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Legal Transplant to Decolonization in the Evolution of India's Corporate Legislation

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ABSTRACT: In India, most existing legislation resulted from a "legal transplant" that gradually occurred in colonial times. India is a common law country that follows the colonial pattern of law-making. Most of the legislation owes the British East India Company, including regulation of modern business corporations. This paper aimed to examine the history and formation of corporate legislation in India and its deviation from the legislation of the origin country, England. It pointed out the relevance of local conditions in India that led to a different approach to forming corporate law in India. The local conditions in India prevailed over the process of legal transplant. The social, economic, and political factors played a significant role in forming corporate law in India. To such an extent, India deviated from the English company laws and followed the trajectory of different jurisdictions. Using normative legal research, this paper is structured chronologically and progressively to trace the evolution of Indian corporate law. The central premise of the study is that India has strayed from colonial law and current legislation, and its development shows no evidence of strong dependence on English law and little evidence of following in the footsteps of India's colonial past. The economic liberalization and the SEBI Act 1992 simultaneously led to a new approach in corporate law, heavily under the US. The present Indian corporate law and the statutes revolving around it have departed from the transplanted law.

KEYWORDS: Legal Transplant, Corporate Legislation, Company Law.

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I. INTRODUCTION

There has been a growing discussion on the role of "legal origins" and "legal families" in developing legal rules and institutions within a country, particularly in finance, between comparative law scholars.[1] There has been a growing emphasis on the growth of comparative corporate law within this discussion. A major success of corporate law regimes in any legal family directly links to the success of that legal institution in protecting the interests of shareholders.[2] The countries belonging to the common law family provide better protection to outside investors than civil law countries. At the same time, in common law countries, better access to equity finance is provided to the companies.[3] Comprehensive studies suggest that better legal protection to outside investors leads to capital markets, and the effectiveness of the financial system of a country depends on investor protection based upon the quality of law enforcement.[4] However, there have been different claims about the development of corporate law. Many have criticized this theory because the formation of law and legislation is influenced more closely by the country's political atmosphere.[5] The legal origin does play a significant role in better financial development.[6]

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1 John Amour & Priya Lele, *Law, Finance, and Politics: The Case of India* (Law and Society Review, 2009) at 491, 492.

2 Umakanth Varottil, "The Evolution of Corporate Law in Post-Colonial India: From Transplant to Autochthony" (2015) 31 American University International Law Review 253–325 at 4.

3 Rafael La Porta, et al, "Legal Determinants of External Finance" (1997) 52:3 The Journal of Finance 1131–1150 at 1131, 1137. See also Misbahul Ilham, Bhim Prakoso & Ermanto Fahamsyah, "Compensation Arrangements in Expropriating Goods and Equipment: An Indonesian Experience" (2020) 1:2 Indonesian Journal of Law and Society 199–218 at 210.

4 Rafael La Porta et al, *supra* note 3. Shamila Dawood, "Corporate Social Responsibility and MNCs: An Appraisal from Investment Treaty Law Perspective" (2021) 2:2 Indonesian Journal of Law and Society 197–234 at 208.

5 John Armour & Priya Lele, *supra* note 1 at 493.

6 Holger Spamann Spamann, "Contemporary Legal Transplants: Legal Families and the Diffusion of (Corporate) Law" (2009) 2009:6 BYU Law Rev, online: <https://digitalcommons.law.byu.edu/lawreview/vol2009/iss6/11>.

While India had gone through the legal transplant, the problem that led to the decolonization of corporate law in India was the failure of a successful transplant due to the ignorance of India's local condition by the colonial rulers. In other words, Indian corporate law functioned as a continuum of transplants from English law, which continued for over a century, as elaborated further. The oddity about the Act 1850 was that registration was only optional as it conferred certain privileges. The different factors play a significant role in the success of a legal transplant. These factors include the demand of the law, familiarity of the population to the legal principles of the origin country, and resources for legal change.[7] These factors heavily influence the legal transplant process, and the lack of these factors can lead to ineffective implementation.[8] Similar issues dealing with the corporate legislation of England were imitated in India, but with its legal problems. Then, colonial legislation failed to adapt to India's local economic and political conditions. As a result, the failed transplant of the legal system led to the deviation of transplanted corporate laws in the post-colonial period through decolonization. The relevance of this discussion stems from India's colonial origin, which makes it a part of the common law family.[9]

Focusing on English corporate laws and their imitation in India, the company legislations introduced in India have undergone several amendments due to the apathetic nature of the legislation towards India's local conditions. Before discussing legislations and problems, the critical issue is the motive behind introducing these laws in India. European traders wanted to open trade in India, and recognition as a company, unlike today, could only be obtained through the Royal Charter, which by the end of the 17th century came into the form of Acts of British Parliament and later Indian legislature or a combination of an act and a charter.[10]

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[7] Daniel Berkowitz, Katharina Pistor, & Jean-Francois Richard, "The Transplant Effect" (2003) 51:1 The American Journal of Comparative Law at 163, 168.

[8] *Ibid.*

[9] M P Jain, *Outlines of Indian Legal and Constitutional History*, 6th ed (New Delhi, India: LexisNExis, 2007) at 364-367.

[10] R S Rungsta, "Indian Company Law Problems in 1850" (1962) 6:3 American Journal of Legal History 298–308; Ella Gepken-jager, "The English East India Company and the History of Company Law" in Gerard Van Solinge & Levinus

Therefore, the establishment of the East India Company as a result of the Royal Charter of 1600 authorized the company to trade in India and other markets in Asia.[11]

India's colonial past is silent on the real motive of the company to imitate these legislations. The dissemination of the history of legal transplant describes it as a move to regulate the capital market and serve the interests of colonial rulers.[12] Rungta provided a ground for discussion on the influence of socio-economic factors and political motives in introducing similar laws in India.[13] Thus, the corporate law transplant in the 19th century was well planned, but the problems with the transplant shall not be overlooked to understand India's stand of departing from the transplanted legal system in the post-colonial era. This deviation from the transplanted legal system raised a question on the classification theory of legal systems in understanding the present corporate laws. It also deals with the influence of legal origin in tracing back the development of the recent legislation which deals with corporate and commercial affairs.[14]

The paper has been divided into four major parts of the discussion. The first part provides a historical overview of company legislation. The second part examines the decolonization of company law in Indonesia from 1947 to 1960. The third part analyzes the rise of socialism, following the impact on corporate law in India from 1960 to 1991. The fourth part discusses economic liberalization in corporate law and securities regulations in India. After all, this paper concludes that the economic liberalization and the SEBI Act 1992 simultaneously led to a new approach in corporate law, heavily under the US. The present Indian corporate law and the statutes revolving around it have departed from the transplanted law. Therefore, Indian corporate law, based on the fundamentals of English and American

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Timmerman, eds, *VOC 602-2002: 400 Years of Company Law* (Kluwer Law International, 2005) at 219.

[11] Ella Gepken-jager, *supra* note 10 at 219.

[12] Umakanth Varottil, *supra* note 2 at 16-17.

[13] Radhe Shyam Rungta, *The Rise of Business Corporations in India 1851–1900* (Cambridge: Cambridge University Press, 1970) at 68.

[14] *Report of the Company Law Committee*, by Ministry of Law India (New Delhi, India: Ministry of Law India, 1952) at 16.

law, has managed to subscribe to a separate jurisdictional approach that could define the Indian corporate law regime uniquely.

II. METHODS

This work was in adherence to the normative legal research method, relying on both primary and secondary sources. It was descriptive and followed an analytical approach, using the analysis of the facts to reach a conclusion based on logical reasoning. This research reviewed the current format and established a relationship with the subject matter. To this end, the author relied on current existing laws, treaties between countries, statutes, reports, databases, and various government and non-government documents.

III. HISTORY OF COMPANY LEGISLATION

To understand the evolution of company laws in India, first, it would need to understand the developments of business corporations and legal rules in the colonial period. In this part, the analysis covers the historical products of business laws as a result of transplant to better understand the post-colonial decisions with relation to the socio-economic atmosphere of the country that existed after independence.

A. The Emergence of the Business Corporation in England

The early form of corporation in England was a flexible ecclesiastical entity, unlike today's modern corporations, looked upon as separate legal entities with corporate personalities. These were corporations deemed valid only with the assent of the crown through a Royal Charter. At a lower level, merchants in guilds were the most resembled form of a corporation. However, it was looked upon as a trade protection association instead. There was no need to define separate rights and liabilities of its members as these members of merchant guilds traded in their capacity. Even if less in number, joint trade was possible through partnerships, given that the guild rules were followed. Thus, regulating companies emerged as a replacement

to the guilds, essentially retaining the nature of a domestic guild. Members of a regulating company had traded their stocks individually according to its rules. Finally, joint-stock companies emerged where the members traded joint stocks on a joint account. It is exemplified from the Royal Charter of 1600 that resulted in the East India Company, a joint-stock company that could open trade with the East Indies.[15]

B. Modern Business Corporations in India

Modern business corporations were not present in ancient India. When the Indian merchants came across the operations performed by the European chartered companies, they discovered this form of corporation. Therefore, modern business corporations in India owe them to the European chartered companies.[16] Before the European invasions, ancient business corporations had existed in the form of *sreni*. This term is similar to the guilds of Medieval Europe) since at least 800 BC or even before.[17] These guilds had almost vanished after the European traders arrived, leading to trade expansion between Europe and India when the English East India Company first emerged as a joint-stock company in the 17th Century in South India.[18] The formation and status of a company were no less than a privilege. The East India Company had rarely granted any charters to the companies, especially banking companies, to trade in India until 1850 as the interest of Britain in manufacturing in India was growing.[19] The Charter granted reluctantly by the East India Company to the Oriental Bank Corporation had opened the doors to India.[20] It led to the emergence of modern business corporations in India.

[15] Ella Gepken-jager, *supra* note 10 at 219.
[16] *Ibid* at 1.
[17] Vikramaditya S Khanna, *The Economic History of the Corporate Form in Ancient India* (SSRN, 2005) at 1.
[18] Radhe Shyam Rungta, *supra* note 13 at 1.
[19] R. S. Rungta, *supra* note 10.
[20] *Ibid* at 299.

C. Initiation of Transplant in the 19th Century

The initiation of legal transplant could be traced back to 1850 when the Companies Act 1844 of England was passed. This Act was specifically passed to register Joint Stock Companies in India.[21] The registration of these companies was to be taken up by the Supreme Courts of Bombay, Madras, and Calcutta under this Act.[22] However, there was no provision for conferring limited liability on the members of an unincorporated company with transferrable shares without the consent of their partners or any other company.[23] It was not unexpected from the Act as these developments had not taken place in Act 1844 of England, and the concept of limited liability was relatively lesser-known till now.[24] However, there were other essential provisions in the Act 1844 of England and the 1850 Act of India that brought some significant changes.

The Joint Stock Company Act 1844 had done away with the necessity of charters by providing for the automatic incorporation, replacing the necessity of Charter for the incorporation.[25] The repeal of the Bubble Act 1720 automatically terminated the necessity of charters, which mandated the grant of charters for incorporations.[26] The Act 1844 also introduced the procedure to form a company. The procedure was to file a deed of settlement, similar to registering a joint-stock company under the Indian Act 1850.[27] Like the 1844 Act, the Indian Act 1850 introduced some important provisions related to forming Joint Stock Companies in India. Some essential provisions elaborated on the transferability of shares and their formation as a separate legal entity with its corporate personality. For

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21 Ministry of Law India, *supra* note 14.

22 *Ibid*.

23 *Ibid*.

24 Umakanth Varottil, *supra* note 2 at 13.

25 PM Vasudev, *Capital Stock, its Shares and Their Holders: A Comparison of India and Delaware* (SSRN, 2007) at 17.

26 *Ibid*.

27 *Ibid* at 16-17.

example, a company was allowed to sue or sued by the shareholders.[28] Further, there were provisions for insolvent companies as well.[29]

The Act 1844 did not limit shareholders' liability, leading to the lack of protection. This trend was also evident in the 1850 Act and the problem of optionality in the registration of a company.[30] The problem of limited liability was dealt with in the Limited Liability Act 1855 of England, and it was confronted in the Indian Company Act 1856. In the same year, the Joint Stock Companies Act 1856 was enacted in England to put forth some amendments in incorporating a company.[31] Instead of a deed of settlement, a memorandum of association (MOA) was submitted before the authorities. The submission was to incorporate a company along with reasons and objects of formation. The MOA defined the scope of the companies regarding the business that they would undertake. It led to the emergence of the concept of "*Ultra Vires doctrine*" when the House of Lords, in the case of *Ashbury Carriage Co. v. Riche*[32] ruled that a company cannot act beyond its powers and objects defined at the time of incorporation through the MOA.

These developments show that the development in India as compared to England was slow and more like a regime of mimicking the legal rules without giving due attention to the local conditions in India. Although the Joint Stock Companies Act 1856 introduced limited liability in England, it did not extend this privilege to the Banking and Insurance companies. The exact scenario was repeated in India when limited liability was introduced but not extended to the banking and insurance companies.[33] The same pattern is followed with the English Act 1857[34] and its counterpart, the Indian Company Act 1860. However, the limited liability was extended only to the banking companies and not to the insurance companies this

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[28] Ministry of Law India, *supra* note 14.

[29] *Ibid*.

[30] Radhe Shyam Rungta, *supra* note 13 at 41.

[31] P. M. Vasudev, *supra* note 25.

[32] (1875) LR 7 HL 653.

[33] Radhe Shyam Rungta, *supra* note 13 at 64.

[34] The Joint Stock Companies Act, 1857, No. 19, Ministry of Corporate Affairs, 1857(India).

time.[35] It continued with the English Act1862, followed by Act 1866 of India. As stated in the Bhabha Committee Report, the purpose of these acts was to consolidate and amend "the laws relating to the incorporation, regulation and winding up of Trading Companies and other Associations."[36] Finally, the limited liability as a privilege was extended to the insurance companies.[37] Further, with the beginning of the 20th century, new developments were evident by enacting different amending acts from 1882 to 1913.[38]

D. Developments in the 20th Century

In India, the development of company law in the 20th century resulted from amendments that had taken place in England after 1862. Significant amendments that had taken place in the 1862 Act were finally consolidated in India in the 1882 Act. The English company law was heavily based upon the reports of different committees formed by the Board of Trade at the intervals of 20 years to review company law, as explained by LCB Gower.[39] These reports were comprehensively considered to form subsequent English company law consolidating acts. The Consolidation Act 1908 resulted from the Loreburn Committee (1906), whereas the reports of the Wrenbury and Greene committees were considered while drafting the Companies Act 1929. A similar fashion was followed in the formation of the Companies Act 1948, based on the recommendations of the Cohen Committee (1945).[40] While English company law was reforming with a shift from individual rights to business,[41] India went through a series of

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[35] Radhe Shyam Rungta, *supra* note 13 at 70.
[36] Ministry of Law India, *supra* note 14 at 17.
[37] Radhe Shyam Rungta, *supra* note 13 at 212.
[38] Ministry of Law India, *supra* note 14 at 17.
[39] LC B Gower, *The Principles of Modern Company Law* (London: Stevens & Sons, 1969) at 54.
[40] P. M. Vasudev, *supra* note 25 at 18.
[41] The Act 1844 considered the capacity of individual company members and not the business activities it had undertaken as a company. It was later reformed after enacting the Joint-stock Companies Act 1856, and introducing the concept of "Ultra Vires" with the coming of MOA for incorporation of the companies. *See Ibid* at 17.

amendments even after the consolidating Act 1882.[42] Some amendments included the authorization of companies to modify or alter their objects after taking permission from the High Court, allowing keeping the branch registers of members of certain companies in the UK and the re-issue of redeemed debentures.[43]

The imitation observed in the introduction of company legislations of the 19th Century in India was followed in the 20th century. The consolidating Act 1908, formed based on recommendations made by the Lorneburn committee, was followed by the Companies Act 1913 in India with slight changes.[44] This trend is slowly changing its stance from imitation and re-enactment of English laws to adapting to the local problems prevalent in India. A new act was introduced, an amending act instead of a consolidating act. However, this Act was based on the English Act 1929, the problems of managing agency systems, and a need for provisions specific to banking companies, not explicitly incorporated till now.[45] Even the Statement of Objects and Reasons of the Indian Companies (Amendment) Act 1936 states that the English Company Act 1929 could not be adopted as it had "attracted unfavorable criticism" for not considering the local problems of India. To create laws on banking, the recommendations of the Central Banking Enquiry Committee were taken into consideration.[46] Another case where this proposition could be supported is the case of *Ramanandi Kuer v. Kalawati Kuer.*[47] This case makes it evident that India is a common law country. The judiciary did not hesitate because mere re-enactment of English legislation will not attract a positive enactment of a statute unless the statute's language is examined to interpret clauses properly without considering the statute's origin, which

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[42] Ministry of Law India, *supra* note 14 at 17.

[43] *Ibid.*

[44] There were certain differences between the Indian Act 1913 from the English Act 1908. Later, the Act 1913 was amended from 1914-1932 by the Acts of 1914, 1915, 1920, 1926, 1930 & 1932. *See Ibid* at 17.

[45] *Statement of Objects and Reasons* of Indian Companies (Amendment) Act, 1936.

[46] *Ibid.*

[47] (1928) 30 BOMLR 227.

may be English law.[48]In another case of *Hind Overseas Private Limited v Ragunath Prasad Jhunjhunwalla and Ors,*[49] the Indian court believed that the Indian company law was English. It is crucial for the courts to adjust and adapt limit or extend the principles derived from English decisions entitled as they are to great respect, suiting the conditions of our society and the country in general.

After the amendment, the Act 1913 was further amended almost ten times from 1937 to 1946. These amendments resulted from defects left in the Act 1913 even after the amendment. The different rules were amended to align this Act with other statutes, such as the Government of India Act, 1935.[50] After the independence, India saw a shift in the policy that dealt with corporate laws. It is evident because the government promulgated an ordinance in 1951 after India became a Sovereign Democratic Republic as the Indian companies (amendment) ordinance, 1951. This ordinance aimed to reform the corporate laws by authorizing the government to interfere in the company affairs and authorized the courts to take action against any prejudicial move against any company member.[51]

E. Impact of the Failed Transplant and "Colonial Laissez-Faire"

As discussed previously, the British motivation to introduce these legislations in India is not expressly stated. Various studies and findings suggest that the British colonizers wanted to expand trade in India1 and systematically disrupt the vernacular business structures in India by ignoring the interests of local business forms.[52] Scholars like Rungta and Birla explain the British motives behind introducing these laws in India. Rungta, while analyzing the pattern of mimicking the company legislations in India, observed that there was a common viewpoint that the laws which

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[48] *Ramanandi Kuer v. Kalawati Kuer* (1928) 30 BOMLR 227, § 8.

[49] AIR 1976 SC 565.

[50] Ministry of Law India, *supra* note 14 at 18.

[51] *Ibid* at 19.

[52] *See*, Ritu Birla, *Stages of Capital Law, Culture, and Market Governance in Late Colonial India* (Duke University Press, 2009). Umakanth Varottil, *supra* note 2 at 266-268.

were favorable in England must be favorable in India as well.[53] She accounted that the colonizers did not only ignore the interests of local business forms but also followed the free-market ideology or the "colonial laissez-faire." It completely ignored businesses such as the Hindu Undivided Family (HUF) and other local businesses that operated in Kinships.[54] Birla also states that to serve the British interests, the colonizers took a route of capitalism and the notion of "free-market ideology." It was evident in the legal regime, with some examples in the free circulation of credit and commodities and institutionalization of contract law,[55] which led to the disruption of local businesses.

Even after much emphasis on British interests, an Indian innovation that was not directly related to the colonial interests came into existence known as the "managing agency system." This system was not entirely isolated from the developments taken place by the colonial rulers but somewhat was facilitated by them. It emerged as a result of consideration towards the local conditions in India.

F. Evolution of the Managing Agency System

The managing agency system was a unique arrangement where agents were hired to manage the colonial period's joint-stock companies.[56] Rungta describes the emergence of the managing agency system in India due to necessities of "history, geography, and economics."[57] The system of managing agents advocated the viewpoint of vesting the business in the hands of capable agents who were motivated to run the business and manage it. Although the managed companies generally would constitute their Board of Directors, those were these agents who had the

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53 Radhe Shyam Rungta, *supra* note 13 at 68.

54 Ritu Birla, *supra* note 52. Umakanth Varottil, *supra* note 2 at 267-268.

55 Dipesh Chakrabarty, Rochona Majumdar, & Andrew Sartori, eds, "Capitalist Subjects in Transition" in *From the colonial to the post-colonial : India and Pakistan in transition* (New York: Oxford University Press, 2007).

56 Umakanth Varottil, *Corporate Law in Colonial India: Rise and Demise of the Managing Agency System* (Centre for Asian Legal Studies, 2015) at 1.

57 Radhe Shyam Rungta, *supra* note 13 at 220.

responsibility to handle the management of the business, such as establishing and running the business.[58]

As discussed earlier, the formation of vernacular business corporations in India was based on family relations. Besides those business corporations, people who had the will and capability to hold and manage the business existed. These capable businesspersons came together to contribute as active investors and managers.[59] However, it gave them a higher position and control over the company, leading to the diffusion of shareholders who did not have any financial assistance to check on the powers and functions of the managers. As passive investors were not capable of managing the company, nor did they have any will to manage, managers' control and ownership kept growing.[60] It led to the abuse of powers by the managers to safeguard their interests showing disregard to the interests of the shareholders.[61] This effect was seen in the latter half of the 19th century when the shareholders had fell victim to the large-scale abuse by the British managing agents.[62] It is essential to understand how this concept emerged in India and spread to the rest of the Asian colonies to understand how this happened.

The concept of limited liability did not emerge after the English law mandated it. Surprisingly, it existed thousands of years before transplant had begun.[63] Before establishing modern business corporations, Hindu families handled the businesses jointly. These families were involved in the business as a separate entity from its members, who were not personally liable for the debts and losses.[64] Therefore, limited liability existed within these families where only the head of the family was held personally liable

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58 Robert C Rosen, "The Myth of Self-Regulation or the Dangers of Securities Regulation without Administration: The Indian Experience" (1979) 2:4 University of Pennsylvania Journal of International Law at 263.

59 Radhe Shyam Rungta, *supra* note 13 at 227.

60 Umakanth Varottil, *supra* note 57 at 1-2.

61 *Ibid* at 1.

62 *Ibid* at 2.

63 Robert C. Rosen, *supra* note 58.

64 *Ibid*.

under Hindu law.[65] The other members of the family, who were indulged in the business, had no personal liability of their own and only shared profits.[66] It aided the rise of managing agencies in India which were further aided by the trading system of sterling companies in India which looked like a managing agency system.

With the emergence of the Indian managing agency system, several partnerships have emerged in India. The managing agents of these private and public companies, which were earlier in the form of partnerships, controlled these companies. Given their capabilities, they were able to raise capital by attracting investors. These agents were held personally liable for the loans of their managed companies,[67] similar to the head of the family in Hindu family businesses. Studies suggest that in India, the presence of British managing agents was more than the Indian agents themselves.[68] It facilitated their image in the colonial business sphere as well.[69] However, this could be attributed as one of the primary reasons for the abuse of power by these agents. The grant of proxies by the passive investors further deteriorated this agency problem.[70]

The Indian managing agency system, which existed before the transplant, also had some problems, positively affecting India's economic development. First was the vesting of powers in the hands of incapable family members.[71] Members who were not capable enough to raise finances by attracting investors were made the managing agents, which resulted in poor business management. Agents started misusing their powers by funding weaker entities through the capital of their managed company.[72] Another problem

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65 *Ibid*.

66 *Ibid*.

67 T B Desai, *Economic history of India under the British* (Bombay: Vora, 1968) at 89. *See also* Robert C. Rosen, *supra* note 58.

68 Maria Misra, *Business, Race, and Politics in British India, c. 1850–1960* (Clarendon Press, 1999) at 4. Omkar Goswami, "Sahibs, Babus, and Banias: Changes in Industrial Control in Eastern India, 1918-50" (1989) 48:2 The Journal of Asian Studies 289–309 at 292. Radhe Shyam Rungta, *supra* note 13 at 227.

69 Maria Misra, *supra* note 68.

70 Omkar Goswami, *supra* note 69 at 294.

71 Robert C. Rosen, *supra* note 59 at 264.

72 T. B. Desai, *supra* note 68 at 89-90; *See* Robert C. Rosen, *supra* note 58.

was the power to appoint a board of directors. The managers could appoint the Board of Directors, which could serve their interests, detrimental to the public shareholders.[73] Therefore, problems had existed before the British managing agents had taken over the Indian market.

These problems were dealt with through legislative efforts, however much later. The question arises here is that what could be the plausible reason for such a delay? There was no real motive to introduce legislation to solve these agency problems since the colonizers were ignorant of the local economic conditions. The English lawmakers saw no efforts to draft legislation adaptive to the local conditions to solve the agency problems. Partly, it was because they were unaware of the local conditions in India and these local agency problems. Also, the British managing agents did not face these problems while managing Indian companies as they were in a dominant position. The managing agency system was majorly criticized by the Indian shareholders and businesspersons subject to abuse. Also, there was no political will in introducing legislation as the Companies Act 1913 did not mention these problems once.[74] Misra attributes this lack of political will to the pre-dominance of British agents.[75]

This problem only occurred in 1936 when the Companies Act 1913 was amended. It was the beginning of the statutory restrictions, which slowly led to the demise of this system. The 1936 amendment had restricted the managing agents and limited their powers by allowing them only to appoint one-third of the Board of Directors, making provisions for their removal in case of fraud, insolvency, or breach of trust. Most importantly, it had limited this system to 20 years.[76] In the amendment of 1956, a limit on the number of companies to be managed by each agent was imposed to be ten. The system was abolished after the amendment of 1969 mandated that

[73] M Arokiaswami & T M Royappa, *The Modern Economic History of India* (Newman Book House, 1957) at 151–152.

[74] Robert C. Rosen, *supra* note 59 at 264.

[75] Maria Misra, *supra* note 69 at 7-8.

[76] Arokiaswami & T M Royappa, *The Modern Economic History of India* (Newman Book House, 1957) at 151–152. Robert C. Rosen, *supra* note 59 at 264.

the term of all the agents would be expired. No further agents shall be appointed, which would come in effect from 1st April 1970.[77]

The case study of the rise and demise of the managing agency system in India only further supports the argument that the transplant that had taken place in India was to serve the interests of the colonizers. Further, this also describes that when they were not facing difficulties in managing businesses in India, they were ignorant of the domestic conditions and the repercussions of the transplant. Therefore, the transplant was a failure, and India had to depart from the transplanted legal system, first observed with the introduction of the 1936 amendment.

After the 1936 amendment, the departure from English law was carried forward to the post-independence scenario. The development of company law, like any other law in India post-independence, the development of company law was affected by the political and economic conditions in India that existed after the independence. Therefore, while discussing the development of post-independence and decolonization in detail in the next part, this cannot be done without analyzing the socialist tendencies followed by India's post-independence. Simultaneously comparisons with competition and security regulations shall also be drawn to analyze the broader perspective of Indian commercial laws.

IV. DECOLONIZING COMPANY LAW IN INDIA (1947- 1960)

In this part, this paper analyzes the simultaneous development of commercial laws in the post-independence scenario. The decolonization did not take place immediately after the independence. It was rather unconsciously affected by the political decision-making and the country's economic conditions. The departure from English laws was unsurprisingly observed in other laws. However, the trajectory followed by India in terms of commercial laws, unlike the other laws, was somewhat towards the English laws. This part also discusses India's economic policy shift from capitalism to a "mixed economy" had on corporate law-making. Further, it

[77] *Ibid* at 264.

examines the socialist tendencies and significant shift to capitalism after the economic liberalization of 1991, along with its effect on security regulations and simultaneous developments in corporate affairs.

A. Economic Policy Shift and Its Effect on Corporate Legislation

After gaining independence in 1947, India was decolonized as a country when the decision-making related to the economic policies was in the Indian political leaders. However, corporate law-making was not decolonized. Indians were distrustful about the capitalistic order and the "free market ideology" or the "laissez-faire." The capitalistic order imposed by the colonizers was harmful to the Indian businesses.[78] India was suffering from poverty and illiteracy problems and low life expectancy.[79] This episode made it even more crucial for the policymakers to adopt an economic policy that could solve these problems efficiently. Therefore, there was a debate between eminent policymakers on whether to follow the path of state ownership or liberalization. Finally, when Jawaharlal Nehru became the first Prime Minister, he decided to follow the policy of "Fabian socialism," which advocated state ownership and self-regulation.[80] The first five-year plan, which advocated industrialization, aimed at the success of the mixed economy policy.

The motive behind emphasizing state interference and ownership was to depart from the colonial economic policies. Dwijendra Tripathi and Jyoti Jumani have emphasized it. They stated that "independent India did not abandon the free enterprise system altogether, but what these policies together sought to introduce was a system very different from the one that had operated under colonialism."[81] These measures brought a sea change in

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[78] Radhe Shyam Rungta, *supra* note 13. Ritu Birla, *supra* note 52. Umakanth Varottil, *supra* note 2.

[79] Nirmalya Kumar, "India unleashed" (2009) 20:1 Bus Strategy Rev 4–15.

[80] *See*, B R Thomlinson, *The Economy of Modern India, 1860–1970* (England: Cambridge University Press, 1993).

[81] Dwijendra Tripathi & Jyoti Jumani, *The Concise Oxford History of Indian Business* (New Delhi & New York: Oxford University Press, 2007) at 23.

the business environment.[82] It was the beginning of a departure from colonial policies after the independence.

However, the policies cannot be stated as anti-capitalist as some private capital was still recognized, and private enterprises were not totally abolished.[83] Laws related to the regime of licensing of industrial units are the Industries (Development and Regulation) Act 1952, along with other laws related to the regulation of private enterprises such as the Essential Commodities Act 1955, Capital Issues Control Act 1947, and the Essential Supplies (Temporary Powers) Act 1946. They make it evident that the government was following the policy of socialism with an aversion towards capitalist tendencies given to the colonial experience. Licenses were imposed on these industrial units to regulate and control them and look upon capacity expansion.[84] It clearly shows that the State ownership had prevailed over the private businesses and entrepreneurs as they were subject to the "license raj" of the State. In this atmosphere, was introduced the first companies legislation after the independence.

B. The Companies Act 1956

The introduction of the 1956 Act in India marked the beginning of a new era which was surprisingly another legal transplant from English law. However, this time, it was well planned.[85] The Companies Act 1956 is an example of a contradictory stance of the government in making legislative decisions. Where one way, the government was trying to regulate private enterprises as discussed above, the other way, with the introduction of the 1956 Act, borrowed another colonial legislation from England. The 1956 Act in India referred to the English Companies Act 1948, based on the recommendations of the Cohen's Committee (1945).[86] When a committee

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82 *Ibid*.

83 *See*, *Ibid* at 19.

84 *See*, *Ibid* at 22.

85 *See*, Umakanth Varottil, *supra* note 2 at 24.

86 *Report of the Committee on Company Law Amendment (Cohen Committee Report 1945)*, by Cohen Committee (His Majesty's Stationery Office, 1945). P. M. Vasudev, *supra* note 25 at 18.

presided by CH Bhabha as the chairperson was formed in India to review company legislation and give recommendations, it highly relied upon the recommendations of Cohen's Committee. Varottil observes that in obtaining a better sense of the extent of reliance on English law, a review of the Bhabha Committee Report indicates approximately 148 references to the English Companies Act 1948, adopting with approval 64 of its provisions and modifying or rejecting only 21 provisions.[87] It asserts that the basis on which Bhabha Committee made its recommendations was the colonial legislation. Therefore, India did not depart from English law in company legislation. Other spheres followed the trajectory of "State ownership and regulation."

While understanding the case of contradictory decision-making, the transplant in its nature was not the reason for the failure. Instead, it was the ignorance of the colonizers towards the local conditions while transplanting the legislation in India. As discussed, the British companies were somehow responsible for disrupting the Indian businesses. Therefore, the transplant that had taken place in the colonial period was different from the well-planned one, which the government undertook on the recommendations of the Bhabha Committee.

Though it was a conscious move, there was no intent to depart from the English legislation. Instead, the evolution and departure after independence resulted from the country's political and economic scenario. Varottil states no intention to frame indigenous legislation apt to India's changed circumstances given the enormous shift in its economic policies.[88] This raises a question on the motive of the Parliament in promoting State ownership. Many studies suspect that this could be because of the risk of "immediate break away" from the colonial legislation, specifically because enactments of some other laws have shown this phenomenon.[89]

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87 Umakanth Varottil, *supra* note 2 at 25.

88 Umakanth Varottil, *supra* note 2 at 25.

89 *Ibid*. Rohit De, "'Commodities must be controlled': economic crimes and market discipline in India (1939–1955)" (2014) 10:3 International Journal of Law in Context 277–294. Anil Kalhan et al., "Colonial Continuities: Human Rights, Terrorism, and Security Laws in India" (2006) 20:1 Columbia Journal of Asian Law.

C. What Was the Legislative Approach towards the Private Enterprises?

The Parliament followed a contradictory approach. Tripathi and Jumani described this situation as having no intent to unduly curtail the freedom of private enterprises.[90] There was no "immediate threat" to them as the private enterprises were left undisturbed where they were suspected of expanding.[91] It can be deduced that the socialist approach of Parliament was not observed in the legislative actions taken towards corporate law. Also, the State did not intend to control businesses, not through corporate law. Therefore, even after having a good chance to alter the company law after independence, Parliament decided to follow the same legislation even after turning the path to enact other laws.

By analyzing the Bhabha committee report and its take on the managing agency system, managing the agency system became controversial due to managing agents' exploitation. Even after much of those problems, the Bhabha Committee concluded, "having regard to all the circumstances, we consider that under the present economic structure of the country it would be an advantage to continue to rely on the managing agency system."[92] On the other hand, the planning commission stated that the managing agency system under which industries are controlled and operated by independent firms had disclosed several features that are harmful to the industry's growth in the future.[93] The Bhabha Committee report further stated the shorn of the abuses and malpractices that have disfigured its working in the recent past. The system may yet prove to be a potent instrument for tapping the need for the springs of private enterprise.[94] It clearly shows the reluctance to depart from the colonial State of play. However, the Committee recommended suggestions related to the appointment, remuneration, and powers of managing agents and borrowing loans. It was to minimize the abuse.

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[90] Dwijendra Tripathi & Jyoti Jumani, *supra* note 82 at 25.

[91] *Ibid* at 26.

[92] Ministry of Law India, *supra* note 14 at 84.

[93] *Ibid*.

[94] *Ibid* at 85.

A Parliamentary Committee looked into the matter and suggested the Indian Companies Act Reforms. As a result, these changes were incorporated in the Companies Act 1956, which imposed strict limitations on the managing agents. However, this system was abolished only in 1970, which shows that these problems were not enough for the Parliament to abolish the system altogether. Instead, there was a will to retain the system by reforming it to reduce the problems. This case study of managing the agency system and its retention establishes that independence did not attract self-made legislation. India followed the transplanted laws, and Parliament facilitated this process. Further, the Parliament did not want to reform the transplanted legislation into self-made laws. The Parliament had a different legislative approach while dealing with corporate legislation compared to the broader aspect of promoting State ownership.

V. RISE OF SOCIALISM AND IMPACT ON CORPORATE LAW IN INDIA (1960-1991)

It has already been discussed in the previous part that after independence in 1947, India had not departed from the English transplanted laws and followed the same laws, but after planning it properly. Politics played some part in the development of corporate law, but little.[95] The broader perspective of the following socialism was slowly incorporated into corporate legislation. It was evident in the political actions, based on the recommendations of various committees formed in the 60s, 70s, and 80s from time to time.[96] These recommendations were to reform and contain corporate managements in line with the socialist tendencies of the State.[97]

One such reform was to treat large private companies as "deemed public companies," a concept introduced in India through the amendment of 1960.[98] Public companies under English law were subject to a more controlled regulatory framework. One such example of this could be that

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[95] P. M. Vasudev, *supra* note 25 at 20.
[96] *Ibid* at 21.
[97] *Ibid* at 20.
[98] *Ibid* at 21.

the remuneration paid to the managing director in public companies was regulated by the Companies Act 1956 under Section 310. It had mandated that any increase in such remuneration be subjected to prior approval by the Central Government. Similarly, section 311 stated that prior government approval should be necessary while re-appointing the managing director. Another example could be section 182 of the Act, which states that in a public company, a member shall not be restricted from exercising his/her voting right or the right to transfer shares in a public company.

On the other hand, the English law distinguished private and public companies clearly, and the regulatory framework for these types differed. Under the English Companies Act 1948, private companies were subject to a liberal regulatory framework as these private companies were somewhat closely related to the structure of a Partnership firm.[99] Therefore, they were treated as a closed structure with no strict limitations and regulatory oversight. On the other hand, under section 43A of the 1956 Act, private companies were subject to the provisions of public companies under certain circumstances.

Further, in 1960, new types of companies known as "deemed public companies" emerged. Private companies with large capital and extensive turnover beyond limits, along with control over public companies, were now treated as "deemed public companies."[100] The Committee that had recommended this gave simple reasoning that a private company with control over a public company had investments drawn from other private and public companies and the overall public. It should not be treated as a private company, and the same company should be subject to the same restrictions imposed on public companies as they had drawn the public's money.[101]

The growing socialism in corporate law could be analyzed further with other examples of cognizance towards the public interest, the demise of the managing agency system, the debates, and discussions. They were held in

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[99] *Ibid.*
[100] *Ibid.* Umakanth Varottil, *supra* note 2 at 28.
[101] *See* P. M. Vasudev, *supra* note 25 at 21.

the Parliament with the coming of the 1960 amendment bill and enactment of different statutes which promoted socialism. We shall discuss these to understand the growing socialist tendencies and their effect on corporate law.

The rise of socialism can be analyzed by introducing the concept of public interest incorporated into India's company law. This concept was not mentioned anywhere in Act 1913. The provisions related to "public interest" or "national interest" were only introduced in the 1956 Act and amended several times. For example, section 396 provides that the government shall amalgamate two or more companies into a single company in the National interest. The term "public interest" was later changed to "national interest" through the amendment of 1960. Section 250 empowers the corporate law board to impose restrictions on transfers of shares where such transfers may be prejudicial to the public interest. For example, the exercise of the voting rights on such transfers shall be restricted, or the transfers shall come into effect only after the approval of the Board.

Sectionw 397 and 398 states that a member of a company or a shareholder company is entitled to seek remedy by applying to the Board if the company affairs are mismanaged in a prejudicial way to the public interest, respectively. Section 394 states that an arrangement or a compromise shall not be permitted if it goes against the notion of public interest. These provisions align with the broader socialism evident in the State's political developments. Earlier, where corporate law was following the English model even after the independence, there was a contradictory stance of the Parliament. However, slowly this stance was changing, which was evident through the parliamentary discussions, the demise of the managing agency, and enactments of socialist legislation.

The managing agency system, which was earlier being reluctantly followed, was now on the verge of its abolition. As discussed in the previous parts, the managing agency system slowly became autocratic as the managing agents started abusing their powers. As discussed earlier, it led to the abolition of this system with the amending Act of 1969, which came into

effect in 1970. It could somewhere be attributed to the rising socialism in India. A joint committee was established before the amendment of 1960 to discuss the provisions extensively. The report of this Committee and the parliamentary debates on government control makes it evident that socialism was prevailing in corporate legislation.

Regarding the investment of the funds, it is suggested that the funds of the private company also have to be invested in a particular manner. This paper suggests that all distinctions between public and private companies should be abolished entirely. There is no difference between a private company and a public company so far as the country is concerned. There is no difference in the management of private and public companies so far as business, production, and employment are concerned, and private companies are also mismanaged like public companies.

There should be equal restrictions on the private and public companies regarding the appointment of managing directors or agents.[102] He also stated that the government should exercise greater control over the companies. The auditors' report shall be presented before the shareholders and the government, thus emphasizing the nationalization of the audit services.[103] However, analyzing the arguments stated above, it can be concluded that there was a growing emphasis on government control and State ownership while enacting different statutes.

Coming onto the enactment of new laws which were going in line with the policy of socialism, surprisingly, the process of infusing socialism in India after independence first started through legislation. One of the first statutes enacted after independence as a socialist statute was the Capital Issues Control Act, 1947 (CICA). This Act mandated government control over the issuance of equity by private enterprises.[104] The following table showcases the enactment of different laws not only promote socialism but was also detrimental to protecting creditors:

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[102] Government of India, *Report of the Joint Committee* 464 (1960).
[103] *Ibid* at 464-465.
[104] John Armour & Priya Lele, *supra* note 1 at 500.

Capital Issues Control Act 1947 ('CICA')	Requirement of Government permission and price regulation for new equity issues by private companies.
Companies Act 1956 ('CA 1956')	Powers on the central government (the Department of Companies Affairs via the Company Law Board or the Registrar of Companies) and the judicial system (the High Court) monitor and regulate companies.
Securities Contract (Regulation) Act 1956 ('SCRA')	Government control of securities trading, including operation of stock exchanges. Exchanges can frame their listing regulations provided they meet the minimum criteria set out in the rules.
Monopolies and Restrictive Trade Practices Act 1969 ('MRTP')	Anti-trust/competition rules to prohibit monopolistic and restrictive trade practices. Said to act as a barrier to Indian (private) companies realizing economies of scale.
Foreign Exchange Regulation Act 1973 ('FERA')	Regulated foreign exchange transactions, with severe criminal penalties for breach.
Sick Industrial Companies Act 1985 ('SICA')	State agency (BIFR) takes control of industrial firms with negative net assets; stay of creditors' claims.

Table 1. *Principal components of the regulatory framework for Indian corporations before liberalization*[105]

Table number 1 clearly describes that the wave of socialism in corporate law was aided through the legislative efforts of the Parliament. The MRTP Act 1969 and the FERA 1973 are the key legislative developments, a discussion on which could support the proposition that legislation was a way to infuse socialism in company law. The MRTP Act 1969 is known to be the predecessor of the Competition Act 2002. This Act had restricted the private enterprises to be regulated in a manner that could deteriorate

[105] *Ibid.*

the competition. In other words, it prevented the excess control of power in a few private players.

Further, the FERA 1973 restricted the foreign shareholders from holding more than 40 percent shares in Indian companies.[106] On the other hand, the SICA 1985 had set up a quasi-judicial State-owned agency named the Board for Industrial Financial Reconstruction. As the name suggests, this agency was set up to reconstruct the industrial firms. However, this agency had failed to fulfill the purpose of its formation. As per the BIFR records, 5327 firms entered into the reconstruction. However, only 504 firms were appropriately reconstructed. As a result, SICA was repealed.

Further, FERA was replaced with the Foreign Exchange Management Act 1999 (FEMA). It was done to lift governmental control after India left the path of socialism following the economic liberalization in 1991. All this while, the only statute that was not repealed was the premiere legislation of 1956. Instead, it was replaced with the Companies Act 2013. The Act 1956 went through several amendments. However, these amendments were majorly in line with the changing economic trends in India. The lifting of governmental control from the private enterprises was extensively undertaken post-liberalization. However, some significant amendments brought in the Act 1956 before the liberalization process could be observed as the initiation of removing the governmental barriers.[107]

The socialist legislative developments came when the licensing system and the governmental barriers were prevalent. Further, the industrial manufacturing sector was majorly focused.[108]The governmental barriers made it difficult for the businesses to survive, which had resulted in the concentration of the power in the hands of few family businesses.[109] These industrial groups' emergence and large holding shares in publicly listed companies through banking channels devastatingly affected minority

[106] Umakanth Varottil, *supra* note 2 at 29.

[107] John Armour & Priya Lele, *supra* note 1 at 501.

[108] Umakanth Varottil, "A Cautionary Tale of the Transplant Effect on Indian Corporate Governance" (2009) 21:1 Natl Law Sch India Rev, online: <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1331581>.

[109] *Ibid.*

shareholders, disrupting corporate governance norms.[110] Also, the appointment of the directors was more or less in the hands of these groups. Therefore, infusing socialism in corporate law negatively affected corporate structures.

Following the path of socialism did not prove to be fruitful for India, and this also attracted much criticism by the 1980s.[111] Further, the Indian economy was facing policy paralysis with the poor performance of the public sector, rise in imports and reduction in exports, deficient foreign exchange reserves, debts from International financial institutions, and inflation. All these problems eventually led to the adoption of a liberal economy. It affected corporate law as well.

VI. ECONOMIC LIBERALISATION IN CORPORATE LAW AND SECURITIES REGULATIONS

India after 1991 took the path of economic liberalization, which was mainly an act of opening the economy to foreign investment and lifting the governmental barriers. It also facilitated foreign direct investment and increased foreign shareholders in India. The deregulation and simultaneous privatization also lifted these governmental barriers to some extent. As a result, stock market appreciation was observed akin to the initial public offerings (IPO) and investors' diversification. This whole process impacted India's security regulations, which had resulted in the formation of the Security and Exchange Board of India (SEBI) in 1992.

In the initial years after the liberalization, several amendments promoted capital investment from foreign investors in India. An example of this could be that a greater emphasis was now put upon the employees of the company when they were now provided greater control through employee sweat equity and stock option plan.[112]Further, differential rights of receiving shares of stock (dividend) and voting while issuing shares.[113]

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[110] *Ibid.*
[111] Umakanth Varottil, *supra* note 2 at 31.
[112] Companies (Amendment) Act, 1999.
[113] Companies (Amendment) Act, 2000.

Other reforms were also introduced, such as removing pre-merger notification and non-applicability of anti-trust laws on hostile mergers and acquisitions. Further, the pre-merger notification was enacted in 2011 even when re-introduced in 2002 through the Competition Act. Other reforms such as deletion of the concept of "deemed public companies"[114]and relaxation of capital maintenance[115] were observed to be in line with the US law than the English law.[116]

The socialist path that India was following after the independence also reflected upon the public offerings of securities. The legislative efforts were undertaken after the liberalization was also evident in developing the Indian securities market.[117] The companies which were willing to promote public offerings of securities needed the approval of the Controller of Capital issues[118] as a part of the socialist regime. Later, the Central Government's control was replaced with an independent regulator named SEBI. SEBI's coming up led to the abolition of CCI, which eventually facilitated the companies in raising capital through offering their shares to the public. The development of SEBI started in 1988; however, its role was more or less negligible. This scenario changed entirely by introducing a plethora of security laws in 1992.

SEBI's development is a critical case study to support the proposition that India has followed different jurisdictions regarding security regulations and corporate governance measures. The Securities and Exchange Board of India refers to the Securities and Exchange Commission of the USA. The latter, known as SEC, was established under the Securities Exchange Act 1934. Also, laws in India governing the prohibition on insider trading are somewhat akin to the laws in the US.[119] It has also been dealt with by the judiciary when it had opined that SEBI has extensively referred to the US Law while interpreting the Insider Trading Regulations in the case of the

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[114] *Ibid.*
[115] *Supra* note 121.
[116] P. M. Vasudev, *supra* note 25 at 21.
[117] John Armour & Priya Lele, *supra* note 1 at 501.
[118] Umakanth Varottil, *supra* note 2 at 33.
[119] *Rakesh Agrawal v. Securities and Exchange Board of India*, (2004) 1 CompLJ 193 SAT.

Appellant and SEBI Vs. Hindustan Lever Ltd.[120] Therefore, SEBI's case makes it evident that finally, with the departure from English law, there was a simultaneous process of following the path of different jurisdictions undertaken by India. It could be analyzed as an unconscious move to adapt laws that suit India's best local conditions. The analysis of transforming from socialism to capitalism post-liberalization in India explains that in this period. India borrowed the idea of a securities regulatory framework from the US. The similar aspect was observed in the amendments made in different statutes facilitating a gradual shift from the colonial past. Further, the 1956 Act was replaced by a new statute with a history of its own where the focus was now on the social responsibility, protection of consumers, and strengthening the corporate governance, whether it was to safeguard the minority shareholders or to solve the problem of concentration of power in few hands.[121]

VII. CONCLUSION

The economic liberalization and the enactment of the SEBI Act 1992 simultaneously led to a new approach in corporate law where the US model was heavily relied upon. All these key developments have proved that the present Indian corporate law and the statutes revolving around it have departed from the transplanted law. This process was more or less unconsciously undertaken by the lawmakers. This work gives a two-plane macro comparative examination of the evolution of Indian corporate law. First, it examines the law as it evolved during the colonial period and how decolonization functioned as a break from the past, resulting in post-colonial developments taking on a very different tone. Second, it examines the post-colonial evolution of corporate law in India and England to identify how India differed from its fellow "common law" family members. Therefore, Indian corporate law, based on the fundamentals of English and American law, has managed to subscribe to a separate jurisdictional approach that could define the Indian corporate law regime uniquely.

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[120] *Ibid.*

[121] For a detailed analysis of these problems Umakanth Varottil, *supra* note 2 at 56-66.

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