short list of industries relatedto security and strategic concerns, social reasons, hazardous chemicals and overridingenvironmental reasons and items of elitist consumption listed in Annex II. Similarly, the areas where security and strategic concerns predominate, will continue to be reserved for public sector as listed in Annex I. Originally the Annex I included eight items but it now includes only six items, such as, arms and ammunitions, atomic energy, coal and lignite, mineral oils, minerals specified to the Schedule to the atomic energy, and railway transport.

Foreign Investment: It was decided that approval would be given for foreign direct investment up to 51 percent foreign equity in high priority industries. There shall be no bottlenecks of any kind in this process. Such clearance will be availableif foreign equity covers the foreign exchange requirement for imported capital goods.Accordingly, the Foreign Exchange Regulation Act 1973 shall be amended. Whilethe import of components, raw materials and intermediate goods, and payment of know how fees and royalty will be governed by the general-policy applicable to otherdomestic units, the payment of dividends would be monitored through the Reserve Bank of India so as to ensure that outflows on account of dividend payments are balanced by export earnings over a period of time.

Other foreign equity proposals involving 51 % foreign equity that are not made in high priority areas will continue to need prior clearance. However, to provide access to international markets, majority foreign equity holding up to 51 % will be allowed for trading companies that are primarily engaged in export activities. Both foreign direct investment and portfolio investment are now permitted.

Foreign Technology Agreements: The policy provided for automatic permission for foreign technology agreements in high priority areas up to lump sum payment of Rs. 1 Crore, 5% royalty for domestic sales and 8% for exports, subject to total payment of 8% of sales over a 10 year period from date of agreement or 7 years fromcommencement of production. The prescribed royalty rates are net of taxes to be calculated according to standard procedures. For industries other than those in the high priority category automatic permission will be given if no free foreign exchangeis required for any payment.

All other proposals will need specific approval under the general procedure in force. However, no permission will be necessary for hiring of foreign technicians, foreign testing of indigenously developed technologies. Payment may be made from blanket permits or free foreign exchange according to RBI guidelines.

Public Sector; Portfolio of public sector investments will be reviewed with a view to focus the public sector on strategic, high-tech and essential infrastructure. Whereas, some reservations for the public sector is being retained there would be no bar for areas of exclusivity to be opened up to the private sector selectively. Similarly, the public sector will also be allowed entry in areas not reserved for it.

Public enterprises, which are chronically sick and which are unlikely to beturned around will, for the formulation of revival/rehabilitation schemes^ be referred to the Board for Industrial and Financial Reconstruction or other similar high level institutions created for the purpose. A social security mechanism will be created to protect the interests of workers likely to be affected by such rehabilitation packages.

In order to raise resources and encourage wider public participation, a part of the government’s shareholding in the public sector would be offered to mutual funds, financial institutions, general public and the workers.

Boards of Directors of public sector companies will be made more professional and given more powers. Further, there will be greater thrust on performance improvement through the Memorandum of Understanding system through which management would be granted greater autonomy and will be held accountable.

Monopolies and Restrictive Trade Practices Act : Some years ago it was announced that the Act will be amended to remove the threshold limits of assets in respect of MR TP companies and dominant undertakings. This will eliminate the requirement of prior approval of Central Government for establishment of new

undertakings, expansion of undertakings, mergers, amalgamation and takeovers and appointment of Directors under certain circumstances. Emphasis will be placed on controlling and regulating monopolistic, restrictive and unfair trade practices. Inaccordance with the resolve to amend the MRTP Act for removing the hurdles on theway to the expansion of business activities by those who are efficient and competitive,MRTP Act has been replaced by Competition Act 2002. The Act seeks to promote competition through prohibition of anticompetitive practices and abuse of dominanceand regulation of companies beyond a particular size. Thus, the year 1991 markedthe beginning of an era of Economic Reforms, based on three things: privatization, globalisation andliberalization.

4.5.1 Privatisation and Disinvestments

Privatisation is a process by which the government transfers its economic and commercial activities, represented by production and distribution under its.ownershipand control, to the private sector. Many countries of the world (the former socialist countries and a large number of developing countries of Asia, Africa and Latin America) launched massive programmes of privatisation of the public sector during 1980s and 1990s. Privatisation was resorted to in these countries primarily for reducing the budget deficits of governments resulting from investment of revenuesin those sectors that needed huge investments but paid little in return. Subsequently, World Bank and IMF prescribed privatisation as a part of the economic reform in thepoorer and erstwhile socialist countries for their entitlement to loans and otherassistance from these agencies. Thus, gradually privatisation has spread all over the world as one of the requirements of economic progress.

The method of privatisation, adopted in the UK, consisted in conversion into public limited companies by the sale of government holdings. The shares were not off-loaded to another promoter. One of the greatest advantages of this method is the widening and deepening of the capital market. Because, opening of new investment opportunities in shares provided people a scope to look beyond the governmentbonds and other secured but low-interest bearing investments.

Public sector in India : At the time of Independence, India was economically underdeveloped and technologically backward-basically an agrarian economy with heavy unemployment, low level of savings and investment, and a very narrow capitalmarket. In the situation, the private sector was not in a position to shoulder the

responsibility of developing basic and key industries and the overall industrial infrastructure of the country. Thus, the entrepreneurship of the state was visualizedas the only way to develop these core industries and the infrastructure that needed massive investment. In pursuance of the policy of state entrepreneurship large investments were made in building up capacity in a wide spectrum of infrastructure and industrial activities.

Prior to 1947 the public sector in India included only the Railways, the Post & Telegraph, the Port Trust, the Ordnance and Aircraft factories and some state managed undertakings. But, as a result of the adoption of the new industrial policyin 1956, the number of public enterprises increased from 5 in April 1951 to 240 in March 2003. During the same period the volume of investment increased from Rs.29 crore to Rs. 2,52,554 crore. It can be mentioned here that in industries like fuel, petroleum, basic rnetal and non-ferrous metal industries the public sector accountsfor major portion of the total national production. These industries provide linkagesto a host of other industries, and thus the public sector gradually became the backbone of the industrial economy of India.

Privatisation and Disinvestment : While the government had been expanding the horizon of public sector in conformity with its socio-political objective of a socialistic pattern of society, there has been mounting criticism of their poor performance in the context of the growing budget deficit.

So the Industrial Policy of 1991 restricted the role of direct state entrepreneurshipin the industrial development of the country. It suggested drastic reduction in the number of reserved industries from 17 to ultimately only 5 and at the same time required the state to withdraw itself or limit the size of its stake in selected enterprises through disinvestments of its holdings in such enterprises. Further, by stressing the role of professional management and competition with private sector in raising efficiency, the policy finally relied upon the market mechanism for making Indian industries competitive and vibrant.

Privatisation can be accomplished in two different ways, In the first place, itmay be done through opening up of such areas for entrepreneurship of the private sector, which were hitherto monopolized by the public sector. Recent public-private partnership ventures are a step towards that goal (e.g. in port development). Secondly, it may imply change of ownership of existing public enterprises in favour of the private sector. Of the two different processes mentioned above, the new policy

attached more importance to the first process, that is, widening the area of operation of the private sector through reducing the number of industries so long reserved for the public sector.

Since the announcement of the new industrial policy the government has openedfor private investment, both foreign and Indian, a number of industries such as, electricity, and road transport, air transport, telecommunication, mines, minerals, andmetals.

Side by side direct privatization through sale of majority share to the private sector has also been resorted to on a moderate scale. It has also been observed that, direct privatization evokes serious resistance from political parties and workers principally because of fear of loss of job by the employees and in some cases unwillingness in surrendering the profit making enterprises to the private sector. In some cases, because of non-existence of a developed capital market, the government has to depend upo.n private bidders for sale of its enterprises at prices offered bysuch buyers. Thus, though there is a strong case in favour of direct privatization, in reality it was becoming increasingly difficult to push through the proposals of such privatization. Accordingly, in August 1996 the Disinvestments Commission was set up. Subsequently, a ministry was also created .at the center for looking after the disinvestment of central public sector enterprises.

Since the adoption of the new policy the government has been setting targets in the annual budgets every year for disinvestment of its holdings in public sector. From the beginning of disinvestments in 1993-94 the highest amount, so far, of Rs 15,547 crore was realized in 2003-04. A number of reasons may be ascribed to this limited success. The most important of them being the non-acceptability of shares of public enterprises in the capital market. Again, the token privatization to the extent of 10-20 per cent does not enthuse either the Indian or the foreign investors to risk their capital for the obvious reason that, with a marginal holding they will not be able to exercise any purposeful control over the management of such enterprises. The other reason is resistance from trade unions, opposition political parties and intellectuals against the sale of holdings of the state in the profitable enterprises to the private sector. Thus, it appears that the government has not been able to realize the targetof privatization perfectly either through direct sale or through disinvestment. In 2003,the Supreme Court of India had given its verdict against the privatization of public sector firms without specific approval of the Parliament of India, The verdict has put

the government in a very awkward position in pursuing its disinvestment policy, particularly in case of profit-making industries. However, after the UFA government came to power in 2004, the Ministry of Disinvestments has been abolished, though the policy of the government towards disinvestments has remained unchanged.

4.5.2 Financial Sector in India

The policy of liberalization covered not only the real sector of production but also the financial sector. The financial sector (system or market) is the link between demand for and supply of finance or funds of all kinds. The players in this sector can be classified into three: the household sector, the business sector and the government.These players both supply and demand funds. For supplying funds certain institutionscome into existence. For facilitating the passage of funds from sources of supply to the points of demand certain institutions, instruments and practices are there. This web of institutions, instruments and practices to facilitate the supply of finance is called the financial market. The ultimate source of funds in a country is its savings. These savings make possible investment (capital formation) and development. Onlya part of those savings does not go through the financial market - the taxes collected by the government and the ploughed back profits of business.

The financial market has two parts: 1) money market or market for very short- term near-money assets (e.g. treasury bills), and 2) the capital market or the market for medium-to-long term debt funds (shares, bonds, loans etc.).

In India, an old fashioned capital market, consisting of indigenous ba'nkers and money lenders, originating more than 3000 years ago, functions even today, for small traders and agriculturists. But under the impact of a steadily developing modern-type capital market and government efforts to prevent lending at excessively high interest rates charged by those agencies, this market has tended to wither away at someplaces and has been forced to either withdraw or reorganise itself.

The modem capital market of India came into existence in the later part of the 18th century. While a stock-market was functioning, where sale and purchase of the securities of the East India Company used to take place, the first western-typecommercial bank (the Bank of Hindustan) was founded in Calcutta in 1770. At independence in 1947 the modern-type capital market of India consisted of a British- type central bank, called The Reserve Bank of India, a number of British type privatecommercial banks led by the Imperial Bank of India, a number of private insurance

companies, the managing agency houses (mostly British) through whfch British capital was channelised to India, and some credit co-operatives (mostly for agriculturists). There was virtually no agency for supplying long-term or risk capital to business. This represented a major gap in the.financial system.

There was a sea change in the financial market scenario after 1947. First, there was a wave of nationalization, starting with the nationalization of the Reserve Bank of India in 1949, the Imperial Bank in 1955 and the nationalisation of schedule commercial banks in two phases, the first phase coming in 1969. The second, but more important, a number of development finance institutions came to be set up, one after another, for supplying and facilitating the flow of risk capital and long-dated loans to business for promoting economic development which was never uppermost in the minds of the British rulers in British India. All along there was an increasing control of the State over business (Capital Issues Control Act, Licensing, etc.). This state was almost authoritarian in the economic domain.

But, this boom in State activities could not last long. Corruption, inefficiency started taking a heavy toll primarily in the form of losses and increase in non- performing assets (NPA) or bad unrecoverable loans (for commercial and developmentbanks in particular). So, the 1991 economic policy put an end to ever growing state control and ownership of financial as well as non-financial firms. The new policywas expected to stop an excessive drainage of public money to inefficient concerns and departments. An era of financial sector reforms dawned simultaneously. Strengthening of the financial sector and improving the-functioning of the financial market are the core objectives of financial sector reforms in India. The central plank is a set of prudential norms aimed at imparting strength to banks and financial institutions. These norms include not only capital adequacy, but also accounting standards, exposure and disclosure norms, investment and risk management guidelines,The enactment of the Securitisation Act of 2002 has improved the recovery processof non-performing assets (NPA).

Financial Liberalisation : Financial liberalization has been a multi-phase process.To make the financial system responsive to the needs of economic development,since the mid-eighties, the RBI appointed different committees. It also implemented several recommendations of the two committees appointed by it, such as ChakrabortyCommittee and Voughal Committee, in a phased manner and by the late eighties significant deregulations of the short-term sector of the financial markets in India had

taken place. But, the real inducement for reform of the financial sector came in 1991 with the adoption of the policy of structural adjustment of the Indian economy for implementation of the new economic policy. A vibrant and competitive financial system became necessary to sustain the ongoing reform in the structural aspect of the real economy. Thus, on August 14,1991 the Committee on Financial System was appointed under the Chairmanship of Sri Narasimham. "The Committee's approachto the issue of financial sector reform is to ensure that the financial services industry operates on the basis of operational flexibility and functional autonomy with a viewto enhancing efficiency" (Report of the Committee on Financial System, 1991 p-ii). The Committee submitted its report-on November 14, 1991. The report of the Committee constituted the basis of financial sector reform in India. The principal recommendations of the Committee related to the following : (a) To bring down the SLR of banks in a phased manner to 25 percent over a period of about 5 years,

(b) To use the CRR of banks as an instrument of monetary policy and not as a means of controlling the secondary expansion of credit. The Committee also recommended that the interest rate paid to banks on their SLR investments and on CRR in respectof impounded deposits above the basic minimum should be increased, (c) To phase out directed credit programmes and redefine the priority sector by including in it small and marginal farmers, the tiny sector of industry, small business and transport operators, village and cottage industries, rural artisans and other weaker sections. Thecredit target of the redefined priority sector should be 10 percent of the aggregate credit, (d) To bring down interest rate on borrowing in line with other market- determined interest rates and phase out all concessional rates of interest for the sake of macro-economic discipline, (e) Banks and financial institutions should achieve a minimum 4 percent capital adequacy ratio in relation to risk weighted assets by March 1993. (f) The banks whose operations have been profitable should be permitted to raise capital through fresh issues in the capital market, (g) Banks and financial institutions should adopt uniform accounting practices, particularly in regard to income recognition and provisioning against doubtful debts, (h) In respect of banks and financial institutions, which are following the accrual system of accounting, no income should be recognized in the accounts in respect of non-performing assets, (i) Balance sheets of banks and financial institutions should be made more transparent and full disclosure should be made in balance sheets as recommended by the International Accounting Standards Committee, (j) The structureof banking system should evolve towards a broad pattern consisting of large banks,

national banks, local banks and rural banks, (k) Branch licensing should be abolished and the matter of opening and closing of branches be left to the commercial decision of the individual banks. (1) To liberalise policies towards foreign banks with respect to opening and closing of branches. Foreign banks, when permitted to operate in India, should be subjected to same requirements as are applicable to domestic banks,
(m) The development financial institutions should have full operational flexibility and adequate internal-autonomy in matters of sanctioning and disbursing loans.

A number of recommendations of the committee were implemented without much delay. To begin with, the CRR and SLR were reasonably reduced in a phased manner since 1993-94. Secondly, the structure of lending rates was rationalized and the rates of interest were substantially reduced from 1992-93. Thirdly, for proper internal debt management auctioning of 364 days and 91 days Treasury bills were introduced from 1992-93. In the fourth place, as capital adequacy measures forbanks, a risk-asset ratio system was introduced since 1991-92. A system of income recognition and provisioning for non-performing loans was also introduced. Fifthly, in order to encourage healthy competition among the banks and financial institutions for improving the efficiency of the money and capital markets, branch-licensing policy has been liberalized. Similarly, the process of establishment of new banks in the private sector has also been simplified and the banks have been allowed to raise capital from the capital market by fresh share issues for augmenting their resources. In the sixth place, the banks and financial institutions have been given the liberty to determine their lending and borrowing rates according to commercial consideration. Lastly, restrictions on pricing of capital issues have been removed and the functions of Controller of Capital Issues transferred to The Securities & Exchange Board of India (SEBI) for providing autonomy to the issuers of securities and providing adequate protection to the investors. The SEBI provides guidelines from time to time for issuing securities for ensuring .full disclosure of all information pertaining to the issue and at the same time requires the merchant bankers and issue managers to be particular about their role in protecting the interest of the investors. The nationalised insurance sector was thrown open to private players, both domestic and foreign, to create a more vibrant and competitive atmosphere with greater efficiency, choice of insurance products and satisfaction to customers.

Thus, financial liberalization in India became a part and parcel of the structural adjustment for implementation of the new economic policy since 1991. During the

period of more than a decade since the introduction of financial sector reform, as outlined above, some positive impact on the system has become apparent. It can be mentioned here that as a result of the introduction of financial sector reform there hasbeen considerable improvement in the profitability of the banking system in terms of operating and net profits. What is more important is that the intermediation process has improved, as evident from decline in the ratio of net interest income to total assetof public sector banks from 3.16 in 1996-97 to 2.84 in 2000-01. Further, since the introduction of financial sector reform since the early 1990s, the profile of asset portfolio has improved and the extent of net non-performing loans (NPLs) aspercentage of total assets has declined. Banks are allowed to invest in overseasmoney markets (while individuals and listed companies can invest in overseas companies).

Financial liberalization was closely followed by financial crisis in many countriesof Latin America, East Europe and East Asia. The major lesson from the crisis is that deregulation andinternationalization could trigger a crisis if undertaken without adequate structural safeguards. India therefore needs to strengthen the financial sector through reforms, particularly institutional capacity building. The people of India deserve financial services and the institutions that meet their expectations. This requires dynamic prudential and supervisory norms that anticipate and manage systemic risks proactively. The last quarter of the 20th century was characterized by widespread movement towards financial liberalisation across the world.

4.5.3 Conclusion on Reforms

Liberalisation has meant relaxation/removal of govt. controls on ability of companies to start business, finance risk capital, clgse units, expand capacities, price their shares and procure foreign exchange. Privatisation has meant reducing government ownership below 50% in certain cases and even to zero in others, saying goodbye to the nationalization craze of the 1960s and 1970s. While economists have viewed globalisation as the removal of barriers to free trade and as a means to create one global market, sociologists have described it as the intensification of world wide social relations where local events are shaped by happenings in distant places. Although it promotes economic growth by pressurizing economic efficiency and product quality, widening profit opportunities and export income, it has missed outso far on the goals of equity, poverty eradication and enhanced human security.

However, after a decade of the Reforms, the economic health of the country has improved, stock markets are booming, trade is rising and foreign investors are chasing deals in India. Foreign exchange reserves have crossed $100 billion (early 2005 position), and India has repaid some of its loans to the IMF.

This however does not mean that India has returned to Adam Smith's dreamlandof the neutral police state. The government has retained control in crucial areas and over crucial products and services in the interests of the community. Only undue and unnecessary interference in private enterprise has gone. Labour law reforms are, however, yet to be done.

4.6 Summary

Government's economic policy is a vital factor in the economic environment of business. In British India there was no industrial policy really speaking. The first policy announcement of free India came in 1948. The industrial policy, announcedin 1956, was intended to ensure planned growth under large-scale State participation in major sectors. The public sector was to lead development. But the 1991 industrial policy statement reversed the situation by reducing government's area of operation.It aimed at three things: privatization, liberalization and globalisation.

4.7 Exercises

Essay type questions :

1. Examine the nature of the economic environment of business.
2. Define and explain economic system. State the principal characteristics of different-economic systems.
3. State the principal features of the Industrial Policy 1956 and mention how it sought to secure a socialistic pattern of society.
4. Critically examine the Industrial Policy of 1991.
5. Write an essay on financial liberalization in India.
6. Examine the financial system of India with special reference to its evolution in the last two centuries.

Short answer type questions :

1. What are the principal determinants of the environment of business.?
2. Trace the evolution of Laissez-fare capitalism.
3. State the principal features of the Industrial Policy of 1948.
4. Distinguish between a socialist and a non-socialist economy.
5. State the approach of Industrial Policy of 1991 towards the Indian public sector.
6. Mention the principal recommendations of the Narasimham Committee on financial liberalization.
7. What is a capital market?

Objective type questions :

1. Workers and their unions in business unit form a part of

   (a) environment

   (b) political environment

   (c) policy of government

   (d) economic environment.

2. The first industrial policy of India was announced in

   (a) 1951

   (b) 1956

   (c) 1948

   (d) none of the above.

3. Economic planning was introduced in India in

   (a) 1948

   (b) 1951

   (c) 1950

   (d) none of the above.

4. Privatisation of public sector first began in
   (a) United Kingdom
   (b) USA
   (c) India
   (d) Soviet Union.
5. A treasury bill is an instrument
   (a) of money market
   (b) of capita] market
   (c) of both money and capital markets
   (d) none of the above.
6. Financial liberalization has led to
   (a) increase in non performing assets of commercial banks in India
   (b) decrease in non performing assets of commercial banks of India
   (c) has activated the new issue market
   (d) none of the above.

Answers : 1 (d), 2 (c), 3 (b), 4 (a), 5 (a), 6 (d)

4.8 References

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Unit 5 ❑ Technological Environment

Structure

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5.2 Technology & Society

5.3 Technology & Economy

- **5.3.1 Market for technology**
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5.5 Summary

5.6 Exercises

5.7 References

5.0 Introduction

Since the day mankind moved on the road to civilization, by producing the basic requirements of their life, it is technology upon which their dependence increased from day to day. From the fabrication of rudimentary tools for hunting and cultivation to the development of modern information technology every thing is the product of mankind's hunt for better standard of living at lesser cost and more ease. Technology also influences and changes the way of life and living of people by enabling them to know things around them and by providing the basic knowledgeand skill that are required to face the eventualities of life. Technology has provided mankind the knowledge to fight diseases and other odds of nature. At the same timeit has made life easier by providing them equipment for use in daily life. Further,

technologically equipped manpower has the strength to bargain for-better terms and conditions of service and thereby secure better living condition for them. Revolutionarychanges in information technology have brought the world at our doorsteps. Technology transfer is a regular feature of world trade now-a-days. It helps both the transferers and the transferees, Even India is exporting technology to some countries of Asia and Africa. Science is not technology. Rather it is the mother of technology. Sources of technological progress are three : (1) the inventive and innovative capacity of the home population, (2) import from abroad, and (3) the process of learning by doing'. Some economists treat technological progress as embodied in capital (for, in many cases, it cannot be realised without new investment). Large- scale shift to capital-intensive technology may generate unemployment in over-populated labour-surplus countries in the short run. This is why computerisation was resisted by trade unions in India for quite some time.

In the modern world, technology is not readily accessible, not because it commands a price but also because or the fact that it must be learnt by doing. The idea behind it must be explicitly given by its inventor or owner to others. It is largely embodied knowledge. In market economics, innovations and investments are closely tied, for not only does a potentially profitable innovation stimulates investment, but also a high level of investment tends to encourage innovation for capturing markets, potential or actual. The relationship between technology and development being so intimate, appropriate technology is very much in demand though sometimes very scarce in availability. This diametrically opposite nature of demand and supply of technology has made the market for technology highly imperfect. Therefore appropriatetechnology commands a very high price and they are protected by industrial secrecy, that is property rights. Like many other economic regulations, property rights in favour of modern technology, called intellectual property right, have a history going back to centuries.

The ownership of modem technology is principally concentrated in .the hands of multinational corporations (MNC) of the developed countries. The developing countries on the other hand need these modern technologies for development to take place at home. But the price and the terms and conditions demanded by the suppliers of modern technology in many cases become unaffordable to the developing countries. Hence, with market for technology being highly imperfect, problems arise with respect to the transfer of technology. Non-availability of appropriate technology

means perpetuation of underdevelopment, and on the other hand, transfer of technologyfrom the developed countries may mean immense sacrifice for the present. Thus, every developing country in need of superior technology ought to have a policy for import and adoption of technology that suits their requirement of development and capacity to pay and accept the terms and conditions insisted upon by the MNCs of developed countries. They should also concentrate on research for developing their own technologies.

5.1 Definition

Technology refers to the ratio in which capital is combined with labour andother resources (factors) for producing a particular good or service. If more capitalis used with relatively less labour, technology is capital-intensive. If it is the opposite, technology is labour-intensive. In capital-rich countries, capital is relativelycheap, and hence technology is generally capital-intensive (as in developed countries). In capital-poor labour-surplus countries labour is relatively cheap, and hence technology is generally labour-intensive (as in most low-income developing countries).

Technological progress consists in the invention of new products or new techniques for improving quality and quantity of output at reduced cost. If the same amount of capital and other resources results in a higher level of output, it is technological progress. Both improved quality and improved output imply cost reduction. Development experience of the last few decades the world over shows thattechnological progress is no less important than capital accumulation in economic development.

5.2 Technology and Society

Primitive humans were no better than apes. With practically no technology at their disposal they had to live on raw foodstuff of all kinds. Social life in those days was similar to that of animals. But a time came when man acquired some technology to use raw stuff collected from nature. Stone oriented technology ushered in theStone Age, and the onward march of civilisation began. Then came one after another the Bronze Age, the Iron Age and the Nuclear Age, heralded every time by an appropriate bunch of the technological inventions coming from different sources of technological progress in different periods of human history.

Knowledge of farming transformed the roving nornads into families settled at particular places permanently. Family ties became stronger from epoch to epoch. Then came industry and transport, formerly propelled by human muscle power but subsequently by mechanical devices. Man's demand profile also gradually widened along with steady improvement in living standards. Technological progress in medical and other sciences made life safer and longer than in early times. Output of consumer goods increased both in quantity and variety, raising the level of comfort and enjoyment in families. Man's stock of knowledge has increased manifold. Technology has enabled man to land on the moon. Information technology hasreached a height where the world would be at our doorsteps in the twinkling of an eye. Immortality is the only human objective which is get to be attained.

Revolutionary developments in science and technology in the 20th century have led to a slackening of the hold of religion-backed superstitions, beliefs and attitudes amongst educated people in different countries. Thi s, amongst others, has resultedin an improvement in woman's status inside as well as outside families. Growing respect for all castes and religions, supported by a rising sense of equality of all men, has been another major societal effect.

In four decades since World War II (1939-45), people in developed countrieshad become three to five times richer than their grand fathers in material terms, thanks to science and technology. But had they become three to five times happier? Evidence from surveys, however, suggests that this has not been the case. In a study, Campbell, Converse and Rogers found that the percentage saying they were happy fell from 35% in 1957 to 22% in 1973 in the USA. The biggest falls were recorded for the most wealthy groups. One of the main reasons for emphasising a declining life-quality is that most rates of 'social pathology' (e.g. violence, mental illness, crime, divorce, suicide, alcoholism, feeling of loneliness, etc.) have been increasing. The 'decline of the community' is another factor in this unhappiness episode. The community refers to the affective bonds between individuals in a group and between groups, interaction with familiar people and places through common tasks, concerns and responsibilities. There are many ways in which our technology-intensive economy's ways and objectives have undermined the 'community'. Thus, manypeople are getting mentally unhappy in the midst of increasing affluence. To this maybe added the breakdown of the joint family (a kind of 'community') in course of technology-propelled industrialisation.

5.3 Technology and Economy

Output growth is the chief index of economic growth. Output growth is theresult of the operation of three major forces : resources, culture and technology.Thus, we have output = f (resources, culture, technology).

Resources include both natural resources and man-made resources or capital, as well as human resources. The chief function of technology is to determine how resources would be used. So, technology plays a vital role in economic development,and hence, in the economy.

Just as technology determines the use of available resources, so also the available resources frequently determine the kind of technology the country should adopt. (I) The American Indians came to the New World (America) long before the European settlers from across the Atlantic. They found the two continents laden with mineral and timber wealth. But they did not have the know-how (technology) for using those resources, which the Europeans had. So economic development in the Americas had to wait till the arrival of the Europeans. (II) The predominance of labour-intensive technology in over-populated poor countries is explained by the relative abundance, and hence, cheapness of labour as against scarce, costly capital.

The benefits of growth are mainly three : (1) increase in employment opportunitiesthrough output growth, (2) betterment of life-quality through sustained rise in living standards, and (3) reduction in inequality in the long run, as noticed by Oshima's empirical study relating to Asia.

The most fundamental effect of technology is greater productivity in terms of both quantity and quality. This is the main reason why technology is adopted at all levels. Further, as a result of improvement in productivity, real wages of employees tend to rise and prices of some products decline, which spreads the beneficial economic effects of technology throughout the whole social system. The result is thatemployees and citizens are motivated to innovate and develop new technology. The new innovations are then introduced in business for the benefit of the society.

With scientific knowledge becoming available to people all over the world through publications, science can be studied by anybody who understands the language in which it is written. Naturally, development of technology is also becoming easier day by day. Thus in the competitive world of today a business house

can remain ahead of others if it can have the latest technology. Exactly for this reasonresearch and development has assumed considerable importance in the organizations of today.

5.3.1 Market for technology

Economists, particularly Ricardo, Marx, Schumpeter and Kuznet clearly recognized the importance of appropriating knowledge as the main spring of innovation, Innovation means the commercial application of inventions. Firms will not invest in these resources unless they are sure of getting appropriate return from those investments. They will not get the return if their competitors in the market immediately imitate their innovations.

Consequently, the appropriation of technological innovations is not simply a perverse outcome of increasing specialization. It is a necessary condition for innovation to happen in a market economy, As a corollary, firms innovate in the expectation of the commercial advantages they will derive from monopolistic controlover the new technology. Thus, with respect to patent, the conventional interpretationsince the nineteenth century in economics is as a regulatory response to the failureof the free market to achieve optimal resource allocation for invention. This interpretation is in conformity with the origin and spread of the practice of patenting of inventions since the last quarter of fifteenth century. According to Geroski, "patents are designed to create a market for knowledge by assigning propriety priceto innovators which enable them to overcome the problem of non-excludability whileat the same time, encouraging the maximum diffusion of knowledge by making it public".

The principal assumption behind this view is that knowledge, valuable to mankind in any way, is a public good; that is to say, it is characterized by non-rivalryand non-excludability. Moreover, tbe holder of such knowledge can demonstrate its value only by revealing it. Yet in doing so the innovator can no longer control access to it and thereby get all of its benefits. So through temporary legal monopolies, patents may stimulate greater investment in inventive activity and encourage industrialdevelopment.

But patent monopolies may not always be the possible means of excludability and patent specification may not be the efficient medium for diffusing knowledge anyway. Moreover, patents may be used to block equally legitimate efforts by rivals to achieve excludability for their inventions. Such anti competitive practices are

described as 'clustering' ("building a patent wall around a product") and preferably consisting of a large number of interlocking patents. Sometimes 'bracketing, is also practiced for surrounding a competitor's key patent with so many of one's own that the key patent cannot be commercialized. Thus, patent protection provided by the state in the form of temporary monopoly right is open to abuse on a wide scale. Moreover, generally big business houses, which can spend more on research and development and also for registration, dominate markets for patent. This situation may also encourage free riding by such big firms. They can very easily infringe the property rights of smaller firms, individual inventors and indigenous people's knowledge that is marketable.

"Unlike scientific discoveries which are not commercialized, technology is a commercial asset commanding a price, which affects its relative abundance or scarcity on the market as well as the cost of producing it. The buying and selling of technology, as a marketable item, is thus subject to all kinds of market imperfections and is affected by a variety of obstacles which extend not only to its transfer but also to its effective utilization, adaptation, upgrading or further development".

The fundamental paradox about technology in competitive conditions flowsfrom the fact that from a social point of view, technology is a "public good". Thefact that a particular technology is used by one firm does not in principle diminishits usefulness to another. Knowledge does not get used up when it is applied. The social marginal cost of extending the use of a technology is, strictly speaking, zero. Consequently, in an ideal but unattainable world the "right" social price for technology is zero. But, in the real world of the market economy, new technology would not be produced at all if its actual price were zero and the innovators were obliged to make it instantly and freely available to all who might like to use it.

5.3.2 Transfer of technology

The comparative cost of import of technology being usually lower than the cost of developing technology through research at home, developing countries preferimport of technology for development. Moreover, for the small firms of these countries cost of research is not warranted by their scales of operation. This makes import of appropriate technology economically the most justified proposition for these countries, But, the market for technology being highly imperfect, the developingcountries are to choose the way that benefits them most depending on their specific requirement and the circumstances and factor endowments.

Transfer of technology 'is a commercial operation that takes place through firm-to-firm arrangement and involves flows of knowledge, be they embodied in goods (sale of machinery and equipment) or in the form of ideas, technical information and skills (by licensing, franchising or distribution agreements). Technology transfer can take place at arms length, as in the case of the export of capital equipment or of licensing agreement between unaffiliated firms, or it can be internationalized through the transfer of new production techniques within a transnational corporation, betweenaffiliated firms'.

The formalized methods of transferring technologies include foreign direct investment (FDI), joint ventures with foreign firms, wholly owned subsidiaries,licensing, technical service arrangements, joint R&D (research and development) arrangements, training, information exchanges, sales contracts and management contracts. Heterogeneity of developing countries in terms of endowments, areas of specialization, technological profiles, and development strategies as well as the size of markets and the bargaining strength influence the form of transaction to be negotiated for and entered into by different countries. Accordingly, different countries adopt different policies for transfer and management of technology.

However, in the imperfect market for technologies the extent of IPR protectionin the receiving countries primarily determines the volume and direction of inflow of technology. Thus, it is believed that companies would feel encouraged to transfer proprietary technofogies in countries where the IPR protection is strong enough for them to charge license fees high enough to reflect the costs of innovation, and by means of FDI or joint ventures where they maintain more control over these technologies. Accordingly, FDI in some form or other accounts for over 60 per cent of technology transfer flows to developing countries. World Bank, however, found that in countries with strong IPR protection and enforcement, transnational corporations are likely to favour technology licensing agreements and joiat ventures. In countries with weak IPRs, FDI would be the favoured business strategy for overseas suppliers.

Empirical evidence on the links between strong IPRs, investment flows, R&D and technology transfer is not very clear. Evidence from Turkey, published in 1985, found that the banning of pharmaceutical patents appeared to have no significant effects on levels of direct foreign investment, technology transfer or domestic innovation. Similarly, in Brazil, taking manufacturing industry as a whole, there was no evidence that FDI levels were greatly affected by patent protection. On the other

hand, it was found that a large proportion of respondents from the chemical and pharmaceuticals industries claimed that the levels of IPR protection available affected their FDI decisions. The reason behind this scenario is that no single factor determines the way technology will be transferred.

A foreign firm, the owner of the technology, will take decision about the methodof transfer of technology by taking into consideration not only the extent of protection of intellectual property right (IPR) in the host country, but also its administration, the size of the market and the availability of other factors of production locally.

In this connection it is also interesting to note that the relationship between IPR protection and level of development is found to be non-linear, suggesting that patent protection tends to decline in strength as economies move from the poorest stage toa middle-income stage in which they have greater abilities to imitate new technologies(for a cross- section of 99 countries). From the analysis of the record of origin and development of patent protection in the developed countries it would appear that at the initial stages the countries were not as conservative or rigid with respect to IPRas they are today. Moreover, it is also very pertinent to note that the developed countries of today did not at all favour patenting of innovations in food, chemicals and pharmaceuticafs when they were not developed. The simple reason behind this liberal attitude towards patenting (particularly in the patenting of food, chemicals andpharmaceutical) was that they wanted to encourage more innovations to take placein the areas that vitally concerned the health and well being of people.

5.3.3 IPR and Technological and Economic Development of Developing Countries

Technological and economic development of some developing countries since the end of Second World War attracted serious research. It has already been noted that, though Japan did not allow foreigners to register patents in the country, Japan did never had a strong IPR policy. But, it always favoured technology import through licensing agreements. Further, it was particularly liberal towards short period agreements lasting no longer thaa a year, and by 1964 it had made 3400 suchagreements while India made only 600 such agreements. Japan used these short-term agreements mainly for acquiring production and patented know-how in mining,chemicals and machinery. Again, twenty eight per cent of Japan's technology import agreements were for the use of patent rights only against five per cent of India's

agreements. This liberal and selective policy kept down reliance on the import of technology through foreign subsidiaries. But, in India the policy of technology import through foreign subsidiaries lay behind the development of the chemical and pharmaceutical industries. Technology impoit agreement also enabled Japan produce larger out put and thereby enjoy the benefits of large-scale production than India where the production and management decisions were influenced by foreign subsidiaries.

In fact, in Japan the patent policy was tuned to the requirement of development since its inception in the late nineteenth century. American occupation of Japan after the Second World War also facilitated her easier access to the most modern technology of US and its market. As Japan rose higher in the ladder of technological development, it introduced product patent in medicine and pharmaceuticals from 1976. On the other hand, Latin American countries did not gain in export oriented FDI due to following a more open policy.

Independent India inherited the colonial Patent Act of 1911 that required patenting of all innovations for 16 years excepting those relating to atomic energy. However, since independence, particularly with the spread of education in science and technology, pressure for a new patent regime that provides protection to new processes of production was increasing. Accordingly, the Patent Act of 1970 was passed providing for process patent for 7 years in case of food, chemicals andpharmaceuticals and 14 years for other products. This liberal IPR policy, that grantedmonopoly right to the patent holder only for a short period for processes, encouraged research and development on a large scaie, particularly in the field of food, chemicals andpharmaceuticals. The increasing technological capability has been reflected in rising exports of pharmaceutical products to countries like Mexico, South Korea, Israel, Brazil and even USA. In other East Asian countries, such as, Korea and Taiwan the course of technological development followed more or less the same pathas that of Japan. All these countries absorbed, assimilated and replicated available technology under a weak IPR protection regime during the early phase of their development. As the local technological capabilities matured, the domestic industry sought stronger protection, and as in Japan these countries also strengthened theirIPR regimes under the pressure of the developed countries, particularly the USA. Hence, the course of development of all these Asian newly developed countries is thesame. In India, however, the Patent Act of 1970 had to be amended twice in therecent past for accommodating the changes mandated by the WTO, and a third and

a final amendment has taken place with effect from January 2005. On the other hand, Latin American countries did not gain in export oriented FDI due to following amore open policy.

WTO and the future of technology transfer : The new world order for trade and development came into existence under the leadership of the World TradeOrganization since January 1, 1995. The WTO has brought the administration of IPR within its fold through-trie Agreement on Trade Related Intellectual Property Rights System (TRIPS). The Agreement contains a set of provisions for the implementation of TRIPS by the different groups of member countries, such as developed, developingand the least developed. The TRIPS came into existence on January 1, 1995. Under the TRIPS Agreement no member country was required to apply the provisions ofthe Agreement before the expiry of a general period of one year following the dateof entry into force of the WTO. The developing member countries and the countries in process of transition from a centrally planned into a market economy are entitledto delay the application by a further period of four years. The least developedmember countries are entitled to delay the application by a period of ten years over and above the period of one year granted to all countries.

From the year 2005 the developing countries must grant product patent for 20 years from the date the, applications are filed. Thus, products already patented in onecountry will enjoy patent protection in all other countries and all new patents willalso enjoy the same protection.

The GATT Agreement, by making patenting compulsory for 20 years for products and processes, by treating import of patented products in a country as working of the patent in that country and by making protection of patent granted in one country automatic in other countries, has virtually provided for free access to the technology of the developed countries.

However, there are reasons to believe that the enforcement of IPRS has apositive net impact on prospects of countries with low income levels due to greater trade and FDI flows. On the domestic level, growth is propelled by higher rates of inn-ovation. But, that is possible only after the countries move into the middle- income bracket. Thus, the extent of benefits from enforcement of TPRS would vary according to income level of countries,

Since the creation and diffusion of new knowledge are desirable for growth, itis desirable for the less developed countries to encourage creation and di ffusion of

knowledge by all possible means. At the initial stage, the creation and diffusion of knowledge may be subsidized by the state. After all, it is necessary to trade off perpetuation of technological and economic subjugation with dynamic considerationsof growth.

5.4 Management of Technology

Technology is a high-risk, costly phenomenon. In the present stage of technological development in the world, it is very difficult to make a breakthroughin any new area of knowledge that has high profit potential. At the same time, with the base of scientific and technological development quite strong to day, new developments have become easier. But to exploit the available base of scientific and technological knowledge for new inventions what is necessary is effective research on both the products and processes that minimize cost of production and improves quality of production.

To justify research and development expenditures, firms need potentially high payoffs. But in many industries, such as pharmaceuticals, new products are becomingcostlier as a result of heavy expenditure being incurred on research and development.On the other hand, uninformed public fail to consider the high research investment that precedes production of a successful drug.

There is also the added risk that the new product will quickly be duplicated or closely imitated, thereby reducing the profit potential for the original innovator. As the technology of any industry becomes easier to duplicate, the motivation for furtherinnovation declines. Thus, in seeking more profitable potentials for further growth, management either turns more to manufacturing or distribution process improvements.

Further, there are problems for a management that wants to import technology. First, the cost of import is very high. Then, there is absence of basic infrastructural facilities like testing, repairing, availability of spare parts, replacement etc. Hence, even if a company imports a technology paying high price, management of the technology becomes very difficult in the absence of appropriate infrastructure.

Import of technology is not very easy because the developed countries do not like to part with the secrecy about the latest technology. What they can part with is the obsolete and outdated technology which are neither cost effective nor highly beneficial for the users.

Assuming there are companies willing to transfer technology, there is the problem relating to choosing the right source or the right col laborator and obtaining clearance from the government in time. Inordinate delay in securing the clearance of the'government makes the use of the technology unattractive.

In the circumstances, for proper choice of technology and its effective diffusion by the companies what is necessary is closer interaction between the domestic companies and the domestic research institutions. Unfortunately, in spite of havinga number of highly reputed research institutions and universities and technology- seeking companies in the country, the cooperation between industry and the research institutions has not yet developed to any noticeable extent.

Proper management of technology also requires taking appropriate care of the problems like pollution, industrial resource base and social institutions. Developed countries now prefer to concentrate more on development of service sector and less on environment polluting and hazardous industries. Naturally, they are shifting these industries to the developing countries in the name of helping industrialization ofthese countries. Hence, the government as well as the Indian collaborator should be aware of the long term cost benefit of such ventures. Further, the industrial resource base of a country being the basic factor that determines the prospect of industrializationof a country, what is necessary for proper management of technology in the countryis using the technology that can be harnessed properly with the available resources within the country. Dependence on resources that are not available wifhin the country will lead to increase in the cost of production and failure to satisfy the market demand. Lastly, social values and institutions also accelerate or retard the process of transfer and diffusion of technology in a country. Thus, what is necessary is to educate people about the desirability of introduction of new technology in productionand distribution, training the workers to make them capable of working with the technology and not introduce any such change that goes against ethics, sentiment of people for the time being. Technological and industrial change may take place at rapid strides but social changes take place slowly. Naturally, business and the government must adjust the technological change with change in the social and institutional background (people's likes and dislikes).

5.4.1 Technology Policy

Along with a number of other developing countries, India attained political independence after the Second World War. By that time many European countries

and America had achieved considerable industrial progress. Thus, India had to start industrial development from a very backward stage. So in order to achieve rapid progress in the field of production of basic necessities and at the same time develop infrastructure for heavy core industries the government had to attach considerable importance to the development of modem technology. Accordingly, a number of research institutes, universities and other institutions of higher learning and research were established in India. Government also encouraged the use of foreign technologywherever necessary and possible.

The government ultimately came out with a policy on technology, spelling outits aims and the thrust areas. The salient features of that technology policy arementioned below :

Preamble : Frontiers of knowledge are extending at an incredible speed, opening up wholly new areas and new concepts. Technological advances are influencing lifestyle as well as social expectations.

India is known forits diversity. Technology must suit local needs and make an impact on the lives of ordinary citizens. It must give continuous thought to evensmall improvements, which could make better and more cost-effective uses of existing materials and methods of work.

Aims : The basic objectives of the Technology Policy will be development of indigenous technology and efficient absorption and adaptation of imported technology consistent with national priorities and resources. These include :

(a) attain technological competence and self- reliance, to reduce vulnerability, particularly in strategic and critical areas, making the maximum use of indigenous resources;

(b) provide maximum gainful and satisfying employment to all strata of society;

(c) use traditional skills and capabilities making them commercially competitive;

(d) ensure the correct mix between mass production technologies and production by the masses;

(e) ensure maximum development with minimum capital outlay;

(f) locate obsolescence of technology and arrange for modernization;

(g) develop technologies which are internationally competitive, particularly those with export potential;

(h) improve products speedily through greater efficiency and fuller utilization of existing capabilities, and enhance the quality and reliability of process andoutput;

(i) reduce demands on energy, particularly energy from non-renewable resources (like oil);

(j) ensure harmony with environment, preserve ecological balance and improve the quality of habitats, and;

(k) recycle used materials and make full utilization of by-products.

Strengthening the technological base : Research and development together with science and technology education and training of a high order will be accorded pride-of place. Special attention will be given to the promotion and strengthening of the technology base in newly emerging and frontier areas, such as information and material science, electronics and bio-technology. Education and training to upgrade skills is also of utmost importance. Basic research and the building of centers of excellence will be encouraged.

Skills and skilled workers will be accorded recognition. The quality and efficiency of the technology generation and delivery system will be continuously monitored and upgraded. Technologies relevant to the cottage, village and small industries sector will be upgraded. In all sectors, the potential impact on employmentwill bean important criterion in the choice of technology. This will prove beneficialin the long run.

5.5 Summary

History of economic development of countries or even the history of developmentof human civilization is positively linked with the history of development of science and technology. Scientific developments provided mankind the basic knowledgeabout natural resources and their use.

Technology provided the technique or the-specific knowledge about doing things or tackling different problems. The primitive men found themselves helplessin the midst of all-powerful nature. Hence, there gradually developed in them the strong urge for knowing the causes and effects of every thing that happens around them. Man’s passage from the primitive pre-tech no logy age to the modern age of

quality life has been made possible by bursts of technological inventions in different epochs of history. Today life is far better and longer than in primitive times. Mannow knows a thousand times more than what he knew about, what he saw aroundhim in the early years of human history. Instead of being afraid of nature, he has tamed nature with the help of science and technology. The framework of religion- based superstitions, attitudes and beliefs is gradually crumbling down under theimpact of technology, amongst others. People in different parts of the world have come to know each other, so that not only ideas and aspirations but also technologies have started travelling from country to country through the process of technology transfer. Many countries, including India, have framed their own technology policies for facilitating economic development at home, for technology is one of the basic requirements of economic development.

5.6 Exercises

Long answer type questions :

1. What do you understand by "technology"? Explain the distinction between science and technology. Define technological progress.
2. Trace the impact of technology on society through ages.
3. Illustrate the role of technology on economic development.
4. Write an essay on transfer of technology.
5. Discuss technology management with special reference to India.
6. Mention the features of the technology policy of India.
7. State what technology has given to mankind.

Short answer type questions :

1. What is technological environment?
2. Explain the sources of technological progress.
3. Mention the principal methods of transfer of technology from developed to developing countries.
4. State the principal features of the Indian Patent Act, 1970.

5. Mention what do you understand by management of technology.
6. Why is technology called 'embodied capital'?

Objective type questions :

Find the correct answer :

1. In the modern world
   - (a) technology is easily accessible
   - (b) technology is not easily accessible
   - (c) technology can be very easily copied
   - (d) none of the above is true.
2. Technology raises expectation of people
   - (a) by making available new goods and services
   - (b) by educating people about the new development's
   - (c) by creating desire for new goods and services
   - (d) by the globalisation of production and distribution system.
3. Among all the methods of transfer of technology
   - (a) joint venture is the most popular
   - (b) licensing agreement is the most important
   - (c) foreign direct investment is the most important
   - (d) joint research and development is the most important.
4. According to the Indian Patent Act 1970 food, chemicals and pharmaceuticals are granted
   - (a) product patent only
   - (b) process patent only
   - (c) both product patent and process patent
   - (d) none of the above.

5. Principal aim of the technology policy of Government of India is
   (a) to develop appropriate technology indigenously
   (b) to adopt and assimilate appropriate foreign technology
   (c) to develop technology indigenously and also import and assimilate appropriate technology
   (d) to allow foreign companies conduct research and development in India only.

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Unit 6 ❑ Legal Environment

Structure

6.0 Introduction

6.1 Objective, Meaning and importance

6.2 Companies Act, 1956 as amended in 2013

6.3 Foreign Exchange Management Act, 1999

6.4 The Patent Act, 1970

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6.7 Summary

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6.0 Introduction

Laws relating to business are not the same in all countries, the basic reason beingdifference among the countries in the socio-economic and political objectives and systems. The difference in the socio economic and political systems of countries reflects the state of development of the countries. Thus, the laws regarding businessin countries are formulated keeping in view the hopes and aspirations of people as well as the constraints and prospects of development. Broadly, the laws represent the belief of a society about how business is to be organized, how it is to be conducted, how the different shareholders should behave and above all, how non-compliance is to be dealt with. In the primitive society the scale of operation of economic activities was very much limited and people were closely known to each other. Hence, there was no need for any codified law. But even in those days recognised norms and

practices existed for conducting different economic and commercial activities. With expansion in the size of business there increased complexities in operation and socialtension also began to develop around different activities of business houses. In the circumstances, need was gradually felt for introducing strict discipline in the conductof business through well defined rules and laws that take care of every aspect of business activity. But the codification of what can be done and what can not be done by business entities began with the beginning of industrial revolution in England. Industrial revolution not only revolutionized the system of production by increasing the scale of operation through introduction of machines, but also brought revolutionarychanges in the way of life of the workers and the users of industrial products. The situation called for introduction of different laws and rules governing different activities of business.

With the spread of business activities in other parts of world laws relating to business activities began to be formulated in those countries also. Most of those laws followed the British pattern. India, being a part of the British Empire, had to enact and implement those legislations for allowing Britain and other countries of Europeto have a level playing field in India. However, since the independence of the countryin 1947 and adoption of the policy of planned economic development many new legislations have been enacted and at the same time changes have been introducedin the existing laws for accommodating the hopes and aspirations of both business and society.

6.1 Objective, meaning and importance

Traditionally the term business refers to some economic or commercial activity aimed at making profit. Through economic or commercial activities business Organizations supply goods and services to satisfy the needs of people. Again, forthe purpose of providing goods and services to people, business depends upon the people for securing the supply of raw materials and other factors of production, including capital. People on the other hand depend upon the business houses for satisfying their requirements of goods and services. Thus, both business and the people are dependent upon each other for their survival and growth.

But, both business and the people, the consumers of the goods and services provided by business, being parts of the same society differ fundamentally from each

other from the point of view of their interest. While business wants to make maximum profit from sale of goods and services to the members of the society, members of society want to have the goods and services at minimum prices. This divergence of interest between the two interest groups is a perennial cause of conflictin society. Thus, what is needed is a set of clear-cut principles or rules of operation for both business and the rest of society. This set is expected to ensure good business governance. The government, therefore formulates laws and rules for the proper conduct of business. In reality these laws and rules govern almost each and every aspect of business from formation to ultimate winding up. The rest of society, on the other hand, is also required to observe these laws and rules in dealing with business. Thus, the elaborate rules and lavs that are formulated and enacted by the goveinment provide the legal environment of business of a country for the common benefit of both business and the rest of society. In fact, the legal environment of business provides the basis of understanding between business and the rest of society with duerespect for each other. The modern concept of business is, thus, a very broad one.

Business is viewed as a sub system of the totai system. This legal framework, absent in the early periods of history, has evolved through centuries. Of course, in early history we have instances of good monarchs whose order was law and whotried to control unfair business practices (like usury)) in the interest of the peoplethey ruled. Business law, as understood today, is however a relatively modern phenomenon, originating mostly in the 19th century. In the era of globalization the legal environment also incorporates business legislation and rules of other countries.

6.2 Companies Act, 1956 as amended in 2013

The Indian Companies Act, 1956, the first such Act for independent India, repealed three earlier such Acts of British India : (1) the Indian Companies Act,1866, (2) the Indian Companies Act, 1882, and (3) the Indian Companies Act, 1913. This Act was substantially amended in the year 2013.

Short title, commencement and extent.

Sec. l (l) This Act may be called the Companies Act, 1956 as amended in 2013.

(2) It came into force with effect from 8-3-1956, but the amended Act, 2013 received President's assent on 29 August, 2013.

(3) It extends to the whole of India.

The 1956 Act has been in need of a substantial revamp for quite some time now,to make it more contemporary and relevant to corporates, regulators and other stakeholders in India. While several unsuccessful attempts have been made in thepast to revise the existing 1956 Act, there have been quite a few changes in the administrative portion of the 1956 Act. The most recent attempt to revise the 1956 Act was the Companies Bill, 2009 which was introduced in the Lok Sabha, one ofthe two Houses of Parliament of India, on 3 August 2009. This Companies Bill, 2009was referred to the Parliamentary Standing Committee on Finance, which submitted its report on 31 August 2010 and was withdrawn after the introduction of the Companies Bill, 2011. The Companies Bill, 2011 was also considered by the Parliamentary Standing Committee on Finance which submitted its report on 26 June2012. Subsequently, the Bill was considered and approved by the Lok Sabha on 18 December 2012 as the Companies Bill, 2012 (the Bill). The Bill was then considered and approved by the Rajya Sabha too on 8 August 2013. It received the President's assent on 29 August 2013 and has now become the Companies Act, 2013.

The changes in the 2013 Act have far-reaching implications that are set to significantly change the manner in which corporates operate in India. In this publication, we have encapsulated the major changes as compared to the 1956 Act and the potential implications of these changes. We have also included, where relevant, the provisions of the draft rules, which have been issued by the Ministry of Corporate Affairs (the MCA) till date for public comments. Such inclusions have been highlighted with an asterix at the end of the sentence (*). However, please note that these are only draft rules and will undergo changes before being notified.

The 2013 Act has intorduced several new concepts and has also tried to streamline many of the requirements by introducing new definitions. The chapter covers some of these new concepts and definitions in brief. A few of these significantaspects have been discussed in detail.

1. Companies

1.1 One person company : The 2013 Act introduces a new type of entity to the existing list i.e. apart from forming a public or private limited company, trie 2013 Act enables the formation of a new entity a'one-person company' (OPC). An OPC means a company with only one person as its member [section 3(1) of 2013 Act].

1.2 Private company : The 2013 Act introduces a change in the definition for a private company, inter-alia, the new requirement increases the limit of the number of members from 50 to 200, [section 2(63) of 2013 Act],

1.3 Small company : A small company has been defined as a company, other than a public company.

(i) Paid-up share capital of which does not exceed 50 lakh INR or such higher amount as may be prescribed which shall not be more than five crore INR

(ii) Turnover of which as per its last profit-and-loss account does not exceed two crore INR or such higher amount as may be prescribed which shall not be more than 20 crore INR :

As set out in the 2013 Act, this section will not be applicable to the following:

- A holding company or a subsidiary company
- A company registered under section 8
- A company or body corporate governed by any special Act [section 2(85) of 2013 Act]

1.4 Dormant company : The 2013 Act states that a company can be classified as dormant when it is formed and registered under this 2013 Act for a future projector to hold an asset or intellectual property and has no significant accounting transaction. Such a company or an inactive one may apply to the ROC in such manner as may be prescribed for obtaining the status of a dormant company. [Section 455 of 2013 Act]

2. Roles and responsibilities

2.1 Officer : The definition of officer has been extended to include promoters and key managerial personnel [section 2(59) of 2013 Act].

2.2 Key managerial personnel : The term 'key managerial personnel' has been defined in the 2013 Act and has been used in several sections, thus expanding the scope of persons covered by such sections [section 2(51) of 2013 Act].

2.3 Promoter : The term 'promoter' has been defined in the following ways :* A person who has been named as such in a prospectus or is identified by the

company in the annual return referred to in Section 92 of 2013 Act that deals with annual return ; or

- who has control over the affairs of the company, directly or indirectlywhether as a shareholder, director or otherwise; or
- in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act.

The proviso to this section states that sub-section (c) would not apply to aperson who is acting merely in a professional capacity, [section 2(69) of 2013 Act]

2.4 Independent Director : The term 'Independent Director' has now been defined in the 2013 Act, along with several new requirements relating to their appointment, role and responsibilities. Further some of these requirements are not in line with the corresponding requirements under the equity listing agreement [section 2(47), 149(5) of 2013 Act].

3. Investments

3.1 Subsidiary : The definition of subsidiary as included in the 2013 Act states that certain class or classes of holding company (as may be prescribed) shall not have layers of subsidiaries beyond such numbers as may be prescribed. With such a restrictive section, it appears that a holding company will no longer be able to hold subsidiaries beyond a specified number [section 2(87) of 2013 Act].

4. Financial statements

4.1 Financial year : It has been defined as the period ending on the 31st day of March every year, and where it has been incorporated on or after the 1st day of January of a, the period ending on the 31st day of March of the following year,in respect whereof financial statement of the company or body corporate is madeup. [section 2(41) of 2013 Act]. While there are certain exceptions included, thissection mandates a uniform accounting year for all companies and may create significant implementation issues.

4.2 Consolidated financial statements : The 2013 Act now mandates consolidated financial statements (CFS) for any company having a subsidiary or an associate or a joint venture, to prepare and present consolidated financial statements in addition to standalone financial statements.

4.3 Conflicting definitions : There are several definitions in the 2013 Act divergent from those used in the notified accounting standards, such as a joint venture or an associate,, etc., which may lead to hardships in compliance.

5. Audit and auditors

5.1 Mandatory auditor rotation and joint auditors : The 2013 Act now mandates the rotation of auditors after the specified time period. The 2013 Act alsoincludes an enabling provision for joint audits.

5.2 Non-audit services : The 2013 Act now states that any services to be rendered by the auditor should be approved by the board of directors or the audit committee. Additionally, the auditor is also restricted from providing certain specific services.

5.3 Auditing standards : The Standards on Auditing have been accorded legal sanctity in the 2013 Act and would be subject to notification by the NFRA. Auditors are now mandatorily bound by the 2013 Act to ensure compliance with Standards on Auditing.

5.4 Cognisance to Indian Accounting Standards (Ind AS) : The 2013 Act, in several sections, has given cognisance to the Indian Accounting Standards,which are standards converged with International Financial Reporting Standards,in view of their becoming applicable in future. For example, the definition of a financial statement includes a 'statement of changes in equity' which would be required under Ind AS. [Section 2(40) of 2013 Act]

5.5 Secretarial audit for bigger companies : In respect of listed companies and other class of companies as may be prescribed, the 2013 Act provides for a mandatory requirement to have secretarial audit. The draft rules make it applicable to every public company with paid-up share capital > Rs. 100 crores*. As specified in the 2013 Act, such companies would be required to annex a secretarial audit report given by a Company Secretary in practice withits Board's report. [Section 204 of 2013 Act]

5.6 Secretarial Standards : The 2013 Act requires every company to observe secretarial standards specified by the Institute of Company Secretaries of India with respect to general and board meetings [Section 118 (10) of 2013 Act], which were hitherto not given cognizance under the 1956 Act.

5.7 Internal Audit : The importance of'internal audit has been well acknowledged in Companies (Auditor Report) Order, 2003 (the 'Order'), pursuant to which auditor of a company is required to comment on the fact that the internal audit system of the company is commensurate with the nature and size of the company's operations. However, the Order did not mandate that an internal audit should be conducted by the internal auditor of the company. The Order acknowledged that an internal audit can be conducted by an individual who is not in appointment by the company.

The 2013 Act now moves a step forward and mandates the appointment of an internal auditor who shall either be a chartered accountant or a cost accountant, or such other professional as may be decided by the Board to conduct internal audit of the functions and activities of the company.

The class or classes of companies which shall be required to mandatorily appoint an internal auditor as per the draft rules are as follows :*

- Every listed company
- Every public company having paid-up share capital of more than 10 crore INR
- Every other public company which has any outstanding loans or borrowings from banks or public financial institutions more than 25 crore INR or which has accepted deposits of more than 25 crore INR at any point of time during the last financial year

5.8 Audit of items of cost : The central government may, by order, in respect of such class of companies engaged in the production of such goods or providing such services as may be prescribed, direct that particulars relating to the utilisation of material or labour or to other items of cost as may be prescribed shall also be included in the books of account kept by that class of companies. By virtue of this section of the 2013 Act, the cost audit would be mandated for certain companies, [section 148 of 2013 Act]. It is pertinent to note that similar requirements have recently been notified by the central government.

6. Regulators

6.1 National Company Law Tribunal (Tribunal or NCLT) : In accordance with the Supreme Court's (SC) judgement, on 11 May 2010, on the composition and

constitution of the Tribunal, modifications relating to qualification and experience,etc. of the members of the Tribunal has been made. Appeals from the Tribunal shall lie with the NCLT. Chapter XXVII of the 2013 Act consisting of section 407 to 434 deals with NCLT and appellate Tribunal.

6.2 National Financial Reporting Authority (NFRA) : The 2013 Act requires the constitution of NFRA, which has been bestowed with significant powers not only in issuing the authoritative pronouncements, but also in regulating the audit profession.

6.3 Serious Fraud Investigation Office (SFIO) : The 2013 Act has bestowed legal status to SFIO.

7. Mergers and acquisitions

The 2013 Act has streamlined as well as introduced concepts such as reverse mergers (merger of foreign companies with Indian companies) and squeeze-out provisions., which are significant. The 2013 Act has also introduced the requirement for valuations in several cases, including mergers and acquisitions, by registered valuers.

8. Corporate social responsibility

The 2013 Act makes an effort to introduce the culture of corporate socialresponsibility (CSR) in Indian corporates by requiring companies to formulatea corporate social responsibility policy and at least incur a given minimum expenditure on social activities.

9. Class action suits

The 2013 Act introduces a new concept of class action suits which can be initiated by shareholders against the company and auditors.

10. Prohibition of association or partnership of persons exceeding certain number

The 2013 Act puts a restriction on the number of partners that can be admittedto a partnership at 100. To be specific, the 2013 Act states that no associationor partnership consisting of more than the given number of persons as may be prescribed shall be formed for the purpose of carrying on any business that has

for its object the acquisition of gain by the association or partnership or by the individual members thereof, unless it is registered as a company under this 1956Act or is formed under any other law for the time being in force :

As an exception, the aforesaid restriction would not apply to the following :

- A Hindu undivided family carrying on any business
- An association or partnership, if it is formed by professionals who are governed by special acts like the Chartered Accountants Act, etc. [section 464 of 2013 Act]

11. Power to remove difficulties

The central government will have the power to exempt or modify provisions of the 2013 Act for a class or classes of companies in public interest. Relevant notification shall be required to be laid in draft form in Parliament for a periodof 30 days. The 2013 Act further states no such order shall be made after the expiry of a period of five years from the date of commencement of section 1 of the 2013 Act [section 470 of 2013 Act].

12. Insider trading and prohibition on forward dealings

The 2013 Act for the first time defines 'insider trading and price-sensitiveinformation and prohibits any person including the director or key managerial person from entering into insider trading [section 195 of 2013 Act]. Further, the Act also prohibits directors and key managerial personnel from forward dealingsin the company or its holding, subsidiary or associate company [section 194 of 2013 Act].

The 2013 Act introduces a new form of entity 'one-person company' and incorporates certain new provisions in respect of memorandum and articles of association. For instance, the concept of including entrenchment provisions in the articles of association has been introduced.

Incorporation of a company

1. One-person company

The 2013 Act introduces a new type of entity to the existing list i.e. apart from forming a public or private limited company, the 2013 Act enables the formationof a new entity 'one-person company' (OPC). An OPC means a company with

only one person as its member [section 3(1) of 2013 Act]. The draft rules state that only a natural person who is an Indian citizen and resident in India can incorporate an OPC or be a nominee for the sole member of an OPC. *

2. Memorandum of association

Content : The 2013 Act specifies the mandatory content for the memorandum of association which is similar to the existing provisions of the 1956 Act and refers incer-alia to the following :

- Name of the company with last word as limited or private limited as the case may be
- State in which registered office of the company will be situated
- Liability of the members of the company

However, as against the existing requirement of the 1956 Act, the 2013 Act doesnot require the objects clause in the memorandum to be classified as the following :

(i) The main object of the company

(ii) Objects incidental or ancillary to the attainment of the main object

(iii) Other objects of the company [section 4(1) of 2013 Act]

The basic purpose in the 1956 Act for such a classification as set out in section 149 of die 1956 Act, is to restrict a company from commencing any businessto pursue 'other objects of die company' not incidental or ancillary to the main objects except on satisfaction of certain requirements as prescribed in the 1956 Act like passing a special resolution, filing of declaration with the ROC to the effect of resolution.

Reservation of name : The 2013 Act incorporates the procedural aspects for applying for the availability of a name for a new company or an existingcompany in sections 4(4) and 4(5) of 2013 Act.

3. Articles of association

The 2013 Act introduces the entrenchment provisions in respect of the articles of association of a company. An entrenchment provision enables a company to follow a more restrictive procedure than passing a special resolution for altering

a specific clause of articles of association. A private company can. include entrenchment provisions only if agreed by all its members or, in case of a public company, if a special resolution is passed [section 5 of 2013 Act].

4. Incorporation of company

The 2013 Act mandates inclusion of declaration to the effect that all provisions of the 1956 Act have been complied with, which is in line with the existing requirement of 1956 Act.

Additionally, an affidavit from the subscribers to the memorandum and from the first directors has to be filed with the ROC, to the effect that they are not convicted of any offence in connection with promoting, forming or managing a company or have not been found guilty of any fraud or misfeasance, etc., under the 2013 Act during the last five years along with the complete details of name, address of the company, particulars of every subscriber and the persons namedas first directors.

The 2013 Act further prescribes that if a person furnishes false information, heor she, along with the company will be subject to penal provisions as applicable in respect of fraud i.e. section 447 of 2013 Act [section 7(4) of 2013 Act; Also refer the chapter on other areas]

5. Formation of a company with charitable objects

An OPC with charitable objects may be incorporated in accordance with the provisions of the 2013 Act. New objects like environment protection, education, research, social welfare etc., have been added to the existing object for whicha charitable company could be incorporated.

As against the existing provisions under which a company's licence could be revoked, the 2013 Act provides that the licence can be revoked not only where the company contravenes any of the requirements of the section but also where the affairs of the company are conducted fraudulently or in a manner viotativeof the objects of the company or prejudicial to public interest. The 2013 Act thusprovides for more stringent provisions for companies incorporated with charitableobjects [section 8 of 2013 Act].

6. Commencement of business, etc

The existing provisions of the 1956 Act as set out in section 149 which provide for requirement with respect to the commencement of business for

public companies that have a share capital would now be applicable to allcompanies.

The 2013 Act empowers the ROC to initiate action for removal of the name ofa company in case the company's directors have not filed the declaration related to the payment of the value of shares agreed to be taken by the subscribers tothe memorandum and that the paid-up share capital of the company is not less than the prescribed limits as per the 2013 Act, within 180 days of its incorporationand if the ROC has reasonable cause to believe that the company is not carrying on business or operations [section 11 of 2013 Act].

7. Registered office of company

Where a company has changed its name in the last two years, the company is required to paint, affix or print its former names along with the new name of the company on business letters, bill heads, etc. However, the 2013 Act is silent on the time limit for which the forme! name needs to be kept [section 12 of 2013 Act].

8. Alteration of memorandum

The 2013 Act imposes additional restriction on the alteration of the object clauseof the memorandum for a company which had raised money from the public for one or more objects mentioned in the prospectus and has any unutilised money. The 2013 Act specifies that along with obtaining an approval by way of aspecial resolution, a company would be required to ensure following if it intendsto alter its object clause :

- Publishing the notice of the aforesaid resolution stating the justification of variation in two newspapers
- Exit option can be given to dissenting shareholders by the promoters and shareholders having control in accordance with the regulations to be specified by the Securities and Exchange Board of India (SEBI) [section 13 of 2013 Act].

9. Subsidiary company not to hold shares in its holding company

The existing provision of section 42 of the 1956 Act which prohibits a subsidiary company to hold shares in its holding company continues to get

acknowledged in the 2013 Act. Thus, the earlier concern that if a subsidiary isa body corporate, it may hold shares in another body corporate which is the subsidiary's holding company continues to apply [section 19 of 2013 Act].

Prospectus and public offer

The 2013 Act has introduced a new section [section 23] to explicitly provide theways in which a public company or private company may issue securities. This section explains that a public company may issue securities in any of the following manners :

- To public through prospectus
- Through private placement
- Through rights issue or a bonus issue.

For private companies, this section provides that it may issue securities through private placement, by way of rights issue or bonus issue.

Section 23 also provides that compliance with provisions of part I of chapter III is required for the issue of securities to public through prospectus. For private placement compliance, with the provisions of part II of chapter III are required.

The 2013 Act also introduces certain changes with respect to prospectus and public offers aimed at enhancing disclosure requirements as well as streamliningthe process of issuance of securities.

1. Issue of prospectus

Currently, the matters and reports to be included in the prospectus are specified in parts I and II of Schedule II of the 1956 Act. In the 2013 Act, the information to be included in the prospectus is specified in section 26 of 2013 Act. The 2013Act mandates certain additional disclosures:

- Any litigation or legal action pending or taken by a government department or a statutory body during the last five years immediately preceding the year of the issue of prospectus against the promoter of the company.

Share capital and debentures

The chapter on share capital and debentures introduces some key changes in the 2013 Act. To illustrate, the 2013 Act does not give any cognisance to the

existing requirement of section 90 of the 1956 Act chat provided sums saving grace to private companies. Therefore, the applicability of following sections of the 2013 Act is no longer restricted to public companies and private companies which are subsidiaries of a public company and are now applicable to private companies also.

- Two kinds of shares capital
- New issue of shares capital to be only of two kinds
- Voting rights

1. Voting rights

The provisions of 2013 Act regarding voting rights are similar to the existing section 87 of the 1956 Act. The only change noted in the 2013 Act is theremoval of distinction provided by the 1956 Act with respect to tie entitlement: to vote in case the company fails to pay dividend to its cumulative and non- cumulative preference share holders [section 47 of 2013 Act]

The provisions regarding private placement and additional disclosures in prospectus will also help to strengthen the capital markets,

The 2013 Act proposes to re-instate the existing concept of shares with differential voting rights. Pursuant to this section the company may face hardship with regards to computation of proportionate voting rights.

2. Variation of shareholder's rights

Similar to the other provisions of the 1956 Act, the 2013 Act acknowledges the requirements of section 106 of the 1956 Act with an additional requirement in respect of those classes of share holders whose rights are affected pursuant toany variation. The proviso to section 48(1) of 2013 Act states that if the variation by one class of shareholders affects the rights of any other class of shareholders, the consent of three-fourths of such other class of shareholders shall also be obtained and the provisions of this section shall apply to such variation.

3. Application of premiums received on issue of shares

The 2013 Act lays down a similar requirement in section 52 as that of thesection 78 of the l956 Act in respect of application of premiums received on

issue of shares; however, the section of 2013 Act has a non-obstante provisionin respect of certain class of companies which would be prescribed at a laterdate. The 2013 Act states that these classes of companies would not be able to apply the securities premium towards the below specified purposes, unless the financial statements are in compliance with the accounting standards issued under section 133 of 2013 Act.

- Paying up unissued equity shares of the company as fully paid bonus shares
- Writing of the expenses of or the commission paid or discount allowed on any issue of equity shares of the company
- Purchase of its own shares or other securities

The 2013 Act restricts the application of securities of securities premium for a certain class of companies if they full of comply with the accounting standards. The 2013 Act continues to state that securities premium amount can be utilised forpurpose of writing off preliminary expenses. However, in view of the requirementsof accounting standard 26, intangible asset, the requirements of this sub-sectionappears to be superflouds.

4. Prohibition on issue of shares at a discount

Companies would no longer be permitted to issue shares at a discount The only shares that could be issued at a discount are sweat equity wherein shares are issued to employees in lieu of their services [section 53 and Section 54 of 2013 Act].

Further, explanations I and II to the existing section 79A of the 1956 Act that prescribe the provisions in respect of sweat equity have not been included in the 2013 Act. Explanation I defined company for the purpose of this section and explanation II defined sweat equity.

5. Issue and redemption of preference shares

The existing requirement of sections 80 and 80A of the 1956 Act with respectto the issue and redemption of preference shares continues to be acknowledged by the 2013 Act. The 2013 Act reirerates the existing requirement that a company cannot issue preference shares with a redemption date of beyond 20

years. However, it gives an exemption for cases where preference shares have been issued in respect of infrastructure projects. Infrastructure projects have been defined in Schedule VI of the 2013 Act and these shares would be subject to redemption at such percentage as prescribed on an annual basis at the option of such preference shareholders.

Further, the 2013 Act adds another administrative requirement of obtaining special resolution with respect to the preference shares which could not beredeemed by a company. The 2013 Act states that where a company is not ina position to redeem any preference shares or to pay dividend, if any, on such shares in accordance with the terms of issue, it may, with the consent of the holders of three-fourths in vaiue of such preference shares and with the approvalof the Tribunal issue further redeemable preference shares equal to the amount due, including the dividend thereon, with respect to the unredeemed preference shares. On the issue of such further redeemable preference shares., the unredeemedpreference shares shall be deemed to have been redeemed.

The 2013 Act does not envisage any penalty in respect of non-compliance with the provision of this section, as was prescribed in sub-section (6) and (3) of section 60 and 80A of the 1956 Act respectively [section 55 of 2013 Actl.

6. Refusal of registration and appeal against registration

The provision relating to refusal of registration of transfer or transmission of securities by private and public companies has been separately classified in the 2013 Act. The private and public companies are required to send, notice of refusal within 30 days of the receipt of Instrument of transfer, and aggrieved party may appeal to the Tribunal against the refusal within the specified number of days [section 58(2) of 2013 Act].

7. Further issue of share capital

The existing requirement of section 81 of the 1956 Act in regard to further issue ot'capital would no longer be restricted to public companies and would beapplicable to private companies also, since sub-section 3 of section 81 of the 1956 Act has not been acknowledged in the 2013 Act.

Further, the 2013 Act provides that a rights issue can also be made to the employees of the company who are under a scheme of employees' stock option,

subject to a special resolution and subject to conditions as prescribed. Further, the price of such shares should be determined using the valuation report of a registered valuer, which would be subject to conditions as prescribed [section 62of 2013 Act].

8. Issue of bonus shares

The existing 1956 Act does not have any specific provision dealing with issueof bonus shares although it has referred to the concept of bonus shares at many places. The 2013 Act includes a new section that provides for issue or fully paid-up bonus shares out of its free reserves or the. securities premium iccounc or the capital redemption reserve account, subject to the compliance with certainconditions such as authorisation by the articles, approval in the general meeting; and so on [section 63 or' 2013 Act),

9. Unlimited company to provide for share capital on conversion into limited company

This section corresponds to section 32 of the 1956 Ace and seeks to provide thatan unlimited company having a share capital may be re-registered as a limited company by increasing the nominal amount of each share, subject to the condition that no part of the increased capital shall be capable of being calledup, except in the event and for the: purposes of the company being wound up. The 2013 Act further provides that a specified portion of its uncalled share capiral shall not be capable of being called up except in the event and for the purposes of the company being wound up [section 65 of 2013 Act]

10. Reduction of share capital

The 2013. Act gives cognisance to one of the amendments made in the listing agreement by SEBI. A new clause 24(i) was inserted to the listing agreement which provided that a scheme of amalgamation or merger or reconstruction, should comply with the requirements of section 211 (3C) of the 1956 Act. A similar requirement has been introduced in section 66 of 2013 Act, which states that no an application for reduction of share capital shall be sanctioned by the Tribunal unless the accounting treatment, proposed by the company for such a reduction is in conformity with the accounting standards specified in section 133or any other; provision of the 2013 Act and a certificate to that effect by the company's auditor has been filed with the Tribunal.

Further, the 2013 Act clarifies that no such reduction shall be made if thecompany is in arrears in repayment of any deposits accepted by it, either before or after the commencement of the 2013 Act, or the interest payable thereon,

11. Power of the company to purchase its own securities

The existing provision of section 77A of the 1956 Act has been acknowledged by the 2013 Act. The only difference ife that the option available to companyfor a buy-back from odd lots is no longer available [section 68].

The 2013 Act provides flexibility in management and administration by recognising the electronic mode for notices and voting, which is in line with the MCA's efforts to give cognisance to use at electronic media as evident from a number of green Initiatives' introduced recently, maintenance of registers and returns at a place other than the registered office.

The 2013 Act also intends to improve corporate governance by requring disclosure of nature of concern or interest of every director, manager, any other key managerial pernonnel and relatives of such a director, manager or any other key managerial personnel and reduction in threshold of disclosure from 20% to 2%. The term 'key managerial personnel' has now been defined in the 2013 Act and meansthe chief executive officer, managing director, manager, company secretary whole- time director, chief financial officer and any such other officer as may be prescirbed.

1. Annual return

The 2013 Act states that requirement of certification by a company secretary in practice of annual return will be extended to companies having paid up capitalof five crore INR or more and turnover of 25 crore INR or more* (section 92(2) of 2013 Act and die 1956 Act requires certification only for listed companies).

The information that needs to be included in the annual return has been increased. The additional information required, includes particulars of holding, subsidiary and associate companies, remuneration of directors and key manage- rial personnel, penalty or punishment imposed on the company, its directors or officers [section 92(1) of 2013 Act].

2. Place of keeping registers and returns

The 2013 Act allows registers of members, debenture-holders, any other securityholders or copies of return, to be kept at any other place in India in which more

than one-tenth of members reside [section 94(1) of 2013 Act]. The flexibility in the 1956 Act is limited to a place within the city, town or village in which the registered office is situated.

3. General meetings

The 2013 Act states that the first annual general meeting should be held within nine months from the date of closing of the first financial year of the company [section 96 (1) of 2013 Act], whereas the 1956 Act requires the first annual general meeting to be held within 18 months from the date of incorporation.

Currently, the 1956 Act does not define business hours, which the 2013 Act nowdefines as between 9 am and 6 pm. The 2013 Act states that annual general meeting cannot be held on a national holiday whereas the annual general meeting cannot be held on a public holiday as per the existing provisions of section 166 (2) of the 1956 Act [section 96(2) of 2013 Act].

In order to call an annual general meeting at shorter notice, the 2013 Actrequires consent of 95% of the members as against the current requirement inthe 1956 Act which requires consent of all the members [section 101(1) of 2013 Act].

The 2013 Act states that besides director and manager, the nature of concern or interest of every director, manager, any other key managerial personnel and relatives of such director, manager or any other key managerial personnel ineach item of special business will also need to be mentioned in the notice of the meeting [section 102(1) of 2013 Act]. Also, the threshold of disclosure of share holding interest in the company to which the business relates of every promoter, director, manager and key managerial personnel has been reduced from 20% to 2% [section 102 (2) of 2013 Act].

The 2013 Act states that in case of a public company, the quorum will dependon number of members as on the date of meeting. The required quorum is as follows :

- Five members if number of members is not more than one thousand
- Fifteen members if number of members is more than one thousand but up to five thousand

- Thirty members if number of members is more than five thousand [section 103 (1) of 2013 Act]

A limit has been introduced on the number of members which a proxy can represent. The 2013 Act has introduced a dual limit in terms of number of members, which is prescribed as 50 members and also sets a limit in terms of number of shares holding in the aggregate not more than 10% of the total share capital of the company carrying voting rights* [section 105 (1) of 2013 Act].

Further, it is relevant to note that private companies cannot impose restrictions on voting rights of members other than due to unpaid calls or sums or lien [section 106 (1) of 2013 Act].

Listed companies will be required to file with the ROC a report in the manner prescribed in the rules on each annual general meeting including a confirmation that the meeting was convened, held and conducted as per the provisions of the 2013 Act and the relevant rules [section 121 of 2013 Act].

4. Other matters

Listed companies will be required to file a return with the ROC with respect to the change in the number of shares held by promoters and top ten shareholders within 15 days of such a change [section 93 of 2013 Act]. This requirement again demonstrates the effort made towards synchronising the requirementsunder the 2013 Act and the requirements under SEBI. Additionally, on anannual basis, companies are also currently required to make the disclosures with respect to top shareholders under the Revised Schedule VI the 1956 Act.

The 2013 Act requires every company to observe secretarial standards specified by the Institute of Company Secretaries of India with respect to general and board meetings [section 118 (10) of 2013 Act], which were hitherto not given cognisance under the 1956 Act. Additionally, it is also pertinent to note that these standards do not have a mandatory status for the practicing company secretaries.

Director General

1. Woman director

The category of companies which need to comply with the requirement ofhaving at least of one woman director are ae follows :* [section 149(1) of 2013 Act]

(i) Every listed company, within one year from the commencement of second proviso to sub-section (1) of section 149

(ii) Every other public company that has paid-up share capital or one hundred crore rupees or more, or a turnover of three hundred crore rupees or more within three years from rhe commencement of second proviso to sub-section (1) of section 149.

While this new requirement will go a long way in encouraging gender diversity, it has already created quite a stir lu the manner in which companies will ensure compliance.

2. Number of directorship

The 2013 Act increases the limit for number of directorships that can be heldby an individual from 12 to 15 [section 149(1) of 2013 Act]. 3. One director to be resident in India

A new requirement with respect to directors is that at least one director to have stayed in India for at least 182 days in the previous calendar year [section 149(3)of 2013 Act]. This requirement appears to be a departure from the focus givenin the 2013 Act towards use of electronic mode such as use of video conferencesfor meetings and electronic voting, With the increasing use of electronic media, the need, for a director to be resident in India for a minimum amount of time, becomes redundant.

4. Independent directors

One of the significant aspects of the 2013 Act is the effort made towardsincorporating some of the salient requirements mandated by the SEBI in clause 49 of the listing agreement in the 2013 Act itself. To this effect, the 2013 act requires every listed public company to have at least one-third of the totalnumber of directors as independent directors. Further, the central government in the draft rules has prescribed the minimum number of independent directors in case of the following classes of public companies* [section 149(4) of 2013 Act].

(i) Public companies having paid up share capital of 100 crore INR or more; or

(ii) Public companies having turnover of 300 crore INR or more

(iii) Public companies which have, in aggregate, outstanding loans or borrowings or debentures or deposits, exceeding 200 crore INR

The 2013 Act also states that companies will have a period of one year to ensurecompliance with the 2013 Act and the Rules that are framed.

4.1 Conflicting requirements

While there have been attempts to harmonise the requirements of SEBI and the 2013 Act was made, there are several aspects relating to independent directors where the requirements of the 2013 Act differ from that of clause 49 of the equity listing agreement. The requirements of the 2013 Act and the manner in which they differ from those under the clause 49 of the equity listing agreement include the definition itself. The other main differences are as follows :

- Clause 49 does not require the board to exercise its judgment and opine on whether the independent director is a person of integrity or has relevant expertise or experience. This requirement poses difficultly in terms of the manner in which integrity of an individual can be assessed by the board.
- Clause 49 does not require examination of the independence of the relatives of independent directors. Extending the disqualification of the independent directors to consider the pecuniary relationship of the relatives would pose unnecessary hardship for the independent directors.
- The qualification of the independent director has been left to be specified later,
- The 2013 Act brings the constitution of the board in India at par with other international capital markets i.e., by mandating at least one-third of the board to be independent directors in case of listed companies. Whereas, the SEBI requirements are where the chairman of the board is a non-executive director, at least one-third of the board should comprise of independent directors and where the non-executive chairman is a promoter of the company or is related to any promoter or person occupying management positions at the board level or at one level below the board, at least one-half of the board of the company shall consist of independenc directors.

Differing compliance, requirements with respect to the appoitment of independentdirectors, remuneration thereto, imposed by multiple regulators will lead to hardship as well increased cost of compliance for companies.

The 2013 Act limits the tenure of office of an independent director to a maximum of two tenures of five consecutive years, with a cooling-off period of threeyears between the two tenures. During the cooling-off period of three years, should not be appointed in or be associated with the company in any other capacity, either directly or indirectly [proviso to section 149(11) of 2013 Act].

It is also relevant to note that the MCA had released the corporate governance voluntary guidelines in 2009, which permitted three tenures (with other conditions similar to those discussed above) for an independent director while as per the clause 49 of the equity listing agreement an independent director cannot serve for more thannine consecutive years.

Stock options : As per the 2013 Act, an independent director will nor, be eligibleto get stock options but may get payment of fees and profit linked commission subject to limits specified or to be specified in the rules [section 149 (9) of 2013Act]. This again, is in contradiction with SEBI's requirements, whereby for the purpose of granting stock options, the term employee includes independent directors also.

4.2 Databank of independent directors

The 2013 Act makes the appointment process of the independent directors, independent of the company's management by constituting a panel or a data bank to be maintained by the MCA, out of which companies may choose their independent directors. The proposal has its origins in the report of the 21st Standing Committee on finance, wherein it was acknowledged that preparation of a databank of independent directors would vest with a regulatory body that may comprise of representatives of MCA, SEBI, Reserve Bank of India, professional institutions. Chambers of Commerce and Industry etc [section 150 of 2013 Act].

A drawback of constituting a panel of independent directors is that it maydiscourage people from registering with the panel and in that sense limit the options available to a company for appointment of independent directors.

4.3 Code for independent director

The 2013 Act includes Schedule IV 'Code for Independent Directors' (Code) which broadly prescribes the followiug for independent directors :

- Professional conduct
- Role and functions
- Duties
- Manner of appointment
- Reappointment
- Resignation or removal
- Holding separate meetings
- Evaluation mechanism

The code appeals to be mandatory which would lead to some of the following concerns :

- The code states that an independent director shall uphold ethical standards of integrity and probity, however what would constitute ethical behaviour is not defined and is open to interpretation.
- The code does not give any cognisance to the need for training for the independent directors.
- The code refers to appointment of independent directors by the board after evaluating certain attributes. The concern that remains unaddressed is the manner in which companies need to carry out an assessment of the attributes of anindependent director as specified under 'manner of appointment' in the code from the databank maintained by the MCA.

4.4 Liability of independent directors

The 2013 Act makes an attempt to distinguish between the liability of an,independent director and non-executive director from the rest of the board and has accordingly inserted a provision to provide immunity from any civil or criminal action against the independent directors. The intention and effort to limit liability of independent directors is demonstrated from the section 149(12) of the 2013 Act which inter-alia provides that liability for independent directors would be as under :

"Only in respect of such acts of omisoion or commission by a company which

had occurred with his knowledge, attributable through board processes, with his consent or connivance or where he had not acted diligently."

The section seeks to provide immunity from civil or criminal action against independent directors in certain cases. Further, in accordance with the requirementof section 166 (2) of 2013 Act, whole of the board is required to act in goodfaith in order to promote the objects of the company for the benefit of itsmembers as a whole, and in the best interest of the company, its employees, the shareholders, the community and for the protection of the environment. Byvirtue of this section the duty of independent directors actually goes beyond its nonnal definition and is not restricted to executive directors only.

It is amply clear that independent directors have little or no defence and their obligations continues to remain a debatable topic since they would still betreated equivalent to the other directors by holding them responsible for decisions made through board processes.

5. Appointment of an additional director

It is pertinent to note that in order to discourage inappropriate practices, the2013 Act states that any person who fails to get elected as a director in the general meeting can no longer be appointed as an additional director by theboard of directors [section 161 of 2013 Act].

6. Additional compliance requirements for private companies

There are certain increased compliance requirements mandated for private companies which, till now, were mandated only for public companies and private companies which are subsidiaries of public companies. These include thefollowing :

- Appointment of director to be voted individually
- Option to adopt principle of proportional representation for appointment of directors
- Ineligibility on account of non-companies with section 274(1) (g) now extended for appointment or reappointment as a director in a private limited company also.

Meeting of the board and its powers

There have been significant inroads made by the MCA in the recent past with respect to giving cognisance to use of electronic media in day-to-day operations of corporates. The 2013 Act takes this further by allowing use of electronic mode for sending notice of meetings [section 173)3)of 2013 Act], passing of resolution by circulation (section 175 of 20l3 Act] and other areas. Some of the other significant changes in relation to the board and its functioning include :

1. Audit committee

The requirements relating to audit committees was first introduced by the Companies (Amendment) Act, 2000. Audit committees are a measure of ensuring self discipline, constituted with the object strengthen and oversee management in public companies and to ensure that the board of directors discharge their functions effectively. The 2013 Act acknowledges the importanceof an audit committee and entrusts it with additional roles and responsibilities [section 177 of 2013 Act].

However, the fact that the 2013 Act is not entirely in harmony with the requirements of clause 49 of the equity listing agreement, cannot be ignored. While most of the requirements including establishment of a'vigil mechanism' for directors and employees to report genuine concerns, that are similar to the requirements of clause 49 of the equity listing agreement have been incorporated,in the 2013 Act, the differences are as follows :

- As per the 2013 Act, the audit committee should have majority of independent directors.
- Chairman of the audit committee need not be an independent director.
- A majority of the members of the audit committee should be financially literate, i,e. should have the ability to read and understand the financial statements,
- Every listed company and the following class (es) of companies as prescribed in the draft rules should establish a vigil mechanism for directors and employees to report genuine concerns such as :'*
  - Companies which accept deposits from the public
  - Companies which have borrowed money from banks and public financial institutions in excess of fifty crore rupees

2. Nomination and remuneration committee and shareholders relatinoship committee

The 2013 Act includes this new section requiring constituting the nominationand remuneration committee by every listed company and the following classes of companies as prescribed in the draft rules:*

(A) Every listed company

(B) Every other public company that has a paid-up capital of 100 crore lNR or more or which has, in aggregate, outstanding loans or borrowings or debentures or deposits exceeding 200 crore INK.

The Nomination and Remuneration Committee is required to formulate and recommend to the Board of Directors, the company's policies, relating to the remuneration for the directors, key managerial personnel and other employees, criteria for determining qualifications, positive attributed and independence of a director [section 178(1) of 2013 Act].

Further, a board of a company that has more than 1000 shareholders, debenture- holders, deposit-holders and any other security holders at any time during a financial year is required to constitute a Stakeholders Relationship Committee [section 178(3) of 2013 Act].

3. Contribution to charitable funds and political parties

As per the 2013 Act the power of making contribution to 'bona fide' charitable and other funds is proposed to be available to tho board subject to certain limits [section 181 of 2013 Act]. As per the existing requirement of section 293 of the 1956 Act, such power could only be exercised in the general meeting in case of public companies and subsidiaries of public companies as per the 1956 Act.

Further, the limits of coutribution to political parties is proposed to be increased to 7.5% of the average net profits during the three immediately preceding financial years [section 182 of 2013 Act] from the existing limit of 5% underthe 1956 Act.

4. Disclosure interest by director

The 2013 Act prescribes similar requirements with respect to the disclosure of interest by the director as contained in the existing section 299 of the 1956 Act.

The only change that could be identified is where a contractor or arrangement entered into by the company without disclosure of interest by direccor or with participation by a director who is concerned or interested in any way, directlyor indirecrly, in the contract or arrangement, shall be voidable at the option, of the company [section 184 of 2013 Act].

5. Loans and investments by a company

The 2013 Act states that companies can make investments only through two layers of investment companies subject to exceptions which includes company incorporated outside India [seccton 186 of 2013 Act]. There are no such restrictions which are currently imposed under the 1956 Act.

Further, the exemption available from the provisions of section 372A of the1956 Act to private companies as well as loans or investment given or made bya holding company are no longer available under the 2013 Act.

6. Related party transactions

Most of the provisions under Section 188 of 2013 Act are quite similar to the requirements under sections 297 and 314 of the 1956 Act. Some of key changes envisaged in the 2013 Act include the following :

- Need for central government approval has been done away with.
- The 2013 Act has widened the ambit of transactions such AS leasing of property of any kind, appointment of any agent for purchase and sale of goods, material, services or property.
- Cash at prevailing market price has now been substituted with 'arm's length transaction' which has been defined in the section.
- Transactions entered into with related parties now to be included in the board's report along with justification for entering into such contracts and arrangements.
- Penalty for contravention of the provision of section 297 was covered in general provisions in the 1956 Act. However, this is now covered specifically in the section itself which now extends to imprisonment
- Central government may prescribe additional conditions.

Appointment and remuneration of managerial personnel

The 2013 Act brings significant changes to the existing requirement of the 1956 Act with respect to appointment and remuneration of managerial personnel. One of the major changes that could be identified is in respect of the applicability of these provisions. The provisions for appointment of managing director, whole time directoror manager are no longer restricted to the public companies and the private companies which are subsidiaries of public companies and now applicable to all companies. The overall ceiling in respect of payment of managerial remuneration bya public company remains at 11% of the profit for the financial year computed in the manner laid down in the 2013 Act.

1. Appointment of managing director, whole time director or manager [section 196 of 2013 Act.]

- The re-appointment of a managerial person cannot be made eariler than one year before the expiry of the term instead of two years as per the existing provision of section 317 of the 1956 Act, however; the term for which managerial personnel can be appointed remains a five years.
- The eligibility crtieria for the age limit has been revised to 21 years as against the existing requirement of 25 years. Further, the 2013 Act lifts the upper bar for age limit and thus an individual above the age of 70 years can be appointed as key managerial personnel by passing a special resolution.
- Provision is respect of appoiniment of managerial personnel has been specified in section 196 and Schedule V to the 2013 Act.

2. Overall maximum managerial remuneration and managerial remuneration in case of absence or inadequacy of profits [section 197 of 2013 Act].

- As against the existing requirement of section 198 of the 1956 Act, which specifically provides that the provisions of managerial remuneration would be applicable to both public companies and private companies which are subsidiaries of public companies; the 2013 Act states that such provisions would be applicable only to public limited companies.
- Listed companies have been mandated to disclose in their board report the ratio

of remuneration of each director to median employee's remuneration and such other details which are quite extensive as proposed in the draft rules.*

- The existing 1956 Act under section 309 provides that a managing director or a whole time director of a subsidiary company who is in receipt of commission from the holding company cannot receive any commission or remuneration from the subsidiary company. The said restriction has been removed by the 2013 Act, however, such receipt has to be disclosed in the Board's report [section 197(14) of 2013 Act].
- The provisions of existing Schedule XIII of the 1956 Act have been incorporated in Schedule V of the 2013 Act and the requirements have been structured around the same rules, with revised remuneration limits and certain additional requirements, for example, the managerial personnel should not have been convicted of an offence under the Prevention of Money Laundering Acr, 2002.
- The 2013 Act has liberalised the administrative procedures by relaxing the raquirement of obtaining the central government approval provided the company complies with certain requirements including seeiding approval by way of special resolution for payment of managerial remuneration. Similar relaxation norms as envisaged in the 2013 Act had been incorporated in Schedule XIII of the 1956 Act by virtue of the recent circulars issued by MCA.
- Definition of remuneration has undergone few changes in the 2013 Act. The 2013 Act in section 2(7S), defines remunerations as any money or its equivalent given or passed to any person for services rendered by him and includes perquisites as defined under the income-tax Act, 1961. The remuneration thus defined includes reimbursement of any direct taxes to managerial personnel. The1956 Act defined remuneration under section 198 by way of an explanation and provided for the certain specific inclusions that would be construed as remuneration. Section 200 of the 1956 Act specifically prohibited tax fiee payments. The 2013 Act has indirecdy incorporated the same requirement by clarifying that the term remuneration includes any reimbursement of directtaxes.
- The 2013 Act clarifies that premium paid by a company for any insurance taken by a company on behalf of its managing director, whole time director. manager, chief executive officer, chief financial officer or company secretary for

indemnifying any of them against any liability in respect of any negligence, default, misfeasance, breach of duty or breach of trust for which they may be guilty in relation to the company would not be treated as part of remuneration except for the case where person is proved to be guilty. The provisions cited above are similar to that of the existing provisions of section 201 of the 1956 Act.

3. Calculation profits [section 198 of 2013 Act]

The 2013 Act sets out in detail about the allowances and deductions that a company should include while computing the profits for the purpose of determining the managerial remuneration. To illustrate, the 2013 Act states that while computing its profits, credit should not be given for any change in the carrying amount of an asset or of a liability recognised in equity reservesincluding surplus in profit and loss account on measurement of the asset or the liability at fair value.

4. Recovery of remuneration in certain [section 199 of 2013 Act]

The 2013 Act contains stringent provisions in case the company is required to restate its financial statement pursuant to fraud or no-compliance with anyrequirement under the 2013 Act and the Rules made there under. As against the existing requirement of section. 309 of the 1956 Act which only refers to the fact that excess remuneration paid to managerial personnel cannot the waived except with the previous approval of the central government, the 2013 Actmoves a step forward and enables the company to recover the excess remuneration paid (including stock options) from any past or present managing director or whole time director or manager or chief executive officer who, during the period for which the financial statements heve been restated, has acted in such capacity.

5. Appointment of key managerial personnel [section 203]

The 2013 Act provides for mandatory appointment of following whole time key managerial for every listed company and every other company having a paid-up share capital of five crore NIR or more* :

(i) Managing director, or chief executive officer or manages and in their absence, a whole-time director

(ii) Company secretary

(iii) Chief financial officer

Further, the 2013 Act also states that an indrvidual cannot be appointed or reappointed as the chairperson of the company, as well as, the managing directoror chief executive office of the company at the same time except where the articles of such a company provide otherwise or the company does not carry multiple business.

Accounts

The 2013 Act has introduced certain significant amendments in this chapter. It has also introduced several additional requirements such as preparation of consolidated financial statements, additional reporting requirements for the directors in their report such as the development and implementation of the risk management policy, disclosures in respect of voting rights not exercised directly by the employees in respect of shares to which the scheme relates, etc., in comparison with the requirementsof the 1956 Act.

1. Books of accounts

Every company, similar to the requirement of the existing 1956 Act, is required to maintain books of accounts at its registered office. [section 126(1) of the 2013Act]. 'Books of accounts' are required to show (a) all money received and spent and details thereof, (b) sales and purchases of goods, (c) assets and liabilitiesand (d) items of cost as may be prescribed. The books of accounts of a company essentially provide the complete finnancial information of a company.

Further, with respect to branches, while the existing 1956 Act provides that where company has a branch office(s) proper summarized returns, made up to date at interval of not more than three months was supposed to be sent by branchto the company at its registered office or another place etc., such a requirement has now been done away with and only returns are to be periodically sent by the branch to the registered office [section 128(2) of 2013 Act].

Also, in keeping with the times, books of accounts and relevant papers can now be maintained in electronic mode [section 128(1) of 2013 Act].

2. Congnisance of accounting standards

In several instances across the 2013 Act, there are provisions which are also covered within the accounting standards currently notified under section 211(3C)of the 1956 Act and the Companies (accounting standards) Rules. 2006 there under.

There are certain differences in the manner in which a few terms have been defined under the 1956 Act. While the differences in some of these terms may not have any adverse impact, in certain cases, these differences may create implementation issues. Differences in definitions exist in the following cases :

- Associate company
- Control
- Subsidiary company
- Related party

Aasociate company : The definition of an associate company poses certain challenges since :

- It includes joint ventures
- Significant influence is defined to mean 'control ... of business decisions under an agreement'
- It differs from the definition of an associate as per the Accounting Standard 23: Accounting for Investments in Associates in Financial Statements
- The status of an associate and a joint venture cannot be equated since, the degree of control that a company can exercise in such entities, varies significantly. While 'joint control' is the driving factor in case of joint ventures, a company can, at the most only 'participate' in the operating or financing decisions in case of an associate company.
- With regard to the explanation to the section in the 2013 Act, which defines the term 'significant influence, it is to be noted that if a company has 'control' [control has been defined in section 2(27) of the 2013 Act] with respect to business decisions of another company, such other company will in fact be tantamount to a subsidiary and not an associate company. Hence, the use of the term 'control' within the definition of significant influence leads to a conflict between the two definitions (associate company and subsidiary company).

Further, the definitions of the terms 'associate' and 'significant influence' are also not consistent with the definitions provided within the Accounting Standard1S; Related Party Transactions and Accounting Standard 23 : Accounting for [investments in. Associates in Consolidated Financial Statements (AS 23).

Subsidiaries : The term 'control', which is relevant with, respect to identifying subsidiaries, has been defined in section 2(27) of the 2013 Act. While this definition mandates consideration of 'share holding' as one of the factors, the corresponding definition in AS 21: Consolidated Financial Statements (AS 21), refers to voting power'. This issue is an existing one since a similar difference exists between the definition of 'subsidiary', where the term 'control' is relevantunder the existing 1956 Act [section 4(l) of the 1956 Act]. Accordingly, while for consideration of an entity at a subsidiary for the purpose of consolidated financial statements (CFS), reference is made to AS 21, for the purpose of any compliance with the 1956 Act, reference is made to section 4(1) of 1956 Act.

Now that the requirement of preparing consolidated financial statements has been included within the 2013 Act itself, a conflict arises as to whether the definition as per the 2013 Act should be considered for identifying a subsidiary or the definition as per the AS 21. In any case, the company will be non- compliant with the requirement of either the 2013 Act or the AS.

With regard to related party, while there is a substantial difference between the definition under the 2013 Act and AS l6, the difference does not impact the financial statement, since the disclosures in the financial statements will be continued to be made as per AS 16.

3. Consolidate financial statements

The 2013 Act now mandates CPS for any company having a subsidiary, associate or a joint venture [section 129(3)]. The manner of consolidation is required to be in line with the requirements of AS 21 as per the draft rules.* Further, the 2013 Act requires adoption and audit of CFS in the same manneras standalone financial statements of the holding company [section 129(4)].

Apart from CFS, the 2013 Act also requires a separate statement, containing the salient features of financial statements of its subsidiary (ies) in a form as prescribed in the draft rules' [First proviso to section 129 (3)]. Further, section 137(1), also requires an entity to file accounts of subsidiaries outside of lndia, along with the financial statements (including CFS).

While section 129 of the 2013 Act, requires all companies to file a statement containing sailent features of the subsidiaries financial statements, in addition to

the CFS, section 137 of the 2013 Act further requires entities with foreign subsidiaries to submit individual financial statements of such foreign subsidiaries along with its own standalone and consolidated financial statements. Thereseems to be significant amount of overlap and additional burden on companies with respect to these compliances.

To illustrate this point, in order comply with these requirements, a company which has a global presence, with subsidiaries both within as well as outside India will need to comply to the following :

- Prepare its standalone financial statements [section 129(1) of the 2013 Act]
- Prepare a CFS, including all subsidiaries, associates and joint ventures (whether in India or outside) [section 129(3) of the 2013 Act]
- Prepare a summary statement for all its subsidiaries, associates and joint ventures of the salient features of their respective financial statements. (Proviso to section 129(3) of the 2013 Act]
- Submit the standalone financial statements of subsidiary(ies) outside India to the Registrar of Companies (RoC) [section 137(1) of the 2013 Act),

This situation clearly indicates the extent of duplication and additional costs which will be incurred by entities in order to provide the same information in multiple forms or formats.

4. Re-opening of accounts and voluntary revision of financial statements or the board's report

A company would be able to re-open its books of accounts and recast itsfinancial statements after making an application in this regard to the central government, the income tax authorities, the SEBI, or any other statutory regulatory body or authority or any other person concerned, and an order ismade by a court of competent jurisdiction or the Tribunal under the following circumstances (section 130 of the 2013 Act) :

- Relevant earlier accounts were prepared in a fraudulent manner
- The affairs of the company were mismanaged during the relevant period, casting a doubt on the reliability of the financial statements

Further, a company would be able to undertake voluntary revision of financial statements or Board's report if it appears to the director of a company that the financial statement of the company or the board report does not comply with the provisions of section 129 (financial statement) and section 134 of Act 2013 Act (financial statements and board reports) in respect of any of three preceding financial years, after obtaining approval from the Tribunal. The Tribunal shall give notice to the central government and the income tax authorities and shall take into consideration the representations, if any, made by the government or the authorities before passing any such order.

To prevent misuse of these specific provisions, the section contains a proviso which states that such a revised financial statement or report shall not be prepared or filed more than once within a financial year and the detailed reasons for revision of such financial statement or report shall also be disclosed in the board's report in the relevant financial year in which such a revision is being made (section 131 of 2013 Act).

5. Financial year

The 2013 Act has introduced a significant difference in the definition of theterm, 'financial year', which has been defined in section 2(41) of the 2013 Actto mean April to March.

There are several reasons for a company to use a year-end which is different from April to March. These include companies which are subsidiaries of foreigncompanies which follow a different year-end or entities which have significant subsidiaries outside India which need to follow a different year-end, etc. Accordingly, it would not be appropriate to mandate a single year-end for all companies. Since the 2013 Act does not mandate any specific rules or requirements on the basis of a specific year, as in the case of tax laws, the reasonfor requiring a uniform year-end under the 2013 Act, seems to be unclear.

Further, recent notifications or circulars of the Ministry seem to indicate relaxation in the norms for requiring approvals from the Tribunal or the central government, etc. for matters which are administrative or procedural in nature. Accordingly, the option available with companies to seek an exemption from theTribunal will create additional administrative and procedural roadblocks, withno benefits to the companies. Rather, they will need to expend additional costsas well as time either by way of seeking an exemption or preparing multiple setsof financial statements.

Audit and auditors

The 2013 Act features extensive changes within the area of audit and auditors with a view to enhance audit effectiveness and accountability of the auditors. These changes undoubtedly, have a considerable impact on the audit profession. However,it needs to be noted that these changes will also have a considerable impact on the company in terms of time, efforts and expectations involved. Apart from introductingnew concepts such as rotation of audit firms and class action suits, the 2013 Act also Increases the auditor's liability substantially in comparison with the 1956 Act.

1. Appointment of auditors

Unlike the appointment process at each annual general meeting under the 1956 Act, the auditor will now be appointed for a period of five years, with a requirement to ratify such an appointment at each annual general meeting [section 139(1) of 2013 Act].

Further, the 2013 Act provides that in respect of appointment of a firm as the auditor of a company, the firm shall include a limited liability partnership incorporated under the Limited Liability Partnership Act, 2008 [Explanation to section 139(4) of 2013 Act].

Also, the 2013 Act specifies that where a firm, including a limited liability partnership is appointed as an auditor of a company, only those partners who arechartered accountants shall be authorised to act and sign on behalf of the firm. [section 141 of 2013 Act].

Section 141 of the 2013 Act further prescribes an additional list of disqualification,and extends the disqualification to also include relatives. The Section of the2013 Act states that a person who, or his relative or partner is holding and security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company of face valueexceeding one thousand rupees or such sum as may be prescribed; is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, in excess of Rs. 1,00,000*; or has givena guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for Rs.1,00,000*, will not

be eligible to be appointed as an auditor. Additionally, a person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed, will be disqualified from being appointed as an auditor.

It would be relevant to note that the draft rules include 15 relationships in thelist of relatives including step son/daughter and step brother/sister.

The ineligibility also extends to person or a partner of a firm who holds appointment as an auditor in more than twenty companies as well as a person who is in full time employment elsewhere, [section 141 (3)(g) of the 2013 Act].

The definition of a relative does not give cognisance to the Code of Ethics prescribed by the Institute of Chartered Accountants (ICAI) and thus, there are likely to be interpretational issues. Also, the 2013 Act does not specify as towhat would constitute as indirect interest and thus in absence of guidance it would be difficult to assess the extent of implication on the audit profession.

2. Mandatory firm rotation

The 2013 Act has introduced the concept of rotation of auditors as well as audit firms. It states that in case of listed companies (and other class(es) of companies as may be prescribed) it would be mandatory to rotate auditors every five years in case of the appointment of an individual as an auditor and every 10 years in case of the appointment of an audit firm with a uniform cooling off period offive years in both the cases. Further, firms with common, partners in the outgoing audit firm will also be ineligible for appointment as auditor during the cooling off period. The 2013 Act has allowed a transition period of three years for complying with, the requirements of the rotation of auditors [section 139(2) of the 2013 Act]. Further, the 2013 Act also grants an option to shareholders to further require rotation of the audit partner and staff at such intervals as theymay choose [section 139(3) of the 2013 Act].

Currently, while the 1956 Act does not have any requirements relating to the auditor or audit firm rotation, the Code of Ethics issued by the ICAI has a requirement to rotate audit partners, in case of listed companies, after every seven years with a cooling-off period of two years.

3. Non-audit services to audit clients

The 2013 Act states that any service to be rendered by the auditor needs to be approved by the board of directors or the audit committee. Additionally, the auditor is restricted from providing specific services, which include the following :

- Accounting and book keeping services
- Internal audit
- Design and implementation of any financial information system
- Actuarial services
- Investment advisory services
- Investment banking services
- Rendering of outsourced financial services
- Management services and any other service which may be prescribed (to other service has been, prescribed*)

Further, the 2013 Act provides that such services cannot be rendered by theaudit firm either directly or indirectly through itself or any of its partners, its parent or subsidiary or through any other entity whatsoever, in which the firmer any other partner from the firm has significant influence or control or whose name or trademark or brand is being used by the firm or any of its partners [section 144 of the 2013 Act]. The 1956 Act currently does not specify any requirements relating to non-audit services.

These restrictions are aimed at achieving auditor independence. Auditor independence is fundamental to public confidence on the reliability of the auditors' reports. This concept adds credibility to the published financial information and value to investors, creditors, companies, employees as well as other stakeholders. Independence is the audit profession's primary means of demonstrating to the public as well as the regulators that auditors and audit firmsare performing in line with established principles of integrity and objectivity. To comply with these independence norms, the 2013 Act provides for a transitional period of one year, that is, an auditor or an audit firm who or which has been performing any non-audit services on or before the commencement of the 1956 Act shall comply with these provisions before closure of the first financial year after the date of commencement.

4. Joint audits

The 2013 Act provides that members of the company may require the audit process to be conduct by more than one auditor [section 139(3) of the 2013 Act].

5. Auditors liability

The scope and extent of the auditor's liability, has been substantially enhanced under the 2013 Act. Now, the auditor is not only exposed to various new forms of liabilities, however, these liabilities prescribed in the easting 1956 Act have been made more stringent. The auditor is now subject to oversight by multiple regulators apart from the ICAI such as The National Financial Reporting Authority (NFRA, and the body replacing the NACAS) is now authorised to investigate matters involving professional or other misconduct of the auditors. The penalty provisions and other repercussions that an auditor may now be subject to as per the 2013 Act includes monetary penalties, imprisonment, debating of the auditor and the firm and in case of frauds, can even be subjectto class action suits.

6. Additional responsibilities of the auditor

The 2013 Act requires certain new aspects which need to be covered in an auditors' report. These include the following :

- The observations or comments of the auditors on financial transactions or matters which have any adverse effect on the functioning of the company [section 143(3)(f) of the 2013 Act]
- Any qualification, reservation or adverse remark relating to the maintenance of accounts and other matters connected therewith [section 143(3)(h) of the 2013 Act]
- Whether the compauy has adequate internal financial controls system in place and the operating effectiveness of such controls [section 143(3)(i) of the 2013 Act]

There are other reporting requirememts specified in draft rules which include reporting on pending litigations, etc which are already covered either by the accounting standards or guidance from the ICAI, and thus result in duplication".

The 2013 Act requires an auditor to report to the central government within 30 days in a format prescribed within draft rules, if he or she has any reasons to believe that any offence involving fraud is being committed or has been committed against the company by its officers or employees * [section 143(12) of the 2013 Act]. Further, where any auditor does not comply with the above requirements, he or she shall be punishable with a fine which shall not be less than 1 lakh INR, but which may extend to 25 lakh ENR [section 143 (15) of the 2013 Act]. The above requirements are in addition to the existing requirements under the 1956 Act,

The 2013 Act proposes to introduce significant changes to the existing provisionsof the 1956 Act in respect declaration of dividend. The changes are likely to affectthe existing practices followed by companies with regard to the declaration of dividend.

The existing provisions of the 1956 Act in relation to the transfer of a specified percentage of profit to reserve is no longer applicable and thus, companies will be free to transfer any or no amount to its reserves.

Schedule It of the 2013 Act, relating to depreciation defines the useful life of assets as against the depreciation specified in the 1956 Act.

1. Declaration of dividend

- The existing requirement of the 1956 Act with regard to the transfer of aspecified percentage of profits not exceeding 10% to reserve [that is, Companies(Transfer of Profits to Reserve) Rules, 1975] has not been acknowledged in the 2013 Act and thus companies are free to transfer any or no amount of profitsto reserves [section 123 (1) of the 2013 Act].
- Similar to the existing provisions of the 1956 Act, The 2013 Act also provides that no dividend shall be declared or paid in case of inadequate profits by a company subject to the Rules yet to be notified. The company also cannot declare or pay dividend from its reserves other than free reserves [section 123(1)of the 2013 Act]. This could mean that the requirements provided in Companies (Declaration of Dividend out of Reserves) Rules. 1975 have, been retained,
- As per die existing provisions of the 1956 Act, dividend includes interim dividend and all provisions of the 1956 Act which applies to the final dividend equally apply to interim dividend. The 2013 Act, however, imposes a further

restriction on the declaration of interim dividend. The 2013 Act specifically provides that in case a company has incurred loss during the current financial year, up to the end of the quarter immediately preceding the date of declaration of the interim dividend, then the interim dividend cannot be declared at a rate higher than the average dividends declared by the company during the immediatelypreceding three financial years [section 123(3) of the 2013 Act].

- The 2013 Act states that if a company fails to comply with the provisions of acceptance of deposits and repayment of deposits accepted prior to the commencement of this 1956 Act, it will not be able to declare any dividend on equity shares, as against the non-compliance of section 80A of the 1956 Am regarding redemption of irredeemable preference shares, etc [section 123(6) of the 2013 Act].
- The provisions of the existing Schedule XIV of the 1956 Act has been acknowledged under Schedule II of the 2013 Act. Important highlights from the Schedule II are as follows
- The useful life or residual value of an asset have been specified in Part C of the Schedule. Companies will be required to give disclosure for cases where the useful life or residual value is different from the useful life or residual value as specified in Part C of the Schedule.
- It is clarified in the 2013 Act that the requirements of Part C will not be applicable for companies in respect of which the useful life or residual value is notified by a regulatory authority.
- The 2013 Act does not give cognisance to the existing requirements of section 208 of the 1956 Act that deals with the power of a company to pay interest out of capital in certain cases.

2. Transfer of shares to the investor education and protection fund (IEPF)

As against the existing requirement of section 205C of the 1956 Act, the 2013 Act proposes that all shares in respect of which unpaid or unclaimed dividend has been transferred to the IEPF shall also be transferred by the company in name of the fund along with a statement with certain specified details [section 124 of the 2013 Act].

In addition to above, following amounts also need to be transferred by the company to the IEPF [section 125 (2) of the 2013 Act] :

- Gain, through the seizure and disposal of securities in possession of a person who fictitiously acquires or subscribes for a company's securities.
- Sale proceeds of fractional shares arising out of inauance of bonus shares, merger and amalgamation for seven or more years
- Redemption amount of preference shares remaining unpaid or unclaimed for seven or more years

Additionally, the 2013 Act specifies the following modes of utilisation ofamounts available in the IEPF;

- The refund of unclaimed dividends, matured deposits, matured debentures, application money due for refund and interest thereon
- Distribution of any disgorged amount among investors who have suffered losses due to wrong action by any person in accordance with the order of the Court that had decided for such disgorgernent. In order to prevent misuse of underlying securities, investors can claim them back from the IEPF through the provisions in the rules.
- Reimbursement of legal expenses incurred in pursuing class action suits under sections 37 (misleading prospectus) and 245 of the 2013 Act (management or conduct of affairs of the company being overseen in a manner prejudicial to the interests of the company or its members or depositors) by members, debenture holders or depositors as sanctioned by the Tribunal.
- Any other purpose incidental thereto, in accordance with such rules as prescribed

• Winding up

Sucessful companies often overlook the need to revitalize, and they breakdown one day after years of success due to nothing but under-performance.

Modes of winding up

Sec. 425. (1) The winding up of a company may be either

(a) by the tribunal; or

(b) voluntary

(1) The provision of this Act with respect to winding up apply, unless the contrary appears, to the winding up of a company in any of those modes.

Contributories

Liability as contributories of present and past members

426. (1) In the event of a company being wound up, every present and past member shall be liable to contribute to the assets of the company to an amount sufficient for payment of its debts and liabilities and the costs, charges and expenses of the winding up, and for the adjustment of the rights of the contributories among themselves, subject to the provisions of section 427 and subject also to the following qualifications, namely

(a) a past member shall not be liable to contribute if he has ceased to be a member for one year or upwards before the commencement of the winding up;

(b) a past member shall not be liable to contribute in respect of any debt or liability of the company contracted after he ceased to be a member;

(c) no past member shall be liable to contribute unless it appears to the Tribunal that the present members are unable to satisfy the contributions required to be made by them in pursuance of this Act;

(d) in the case of a company limited by shares, no contribution shall be required from any past or present member exceeding the amount, if any, unpaid on shares in respect of which he is liable as such member;

(e) in the case of a company limited by guarantee, no contribution shall, subject to the provisions of sub section (2) be required from any past or present member exceeding the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up;

(f) nothing in this Act shall invalidate any provision contained in any policy of insurance or other contract whereby the liability of individual members on the policy or contract is restricted, or whereby the funds of the company are alone made liable in respect of the policy of contract;

(g) a sum due to any past or present member of the company in his character as such, by way of dividends, profits or otherwise, shall not be deemed to be a debt of the company payable to that member over the claims of other creditors, but such sum shall be taken into account for the purpose of final adjustment of the rights of the contributories among themselves.

(2) In the winding up of a company limited by guarantee having a share capital, every member of the company shall be liable, in addition to the amount undertakento be contributed by him to the assets of the company in the event of its being wound up, to contribute to the extent of any sums unpaid on any shares held by him as ifthe company were a company limited by shares.

Obligations of directors and managers whose liability is unlimited

Sec. 427. In the winding of a limited company, any director or manager whether past or present, whose liability is, under the provisions of this Act, unlimited, shall,in addition to his liability, if any, to contribute as an ordinary member, be liable to make a further contribution as if he were, at the commencement of the winding up,a member of an unlimited company.

Provided that

(a) a past director or manager shall not be liable to make such further contribution, if he has ceased to hold office for a year or upward before the commencement of the winding up;

(b) a past director or manager shall not be liable to make such further contribution in respect of any debt or liability of the company contracted after he ceased to hold office;

(c) subject to the articles of the company, a director or manager shall not be liable to make such further contribution unless the Tribunal deems it necessary to require the contribution in order to satisfy the debts and liabilities of the company, and the costs, charges and expenses of winding up.

Definition of "contributory"

Sec. 428. The term "contributory" means every person liable to contribute to theassets of a company in the event of its being wound up, and includes the holder ofany shares, which are fully paid-up.

Winding up by the Tribunal

Circumstances in which company may be wound up by Tribunal

Sec 433. A company may be wound up by the Tribunal

(a) if the company has, by special resolution, resolved that the company be wound up by the Tribunal;

(b) if default is made in delivering the statutory report to Registrar or in holding the statutory meeting;

(c) if the company does not commence its business within a year from its incorporation, or suspends its business for a whole year;

(d) if the number of members is reduced, in the case of a public company, below seven, and in the case of a private company, below two;

(e) if the company is unable to pay its debts;

(f) if the Tribunal is of the opinion that it is just and equitable that the company should be wound up;

(g) if the company has made a default in filing with the Registrar its balance sheet and profit and loss account or annual return for any five consecutive financial years;

(h) if the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency and morality;

(i) if the Tribunal is of the opinion that the company should be wound up under the circumstances specified in section 424G;

Provisions as to applications for winding up

Sec. 439. (1) An application to the Tribunal for the winding up of a company shall be by petition presented, subject to the provisions of this section,

(a) by a company; or

(b) by any creditor or creditors; or

(c) by any contributory orcontributories; or

(d) by all or any of the parties specified on clause (a), (b) and (c), whether together or separately; or

(e) by the Registrar; or

(f) in a case falling under clause (h) of section 443, by the Central or State Government

(2) A second creditor, the holder of any debentures (including debentures stock).

Power of Tribunal on hearing petition

Sec. 443. (1) On hearing a winding up petition, the Tribunal may

(a) dismiss it, with or without costs; or

(b) adjourn the hearing conditionally or unconditionally; or

(c) make any interim order that it thinks fit, or

(d) make an order for winding up the company with or without costs, or any other order that it thinks fit.

Official Liquidator

Appointment of Official Liquidator

Sec. 448. (1) For the purpose of this Act, so far as it relates to the winding upof a company by the Tribunal, there shall be an official liquidator who-

(a) may be appointed from a panel of professional firms of chartered accountants, advocates, company secretaries, cost and works accountants or firms having a combination of these professions, which the Central Government shall constitute for the Tribunal; or

(b) may be a body corporate consisting of such professionals as ‘may be approved by the Central Government from time to time; or

(c) may be a whole-time or a part-time officer appointed by the Central Government.

(2) The terms and conditions for the appointment of the Official Liquidator and the remuneration payable tahim shall be approved by the (a) Tribunal for those appointed under clause (a) and (b) of sub section (1) and (b) Central Government for those appointed under clause (c) of the Sub-section (1).

Powers of liquidator

Sec. 457. (1) The liquidator in a winding up by the Tribunal shall have power, with the sanction of the Tribunal-

(a) to institute or defend any suit, prosecution, or other legal proceeding, civil or criminal, in the name or on behalf of the company;

(b) to carry on the business of the company so far as may be necessary for the beneficial winding up of the company;

(c) to sell the immovable or movable property and actionable claims of the company by public auction or private contract, with power to transfer the whole thereof to any person or body corporate, or to sell the same in parcels;

(ca) to sell whole of the undertaking of the company as a going concern;

(d) to raise on the security of the assets of the company any money requisite;

(e) to do all such other things as may be necessary for winding up the affairs of the company and distributing its assets.

(2) The liquidator in a winding up by the Tribunal shall have power (i) to doall acts to execute in the name and on behalf of the company all deeds, receipts etc., (ia) to inspect the records of the company, (ii) to prove rank and claim in theinsolvency of any contributory, (iii) to draw, accept, make or endorse any bill of exchange, promissory note etc., (iv) to take out, in his official name, letters ofadministration to any deceased contributory and to do in his official name any other act necessary for obtaining payment of money due from any contributory, (v) to appoint an agent to do any business which the liquidator is unable to do himself.

Voluntary Winding up

Circumstances in which a company may be wound up voluntarily

Sec. 484. (1) A company may be wqund up voluntarily-

(a) when the period if any, fixed for the duration of the company by the articles has expired, or the event if any has occurred, on the occurrence of which the articles provide that the company is to be dissolved, and the company in general meeting passes a resolution requiring the company to wind up voluntarily;

(b) if the company passes a special resolution that the company be wound up voluntarily.

Publication of resolution to wind up voluntarily

Sec. 485. (1) Within fourteen days from the passing of the resolution of windingup of the company it must be advertised in newspapers and Official Gazette.

(2) Default in complying with the requirement of sub-section will attract punishment to the extent of fine of rupees five-hundred for every day of default for every officer responsible.

Commencement of voluntary winding up

Sec. 486. A voluntary winding up shall be deemed to commence at the time when the resolution for voluntary winding up is passed.

Declaration of solvency in case of proposal to wind up voluntarily

Sec. 488. (1) When it is proposed to wind up a company voluntarily, its directorsor the majority of the directors, may, at a meeting of the Board, make a declaration verified by an affidavit, to the effect that they have made full enquiry of the affairsof the company and is of the opinion that the company has no debts or that it willbe able to pay its debts in full within such period not exceeding three years from the commencement of the winding up as may be specified in the declaration.

(2) A declaration made as aforesaid shall have no effect for the purpose of this Act, unless-

(a) it is made within the five weeks immediately preceding the date of the passing of the resolution for winding up the company and is delivered to the Registrar for registration before that date; and

(b) it is accompanied by a copy of the report of the auditor of the company on "the profit and loss account of the company for the period commencing from the date up to which last such account was prepared and ending with the latest practicable date immediately before making the declaration andthe balance sheet of the company made out as on the last-mentioned dateand also embodies a statement of the company's assets and liabilities as at that date.

(3) Any director making declaration under this section without having reasonable ground for the opinion that the company will be able to pay its debts in full within the period shall be punishable with imprisonment up to six months or fine up to fifty thousand rupees or both.

Power of company to appoint and fix remuneration of liquidators

Sec. 490. (1) The company in general meeting shall-

(a) appoint one or more liquidators for the purpose of winding up the affairs and distributing the assets of the company; and

(b) fix remuneration, if any, to be paid to the liquidator or liquidators.

(2) Any remuneration so fixed shall not be increased in any circumstances whatever, with or without the sanction of the Tribunal"

(3) Before the remuneration of the liquidator or liquidators is fixed as aforesaid, the liquidator, or any of the liquidators, as the case may be, shall not take charge of his office.

Duty of liquidator to call general meeting at end of each year

Sec. 496. (1) Subject to the provisions of section 498, in the event of thewinding up continuing for more than one year, the liquidator shall

(a) call a general meeting of the company at the end of the first year from the commencement of the winding up, and at the end of each succeeding year or within three months from the end of the year; and

(b) lay before the meeting an account of his acts and dealings and of theconduct of the winding up during the preceding year together with a statement in the prescribed form on the position of liquidation.

(2) If the liquidator fails to comply with sub-section (1), he shall be punishable, in respect of each failure with fine, which may extend to one thousand rupees.

Provisions applicable to a creditors' voluntary winding up Meeting of creditors

Sec. 500. (1) The company shall cause a meeting of the creditors of the companyto be called for the day, or the day next following the day, on which there is to be held.the general meeting of the company at which the resolution for voluntary winding up is to be proposed, and shall cause the notices of the meeting to be sentby post to the creditors simultaneously with the sending of notices of meeting of the company.

(2) The company shall cause notice of the meeting of the creditors to be advertised once at least in the Official Gazette and once at least in two newspapers circulating in the district where the registered office or principal place of business of the company is situated.

(3) The Board of directors of the company shall (a) cause a full statement of the position of the company's affairs together with a list of creditors of the company and the estimated amount of their claims to be laid before the meeting of the creditors to be held as aforesaid; and (b) appoint one of their members to preside at the said meeting.

(4) It shall be the duty of the director appointed to preside at the meeting of the creditors to attend the meeting and preside thereat.

Appointment of liquidator

Sec. 502. (1) The creditors and the company at their respective meetings mentioned in section 500 may nominate a person to-be liquidator for the purpose of winding up the affairs and distributing the assets of the company.

(2) If the creditors and the company nominate the different persons the person nominated by the creditors shall be liquidator

(3) If no person is nominated by the creditors, the person, nominated by the company shall be liquidator.

(4) If no person is nominated by the company, the person nominated by the creditors shall be liquidator

Fixing of liquidator's remuneration

504. (1) The committee of inspection, or if there is no such committee, thecreditors, may fix the remuneration to be paid to the liquidator or liquidators.

(2) Where the remuneration is not so "fixed, it shall be determined by the Tribunal.

(3) Any remuneration fixed under the section shall not be increased in any circumstance whether with or without the sanction of the Tribunal.

Board's power to cease on appointment of liquidator

Sec. 505. On the appointment of a liquidator, all the powers of the Board of directors shall cease, except in so far as the committee of inspection, or if there isno such committee, the creditors in general meeting, may sanction the continuance thereof.

Duty of liquidator to call meetings of company and of creditors at the end of each year

Sec. 508. (1) In the event of the winding up continuing for more than one year, the liquidator shall -

(a) call a general meeting of the company and a meeting of the creditors at the end of the first year from the commencement of the winding up and at the end of each succeeding year or within three months from the end of theyear; and

(b) lay before the meeting an account of his acts and dealings and of theconduct of the winding up during the preceding year with a statement in the prescribed form about the position of winding up.

(2) If the liquidator fails to comply with sub-section (1), he shall be punishable, in respect of each failure with fine, which may extend to one thousand rupees.

6.3 Foreign Exchange Management Act, 1999

Sec. 1. Short title, extent, application and commencement- (1) This Act may be called the Foreign Exchange Management Act, 1999.

(2) It extends to the whole of India.

(3) It shall also apply to all branches, offices and agencies outside India owned or controlled by a person resident in India and also to any contravention there under committed outside India by any person to whom this Act applies.

(4) It shall came into force on 1-6-2000.

Sec. 2. Definitions- In this Act, unless the context otherwise requires -

(c) "authorized person" means an authorized dealer, money changer, off-shore banking unit or any other person for the time being authorized under sub-section (1) of section 10 to deal in foreign exchange or foreign securities;

(e) "capital account transaction" means a transaction which alters the assets or liabilities, including contingent liabilities, outside India of persons residentin India or assets or liabilities in India of persons resident outside India and includes transactions referred to in sub-section (3) of section 6;

(j) "current account transactions" means a transaction other than a capital account transaction and without prejudice to the generality of the foregoing such transactions include-

(i) payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business,

(ii) payments due as interest on loans and as net income from investments,

(iii) remittances for living expenses of parents, spouses and children residing abroad, and

(iv) expenses in connection with foreign travel, education, medical care of parents, spouse and children;

(n) "foreign exchange" means foreign currency and includes

(i) deposits, credits and balances payable in any foreign currency,

(ii) drafts, travelers' cheques, letters of credit or bills of exchange, expressed or drawn in Indian currency but payable in any foreign currency;

(iii) drafts, travelers' cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency;

(iv) "person resident in India" means-

(i) a person resident in India for more than one hundred and eighty-two days during the course of the preceding financial year but does not include-

(A) a person who has gone out of India or who stays outside India, in either case

(a) for or on taking up employment outside India, or

(b) for carrying on outside India a business or vocation outside India, or

(c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;

(B) a person who has come to or stays in India, in either case, otherwise than

(a) for or on taking up employment in India, or

(b) for carrying on a business or vocation in India, or

(c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period:

(ii) any person or body corporate registered or incorporated in India,

(iii) an office, branch or agency in India owned or controlled by a person resident outside India,

(iv) an office, branch or agency outside India owned or controlled by a person resident in India;

Sec. 3. Dealing in foreign exchange, etc.-Save as otherwise provided in this Act, rules or regulatios made there under, or with the general or special permissionof the Reserve Bank, no person shall-

(a) deal in or transfer any foreign exchange or foreign security to any person not being an authorized person;

(b) make any payment to or for the credit of any person resident outside India in any manner;

(c) receive otherwise than through an authorized person, any payment by order or on behalf of any person resident outside India in any manner;

(d) enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire any asset outside India by any person.

Sec. 4. Holding of foreign exchange, etc.-Save as otherwise provided in this Act, no person resident in India shall acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India.

See. 5. Current accouut transaction-Any person may sell or draw foreign exchange to or from an authorized person if such sale or drawal is a current account transaction:

Provided that the Central Government may, in public interest and in consultationwith the Reserve Bank, impose such reasonable restrictions for current accounttransaction as may be prescribed.

Sec.6. Capital account transaction-(l) Subject to the provisions of sub-section (2), any person may sell or draw foreign exchange to or from an authorized personfor a capital account transaction.

(2) The Reserve Bank may, in consultation with the Central Government, specify-

(a) any class or classes of capital account transactions which are permissible;

(b) the limit up to which foreign exchange shall be admissible for such transaction:

Provided that the Reserve Bank shall not impose any restriction on the drawalof foreign exchange for payment due on account of amortisation of loans or for depreciation of direct investment in the ordinary course of business

(3) Without prejudice to the generality of the provisions of sub-section (2), the Reserve Bank may, by regulation, prohibit, restrict or regulate the following:

(a) transfer or issue of any foreign security by a person resident in India;

(b) transfer or issue of any security by a person resident outside India;

(c) transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India;

(d) any borrowing or lending in foreign exchange in whatever form or by whatever name called;

(e) any borrowing or lending in rupees in whatever form or by whatever name called between a person resident in India and a person resident outside India;

(f) deposits between persons resident in India and persons resident outsideIndia;

(g) export, import or holding of currency or currency notes,

(h) transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident in India;

(i) acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident in India;

(j) giving of a guarantee or surety in respect of any debt, obligation or other liability incurred -

(i) by a person resident in India and owed to a person resident outside India; or

(ii) by a person resident outside India.

(4) A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India.

(5) A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India.

(6) Without prejudice to the provisions of this section, the Reserve Bank may, by regulation, prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business.

Sec. 7. Export of goods and services- (1) Every exporter of goods shall -

(a) furnish to the Reserve Bank or to such other authority a declaration in such form and in such manner as may be specified, containing true and correct material particulars, including the amount representing the full export value or, if the full export value of goods is not aseertainable at the time of export, the value which the exporter, having regard to the prevailing market conditions, expects to receive on the sale of the goods in a market outside India;

(b) furnish to the Reserve Bank such other information as may be required for the purpose of ensuring the realization of the export proceeds of such exporter.

(2) The Reserve Bank may, for the purpose of ensuring that the full export value of the goods or such reduced value of the goods as the Reserve Bank determines, having regard to the prevailing market conditions, is received without delay, direct any exporter to comply with such requirement as it deems fit.

(3) Every exporter of services shall furnish to the Reserve Bank or to such other authorities a declaration in such form and in such manner as may be specified, containing the true and correct material particulars in relation to payment for such services.;

Sec. 8. Realisation and repatriation of foreign exchange- Save as otherwise provided in this Act, where any amount of foreign exchange is due or has accrued

to any person resident in India, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank.

Sec. 9. Exemption from realization and repatriation in certain cases- The provisions of sections 4 and 8 shall not apply to the following, namely :

(a) possession of foreign currency or foreign coins by any person up to such limit as the Reserve Bank may specify;

(b) foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify;

(c) foreign exchange acquired or received before the 8th day of July, 1947 or any income arising or accruing thereon which is held outside India by any person in pursuance of a general or special permission granted by the Reserve Bank;

(d) foreign exchange held by a person resident in India up to such limit as the Reserve Banlcmay specify, if such foreign exchange was acquired by way of gift or inheritance from a person referred to in clause (c), including any income arising there form; .

(e) foreign exchange acquired from employment, business, trade, vocation, services, honorarium, gifts, inheritance or any other legitimate means up to such limit as the Reserve Bank may specify; and

(f) such other receipts in foreign exchange as the Reserve Bank may specify.

Sec. 10. Authorised person- (1) The Reserve Bank may, on an application made to it in this behalf, authorise any person to be known as authorized person to deal in foreign exchange or in securities, as an authorised dealer, money changer or off-shore banking unit or in any manner as it deems fit.

(2) An authorization under this section (1) shall be in writing and shall be subject to the conditions laid down therein.

(3) An authorization granted under sub-section (1) may be revoked by the Reserve Bank at any time if the Reserve Bank is satisfied that

(a) it is in public interest so to do; or

(b) the authorized person has failed to comply with the condition subject to which the uthorization was granted or has contravened any of the provisionsof the Act or any rule, regulation, notification, direction or order made there under:

Provided that no such authorization shall be revoked on any ground referred toin clause (b) unless the authorized person has been given a reasonable opportunityof making a representation in the matter.

(4) An authorized person shall, in all his dealings in foreign exchange or foreign security, comply with such general or special directions or orders as the Reserve Bank may, from time to time think fit to give.

(5) An authorized person shall, before undertaking any transaction in foreign exchange on behalf of any person, require that person to make such declaration and to give such information as will reasonably satisfy him that the transaction will not involve, and is not designed for the purpose of any contravention or evasion of the provisions of this Act or of any rule, regulation, notification* direction or order made thereunder. Where the said person refuses to comply with any such requirement or makes only unsatisfactory compliance, the authorized person shall refuse in writing to undertake any transaction.

Sec. 11. Reserve Bank's power to issue directions to authorized person- (1) The Reserve Bank may, for the purpose of securing compliance with the provisionsof this Act and of any rules, regulations, notifications or directions made thereunder, give to the authorized persons any direction in regard to making of payment or the doing or desist from doing any act relating to foreign exchange or foreign security.

(2) The Reserve Bank may, for the purpose of ensuring the compliance with the provisions of this Act or of any rule, regulation, notification, direction or order made there under, direct any authorized person to furnish such information, in such manner, as it deems fit.

(3) Where any authorized person contravenes any direction given by the Reserve Bank, the Reserve Bank may, after giving reasonable opportunity of being heard, impose on the authorized person a penalty, which may extend to ten thousand rupees.

Sec.12. Power of Reserve Bank to inspect authorized person-(l) The Reserve Bank may, at any time, cause an inspection to be made, by any officer of the Reserve

Bank of the business of any authorized person as may appear to be necessary orexpedient for the purpose of

(a) verifying the correctness of any statement, information or particulars furnished to the Reserve Bank;

(b) obtaining any information or particulars which such authorized person has failed to furnish on being called upon to do so;

(c) securing compliance with the provisions of this Act or of any rules, regulations, directions or order made thereunder.

(2) It shall be the duty of every authorized person, and where such person is a company or a firm, every director, partner or other officer of such company or firm, as the case may be, to produce to any officer making inspection under sub-section(1), such books of accounts and other documents in his custody as the said officer may direct.

Sec. 46. Power to make rules- (l) The Central Government may, by notification,make rules to carry out the provisions of this Act.

(2) Without prejudice to the generality of the foregoing power, such rules may provide for -

(a) the imposition of reasonable restrictions on current account transactions under section 5;

(b) the manner in which the contravention may be compounded under sub-section (1) of section 15;

(c) the manner of holding an inquiry by the Adjudicating Authorities under subsection (1) of section 16;

(d) the forrri of appeal and fee for filing such appeal under section 17 and 19;

(e) the salary and allowances payable to and other terms and conditions of services of the Chairperson and other Members of the Appellate Tribunal and Special Directors (Appeals) under section 23;

(f) the salaries and allowances and other conditions of services of the officers and employees of the Appellate Tribunal and the office of the Special Director;

(g) the additional matters in respect of which the Appellate Tribunal and the Special Director may exercise power;

(h) the authority or person and the manner in which any document may be authenticated under clause (ii) section 29; and

(i) any other matter which is required to be, or may be, prescribed.

Sec.47. **Power to make regulations-** (1) The Reserve Bank may, by notifica- tion, make regulations to carry out the provisions of this Act and the rules made thereunder.

(2) Without prejudice to the generality of the foregoing power, such regulation may provide for-

(a) the permissible classes of capital account transactions, the limits of admissibility of foreign exchange for such transactions and the prohibition, restriction or regulation of certain capital account transactions under section 6;

(b) the manner and the from in which the declaration is to be furnished under clause (a) of sub-section (1) of section 7;

(c) the period within which and the manner of repatriation of foreign exchange under section 8;

(d) the limit up to which any person may possess foreign currency or coins under clause (a) of section 9;

(e) the class of persons and the limit up to which foreign currency account may be held or operated under clause (b) of section 9;

(f) the limit up to which foreign exchange acquired may be exempted under clause (d) of section 9;

(g) the limit up to which foreign exchange acquired may be retained under clause (e) of section 9;

(h) any other matter which is required to be, or may be, specified.

Sec. 48. Rules and regulations to be laid before Parliament- Every rule and regulation made under this Act shall be laid, as soon as may be after it is made,before each House of Parliament for final approval with or without modification.

However, any such modification or annulment shall be without prejudice to thevalidity of anything previously done under that rule or regulation.

6.4 The Patents Act, 1970

The earliest record of a patent granted for a true industrial invention is found in 1421 in Florence to the engineer architect Brunelleschi. Venice isued the first patent law in 1474. Then other States followed suit one after another. It remains to be seen how these patent acts match with the Trade Related Intellectual Property Rights inthe WTO regime. In this connection itmay be mentioned that since the coming into operation of WTO Indian Patent Act 1970 has been amended in 1999, 2002 and 2005for incorporating the mandated provisions of the TRIPS.

Sec.1. Short title, extent and commencement- (1) This Act may be called the Patents Act, 1970.

(2) It extends to the whole of India.

(3) It came into force with effect from April 20th 1972.

Sec. 2. Definition and interpretation- (1) In this Act, unless the context otherwise requires

(b) "Controller" means the Controller-General of Patents, Design and Trade Marks referred to in section 73;

(f) "exclusive license" means a license from a patentee which confers on the licensee, or on the licensee and persons authorized by him, to the exclusion of all other persons (including the patentee), any right in respect of the patented invention, and "exclusive licensee" shall be construed accordingly.

(j) "invention" means any new and useful -

(i) art, process, method or manner of manufacture

(ii) machine, apparatus or other article;

(iii) substance produced by manufacture, and includes any new and useful improvement of any of them, and an alleged invention;

j(a) "inventive step" means a feature of an invention that involves technicaladvance as compared to the existing knowledge or having economic signifi-

cance or both and the makes the invention not obvious to a person skilledin the art;

(1) "new invention" means any invention or technology which has not been anticipated by publication in any document or used in the country or elsewhere in the world before the date of filing of patent application with complete specification, i.e. the subject matter has not fallen in public domain or that it doed not form part of the state of the art;

Substitute (m) "patent" means a patent for any invention under this Act;

(ta) "pharmaceutical substance" means any new entity involving one or moreinventive steps;

(n) "patent agent" means a person for the time being registered under this actas a patent agent;

(p) "patentee" means the person for the time being entered on the register as thegrantee or proprietor of the patent;

Sec. 3. What are inventions- The following are not inventions within the meaning of this Act-

(a) an invention which is not frivolous or which claims any thing obviously contrary to well established natural laws;

(b) an invention the primary or intended use of which be contrary to law or morality or injurious to public health;"

(c) the mere discovery of a .scientific principle or the formulation of an abstract theory;

(d) the mere discovery of a new form of a known substance which does result in the enhancement of the known efficacy of that substance or the mere discovery of a new property or new use for a known substance or of the mere use of a known process, machine or apparatus unless such known process results in a new product or employs at least one new reactant.

(e) a substance obtained by mere admixture resulting only in the aggregation of the properties of the components thereof or a process for producing such substance;

(f) the mere arrangement or re-arrangement or duplication of known devices each functioning independently of one another in a known way;

(g) a method or process of testing applicable during the process of manufacture for rendering the machine, apparatus or other equipment more efficient or for the improvement or restoration of the existing machine, apparatus or other equipment or for the improvement or control of manufacture;

(h) a method of agriculture or horticulture;

(i) a process for the medical, surgical, curative, prophylactic or other treatment of human beings or any process for a similar treatment of animals or plants to render them free of disease or to increase their economic value or that of their products.

Sec. 4. Inventions relating to atomic energy not patentable- No patent shallbe granted in respect of an invention relating to atomic energy falling within sub- section (1) of section 20 of the Atomic Energy Act, 1962 (63 of 1962)

Sec. 6. Persons entitled to apply for patents- (1) Subject to the provisions contained in section 134, an application for a patent for an invention may be madeby any of the following persons, that is to say,-

(a) by any person claiming to be the true and first inventor of the invention;

(b) by any person being the assignee of the person claiming to be the true and first inventor in respect of the right to make such an application;

(c) by the legal representative of any deceased person who immediately before his death was entitled to make such an application;

(2) An application under sub-section (1) may be made by any of the persons referred to therein either alone or jointly with any other person.

Sec. 9. Provisional and complete specification.- (1) Where an application fora patent (not being a convention application or an application filed under the Patent Corporation Treaty designating India) is accompanied by a provisional application,a complete specification shall be filed within twelve months from the date of filingof the application, and if the complete specification is not so filed, the application shall deemed to be abandoned.

Provided that the period of time under sub-section (1) shall be reckoned fromthe date of filing of the earliest provisional specification.

Sec.10, Contents of specification- (1) Every specification, whether provisional or complete, shall describe the invention and shall begin with a title sufficiently indicating the subject-matter to which the invention relates.

(2) Subject to any rules that may be made in this behalf under this Act, drawings may, and shall, if the controller so requires, be supplied for the purpose of any specification and such drawing may be deemed to form part of the specification.

(3) If in any particular case, the Controller considers that an application should be further supplemented by a model or sample of anything illustrating the invention or alleged to constitute an invention, such model or sample as he may require shallbe furnished before the application is found in order for grant of a patent.

(4) Every complete specification shall-

(a) fully and particularly describe the invention and its operation or use and the method by which it is to be performed;

(b) disclose the best method of performing the invention which is known to the applicant and for which he is entitled to claim protection; and

(c) end with a claim or claims defining the scope of the invention for which protection is claimed.

(5) The claim or claims of acomplete specification should relate to a single invention clearly.

(6) A declaration as to the inventorship of the invention should accompany the specification.

Sec.12. Examination of. application- (1) When the complete specification has been filed in respect of an application for a patent, the application and the specification relating thereto shall be referred by the Controller to an expert examinerfor making a report to him in respect of the following matters, namely,

(a) whether the application and the specification relating thereto are in accordance with the requirements of this Act and of any rules made there under;

(b) whether there is any lawful ground of objection to the grant of the patient under this Act in pursuance of the application;

(c) the result of investigations made under section 13; and

(d) any other matter which may be prescribed.

(2) The examiner to whom the application and the specification relating thereto are referred under sub section (1) shall ordinarily make the report to the Controller within such period as may be prescribed.

Sec.14. Consideration of report of examiner by Controller- Where in respect of an application for a patent, the report of the examiner received by the Controlleris adverse to the applicant or requires any amendment of the application, the specification or other documents to ensure compliance with the provision of this Act or of the rules made thereunder, the Controller, before proceeding to dispose of the application in accordance with the provisions hereinafter appearing, shall communi- cate as expeditiously as possible the gist of the objections to the applicant and shall, if so required the applicant within the prescribed period, give him an opportunity of being heard.

Sec. 15. Power of Controller to refuse or require amended application in certain cases- (1) Where the Controller is satisfied that the application or any specification or any other document filed in pursuance thereof does not comply with the requirements of this Act or of any rules made there under, the Controller may refuse the application or may require the application, specification or the otherdocuments, as the case may be, to be amended to his satisfaction before he proceeds with the application and refuse the application on failure to do so.

Sec.19. Power of Controller in case of potential patent infringement- (1) If, in consequence of the investigation required under the Act, it appears to the Controller that an invention in respect of which an application for a patent has been made cannot be performed without substantial risk of infringement of a claim of any other patent, he may direct that a reference to that other patent shall be inserted inthe applicant's complete specification by way of notice to the public, within suchtime as may be prescribed-

(a) the applicant shows to the satisfaction of the Controller that there are reasonable grounds for contesting the validity of the said claim of the other patent; or

(b) the complete specification is amended to the satisfaction of the Controller.

(2) Where, after a reference to another patent has been inserted in a complete specification in pursuance of a direction under sub-section (1)

(a) that other patent is revoked or otherwise cease to be in force; or

(b) the specification of that other patent is amended by the deletion of the relevant claim; or

(c) it is found, in proceedings before the court of the Controller, that the relevant claim of that other patient is invalid or is not infringed_by any working of the applicant's invention, the Controller may, on the application of the applicant, delete the reference to that other patient.

Sec.21. An application for a patent shall be deemed to have been abandoned unless, within such period as may be prescribed, the applicant has complied with all the requirements imposed on him by or under this Act, whether in connection withthe complete specification or otherwise in relation to the application from the dateon which the first statement of objections to the application or complete specificationor other documents related thereto is forwarded to the applicant by the Controller.

Sec.25 (1) Where an application for a patent has been published but a patent has not been granted, any person may, in writing, represent by way of opposition to the Controller against the grant of patent on the ground -

(a) that the applicant for the patent or the person under or through whome he claims, wrongfully obtained the invention or any part thereof from him or from a person under or through whom he claims;

(b) that the invention so far as claimed in any claim of the complete spedification has been published before the priority date of the claim;

(c) that the invention so far as claimed in any claim of the complete specification is claimed in any claim of a complete specification published in or after the priority date of the applicant's claim and filed in pursuance of an application for a patent in India, being a claim of. which the priority date is earlier than that of the applicant's claim;

(d) that the invention so far as claimed in any claim of the complete specification was publicly known or publicly used in India before the priority date of the claim;

(e) that the invention so far as claimed in any claim of the complete specification is obvious and clearly does not involve any inventive step.

(f) that the subject of any claim of the complete specification is not an invention within the meaning of this Act, or is not patentable under this Act;

(g) that the complete specification does not sufficiently and clearly describe the invention or the method by which it is to be performed;

(h) that the applicant has failed to disclose to the Controller the information required under this Act for the purpose or submitted false information;

(i) that in the case of convention application, the applicant was not made within twelve months from the date of first application for protection for the invention made in a convention country;

(j) that the application does not disclose or wrongly mentions the source or geographical origin of biological material used for the invention;

(k) that the invention so far as claimed in any claim of complete specification is anticipated having regard to the knowledge, oral or otherwise, available within any local or indigenous community in India or elsewhere,

(2) At any time after the grant of patent but before the expiry of a period of one year from the date of publication of grant of a patent, any person interested may give notice of opposition to the Controller in the prescribed manner in any of the following grounds :

(a) that the applicant has wrongfully obtained the invention or any part thereof from him or from a prson under or through whom he claims;

(b) that the invention so far as claimed in any claim of the complete specification has been published before the priority date of the calim

(c) that the invention so far as cliamed in any claim of the complete specification was publicly known or publicly used in India before the priority date of the claim;

(d) that the invention so far as claimed in the complete specification is obvious and does not involve any inventive step;

(e) that the complete specification does not sufficiently and clearly describe the invention;

(f) that the subject of the claim of the complete specification is not an invention within the meaning of this Act;

(3) Where any such notice of opposition is duly given under sub-section (2), the Controller shall notify the Patentee. On receipt of the notice of opposition the Controller shall, by order in writing, constitute a Board to be known as Opposition Board consisting of such officers as he may determine and refer such notice of opposition along with the documents to that Board for examination and submission of its recommendations to the Controller.

On reciept of recommendations of the Opposition Board and after giving the patentee and the opposition an opportunity of being heard, the Controller shal 1 ordereither to maintain or to amend or to revoke the patent.

In case the Controller issues an order that the patent shall be maintained subject to amendment of the specification or any other document, the patent shall stand amended accordingly.

Sec. 43. Grant and sealing of patent- (1) Where an application for a patent has been found to be in order for grant of the patent and either-

(a) the application has not been refused by the Controller by virtue of any power vested in him this Act; or

(b) the application has not been found to be in contravention of any of the provisions of this Act.

the patent shall be granted as expeditiously as possible to the applicant or,in the case of a joint application, to the applicants jointly, with the seal ofthe patent office and the date on which the patent is granted shall be entered in the register.

(2) On grant of the patent, the Controller shall publish the fact that the patenthas been granted and thereupon the application, specification and other documents related thereto shall be open for public inspection.

Sec. 53. Term of patent- (1) Subject to the provisions of this Act,

(1) the term of every patent granted after the commencement of the Patent (Amendment) Act 2002 and the patents that has not expired or has not ceased to have effect, shall be twenty years from the date of filing of the application for the patent.

Explanation-For the purpose of this sub-section, the term of patent in case of International application filed under the Patent Cooperation Treaty designating Inida,

shall be twenty years from the international filing date accorded under the Patent Cooperation Treaty.

(2) A patent shall cease to have effect notwithstanding any thing therein or in this Act on the expiration of the period prescribed for the payment of renewal fee,if that fee is not paid within such extended period as may be prescribed.

6.5 Trade and Merchandise Marks Act, 1958

Sec. l Short title, extent and commencement.- The Act may be called theTrade and Merchandise Marks Act, 1958.

(2) It extends to whole of India.

(3) It came into effect from 25th November, 1959.

Sec. 2 Definitions and interpretations.- (1) In this Act, unless the context otherwise requires-

(b) "associated trade marks" means trade marks deemed to be, or required to be,registered, as associated trade marks under this Act:

(d) "deceptively similar" - A mark shall be deemed to be deceptively similar to another mark if it so nearly resembles that other mark as to be likely to deceive or cause confusion;

(g) "goods" means anything which is the subject of trade or manufacture;

(m) "permitted use", in relation to a registered mark, means the use of trademark

(i) by a registered user of the trade mark in relation to goods-

(a) with which he is connected in the course of trade; and

(b) in respect of which the trade mark remains registered for the time being; and

(ii) which complies with any conditions or restrictions to which the registration of the trade mark is subject;

(r) "registered trade mark" means a trade mark which is actually on the register;

Sec. 4. Registrar of Trade Marks.- (1) The Central Government may, bynotification in the Official Gazette, appoint a person to be known as the Controller General of Patents Designs and Trade Marks, who shall be the Registrar of Trade Marks for the purpose of this Act.

(2) The Central Government may appoint such other officers with such desig- nations as it thinks fit for the purpose of discharging, under the superintendence and direction of the Registrar, such functions of the Registrar under this Act as he may from time to time authorize them to discharge.

Sec. 5. Trade Marks Registry and offices thereof- (1) For the purpose of this Act there shall be established a Registry which shall be known as the Trade Marks Registry.

(2) The head office of the Trade Marks Registry shall be at such place as the Central Government may specify, and for the purpose facilitating the registration of trade marks, there may be established at such places as the Central Government may think fit branch offices of the Trade Marks Registry.

(3) The Central Government may by notification in the Official Gazette, define the territorial limits within which an office of the Trade Marks Registry may exercise its functions.

Sec. 6. The Register of Trade Marks- (1) For the purposes of this Act, a recordcalled the Register of Trade Marks shall be kept at the head office of the TradeMarks Registry, wherein shall be entered all registered trade marks with the names, addresses and descriptions of the proprietors, notifications of assignments and transmissions, the names, addresses and descriptions of registered users, disclaimers, conditions, limitations and such other matters relating to registered trade marks as may be prescribed.

(2) No notice of any trust, express or implied or constructive, shall be entered in the register and no such notice shall be receivable by the Registrar.

(3) Subject to the superintendence and direction of the Central Government, the register shall be kept under the control and management of the Registrar

(4) There shall be kept at each branch office of the Trade Mark Registry a copy of the register and such of the other documents mentioned in Sec. 125 as the Central Government may, by notification in the Official Gazette, direct.

Sec. 7. Part A and Part B of the register- (1) The register referred to in Sec.6 shall be divided into two parts called respectively Part A and Part B.

(2) The Register of Trade Marks existing at the commencement of this Act shall be incorporated with and form part of Part A of the register, and this Part shall comprise all trade marks entered in the Register of Trade Marks existing at the commencement of this act and all trade marks which after such commencement may be entered in Part A of the register.

(3) Part B of the register shall comprise all trade marks which after the commencement of this Act may be entered in Part B of the register.

Sec. 8. Registration to be in respect of a particular good- (1) A trade mark may be registered in respect of any or all of the goods comprised in a prescribed classof goods.

(2) Any question arising as to the class within which any goods fall shall be determined by the Registrar whose decision in the matter shall be final.

Sec. 9. Requisites for registration in Parts A and B of the register- (1) A trade mark shall not be registered in Part A of the register unless it contains or consists of at least one of the following essential particulars, namely:

(a) the name of the company, individual or firm represented in a special or particular manner;

(b) the signature of the applicant for registration or some predecessor in his business;

(c) one or more invented words;

(d) one or more words having no direct reference to the character or quality of the goods and not being, according to its ordinary significance, a geographical name or a surname or a personal name or any common abbreviation thereof or the name of a sect, caste or tribe in India;

(e) any other distinctive mark.

(2) A name, signature or word, other than those under sub-section (1), shall not be registered in Part A of the register except upon evidence of its distinctiveness.

(3) For the purpose of this Act, expression distinctive means adapted to

distinguish the goods from the goods in the case of which no such connectionsubsists.

(4) A trade mark shall not be registered in Part B of the register unless the trademark in relation to the goods in respect of which it is proposed to be registered is distinctive, or is not distinctive but is capable of distinguishing goods with which the proprietor of a trade mark is or may be connected in course of trade.

Sec. 11. Prohibition of registration of certain marks.- A mark

(a) the use of which would be likely to deceive or cause confusion;

(b) the use of which would be contrary to any law for the time being in force; or

(c) which comprises or contains scandalous or obscene matter, or

(d) which comprises or contains any matter likely to hurt the religious susceptibilities of any class or section of the citizens of India; or

(e) which would otherwise be disentitled to protection in a court, shall not be registered as a trade mark.

Sec. 12. Prohibition of registration of identical or deceptively similar trade marks- (1) Save as provided in sub-section (3), no trade mark shall be registered in respect of any goods or description of goods which is identical with or decrepitly similar to a trade mark which is already registered in the name of different proprietor in respect of the same goods or description of goods,

(2) Where separate, applications arte made by different persons to be registered as proprietors respectively of trade marks which are identical or nearly resemble-each other in respect of the same goods or description of goods, the Registrar may differ the acceptance of the application or applications bearing a later date until after-the determination of the proceedings in respect of earlier application.

(3) In the case of honest concurrent use, or of other special circumstances which, in the opinion of the Registrar, may make it proper so to do, he may permit the registration by more than one proprietor of trade marks which are identical or nearly resemble each other, subject to such conditions and limitations as he may impose.

Sec. 18. Application for registration.- (1) Any person claiming to be the proprietor of a trade mark used or proposed to be used by him, who is desirous of

registering it, shall apply in writing to the Registrar in prescribed manner for registration of his trade mark either in Part A or Part B of the register.

(2) An application shall not be made in respect of goods comprised in more than one class of goods.

(3) Every application under sub-section (1) shall be filed in the office of the Trade Mark Registry within whose territorial limit the principal place of business in India of the applicant is situated.

(4) Subject to the provisions of this Act, the Registrar may refuse the application or may accept it absolutely or subject to such amendments, modifications, conditions or limitations, as he may think fit.

Sec. 23. Registration- (1) When an application for registration of a trade mark in Part A or Part B of the register has been accepted and either

(a) the application has not been opposed and that the time for notice of opposition has expired; or

(b) the application has been opposed and the opposition has been decided in favour of the applicant; the Registrar shall, unless the Central Government otherwise directs, register the said trade mark in Part A or Part B of the register, as the case may be, and the date of trade mark shall be deemed to be the date of registration of the trade mark.

(2) On the registration of the trade mark, the Registrar shall issue to the applicant a certificate in the prescribed form of the registration thereof, sealed with the seal of the Trade Mark Registry.

Sec. 25. Duration, renewal and restoration of registration- (1) The registra- tion of a trade mark shall be for a period of seven years, but may be renewed from time to time in accordance with the provisions of this section.

(2) The Registrar shall, on application, made by the registered proprietor in the prescribed manner and in the prescribed form, paying the prescribed fee, renew the registration of trade mark for a period of seven years from the date of expiration of the original registration or of the last renewal of registration.

Sec. 28. Rights conferred by registration- (1). Subject to the other provisions of this Act, the registration of a trade mark in Part A or Part B of the register shall,

if valid, give to the registered proprietor of the trade mark the exclusive right to the use of the trade mark in relation to the goods in respect of which the trade mark is registered and to obtain relief in respect of infringement of the trade mark in the manner provided by this Act.

(2) The exclusive right to the use of a trade mark given under sub-section (1) shall be subject to any conditions and limitations to which the registration is subject.

(3) Where two or more persons are registered proprietors of trade marks, which are identical with or nearly resemble each other, the exclusive right to the use of any of those trade marks shall not be deemed to have been acquired by anyone of those persons as against any other of those persons, but such of those persons has otherwise the same rights.

Sec. 29. Infringement of trade marks- (1) A registered trade mark is infringed by a person who, not being the registered proprietor of the trade mark or a registered user thereof using by way of permitted use, uses in course of a trade, mark whichis identical with, or deceptively similar to, the trade mark, in relation to any goodsin respect of which the trade mark is registered and in such manner as render the use of the mark likely to be taken as being used as a trade mark.

(2) In an action for infringement of a trade mark registered in Part B of the register an injunction or other relief shall not be granted to the plaintiff if thedefendant establishes to the satisfaction of the Court that the use of the trade markof which the plaintiff complains is not likely to deceive of cause confusion or to be taken as indicating a connection in respect of trade between the goods in respect of which the trade mark is registered and some person is having the right, either as registered proprietor or as registered user of the trade mark.

6.6 Consumer Protection Act, 1986

Sec. 1. Short title, extent, commencement and application.

(1) This Act may be called the Consumer Protection Act, 1986.

(2) It extends to whole of India except the State of Jammu and Kashmir.

(3) It came into force with effect from April, 15, 1987.

Sec. 2. Definitions (1) In this Act, unless otherwise requires,

(b) "complainant" means

(i) a consumer; or .

(ii) any voluntary consumer association registered under the Companies Act, 1956 or under any other law for the time being in force; or

(iii) The Central Government or any State Government, who or which makes a complaint;

(iv) one or more consumers, where there are numerous consumers having the same interest;

(v) in case of death of a consumer, his legal heir or representative.

(c) "Complaint" means any allegation in writing made by a complainant that

(i) an unfair trade practice or a restrictive trade practice has been adopted;

(ii) the goods bought by him or agreed to be bought by him suffer from some defects

(iii) the services hired or availed of or agreed to be hired or availed by him suffer from deficiency in any respect;

(iv) a trade or service provider, as the case may be, has charged for the goods or for services mentioned in the complaint, a price in excess of the price

(a) fixed by or under any law for the time being in force

(b) displayed on the goods or any package of containing such goods;

(c) displayed on the price list exhibited by him by or under any law for the time being in force;

(d) agreed between the panics;

(v) goods which will be hazardous to life and safety when used are being offered for sale to the public either in contravention of any standards or out of lack of appropriate knowledge.

(vi) services which are hazardous or likely to be hazardous to life and safety of the public when used, are being offered by the service provider when such person could have known with due diligence to be injurious to life and safety; with a view to obtaining any relief provided by or under this Act.

(d) "consumer" means any person who -

(i) buys any goods for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment and includes any user of such goods other than the person who buys such goods for consideration paid or promised or partly paid or partly promised, or under any system of deferred payment when such use is made with the approval of such persons, but does not include a person who obtains such goods for resale or for any commercial purpose; or

(ii) hires or avails of any services for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment and includes any beneficiary of such services other than the person who hires or avails of the services for consideration paid or promised or partly paid and partly promised, or under any system of deferred payment, when such services are availed of with the approval of first mentioned person but does not include a person who avails of .such services for any commercial purpose.

(e) "consumer dispute" means a dispute where the person against whom a complaint has been made, denies or disputes the allegations contained in the complaint.

(mm) "restrictive trade practice" means a trade practice which tends to bring about manipulation of price or its condition of delivery or to affect flow of supplies in the market relating to goods or services in such a manner as to impose on the consumers unjustified costs or restrictions.

(r) "unfair trade practice" means a trade practice which, for the purpose of promoting the sale, use or supply of any goods or for the provision of any service, adopts any unfair method or unfair or deceptive practice.

Note that this Act to some extent supplements the erstwhile MRTP Act, now replaced by the competition Act.

Consumer Protection Councils

Sec. 4. The Central Consumer Protection Council- The Central Consumer Protection Council shall consist of the following members, namely -

(a) Minister in charge of consumer affairs in the Central Government, who shall be the Chairman, and

(b) such number of other official or non-official pembers representing such interests as may be prescribed.

Sec.6. Objectives of the Central Council - **The** objectives of the Central Council shall be to promote the rights of the consumers such as,-

(a) the right to be protected against the marketing of goods and services which are hazardous to life and property;

(b) the right to be informed about quality, quantity, potency, standard and price of goods and services;

(c) the right to be assured of access to a variety of goods and services at competitive prices;

(d) the right to be heard and to be assured that consumer's interests will receive due consideration at appropriate forums;

(e) the right to seek redressal against unfair or restrictive trade practices and exploitation of consumers.

(f) the right to consumer education.

Sec.7. The State Consumer Protection Councils - The State Government shall, by notification, establish a Council to be known as the Consumer Protection Council for the State.

(2) The State Council shall consist of the following members, namely-

(a) the Minister in-charge of consumer affairs in the State Government who shall be its Chairman;

(b) such number of other official or non-official members representing such interests as may be prescribed by the State Government;

(c) Such number of other official or non-official members, not exceeding ten, as may be nominated by the Central Government.

(3) The State Council shall meet as and when necessary but not less than two meetings shall be held in each year at such time and place as the Chairman may think fit.

Sec. 8. Objectives of the State Council- The objects of every State Council shall be to promote and protect within the State the right of the consumers laid down-in clauses (a) to (f) of section 6.

Sec. 8A. The District Consumer Protection Council- (1) The State Govern- ment shall establish for every district, by notification, a council to be known as the District Consumer Protection Council with effect from such date as it may specifyin such notification.

(2) The District Consumer Protection Council shall consist of the following members, namely

(a) the Collector of the District, who shall be its Chairman; and

(b) such number of other official and non-official members representing such interests as may be prescribed by the State Government.

(3) The District Council shall meet as and when necessary but not less than two meetings shall be held every year, at such time and place as may be prescribed by the State Government.

Sec. 8B. Objectives of the District Council- The objectives of every District Council shall be to promote and protect within the district the rights of the consumerslaid down in clauses (a) to (f) of section 6.

Consumer Disputes Redressal Agencies

Sec. 9. Establishment of Consumer Disputes Redressal Agencies- There shallbe established for the purpose of this Act, the following agencies, namely:

(a) a Consumer Dispute Redressal Forum to be known as the "District Forum" established by the State Government in each District of the State by notification.

(b) a Consumer Dispute Redressal Commission to be known as the "State Commission" established by the State Government in the State by notifica- tion; and

(c) a National Consumer Dispute Redressal Commission established by the Central Government by notification.

Sec. 10. Composition of the District Forum- Each District Forum shall consist of,

(a) person who is, or has been, or is qualified to be, a District Judge, who shall be President;

(b) Two other members one of whom sjiall be a woman, who shall not be below thirty-five years of age, possess a bachelor's degree and a person of ability and integrity.

Provided that a person shall be disqualified for appointment as a member if heis, convicted and sentenced to imprisonment for an offence involving moral turpi- tude, an undiscouraged insolvent, a person of unsound mind, he has been removedor dismissed from government job, or possesses such other disqualification as maybe prescribed by the State Government.

Every member of the District Forum shall hold office for a term of five yearsor up to the age of sixty five years, whichever is earlier. Provided that a member shallbe eligible for re-appointment for another term of five years or up to the age of sixty-five years, whichever is earlier.

Sec. 11. Jurisdiction of the District Forum- (1) District Forum shall entertain complaints where the value of the goods or services and compensation claimed does not exceed rupees twenty lakhs.

(2) A complaint shall be instituted in a District Forum within the local limits of whose jurisdiction- (a) the opposite party or each of the opposite parties, where there are more than one, at the time of institution of the complaint actually or voluntarily resides or carries on business or has a branch office or personally works for gain or
(b) the cause of action, wholly or in part, arises

Sec. 14. Finding of the District Forum- If, after the proceeding conducted under section 13, the District Forum is satisfied that the goods complained against suffer from any of the defects specified in the complaint or that any of the allegationscontained in the complaint about the services are proved, it shall issue an order tothe opposite party directing him to do any or more of the following things, namely:-
(a) to remove the defects pointed out, (b) to replace the goods with new goods,
(c) to return to the complainant the price, (d) to pay such amount as compensation,
(e) to discontinue unfair trade, (f) not to offer hazardous goods for sale and (g) to withdraw hazardous goods and cease manufacture of hazardous goods.

Sec. 16. Composition of the State Commission- Each State Commission shallconsist of,-

(a) person who is, or has been, or is qualified to be, a District Judge, who shall be its President;

(b) Two other members one of whom shall be a woman, who shall not be below thirty-five years of age, possess a bachelor's degree and a person of ability and integrity.

Provided that a person shall be disqualified for appointment as a member if heis, convicted and sentenced to imprisonment for an offence involving moral turpi- tude, an undischarged insolvent, a person of unsound mind, he has been removed or dismissed from government job, or possesses such other disqualification as may be prescribed by the State Government.

Every member of the District Forum shall hold office for a term of five yearsor up to the age of sixty seven years, whichever is earlier. Provided that a member shall be eligible for re-appointment for another term of five years or up to the ageof sixty-seven years, whichever is earlier.

Sec. 17. Jurisdiction of the State Commission- (1) Subject to other provisions of this section, the State Commission shall have jurisdiction to entertain
(a) complaints where the value of the goods or services and compensation, if any, claimed exceeds rupees twenty lakhs but does not exceed rupees one crore and (b) appeals against the order of any District Forum within the State.

(2) A complaint shall be instituted in a State Commission within the limits of whose jurisdiction (a) the opposite party or each of the opposite parties, where there are more than one, at the time of institution of the complaint actually or voluntari ly resides or carries on business or has a branch office or personally works for gain or
(b) the cause of action, wholly or in part, arises

Sec. 20. Composition of the National Commission- (1) The National Commission shall consist of,

(a) a person who is or has been a judge of the Supreme Court, to be appointed by the Central Government, who shall be its President;

(b) not less than four, and not more than such number of members as may be prescribed, and one of whom shall be woman, who shall not be below thirty-five years of age, possess a bachelor's degree and a person of ability and integrity.

Provided that a person shall be disqualified for appointment as a member if heis, convicted and sentenced to imprisonment for an offence involving moral turpi- tude, an undischarged insolvent, a person of unsound mind, he has been removed or dismissed from government job, or possesses such other disqualification as may be prescribed by the State Government.

Every member of the National Commission shall hold office for a term of five years or up to the age of seventy years, whichever is earlier. Provided that a member shall be eligible for re-appointment for another term of five years or up to the ageof seventy years, whichever is earlier.

Sec.21. Jurisdiction of the National Commission- Subject to the other provision of this Act, National Commission shall have jurisdiction-(a) to entertain

(i) complaints where the value of the goods or services and compensation, if any, claimed exceeds rupees one crore; and

(ii) appeals against the orders of any State Commission; and

(b) to call for the records and pass appropriate orders in any consumer dispute which is pending before or has been decided by any State Commission where it appears to the National Commission that such State Commission has exercised a jurisdiction not vested in it by law, or has acted in the exercise of its jurisdiction illegally or with material irregularity.

6.7 Summary

Business is there every where in the world since the ancient time, but as societies developed the activities of business came under serious scrutiny, as the interests of business and the rest of the society sometimes were in conflict. Graduallythe governments, the representatives of both business and the rest of society, were entrusted with the responsibility of formulating rules and regulations about the methods and practices of businesses of different kinds. These rules and regulations formed the legal environment of business. Under globalisation foreign rules and regulations also affect home business. But, the laws relating to business are not the same in all the countries and in the same country at all times. The principal reason behind this phenomenon is that laws reflect the hopes and aspirations of the peopleof the countries concerned as well as the problems and prospects of economic and

commercial activities. Thus, along with changes in the economic conditions of people and problems and prospects of business change in every country.

India, being a developing country, a business house has to operate in a situation where there are many restraints and laws governing business activities reflect those restraints. In fact, in India there exists an elaborate framework of laws and regula- tions for guiding and regulating the activities of business firms from incorporationto the winding up for the common good.

6.8 Exercises

Essay type questions :

1. What do you understand by the legal environment of business? Examine the importance of legal environment for business in a country.
2. What do you understand by the memorandum of association of a company? Mention the contents of the memorandum of association and state how the name clause of the memorandum can be changed.
3. Examine the provisions of holding of annual general meeting of public limited company, as provided in the Indian Companies Act.
4. Mention the principal provisions about capital account transactions, as provided in Sec.6 of the Foreign Exchange Management Act, 1999.
5. State what you understand by "invention" according to Sec. 3 of the Patent Act 1970. Mention who are entitled to apply for patents under Sec.6 of the Act.
6. State the requirements for registration of trade marks in Part A and Part B of the register in accordance with the provisions of the Trade and Merchan- dise Marks Act 1958.
7. Sfate how the Consumer Protection Act, 1986 seeks to protect the interests of consumers. Is there any deficiency in that act?

Short answer type questions :

1. Distinguish between "private company" and "public company" in accor- dance with Sec. 3 of the Indian Companies Act 1956.

2. Define “foreign exchange” in accordance with Sec. 2(n) of the Foreign Exchange Management Act.
3. State who can apply for registration of trade mark under Sec. 18 of Trade & Merchandise Marks 1958.
4. Explain what is meant by the term ‘patent’ under Sec. 53 of the Patent Act 1970.
5. Can a fee-receiving doctor be sued in a consumer court for negligence in treatment?
6. Mention a suit which is unjustifiable in a consumer court.

6.9 References

1. (a) The Companies Act, 1956, Govt. of India, New Delhi.

   (b) The Companies Act, 2013, Govt. of India, New Delhi.
2. The Patents Act, 1970, Govt. of India, New Delhi
3. The Consumer Protection Act, 1986, Govt. of India, New Delhi
4. The Foreign Exchange Management Act, 1999, Govt. of India, New Delhi
5. The Trade and Merchandise Marks Act, 1958, Govt. of India, New Delhi

Note : Latest editions of all these Acts must be studied in detail.

Unit 7 ❑ International Environment

Structure

7.0 Nature

7.1 Globalisation

7.1.1 Globalisation in India

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7.3.1 The Agreement on Trade Related Intellectual Property Rights (TRIPs)

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7.3.3 General Agreement on TVade in Services (GATS)

7.3.4 Agriculture

7.4 Summary

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7.6 References

7.0 Nature

The international or global environment of business in a particular country is thetotality of forces, originating from outside the country and having impact, good or bad, upon domestic business. This issue does not arise for a closed economy. Onlyan open economy, having trade connections with foreign countries through exports

and imports, becomes exposed to these forces emanating from abroad. Obviously, thegreater the degree of globalisation, greater becomes the importance of global environment for home business.

Both economic and non-economic forces form part of this environment. Boom conditions abroad stimulate demand for exports, while depression abroad reduces demand for exports of a country. The Great Depression of the 1930s, starting fromthe USA, was transmitted to many other countries through trade channels. Oil price hikes by the OPEC in the 1970s adversely affected oil-importing countries, includingIndia. A non-economic happening like a coup or the assassination of the head of a State may send heavy shocks to businesses far and near.

The advantages of international trade have lured adventurous people to voyageto distant lands since early times. They carried with them not only their mercandise but also their culture and technology, which enriched the lands they visited. This brand of globalisation has been the mother of modern civilization in many countries, including America, India and Australia. In our times the modes and operations of international agencies like the UNO, IMF, World Bank and World Trade Organisationdo also influence the international environment of business.

7.1 Globalisation

While economists have viewed globalisation as the process of removal of barriers to free trade and creation of one global market-where both national and international firms would compete, sociologists have described it as the intensifica- tion of worldwide social" relations where local events and lives are shaped byhappenings in distant places. It results in both economic and social integration of countries far and near.

At the company level, globalisation means two things : (a) the company commits itself heavily with several manufacturing locations around the world and offers products in several diversified industries, and (b) the ability to compete in domestic markets with foreign competitors. In the popular sense, globalisation is multi-plant operation located in different countries.

A company which has gone global is called a Multinational Corporation. The MNCs view the world as one market, minimizes the importance of national boundaries, operate wherever they can do the job best.

In a sense, the East India Company of the 17th century was a kind of MNC, having its head office in London but carrying on business in India and remitting the profits to the parent country. The company had indigo plantations in Bengal. But MNCs of old times were not just exploiters. They used to help both their parent countries and the countries where they operated. This occurs mainly through the transfer of technology and capital (both physical capital and finance capital).

As far as dismantling of barriers to international economic transactions is concerned, the first step in this direction was trade liberalization since coming into existence of the Britton Woods system consisting of the International MonetaryFund, the World Bank and the General Agreement on Tariffs and Trade. The three institutions stood for free flow of aid, development and trade respectively, which led to an unprecedented expansion of international trade between 1950 and 1970. The growth in trade was particularly facilitated by the international movement of investment since the early nineteen sixties with reconstruction of war-torn economies of Europe gaining momentum. Finally, came financial liberalization in the early nineteen eighties with the prescription of World Bank as the way out for efficient allocation of financial resources and relieving the governments of developed coun- tries of Europe and the developing countries from budgetary deficits. The financial liberalization had two major dimensions: (a) the deregulation of the domestic financial sector in the industrialized countries, and (b) the introduction of convertibil- ity on capital account in the balance of payments. However, convertibility on capital account in the balance of payments was not introduced simultaneously by all the developed countries. The United States, Canada, Germany and Switzerland removed restrictions on movements of capital in 1973, Britain in 1979, Japan in 1980, while France and Italy removed the restrictions in 1990. The globalisation of finance that gathered momentum since the mid-1980s accelerated the pace of deregulation and decontrol of foreign trade.

The technological revolution in transport and communication played a crucial part in the progress of globalisation by adding speed and accuracy in the movement of finance and merchandise. The advent of computers and satellites leading to massive expansion in the field of information technology has revolutionized theentire communications system.

The emerging flexible production system, shaped by the nature of technical progress, the changing output mix and the organizational characteristics, is forcing firms to constantly choose between trade and investment in their drive to expand activities across borders. The declining share of wages in production cost, the increasing importance of proximity between producers and consumers, and the growing externalization of services are exercising a strong influence on the strategies and behaviour of firms. Recent research point to twin effects of globalisation on employees. On the one hand, they face a more uncertain stream of earnings and riskier employment prospects. On the other hand, they enjoy a more rapid career and
/ or have more opportunities to train and upgrade their skills.

Political development of recent times have helped globalisation. The process of globalisation beginning from 1980s was greatly influenced by the breakdown of communist regimes and emergence of a uni-polar world with the most powerful capitalist country of the world, the United States, exerting its political influence in shaping the system of production and distribution. Globalisation requires a dominant economic power with a national currency that is accepted as the equivalent ofinternational money.

Economic theorizing also supported globalisation in the context of failure of economic planning to ensure best allocation of resources and distribution of income. Large number of developing countries that embraced economic planning from the Soviet Russia's early successful experiments were ultimately disillusioned by grow- ing budget deficits and inefficient allocation of resources in productive activities. Under the situation the protagonists of the free market mechanism and globalisation provided the rationale. The essence of their arguments can be summed up as follows:
(i) governments should reduce interference in the operation of market forces, (ii) freemarket mechanism ensures more efficient allocation of resources among the users,
(iii) flow of foreign capital and technology to capital-deficient and technologically backward developing countries is necessary in the interest of economic development of these countries. It was also suggested that all the above virtues can be secured through globalisation, that is, abolition of all restrictions over the movement offinance, technology and goods across the countries.

7.1.1 Globalisation in India

Globalisation involves the integration of economy of the country with the world economy. This, in turn, implies opening up the economy to foreign direct investment by providing facilities to foreign companies to invest in different fields of economic activity in the country. For facilitating the entry of foreign companies in the country all obstacles on the entry of foreign capital and imports must be removed and at the same time government policy on the operation of foreign companies in the country must be transparent.

In India the period since 1980-81 was marked by severe balance of payment difficulties. The second oil price hike in 1979-80 pushed up India's import bills substantially while exports lagged considerably behind. During the seventh planprivate remittances also showed a tendency to decline, thus trade deficit rose to astronomical heights. Gulf War in 1990-91 and consequent reliance on high-cost external commercial borrowings compounded the problem. Foreign exchange re- serves dwindled to $1.1 billion in June 1991-less than sufficient for two weeks of import requirements. In the situation default on debt servicing appeared imminent and the Government of India finding no way out approached the World Bank and IMF for assistance. The assistance was made available by these institutions only on their terms and conditions, that is, adoption of 'stabilisation and structural adjustmentprogramme' by India. The acceptance of the programme was announced through the adoption of the New Economic Policy in July 1991.

Steps towards globalisation in India : The main policy measures adopted by the Government of India towards globalisation can be discussed under the following heads:-

Exchange rate adjustment and rupee convertibility : The principal measure of integrating the economy of a country with the global economy is to make its currencyfully convertible, that is, allow it to determine its own central value without official intervention. Transition from a fixed to a flexible exchange rate regime has to be accompanied by the lifting of exchange control measures in a phased manner. As a first step towards this measure, the IMF insisted on devaluation of the rupee in July 1991 as it felt that the Reserve Bank of India was artificially keeping the value ofthe rupee high. The government, in order to appease the IMF, devalued the rupee by 22 percent in two phases in 1991. Consequent upon the devaluation, the value of five major currencies appreciated in terms of rupee by 22 percent.

In the subsequent years India progressively moved towards convertibility of rupee. In 1993 rupee was made convertible on trade account. India achieved full convertibility of rupee on current account in August 1994. The Reserve Bank also accepted obligation under Article VIII of the IMF, under which it committed to forsake the use of exchange restrictions on current international transactions as an instrument in managing the balance of payments.

Import liberalization : In conformity with the suggestion of the World Bank, the1992-97 export-import policy allowed the free import of all items including capital goods, except a negative list. In addition, import duties on a wide range of commodities were drastically cut down in the subsequent years.

In addition to the phased reduction of import duties, India, as a member ofWorld Trade Organisation (WTO), has also committed itself to phasing out quanti- tative restrictions over a period of five years -beginning from 1995. Moreover, as part of Trade Related Intellectual Property Rights (TRIPs) the Government of India has granted exclusive marketing rights to foreign patent holders from 2000 and full product patent in pharmaceuticals, chemicals and drugs for 20 years from 2005. Asa further step towards globalisation and 'opening up', India notified the Trade Related Investment Measures (TRIMs) maintained by it.

Opening up to foreign capital : In a bid to attract foreign capital the Governmentof India had thrown open the doors to foreign investors by the economic policy of 1991. In December 1996, the government allowed automatic approval of foreign direct investment up to 74 per cent by the Reserve Bank of India in 9 categories of industries. The list was enlarged in several stages in the subsequent years. Govern- ment at first relaxed the provisions of Foreign Exchange Regulation Act (FERA) for enabling the foreign investors to invest in Indian industries on substantial scale and ultimately replaced FERA by a foreign Exchange Management Act 1999 (FEMA) to facilitate adoption of a more flexible policy with respect to foreign investment in India.

Effects of globalisation : The process of globalisation initiated in India in 1991 along with far reaching changes in industrial and other relevant policies of the country considerably improved the position of the external sector of the country. In the first place, ourforeign currency reserve, which had fallen to barely one billion in

June 1991 continued to increase since the adoption of the policy of globalisation and by the end of 2003 the foreign currency reserve rose to over $100 billion. Thebalance of payments (BOP) has been in an overall surplus since 1996-97. Secondly, Exports from the country increased considerably during the last few years. This would be clear from the fact that as against a fall in the dollar value of exports by1,5 per cent in 1991-92, the exports grew by over 17 per cent in the first 10 monthsof 1994-95. However, imports also increased substantially during the same period. Thirdly, contrary to what many feared, the exchange rate of the rupee has remained remarkably steady despite the introduction of full convertibility in the current account. Lastly, international confidence On India has been restored. As a result, foreign direct and portfolio investment has increased rapidly in the last few years.

The effects of globalisation on Indian enterprises have been mixed. In the one side some industries, like information technology and telecommunication are doing very well and in fact in IT India is looked upon as the world power. Whereas as in some traditional industries like iron and steel, pharmaceuticals, textiles, etc., the Indian companies are facing uneven competition with superior technology-basedforeign multinationals. Further, as a result of the introduction of the policy of liberalization the foreign multinationals are gaining steady foothold in India and in many cases they are entering into joint venture and licensing agreement with the Indian companies for the purpose of easier access to Indian market. Under thesituation the competitive strength of Indian enterprises vis-a-vis the foreign multina- tionals should be enhanced through greater research and development and technologytransfer agreements. Equally important is diversification of Indian industries. For example, there is ample scope for more investment in agro based industries, leather industry, chemicals and metal industries.

It is not just large companies that have a global focus. Increasingly, smallbusinesses are also going global. Reservation (of more than 650 consumer products) have condemned the SSI sector to low economies of scale and low productivity. The SSI (Small Scale Unit) sector in our country accounts for 44 percent of our total exports. Hence, the SSI sector is facing the neetfto take on the foreign competitors more purposefully through the adoption of better technology and cost-efficiency measures. Increasing globalisation poses its own challenges to trading countries. The gains from globalisation, supported by trade liberalization, have been spectacular in

the case of Chile of Latin America. Industry grew as trade barriers fell. Opening the economy connected home companies with global customers and supply sources. Exports and imports both grew. Foreign investment has been around 6-7% of GDPof late, compared to India's 1%. Most industrial sectors improved their efficiency by adopting better technology. Production has tended to shift towards sectors where Chile has a comparative advantage. Good economic performance cut Chile's poverty rate from 39% in 1990 to 21% in 2000. Chile is the fastest growing economy in LatinAmerica.

7.2 Multinational Corporations

Identification and the characteristics of Multinational Corporations : By the term multinational enterprise is understood those business enterprises which own and control business activities in different countries. Certain qualifying criteria are often insisted upon in respect of the types of activity or the importance of the foreign component in the total activity. The Economic and Social Council of the United Nations used the term multinational corporation in a very broad sense "to cover all enterprises which control assets-factories, mines, sales offices and the like-in two or more countries."

In the sphere of international trade, the post-war era has been characterized by the emergence of giant multinational corporations, which epitomizes Adam Smith's dream of a world political economy based upon global division of labour and mobility of both factors and products. The multinational operations by private business corporations are comparatively recent in human history. But the idea andthe practice of trading by corporations existed even in the 17th and 18th centuries. The companies of merchant traders of the English and Dutch origin of those days were the real forerunners, though not true prototypes, of today's multinationals. Multinationality in business, as it is understood today, emerged in the second half of the nineteenth century when businessmen of one country began to establish produc- tion facilities in other countries. These businessmen were motivated by the prospect of new markets, lower production and distribution costs and competitive advantages over their rivals. The establishment of production facilities in New York in the year 1865 by a German chemical firm 'Bayer' actually signaled the new era of interna- tionalization of production and ownership.

Historical ly, since the days of the colonial companies, the activities of the multinational or international corporations had developed in extractive industries andpublic utility services. But gradually after the Second World War, they started taking more and more interest in manufacturing and then also in commercial services. The decline in the share of extractive sector in the total investment stock is attributableto the nationalization of petroleum and mining assets in many developing countries since the end of the Second World War when many of those countries became politically independent. The investment in manufacturing and commercial services increased because of expansion of market for such goods in the developing countries.

In terms of direct investment stock the multinational corporations have contin- ued to expand rapidly since the early 1970's.In 1971 the total volume of foreigndirect investment of the MNCs was $158 billion. Whereas, in 1996 it increased to
$349 billion and in 1999 to $ 800 billion. The data provided here give quantitative information about growing investment of MNCs, but the most important fact thai emerges from the detailed country wise analysis of the data is that these investments have the central tendency of concentrating in the developed countries. For example, in 1999 developed countries accounted for 73.36 percent of the FDI of the MNCsand the share of developing countries was 23.99 per cent and the rest went to the erstwhile socialist countries of East Europe.

The MNCs thus tend to concentrate their operations in the countries possessing wider markets, rising per capita income, and abundant supply of skilled labour and political stability. Further, among the developed countries, the largest share, 31.84per cent of the total FDI of the MNCs went to the US closely followed by the European Union.

Since late 1980s the term 'transnational corporation' (TNC) has been used to denote a particular type MNC. It is a network of units, with attention paid to managing integrative linkages between local units, as well as with the center. The subsidiary becomes a distinctive asset rather than simply an arm of the parent company (See Financial Express of 5-2-04).

7.2.1 The agents of change and development

The MNCs have come to be recognized throughout the world as the agents of change and development. Their ability to tap financial, physical and human resources

and translate them into output has proved to be outstanding. In today's globalised business they operate in every part of the globe with least restrictions$_v$ln spite of their

operations being insignificant in developing countries compared to the total volume,
they can contribute to the economic development of host developing countries in a number of ways. In the first place the resource gap, that exist in the developing countries due to the dearth of investible surplus, can very easily be filled up by the MNCs from their own resources. Secondly, they can also help immensely in meeting the foreign exchange requirement of the developing countries by bringing in foreign capital and export earnings. Thirdly, being the owners of superior technology, they can meet the requirements of technology of the developing countries. Fourthly, the MNCs can also fill the management gap of the developing countries by supplying the appropriate managerial skill and training to local talents. Fifthly, the MNCs can help the developing countries in marketing their products through their network and thus enable the developing countries earn foreign exchange. Finally, in the countriesisolated from the general stream of development, the MNCs can generate an atmosphere of growth and development by encouraging local entrepreneurs through subcontracts etc., and developing local markets and establishing links with foreign markets and institutions.

But historical evidences suggest that neither today's MNCs nor yesterday's colonial companies were only the agents of development. Their activities were not always geared to the goals of development of host countries. They can be effective agents of development and at the same time potential sources of political conflict andtension. Hence, what is needed at the present moment is a clear understanding oftheir potentials as well as limitations.

7.2.2 Problems

The problems emanating from direct investment by MNCs vary from one group of countries to another. The expansion and growth of multinational activities in the developed countries do not pose any serious problem, since these countries areeconomically developed and the flow investment is'not one sided. But in the developing countries the situation is completely different, the problems are mainly economic and political and hence more vital and immediate. Although, the develop- ing countries have received only about a quarter of the total estimated stock of direct investment and their share, in terms of percentage has declined from 27 per cent in

1975, the presence of foreign MNCs in these countries is of greater relative significance, since their economies are weaker and the rate of overall economic growth is much lower than the rate of growth of MNCs in these countries. Moreover,governments organized on national levels, which are in many cases smaller in economic power than some of these enterprises, find it difficult to exert effective control over them in the fear of losing whatever aid they might get in the economic development from these enterprises and also falling in the bad book of the im- mensely powerful governments of the home countries of those MNCs.

Some very serious drawbacks are also associated with the functioning of MNCs in the developing countries. In the first place, they operate in utter disregard to the importance of appropriate natural environment of the host countries. Secondly, in order to avoid paying taxes properly to the host governments, such enterprises resort to transfer pricing for siphoning off the profits of their operations to countries where the tax rates are lower. **Thirdly,** the subsidiaries and licensees through whom they operate in the developing countries are not allowed complete freedom in buying raw materials and choosing marketing outlets. Thus, in many cases they are required to buy costly raw materials supplied by the MNGs and doing business through the retail outlets of their choice there by making goods and services costlier for the end users. **Fourthly,** the contributions of MNCs to the development of technological know-howof the developing countries are also very insignificant. The MNCs conduct most of their R&D activities in their home countries and transfer only those technologies thatare obsolete or out-dated. **Fifthly,** the MNCs cow-down and rankle the weaker host governments by threatening to withdraw or by curtailing their activities in the countries that try to suggest terms of business that benefits them. It is in this context the MNCs play the individual developing countries against each other in the nameof "good climate" for foreign investment and ultimately succeed in extracting excessive concessions from countries that need them badly. Lastly, the developing countries' hope of the much needed foreign capital is also shattered by their technique of local sourcing of capital for investment, borrowings and reinvestmentof affiliates' profits in the host country.

The issue of controlling the activities of MNCs in the developing countriesarises in view of the above drawbacks associated with their functioning. The developing countries are quite large in number and they need the services of MNCs,

but most of these countries are very weak and small compared to the economic and political muscle of the MNC, hence they cannot bargain effectively. So, what is needed is an understanding among the developing countries themselves about the terms and conditions they should offer to the MNCs. However, with the establishment of the WTO, a world platform has emerged for discussion among countries on terms and conditions for negotiations on foreign investment and transfer of technology. India, along with other developing countries, have shown their bargaining strength vis-a-vis the developed countries in the last two WTO ministerial conferences, andwe must depend on our bargaining strength for future negotiations also. At the same time we must develop our own technological capability through research and development and introduce appropriate reform in our markets for mobilizing necessary resources for investment in industries from within the country.

7.3 World Trade Organisation

The background

The World War II (1939-45) broke the imperialistic ambitions of certain countries (Germany and others) and the actual empires of certain other countries (Britain etc.). The new world order that emerged from the ruins of the world war-II visualised a system of globalised development through free flow of aid, investmentand trade. Accordingly, on the basis of the resolutions adopted at the United Nations Monetary and Financial Conference at Bretton Woods in 1944 came the IMF and the World Bank. But the Havana Charter, embodying the International Trade Organisation, was not ratified by the member nations. Subsequently, in 1948 the General Agree- ment on Tariffs and Trade was established in Geneva to pursue the objectives of free trade for growth and development of all member nations. The principal purpose of GATT was to ensure competition in commodity trade through removal / reduction of all trade restrictions, particularly the tariff barriers. The GATT, unlike the IMFand the World Bank, did not contain a fixed or rigid agenda but depended exclusively on negotiation and understanding for removal / reduction of tariffs and other barriers (e.g. quotas).

However, the post-war arrangement paved the way for an unprecedented growth of production and trade: "From 1950 to 1970 world industrial production rose more

than two-and-a-half fold and world trade more than four-and-a-half fold.” The developing countries gained only marginally during the period from the reconstruc- tion of the war-torn economies of Europe and the buoyant activities of the developed countries.

Meanwhile, protectionist sentiment and the economic disorder of late 1970s as well as the recession of early’ 1980s brought about far-reaching changes in world economy. The emergence of Japan as an industrial power and steady progress of some other small Asian countries in manufacturing led the industrially developed countries of West to take recourse to retaliatory protective measures. Non-tariffbarriers restraining exports by its competitors had appeared in the USA with successful negotiation of a Short Term Cotton Textile Arrangement in 1961. On the other hand, the imperatives of development necessitated the provision of tariff protection for infant industries and special and differential treatment of countries for gaining access to the markets of developing countries. Thus, by the early 1980s, international trade came to be dominated largely by tariff and non-tariff restrictions.

It also became necessary that the US trade policy be geared to ensure theopening of markets in other countries. Liberalisation of trade around the world was considered the best way to realize the above objectives, as retaliatory barriers would- further compartmentalize the global market and limit the horizon of accessibility. Accordingly, the Uruguay round of the GATT was considered the most appropriate scope for successful negotiation of multilateral cuts in barriers to rebuild global momentum for trade liberalization and opening of markets for the export drive of developed countries.

The Uruguay Round : A new role was thus visualized for the GATT bybringing within its purview intellectual properly rights, foreign investments, trade in services and agriculture. As the GATT is one of the three pillars of the Bretton Woods system and as the foundation of the post-war world order rests upon these three institutions, giving additional teeth to GAIT was considered the most effective way of influencing the macro-economic scenario of the post cold-war world.

Thus, the Uruguay Round of GATT negotiations, held at Punta del Este in Uruguay, the .seventh of its kind since the initiation of GATT in 1948, began on 20th

September 1986. After negotiations for about five years, the Director General of GATT, in his capacity as the Chairman of the Trade Negotiation Committee, placed the Draft Final Act on December 20, 1991 for the consent of all the member countries. The member countries signed the agreement on April 15, 1994, givingbirth to the World Trade Organisation (WTO) which now has 164 members till 29, July, 2016. The process or globahsation was hastened through the GATT and subsequently via the WTO. This was expected to help both the developed and the poor developing nations through lower tariffs and subsidies.

7.3.1 The Agreement on Trade Related Intellectual Property Rights (TRIPs)

The Intellectual Property Rights (IPR) has always been a contentious issue for the developed countries as the IPR, granted in the form of patents, entitle the patentee to the commercial exploitation of rights embodied in the patent to the exclusion of others. Thus, in order to ensure the perpetuation of their hold over the emerging horizon of development, as well as regaining the ground they had already lost orwere on the verge of loosing to the newly industrialized countries, the developed countries led by the USA pleaded for the inclusion of IPR within the agenda ofGATT The agreement on IPR is known as the Trade Related Intellectual Property Rights (TRIPs).

The TRIPs requires the countries to provide a 20-year patent protection for all products or processes in all fields of technology, provided they are new, contain an inventive step and are capable of industrial application. The patent would be available without discrimination as to the place and destination of invention and the field of technology.

A patent would confer on the patentee the exclusive right to make, use, and offerfor sale, sell or import the patented product. The right shall be available equally toall the patentees. However, a patented invention may be used without authorizationin case of public emergency and also in cases where the patentee does not grant a license for use of the patent on reasonable terms and within a reasonable time. But,in all such cases the patentee shall be entitled to adequate remuneration,

The TRIPS came into existence from January 1, 1995. Under the TRIPS Agreement member countries have been given specific time periods for adjustments

prior to implementation of the provisions of the Agreement. No member country wasrequired to apply the provisions of the Agreement before the expiry of a general period of one year following the date of entry into force of the WTO Agreement. Thedeveloping member countries are entitled to delay the application by a further period of four years. The least developed member countries are entitled to delay the application by a period of ten years over and above the period of one year grantedto all the countries. The countries are also required to grant exclusive right for marketing the products for five years with respect to which applications for product patent have been filed, provided that such products, are already patented in any other country.

In the year 2000 the developing countries must apply the criterion for patentabil-ity of the applications that have been filed. From the year 2005 the developing countries must grant product patent for 20 years from the date of application. Thus, products already patented in one country will enjoy patent protection in the devel- oping countries and all new patents will enjoy the same protection. The least developed countries would get an extra grace period of five years in the above cases.

In India the patenting of inventions is provided for by the Patent Act of 1970that replaced the Patents and Designs Act of 1911. Under the Patent Act of 1970, drugs can be patented for a period of 5 years from the date of sealing or 7 years from the date of filing of complete specification, whichever is shorter. For other products the duration of patent is 14 years. The Act categorically states that drugs and foodand those manufactured by chemical processes can be patented only for method or process of manufacture, not for product as such. Moreover, for a particular product only one process could be patented. This left enormous scope for research on processes. The developed countries argued that such compulsory licensing distorts trade by reducing the market and not allowing the patentee to operate the patent by export.

The GATT by making patenting compulsory for 20 years for products andprocesses, by treating import of patented products in a country as working of the patent in that country and by making protection of patent granted in one country automatic in other countries, has virtually provided for free access of the technology of the developed countries. In course of time this will result in cessation of research

and development of technology in the developing countries, on the one hand, and perpetuation and consolidation of monopolistic control of the developed countries over technology, production and trade, on the other hand. Complementary to the above, the GATT Agreement has also robbed the weaker nations of their solemn rights, as sovereigns, to bargain for better terms and conditions for operation of patents through compulsory licensing for non working of patents and fixing ceilingon royalties. Further, by putting the burden of proof on the defendant in case of disputes involving patents, the prospective late comers, largely the developing andthe least developed countries, have been assigned the extreme receiving end in the whole process.

7.3.2 The Trade Related Investment Measures (TRIMs)

Flow of investment from one country to another is one of the principal ways of securing and influencing transfer of technology and capital. Here again, among the recipients are the developing and the least developed countries. Since World War-II, the MNCs off' developed countries have gradually become the principal source of supply of foreign investment and new technology of production. The developing countries throughout the world were trying to have investment and technology from the MNCs with least cost in terms of payment in foreign exchange for import and transfer of technology for development of capacity to produce and export. As the investments in foreign countries provided an expanding horizon of trade and income,the volume of such investment also expanded significantly.

The Agreement on TRIMs required removal of all trade- related investment measures that are inconsistent with the two provisions of GATT; (i) requirement of national treatment under Article 111 and (ii) prohibition of all quantitative trade restrictions. TRIMs are a part of the GATT proper like the TRIPS, since GATT requires internal regulations and border measures governing goods to conform to Article 111 and XI; TRIMs require investment measures to conform to these two Articles.

National treatment under the GATT requires that internal laws and regulations providing protection to domestic production and/or discouraging imports should not be there. Thus, in accordance with the agreement on TRIMs, measures for encour- aging domestic production over imports cannot be there.

After the removal of investment measures, the nationals of developed countries, the MNCs particularly, are not supposed to have any performance obligations tied to their investment proposals. The investors from foreign countries, without having any obligation to use local component, including manpower, export or produce for local market, would be at liberty to invest in any area of their choice. The new regime will pave the way for exploitation of the resources of the countries with weaker bargaining power by the nationals of developed countries for their exclusive benefit.

7.3.3 General Agreement on Trade in Services (GATS)

In course of time, as the volume of international trade in services of developed countries increased with skill-intensive innovations in bio-technology, computer science, information system and communication, the demand for multilateral frame- work of principles and rules for trade in services gathered momentum. Under continuous pressure from the United States, GATT members agreed in September 1986 to include services in the Uruguay Round of the multilateral trade negotiations.

The agreement that emerged from the Uruguay Round of multilateral trade negotiations in services constituted GATS. The GATS created a legal framework for trade in services and allowed the countries specify the specific commitments to be undertaken in the schedule of commitments to secure an overall balance of rights andobligations.

The GATS applies to services provided by a service supplier in the territory of one country and sold in the territory of another, services provided by a service supplier in the territory of one country and sold to consumers of another country (e.g. tourism), services provided by the commercial presence of a supplier of one country in the territory of another (e.g. banking) and services supplied by the presence of natural persons of one country in the territory of another. However, GATS does not cover the services provided by the Governments of member countries, which are neither supplied on commercial basis nor in competition with other suppliers of services.

The GATS sought to ensure multilateral trade in services through three stages;
(a) general obligations, (b) specific commitments and (c) commitments relating to specific reforms. Under general obligations, GATS requires countries to provide most-favoured nation (MFN) treatment on reciprocal basis for integration of market

for services. It also requires the countries to make rules governing the service sector in a transparent fashion. Under specific commitments, (i) a country must provide national treatment to foreign service suppliers and (ii) a country, which has under- taken market access commitments in its schedule should not impose limitations on number of service suppliers, types of services provided, value of services rendered, number services operated, number of persons employed in the service sector, the typeof legal entity of the supplier and the amount of capital employed. Under commit- ments relating to specific reforms, the GATS requires that (a) countries must eliminate rights in supply of financial service (this includes supply of services even by public entities), (b) governments of member countries must not discriminatebetween domestic and foreign suppliers of financial services when purchasing services for their own use, (c) a country must allow its residents to purchase financialservices like banking, insurance and communication in the territory of another country, (d) each country must allow the suppliers of financial services to establishor expand its commercial presence within its territory, (e) the entry of foreign personnel for supply of financial services should be permitted on no-discriminatory basis, and (0 a country must provide foreign financial service suppliers access to infrastructural facilities given by public utilities on non-discriminatory basis.

The multilateral framework of principles and rules for trade in services, asvisualized by the GATS, did not take into account the widely differing situations of developed, developing and least developed countries. Some of the liberalizationmeasures on services, such as, the exchange of the right of commercial presence and national treatment of foreign enterprises in host countries would effectively open up markets for MNCs in the developing countries, without any reciprocal benefit accruing to the enterprises of those countries. The developed countries can make quick profits from trade in highly capital-intensive services such as banking, insurance, communication and information, without massive movement of persons from home country.

7.3.4 Agriculture

Apart from the TRIPS, the TRIMs and the GATS, the GATT Agreement 1994 also include special provisions "for trade in agriculture and textiles. Trade in agricultural commodities was not subject to the regime of international discipline visualized by the GATT. The post-war liberalization agenda embodied in the GATT

system did not include agriculture, because the United States and the major devel- oped countries of Europe were generally captive to strong protectionist lobbies that had constructed elaborate mechanisms of agricultural income support through subsi- dies. At the same time, the major developing countries were not interested in lobbying for agricultural trade liberalization.

In the GATT proper, first, there was no discipline on domestic support except consultations in the event of serious prejudice, secondly, in the sphere of export subsidies there was virtually no waiver for agriculture specified in Article XVI on subsidies, and thirdly, imports of agriculture were spared of quantitative restrictions set out in Article XI for food stuff and critical raw materials. Under the circum- stances, two sets of policies were pursued for the development of agriculture in developed and developing countries. In the developed countries, in the context of steady improvement in production and conditions of work in industries, the terms of trade for agriculture had to be improved through subsidies and trade measures. Onthe other hand, the newly independent developing countries had to exploit agriculture for the development of modern industries.

The GATT Agreement, 1994, by bringing agriculture within its discipline, transgressed into the sovereign economic space kept reserved so long for manipula- tion in the interest of and in conformity with domestic requirements. About the market access measures it is being said that, even in spite of the minimum access quota, there is no possibility of any import of agricultural products in the near future. This is because, imports of various agricultural commodities in India and otherdeveloping countries are subject mainly to quantitative restrictions for balance of payments reason. Again, when there will be the need for balance of payments cover, there will be no import, as prices of agricultural products in domestic markets are below the international price. This argument will not hold good for long, since prices of products in the domestic market will also rise when the free market mechanism begins to operate.

Conclusion

The WTO, came into being in January, 1995, replacing the GATT, as a truly multilateral trade organization for benefiting its member countries, some rich and some poor. But in fact the opening up of economies has resulted in the creation of

new markets for the big firms in the USA, EU and Japan. The rich countries have gained much, the poor countries very little. The bone of contention has been agriculture - the most protected sector in some rich countries. Having got all the tradeconcessions in the earlier rounds of negotiations, the developed world was in no mood to compromise on agriculture. Cut in subsidies given to farmers of developing countries would make their products costlier and deprive them of the benefit they could get from access to the rich markets of USA and EU. The breakdown of WTO ministerial meet at Cancun (2003) has exposed the great divide between developed and less developed countries on trade related issues. The inability to compromise andreach a consensus among nations can jeopardize the free multilateral trade system. Some countries like the USA are pursuing aggressive bilateral trade talks at the expense of the WTO trade agenda is a worrying sign. If the US withdraws export subsidies for fanners, American farmers would not die. But it would enable farmersin India and Africa to survive in the international environment. Of course, a group of 21 developing countries, including India and China, has formed an alliance for safeguarding their interests.

7.4 Summary

A closed economy does neither export nor import, so that it has to produce allit needs within its border. But it was soon found, even in very ancient times, that autarky (closed economic system) does not pay. So nations commenced trade among themselves much to the benefit of all. It meant that nations having trade with other nations went global.

But this exposure to the global environment could not exert much influence ovtr domestic businesses as a whole because of distance, slow transport and bad communication system.

But with revolutionary changes in transport, communication and information system, this exposure to forces abroad through trade is giving both advantages and disadvantages to nations with open economies. Trade barriers help to mitigate these disadvantages only for short periods. So the need was felt for the creation of international agencies to promote multilateral trade, free from barriers and restrictions,in a way as would help both rich and poor countries. After World War II the Brittaoin

Wood System, consisting of the IMF, the World Bank and the GAIT, started to work for trade liberalization, supported by financial aid for war-torn and poor countries. The MNCs, as we know them, sprang up one after another benefiting both the parent and the market countries. The GATT was replaced by the WTO in the 1990s.Reconciling the conflicting interests of the rich and the poor member countries has not been an easy task. Successful reconciliation is yet to be achieved. The trend of regionalism (regional trade agreements) may undermine the existence of the WTO in the long run if the great divide between the developed and the developing countries persists.

7.5 Exercises

Long answer type questions :

1. What do you understand by the international environment of business? Explain why the companies globalise their operations.
2. State how globalisation was introduced in India and its effect on-Indian economy.
3. Trace the origin and growth of multinational corporations.
4. Mention how the developing countries can gain from the operations of MNCs in their countries.
5. State the background in which the WTO was brought into existence. Has it been a success?
6. Examine the provisions of the TRIPS and mention how far they are beneficial to the interest of the developing countries.

Short answer type questions :

1. Mention and explain the factors that made globalisation possible.
2. Explain the effects of globaloisation..
3. Explain the problems that are associated with the operation of the MNCs in developing countries.

4. State the principal provisions of the TRIMs.
5. Mention the provisions of the GATS.
6. Why was the World Trade Organisation brought into existence?

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Unit 8 ❑ Natural Environment

Structure

8.0 Introduction

8.1 Definition

8.2 Sustainable development and Global reality

8.3 Resource – Environment Management for Sustainable Development

8.4 Summary

8.5 Exercises

8.6 References

8.0 Introduction

The extent of human influence on the environment was explored for the firsttime scientifically by G.P. Marsh in a book 'Man and Nature', published in 1861.The possibility of resource shortage was pinpointed by Malthus and Ricardo in the 19th century. The destructive exploitation of environmental resources was the concern of the German writer Friedrich in 1904, who was supported by the French writer Jean Brunhes in 1920.

But interest in long-term resource-environment problems exploded as a reaction to the publication of the Club of Rome's report, entitled 'Limits to Growth' in 1972, This was followed in the same year by the Stockholm Declaration made at the endof the United Nations Conference on Human Environment, held in Stockholm. The Limits established that excessive production and consumption, both results of high economic growth and rising living standards, give rise to (1) resource depletion [(a) early exhaustion of non-renewable natural resources and (b) exhaustion of renewablenatural resources due to use rates exceeding natural regeneration rates in the form of

overploughing, overlumbering, overfishing and overgrazing] and (2) environment destruction resulting from excessive waste generation (coming from both production and consumption) which the natural environment fails to assimilate and render harmless.

Since the 1970s there has been an increasing concern in many quarters over whether a high output growth rate can be maintained indefinitely in the context ofthe fixed supply of many physical resources and environment quality of this planet. Not only has the environment been deteriorating in many parts of the world, posing threat to man's physical and mental health, but resources are being depleted at an alarming high rate, so that before the close of the 21st century we may run short of many resources that are in high demand. That would be disastrous for our civilization.

However, today even ordinary people are more environment conscious than in earlier iods. In 1983 the then Prime Minister Indira Gandhi had to postpone the implementation of the Silent Valley Hydro-elective power project in the face of strong protests coming from India's environment conscious intellectuals. Since the 1970s the World Bank has adopted the policy of scrutinising projects for their environmental impact and withholding approval where the safeguards are found insufficient. We have seen the emergence of groups and organisations devoted to the preservation of eco-biological systems, besides the United Nations Environment Programme.-In many countries, including India, laws have been enacted for protecting the environment. The literature on resource and environment studies is now quite substantial. Modern planning has been searching for methods for harmonising the two frequently conflicting objectives of output maximization and environment protection. In recent times the term 'sustainable development' has gained currency.

8.1 Definitions

In a broad sense the natural environment is the sum total of natural resourcesand the non-material conditions surrounding those material.resources. In a narrow sense, these non-material conditions are referred to as the natural environment. But because of the largely subjective nature of environment quality, difficulties arise while analysing the magnitude and valuation of environment. Environment quality does not mean the same thing to everyone. To a layman water quality is fitness of

water for drinking and bathing, while a scientist judges it in term of absence of pollution. In recent years discussions on the natural environment, the term 'ecology' has been frequently used. Ecology is the science concerned with the study of living organisms in, and in relation to, their respective surroundings or environs. It-is not possible to appreciate fully the reasons for a living organism's behaviour without an understanding of the nature of the environment in which it originated. This is trueof every species, including human being. Man is a part of the world's eco-system.But man's position is a special one because he (individually as well as through his business organisation) can substantially change the eco-system and the environment of which he is a part, unlike other organism. All living organism in the natural environment form a kind of mutual life-support system where one species support theexistence of many others. So, if one species becomes extinct for some reason orother, the existence of many other becomes endangered. Taken together, livingorganisms and nonliving matter with which they interact constitute an 'eco-system[1].

The human impact on the natural environment received little attention until the 19th century. Overall it has been less central in the history of economic thought than the issue of the impact of the environment on humans their economic and non- economic activities together with their physical traits and culture.

8.2 Sustainable Development and Global Reality

The term 'sustainable development' was defined by the United Nations World commission on Environment and Development (1987), also known as the Brundtland'Commission. It is that development which enables people to raise their living standards without an excessive of depletion of precious natural resources, renewable as well as non-renewable, which may reduce the ability of future generations to meet their own needs, and which also avoids unnecessary destruction of environment quality, endangering the health or existence of many species including man. Not maximum, but sustainable, growth is the objective today. Development plans in most socialistic and mixed economies (including India) had, before the 1980s, failed to incorporate resource-environment considerations in their basic plan frames. The concept of sustainable development attempts a compromise between high output growth and resource-environment conservation.

The great stress on the global environment has its roots in the rising volume of global production by businesses of all kinds for satisfying the rising demand of a rising global population for more goods and better goods (better life-styles). Many new 'superior' technologies and goods are more environment-disruptive than those they have replaced. Undoubtedly, modern mass-producing techniques, increased recourse to sophisticated packaging, production of more complex processed goods, increasing use of energy-intensive methods, and development of synthetic substanceslike plastic have all added to the pressure placed on the natural eco-system. Environment degradation has taken various forms. The major ones are given below.

Forms of Environment degradation

1. **Effects on Mental Health :** Scientists are of opinion that when people in over-crowded areas (over-populated cities and industrial belts), they suffer frommental stress whose symptoms are hypertension, impotence, imsomnia, feeling of loneliness, different forms of crime and aggressive behaviour.

2. **Effects on Physical Health :** Although our longevity has increased through revolutionary inventions in medicine and development-induced rise in living standards, our physical health has been affected by environmentally induced diseases which results from the introduction of toxic materials into the environment causing air pollution, water pollution and land pollution. By contaminating the food we eat, the air we breathe and water we drink with traces of many chemicals poured into environment through different channels of production and consumption, we are contributing to a rising incidence of diseases related to our hearing, our heart and our lungs. To this we should add the introduction of harmful radioactive materials into air and water by nuclear leaks through accidents or experimental explosions.

3. **Wild Life Destruction and Biological Simplification :** The list of endangered/ extinct animal and bird species has been on the increase as human activities have increased in size and variety. This decline in bio-diversity has certainly been disturbing the old ecological balance under which one species directly and indirectly supports 10 to 15 other species in this planets mutual life-support system.

4. **Euthrophication :** Many water-bodies (like lakes) have been facing slow death through excessive bacteria formation promoted by the chemical fertilizers from adjacent farm lands or chemicals in sewage water (containing nitrates and phosphates).

5. **Soil Damage :** A 199J study found that the soils of 17% of the Earth's vegetated land have degraded in quality. This soil damage has various forms like erosion, desertification through over-grazing in range lands chemical agriculture and over-ploughing in old fashion cultivation, salination of ground water in itrigation in some countries of the Middle-East. Top soil is also damaged by acid rain - fall out of acid particles, particularly those of sulpheuric acid, originating from sulphur from burning fossil fuel (oil and coal) in transport and thermal power plants. In many countries soil erosion has been due to deforestation.

6. **Climate Change :** In recent years human activity is altering the composition of the atmosphere so rapidly that perceptible changes in climate can occur. In fact, scientists have warned us about global warming. On average, the period 1950-80 was about 5°C warmer than the period 1870-1900. The day may not be too far when the earth would be too hot for any life to survive. Two phenomena have been primarily responsible for this global warming: the ozone problem and the greenhouse effect. The ozone gas layer in the stratosphere is a significant absorber of solar radiation, and as such, a major factor in world climate control. In the late 1980s scientists pointed out that not only has the ozone layer thinned out but it has also shown 'holes' at places. So, more heat has started reaching the earth than necessary for the existence of the life system. On a report it has been stated that ozone here is getting back to original state level. The greenhouse effect refers to the effect of green house gases, led by carbon dioxide (CO_2) on the atmosphere. These gases absorb infra-red rays of the sun causing the atmosphere to heat up. Heavy concentrations of such greenhouse gases are being built up in the lower atmosphere after they are generated by our transport, industrial, agricultural and forestry activities. In 1987, just 5 countries – The USA, the USSR, Brazil, China and India -contributed 50% of the total emissionson our earth. Sometimes pollution spreads from one country to another. Thus,the transfer of acid particles from Britain and the ; continent was reducing fishin the waters of south Norway in the 1970s and 1980s.

8.3 Resource-Environment Management for Sustainable Development

The Indian Scenario

India's main environmental problems are : air pollution, water pollution(both inland ans marine), soil damage (including desertification in areas like Rajasthan),deforestation, over-fishing and destruction of wild life habitat. Created in 1985, the Central Government Department of Environment, Forests and Wild Life serves as thefocal point in the administrative structure of the Central Government for the planning, promotion and coordination of forestry and environmental programmes. Main activities of this Department are mentioned below.

Surveys : The Botanical Survey of India and the Zooloical Survey of India havecompleted the survey of the plant resources and the faunal resources of India respectively. From the studies of the Forest Survey of India we come to know thatthe forest cover of India is yet less than the desirable minimum of 33%,

Conservation of natural resources : As a part of the conservation policyenvironmental impact assessment has been introduced to ensure that development is associated with the minimum environmental damage. Such assessment, through Environmental Appraisal Committees, is required in the case of large development projects (as in mining, river valley and thermal power). Thus, in 1987-88,255 development projects were appraised, of which only 89 were cleared. A Human Exposure Assessment Location Project was initiated some years ago to monitor the exposure of humans to pollutants. The Forest (Conversation) Act of 1980 aims at preventing indiscriminate tree cutting and diversion of forest lands towards non- forest activities. Afforestation is encouraged. Use of substitutes of timber is also encouraged. A National Wildlife Action Plan, formulated in 1982 under the aegis of the Indian Board for Wild Life, N. Delhi, continues to provide the blueprint of wild life management in the country, as a result of which we have national parks and sanctuaries, zoological parks and biosphere reserves in different parts of India. We also have a National Wetland Committee and a National Mangrove Committee for the conservation and management of wetlands and mangroves respectively. Wetlands are submerged lands, the depth of which does not exceed six meters for the major

portion of the year, according to the World Resources Institute, serving as habitatsfor fish and water fowls. Mangroves are salt-tolerant forest lands near the sea, which are reserviors of a host of plant and animal species, sheltering a host of fish speciesin the adjacent waters (as, for instance, in the Sundarbans of West Bengal).

Pollution Control : The main control instruments are (i) the Water (Prevention and Control of Pollution) Act, 1974, (ii) the Air (Prevention and Control of Pollution) Act, 1981, and the Environment (Protection) Act, 1986. The first two Actsare implemented by the Central Pollution Board with the assistance of the State Pollution Boards, defaults penalized by court action for violation of standards by firms using hazardous chemicals. A National Environment Awareness Campaign hasbeen launched.

Regeneration and Development : So far regeneration of degraded naturalresources is concerned, the most important job so far done is the Ganga Action Plan (1985) for restoring the water quality of the river Ganga. The National Wasteland Development Board (1985) aims at restoration of greenery of wastelands mainly through afforestation.

Research : Research in environmental science and eco-friendly technology is needed for promoting environment protection and improvement. In this connection the Department of Environment, Forests and Wildlife operates a scheme for providingsupport to several institutions and universities in the country.

The important institutions are : the Centre for Environment Education (Ahmedabad), the Ecological Research and Training Centre at the Indian Institute of Science (Bangalore), the Centre of Mining Environment at the Indian School of Mines (Dhanbad), the Forest Research Institutes (Dehra Dun, Coimbatore and Peechi), the Govinda Ballav Institute of Himalayan Development (Almora), theNational Remote Sensing Agency (Hyderabad), the Garhwal University, the Kumaon University (Nainital) and the Indian Institute of Forest Management (Bhopal)

Education and Information : The Central Government gives high priority for promoting non-formal environmental education, dissemination of information and creation of awareness amongst all citizens through training programmes, exhibitions, eco clubs, eco-development camps, etc. The National Environment Awareness

Compaign, started in 1986, has continued to focuss attention on all major environmentalissues of the country. As a part of this campaign, a National Environment Month is observed every year. Attention is being drawn through publicity to the need for economizing the use of conventional energy and fresh water.

India cooperates with the World Bank, the FAO and the UN DevelopmentProgramme on environmental and forestry programmes. India participated in the Stockholm Conference on Human Environment (1972) where it was pledged that no country should use its resources by harming the environment of other countries. This principle has since been incorporated into numerous regional and global conventions.In 1979 the UN general Assembly adopted a set of resolutions for the conservation and harmonious utilization of natural resources (e.g. rivers) shared by two or more countries. There appears to be a growing recognition that issues of shared resources and transboundary pollution require concerted international action.

Conclusion : The concept of sustainable development has thrown up the question: how far can we afford to sacrifice environment quality for the sake of output growth? And what percentage of current resources should be earmarked for use by future generations without imposing undue hardship upon the present generation in the form of a low living standard? The answer would vary from countryto country. The tasks involved would be complex with various dimensions. Much would depend on the development of science and technology, given favourable conditions in respect of the political, legal, and social environment. If science takes technological progress to such a height that all natural resources are capable of infinite regeneration and the environment has an infinite capacity to absorb all wastesproduced by man's production and consumption activities, there would be no resource problem and no environment problem, so that exercises for sustainable development would be safely left to mathematical economists.

8.4 Summary

The natural environment is the sum total of natural material resources and the non-material conditions surrounding those material resources which both influences and is influenced by man's ways and organizations. Man has been damaging his environment almost from the beginning of civilization. But the impact went unnoticed.

Only in the last century did the problem become sizeable enough to attract attention. The great stress on the global environment (its resources and quality) has emerged from the rising volume of global output and associated rise of consumption. Environment degradation has assumed various forms, doing harm to both man and other living species. Over-use of many natural resources has led to the possibility of their early exhaustion much to the detriment of future generations. As one solution to these two inter-linked problems of resource-depletion and environment degradation the concept of 'sustainable development' has been developed. Governments in many countries, including India, have been working to this end individually as well as in cooperation with other countries and international agencies. Science and technology are being used to solve resource-environment problems. The growing awareness of social responsibility in the business world is a healthy development in this context.

8.5 Exercises

Long answer type questions :

1. Define 'Natural Environment', 'Ecology' and 'Eco-system*
2. Trace the evolution of thought on the impact of human activities on the natural environment.
3. Explain the concept of sustainable development. Examine the root causes of the great stress on global environment in our times.
4. Discuss the chief forms of environment degradation in modern times.
5. Discuss Indian efforts of resource-environment management for sustainable development.

Short answer type questions :

1. Mention India's main resource-environment problems.
2. Write notes on the two major factors that may result in perceptible climate changes.
3. What is enthropication of water bodies?

4. Mention the main forms of renewable resource depletion on earth.
5. Can we do away with the hard exercises of sustainable development?

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