Weekly Notes

Narrowly-Held Companies

IF his object is to hit at the root of concentration in the Corporate Sector, the Finance Minister has certainly aimed his blow correctly in discriminating against narrowly-held companies and raising the super tax in the case of such companies by 10 per cent in the budget proposals. But is his shot aimed at only those whom he intends to hit or is he proposing a volley charge against a whole crowd, hoping that he will get those whom he wants, not caring that there would be also unintended victims? And their number must be legion, considering that two-thirds of the 9,500 resident companies assessed to tax in 1960-61 — the latest year for which data are available — were private companies which, being private, are by definition narrowly held. It takes unconscionably long for a company which has ceased to function to finally drop out from the company register, which therefore accumulated much dead wood. This probably explains why as against 9.500 companies assessed to tax, the total number of companies registered in India was about 25,000, of which 19,000 were private companies. Not that all the 6,000 public companies have substantial public holdings to save them from the higher tax now proposed and this would give some idea of the magnitude of the problem of narrowly-held companies which is now sought to be tackled.

The narrowly-held private company is certainly an important instrument, if not *the* instrument, through which both development is most speedily effected and concentration is retained intact or intensified. That this type of company is the most dynamic element in the corporate sector of industry, if one cares for the particular pattern of development it promotes, has been ably argued by a contributor elsewhere in this issue in his defence of the managing agency system. But of the multitude of companies which come under the definition of narrowly-held how many are the dynamic type which are the instruments alike for development and for perpetuation of concentration ?

So though the Finance Minister has undoubtedly shown imagination in going for the offending type, it is surprising that one so astute and knowledgeable about matters of finance should be so little perceptive of the reality of the work-a-day-world.

Not a Homogeneous Group

A NARROWLY held company, the section 104 company of the Income lax Act 1961 (formerly called section 23A company), is defined negatively. It is a company which does not' satisfy all the conditions of a company in which the public is substantially interested, the leading species of this genus being one in which 50 per cent of the voting power is controlled by less than 5 persons, close relatives and nominees being treated as one person. There are others.

These companies had hitherto to distribute compulsorily 50 per cent or more of their profits. This compulsion will no longer apply to such of the narrowly-held companies which engage in manufacturing, processing, mining, power-generation and distribution. In the case of some others too, there will be some relaxation in this respect. But now they are going to be taxed 10 per cent higher while in the past they were taxed at the same rate as the other companies.

There seems to be a conflict of purpose here. While compulsory distribution is waived in order to enable some of these companies to form more capital, the after-tax profit, out of which capital has to be formed, is simultaneously reduced. And the means through which the closely held companies initiate development and deepen concentration — inter-corporate investment — are rendered more potent by the proposed reduction, in tax on inter-corporate dividends. This play of point and counter point, of course, runs through the entire budget, being integral to its basic design.

The Mathai Commission was the first to recommend that there should be discrimination against narrowly-held companies on the ground that they were hardly different from proprietory or partnership firms in which the management could postpone or reduce dividends in such a manner as to reduce the personal tax liability of the shareholders; that the retained profits could be used for personal expenditure rather than capital formation, and that in most other countries, the tax system discriminated against them. It is on the recommendation of the Mathai Commission that the present provisions against them were enacted.

However inconvenient it may be for administrative purposes, the fact is that section 104 companies do not form a homogeneous category. Actually, these companies consist of very different types. There is first the small company formed by a small group of people who have not the means and who have no chance of raising capital by floating shares among the wider public. They do not make inter-corporate transfers and have no scope for any such manipulations and may well be the instrument of operation for the small man coming up. The promotion of the types of enterprise they represent is the professed policy of the government. Or it can be a company which may not need very large capital because of the type of enterprise it engages in and yet must build up adequate reserves. These cannot be marked out as companies which plough back profit in order to help their shareholders, who may be men of only moderate means, to reduce or escape their lax liability. There are so many others. Surely the distinction between one type and another of narrowly-held companies merits examination. It calls for some ingenuity and expertise to separate the tares from the corn. Surely the Finance Ministry is not deficient in such expertise.

Strait-Jacket tor Cooperatives

IS the cooperative movement in danger of being put into a strait jacket through a uniform all-India legislation and standardised operational procedures? This fear stems from the recent proposals to bring cooperatives within the purview of the Banking Companies Act, to put a ceiling on interest rates charged by the cooperatives and to abolish one or more intermediaries in the cooperative federal structure. All