**ROLE OF LAW AND LEGAL INSTITUTIONS IN EMERGINGG ECONOMY: THE INDIAN PERSPECTIVE**

**ABSTRACT**

Role of Law and Legal Institutions is very crucial in the Economic sphere of the State. I will discuss the changes in Law which brought the changes in the economic policy and the changes in the economic policies which brought changes in the Law to highlight the inter-relation of the Law and Economics in the Development of the Indian State. I will examine the process of legislation through which the highly centralized inward-looking economic policies of India came to be transformed into liberalized, outward looking policies. I will show how the country moved towards globalization, liberalization, deregulation and privatization and what were its effects on the economic sphere. What I want to conclude is that in the Government sphere as in the market sphere there is an invisible hand, but operating in the opposite direction from Adam Smiths; an Institution who intents only to serve the public interest by fostering interventions in the economy is led by an invisible hand to promote private interest which was no part of his intention. This concept has been accepted by the Planning Commission of India and that is why it changed its policies by way of the 8th Five year plan and the Role of the Indian State in the private sphere was withdrawn and the private sector was given much wider space to carry on its activities without many interventions, regulations and restrictions.

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**INTRODUCTION:**

Does Law matter for economic development? What is the role of Law and Legal Institutions in the economic development of a country? What are the major economic policies adopted by India after Independence? What is the framework laid down by the Supreme Law of the country i.e. The Constitution of India? What is the way forward and what challenges have been faced by the Constitution in the developing economy of India? How has the Supreme Court of India reacted to the changes? To explore these questions one needs to study the development of economic policies of India after Independence into two main phases one post-independence of a highly regulated, centralized and inward looking import substitution period from 1950 to 1991’s and thereafter to a more liberalized and market friendly approach when India had another tryst with destiny when it had to succumb to the pressure of globalization and International Institutions and change its policies from 1991 onwards. I will showcase the legal structure and the changes in the economic policies and try to analyze and identify the legal changes during different periods. I will try to show the type of legal system on two different aspects: a procedural aspect on whether the legal system is rule based or on administrative discretion; and an allocative aspect whether the distribution of economic resources and means of production is directed to the market or the state. Hence what I will look into and try to find out is whether the legal system is market/rule based; market/discretionary; state/rule based; or state/discretionary.

The economic development for any country has always been full of challenges; throughout history we have seen cases of failures, disappointed expectations, many unsettled questions and unfinished tasks. India embarked its journey when the constitution came into force on 26th January 1950, the people of India resolved to constitute India into a Sovereign, Secular, Democratic Republic.[[1]](#footnote-1) The preamble clearly laid down the grund norm for the development of the country. Economic and development goals were enshrined in the Directive Principles of State Policy (DPSP) which identified certain goals like distribution of material resources for common good, equal pay for equal work, minimum wages, reorganizing the economic system in a way to avoid concentration of wealth in few hands and hence pointing towards the creation of a welfare state. With such high sounding promises and principles India began its tryst with destiny.

The Planning Commission was set up in March, 1950 by a Resolution of the Government of India which defined the scope of its work in the following terms:

“The Constitution of India has guaranteed certain Fundamental Rights to the citizens of India and enunciated certain Directive Principles of State Policy, in particular, that the State shall strive to promote the welfare of the people by securing and protecting as effectively as it may a social order in which justice, social, economic and political, shall inform all the institutions of the national life, and shall direct its policy towards securing, among other things,—

1. that the citizens, men and women equally, have the right to an adequate means of livelihood ;
2. that the ownership and control of the material resources of the community are so distributed as best to sub-serve the common good ; and
3. that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment.”[[2]](#footnote-2)

Having such high sounding objectives to achieve, the planning commission set out its first draft in 1951 for the promotion of the rapid rise in the standard of living of the people. As it is seen from the objectives of the planning commission and the duties created on the state by the DPSP, the economic goals had their origin in the philosophy of the Indian National Congress during the Independence movement which had resolved to adopt a socialist pattern of development.[[3]](#footnote-3) But what happened in reality to the aspirations of millions of people? Did the policies and law alleviate their condition and raise their living standards? How did the state plan its journey towards achieving the ends? What means did it use and to what extend was it able to achieve them? Did the economic plan take us to a dead end having set out to create socialism did we create statism instead?

The emphasis of development theory has always been stifling and shifting like in India from the swadeshi self-dependent movement during the independence struggle to now an interdependent development through the process of “globalization which is considered to be unstoppable and irreversible”.[[4]](#footnote-4) Most of the international institutions and organizations now have a pro-globalization policy and programmes. With the guiding principle of IMF and the World Bank tilting towards free trade and with the creation of World Trade Organization to remove the barriers to trade in goods, services, investment and financial sectors etc. which boasts of a membership of 153 countries[[5]](#footnote-5), the world economy has indeed become more and more interdependent.

1991 is an important landmark year for India; the financial crisis was long brewing mainly due to short term commercial borrowings leading to a serious balance of payment situation. The countries foreign exchange reserves had depleted to a dangerous level and it went through a severe economic crisis, India was almost bankrupt and dialogues were going on with the International Monetary Fund for a bailout package. The crisis was fortunately converted into an opportunity to introduce some fundamental changes in the history of Indian economic thought. India tried to put in place a set of policies at stabilization and structural reforms. The stabilization policies were aimed at correcting the weaknesses creeped into the fiscal and the balance of payment fronts, whereas the structural reforms sought to remove the rigidities that had entered into the various segments of the Indian economy. It opened the economy long closed to foreign investment and trade; it dismantled import controls, lowered customs duties, and devalued the currency; it abolished highly bureaucratized licensing controls on private investment, dropped tax rates, and broke public sector monopolies. Industrial policies were changed to bring about a greater competitive environment domestically and the trade policies were changed to bring about international competitiveness. First time in the history of independent India barriers to entry and the restrictions on growth were removed. First time the private sector was given an opportunity to perform in a competitive environment as many of the areas reserved exclusively for public sector were now allowed for private sector. India was an uncaged tiger now; Gurcharn Das in India Unbound compared the economic reforms with the second independence of the country when he said “we were going to be free from a rapacious and domineering state[[6]](#footnote-6)”. Hence the essence of the reforms in India was to liberalize the market and the market forces. India went through a transition from a socialistic centralized economy into a more liberalized free market economy where the State gradually transferred most of its activities to the private sector. What I will try to examine is the effect of the New Economic Policy and the changes in law and the legal Institution. What challenges it poses to the Constitution of India and how did the Supreme Court react to that?

**Chapter 1: The Legal Structure in India post-Independence**

The Indian State took upon itself the responsibility of the reconstruction and the development of the country as the colonial exploitation had led to the underdevelopment of the economy. The overall objectives of the constitution were to be implemented through the mechanism of the central planned economy. The pre independence experience was combined with that of the experience of the socialist countries in particular the Soviet Union and India’s first five year plan was drafted keeping in mind with that of the first Soviet five year plan. In that period the dominant view in the economic thought was that the government had an important role to play in the development of the economy and there was a complete distrust of the markets. It was believed that the demand for Indian exports would not grow fast enough to be a major source of growth as it would not sustain the international competition, it was believed that private savings would not be adequate to finance capital accumulation and would need to be supplemented by public resource mobilization; it was believed that the growth of the organized industrial sector would not on its own provide for adequate employment creation and hence the need to create direct programs on employment; there was a distrust of foreign companies as well as domestic industrial houses. Along with this distrust of the market forces there was great faith in the ability of the administrative system to allocate resources and fulfill the promises given by the Constitution of India to its people. Hence this lead to the foundation of an elaborate system of direct controls in a market economy that intervened in almost all levels of decision making. We will see how the government through the process of law tried to curb individual freedom and restricted private enterprise and the functioning of market mechanism.

* 1. **Law Governing Property Rights including right to Land:**

Property rights have been defined by Kaushik Das in his article The Right to Property[[7]](#footnote-7) as a bundle of entitlements defining the owner’s rights, privileges and limitations for use of a resource. Universal Declaration of Human Rights, 1948 under Section 17(i) and 17(ii) recognizes right to property as: “17(i) Everyone has the right to own property alone as well as in association with others. (ii) No-one shall be arbitrarily deprived of his property.” Property Rights have to an extent been suppressed in India by the socialist planners as they believe in having all the means of production under the ownership of the state. As private property along with free trade and liberty form the pillars of the free market economy they are considered to be important factors for running the economy in a capitalist society whereas private property in India is considered to be the root cause of disharmony and disparity. The Indian Constitution provides that to promote the welfare of the people concentration of wealth and means of production should not be accumulated to the common detriment[[8]](#footnote-8) and the ownership and control of the material resources should be distributed to sub serve the common good[[9]](#footnote-9). Looking at the land reforms that took place in India, how they tried to achieve the principles enshrined in the Constitutions Directive Principles of State Policy, how it was in conflict with the Fundamental right to property[[10]](#footnote-10) guaranteed under the Constitution of India and how the legislature and judiciary were in constant conflict with each other to change the laws. Let us study the Constitutional position of law relating to property at the beginning of 1960 which was as follows:

i) the individual had a fundamental right to acquire, hold and dispose of the property[[11]](#footnote-11);

ii) the State could not deprive the property of an individual without the authority of law[[12]](#footnote-12);

iii) the State could not acquire any property without granting compensation for the same and either had to fix the amount of compensation or specify the principles on which it would be granted. This was subject to some limitations that the act of acquiring the property could not be questioned on the ground that the compensation fixed was inadequate. The prerogative to fix the amount of compensation whether adequate or not was with the Legislature[[13]](#footnote-13).

The State was however required to acquire or require[[14]](#footnote-14) the land only for public purposes;

(iv) the right of an individual to challenge any legislation relating to land laws was limited, viz., such legislation could not be challenged on the ground that they violate fundamental rights[[15]](#footnote-15); and

(v) the restriction mentioned in (iv) above was supplemented by providing that any act

inserted into the Ninth Schedule to the Constitution could not be challenged on the

ground of violation of fundamental rights[[16]](#footnote-16).

Hence we can see how the right to property was being diluted by the legislatures by bringing Constitutional Amendments and nullifying the decisions of the Supreme Court and how the Supreme Court was adamant in protecting this very fundamental right of the citizens. The major difference between the judiciary and the legislature was with regard to compensation when Supreme Court decided in Vajravelu vs. Sp. Dy. Collector[[17]](#footnote-17) and the Bank nationalization Case[[18]](#footnote-18) held that the constitution guarantees a right to compensation equivalent in money of the property compulsorily acquired. The parliament was dissatisfied with this view and it brought many amendments to the constitution mitigating the scope of compensation and tried to protect the laws aimed at implementing the directive principles of state policy from judicial review. After series of judgments and amendments the debate was sought to be closed with the 44th Amendment Act, 1978 by which article 19(1) (f) the right to acquire, hold and dispose of the property was removed from the fundamental rights and was turned into a mere constitutional right which expanded the power of the state to appropriate property for social welfare purposes without granting sufficient compensation.

Let us now consider the other changes in the land reforms law post independence. They were very much on the socialistic pattern of development that India undertook. It was quite apparent with the way in which legislations were passed and laws were changed. From 1948 onwards every state had started enacting legislations for land reform for the equal distribution of land amongst the people. Zamindari(landlord) System was abolished with every state coming up with its own abolition acts after the identification of certain important factors such as excess land holding, nature of tenancies different forms of land relationships, fixing of land ceiling, acquiring and redistributing excess land etc. The land holdings were identified to ensure that the tiller should also get the ownership rights. While some states went in for a comprehensive legislation[[19]](#footnote-19) others went in for different legislation for each purpose[[20]](#footnote-20).

 Briefly examining the Gujarat Tenancy and Agricultural Lands Act, 1948 to understand the broad pattern of land reforms, the Act, 1948 was brought into force in order to amend the law relating to tenancies of agricultural lands and to make certain other provisions. The reason it was enacted was on account of the neglect of the landholder or disputes between a landholder and his tenant due to which the cultivation of the estate had seriously suffered. It was enacted for the purpose of improving the economic and social conditions of peasants and for ensuring the full efficient use of land for agriculture. The Government therefore thought it fit to assume the management of estates held by landholders and the Government attempted to regulate and impose restrictions on the transfer of agricultural lands, dwelling houses, belonging to or occupied by the agriculturists. The Act, 1948 has various chapters dealing with tenancies, provisions for distribution of land for personal cultivation, management of estates held by landowners, restriction on transfer of agriculture land etc. It has deeming provision whereby a person lawfully cultivating any land belonging to another person become the tenant and thereafter the provisions of the Act, 1948 provide deeming fiction to the tenants to have purchased the land on the tillers day subject to the procedure followed as laid down under the Act, 1948. So the land of the landowner now becomes the land of the tenant. Almost all States enacted similar piece of legislation and they were placed under the 1st Schedule of the Constitution so they were immune from challenge on the grounds of violation of fundamental rights guaranteed under the Constitution.

Another legislation which was passed to enforce the provisions of the Directive principles of state policy was the Urban Land (Ceiling and Regulation) Act, 1976 (hereafter ULCRA). The main objective of the act was preventing the concentration of urban land in select few hands and to bring about an equitable distribution in urban conglomerations to subserve the common good and to accomplish these objectives it tried in every possible manner to curb and restrict the right to property and liberty and also put restraint on the Judiciary to enter into the challenge to such piece of legislation. It imposed a ceiling on the vacant lands in urban agglomerations[[21]](#footnote-21). Land over the ceiling was treated as excess and vested in the state[[22]](#footnote-22). Transactions in such access land were not permitted[[23]](#footnote-23). It had undermined the operation of the land markets to a great extent.

This shows how highly the land markets and the property rights have been regulated despite the right to property being a Fundamental Right guaranteed by the Constitution to every citizen of the Country; state assumed the right to take away the property at its whims and fancy in the name of public good and common detriment. These legislations are a classic example of what Frederic Bastiat termed as “Legal Plunder” where the law has been perverted in order to make plunder look just and sacred to many consciences. The implementation of these acts were also very disappointing as it granted too much of discretionary power to the state, compensation was too low and led to lengthy litigation battles. Rather than increasing the supply it created an artificial scarcity of land and the prices skyrocketed. This is a classic example of what happens when the state tries to meddle with the market mechanism and the market forces therefore it is important for the state unless absolutely necessary to intervene in the demand and supply system of the economy.

**1.2 Labor Laws**:

Indian labor jurisprudence derives its source from the Directive Principle of State Policy which require the State to direct its policies or by passing of legislations towards securing the health and strength of workers[[24]](#footnote-24), securing the right to work[[25]](#footnote-25), securing just and humane conditions for work[[26]](#footnote-26), securing a living wage, conditions of work ensuring a decent standard of life and full enjoyment of leisure and social and cultural opportunities[[27]](#footnote-27), secure the participation of workers in the management[[28]](#footnote-28) by recognizing the right to a union and hence creating a web of social security for a welfare state. Plethora of laws governing all these aspects have been drafted such as The Industrial Disputes Act, 1947, creating a mechanism for ensuring the dispute settlement between the employers and the employees. The Payment of Wages Act, 1936, ensuring the payment of wages on time and without unauthorized deductions. The Minimum Wages Act, 1948, which aims at prevention of exploitation of workers by fixing the minimum wage rates, the Workmen’s Compensation Act 1923, to create an effective mechanism to compensate the injured workmen. The Employees Provident Fund and Miscellaneous Provisions Act 1952, Employees State Insurance Act, 1948, The Maternity Benefit Act, 1961 and the Payment of Bonuses Act, 1961.

The basic structure of the labour legislation is very much pro-labour. For example lets consider one such aspect of removal of workers by the companies. There have been a series of judicial decisions such as Chandulal vs. Management of Pan American Airways[[29]](#footnote-29), Central Inland water transport Cooperation vs. Brojo Nath Ganguly[[30]](#footnote-30) etc. which have completely narrowed down the right of the employer to terminate any employee from service. Termination was limited only after an elaborate domestic enquiry which proved the charges of misconduct against the employee. Retrenchment and layoffs were under numerous controls and even if they were permitted the judiciary would always intervene and protect the labourers[[31]](#footnote-31). The pro-labor provisions of the Industrial Disputes Act 1947 provides that; no workman who was in continuous service for one year can be retrenched without a prior notice of one month[[32]](#footnote-32) and without a prior permission from an appropriate government[[33]](#footnote-33). The employer who intends to close down the undertaking of an industrial establishment has to serve a 90 days’ notice for obtaining the permission of closure from the appropriate government and such permission has to be obtained before the closure[[34]](#footnote-34). Apart from that the employer has to pay compensation to the employees before closing down the industrial establishment[[35]](#footnote-35). The judicial intervention has extended the scope of protecting the weaker sections in trying to comply with the Directive Principles of State Policy though they are not justiciable they have been tried to be implemented in practice. These trends have precluded establishments from carrying out large scale restructuring, relocating or exiting from the industry. Rigid employment laws have led to development of larger informal sector and higher unemployment. Besley and Burgess data on labor regulation shows that the pro-rigidity amendments to the Industrial Disputes Act 1947, are associated with lowered investment, employment, productivity, and output in registered manufacturing, regulations in a more rigid direction is also associated with increase in urban poverty[[36]](#footnote-36). The economic survey undertaken by the Ministry of Finance in India has also shown that “Indian labour laws are highly protective of labour, and labour markets are relatively inflexible. These laws apply only to the organised sector. Consequently, these laws have restricted labour mobility, have led to capital-intensive methods in the organised sector and adversely affected the sector’s long-run demand for labour. Labour being a subject in the concurrent list, State-level labour regulations are also an important determinant of industrial performance. Evidence suggests that States, which have enacted more pro-worker regulations, have lost out on industrial production in general”[[37]](#footnote-37).

The role of competition has also been suppressed in the Indian Markets and is not allowed the proper functioning of the free markets. Milton Friedman explains the importance of competition when he says that “a worker is protected from his employer by the existence of other employers for whom he can go to work. An employer is protected from exploitation by his employees by the existence of other workers whom he can hire. The consumer is protected from exploitation by a given seller by the existence of other sellers from whom he can buy. Why do we have poor postal service? Why poor long distance train service? Why poor schools? Because in each case there is essentially only one place we can get the service.”[[38]](#footnote-38) This is what happens as we try to curb competition thinking it would exploit the laourers, consumers and the general public.

**1.3 Laws Governing the Financial Markets:**

Capital is another important aspect for the means of production let us look at the laws of the Financial Markets. The Bombay Securities Contract Control Act, 1925 was the first legislative piece concerning the legal regime of securities but it was not very effective and had many loopholes such as it made the transactions in violation of the act as void and not illegal. Hence it had to be changed and a new legislation viz. Securities Contracts (Regulation) Act (hereinafter SCRA), 1956 was enacted to provide for direct and indirect control of virtually all aspects of securities trading and the running of stock exchanges and to prevent undesirable transactions in securities by regulating the business of dealing therein as well as in securities and for the purpose of recognition and regulation of stock exchange. Trading in stocks exchange was considered to be very speculative and leading to undesirable transactions and hence the act prohibited trading by “options”[[39]](#footnote-39). As these transactions were conducted in stock exchange the act also sought to regulate the stock exchange itself[[40]](#footnote-40). The act required that the transaction must be routed through a recognized stock exchange[[41]](#footnote-41) and every other transaction were made illegal[[42]](#footnote-42). Therefore the new enactment made the regulation of securities much stricter after independence. Being the central legislation it was uniform throughout India and hence the trading environment in the entire country remained stagnant as it was highly regulated till 1990.

Another legislation The Capital Issues (Control) Act, 1947 was enacted to regulate the market for primary issues of shares or stock in the capital of companies. The requirement of the consent of Central Government was must before any company could be incorporated, require issue of capital, for making a public offer or for sale of any security, or renew or postpone the date of maturity or repayment of any security maturing for payment in the state. The complete control of the central government was exercised by the Comptroller of Capital Issues (CCI) on all matters relating to the primary market. Equity was severely underpriced by the CCI due to which it created a bias in favor of debt as it raised the cost of equity.

Forward trading was also regulated by way of the Forward Contracts (Regulation) Act, 1952, it regulates forward contracts and options in relation to goods, it also empowers the central government to prohibit forward contracts and options in public interest[[43]](#footnote-43). The act outlawed forward contract in notified goods[[44]](#footnote-44). The growth of forward market could have played an important role in providing insurance to the cultivators in the agriculture sector but it was never really allowed under strict regime of rules and regulations prescribed by the Act.

The Negotiable Instruments Act passed in 1882 which is still in existence and operating in the modern Security market in India. This act is quite outdated and cannot hold good for the present day securities market. The definition of negotiable instruments[[45]](#footnote-45) under the act is very rigid and needs to be changed with the modern demands of the time; such a rigid definition does stand in way of the development of the securities markets in India. The laws in India are not keeping in pace with the modern practices, in the commercial market there are many indigenous and modern instruments which change hand to hand which are not given the status of Negotiable Instruments under the rigid definition provided by the act. Until 1988 dishonor of cheque for insufficiency of funds was just a criminal offence and there was just a criminal remedy to it. All these factors led to the under-development of the financial markets in India.

An efficient and well developed financial market is very essential for the sustained economic growth of the country. Intervention in the securities market were created for the government to expropriate much of the revenues and control and direct the flow of funds for favoured uses rather than on sound projects and hence what it did was the rate of return of some investments went into negative while profitable opportunities were foregone. Hence the average rate of return was much lower than it should have been. The chairman of Securities Exchange Board in India in his speech had said “the securities markets could have fostered economic growth, as it would have increased the quantities of real savings and capital formation from a given level of national income and it would have raised productivity of investment by improving allocation of investible funds”**[[46]](#footnote-46).** Market efficiency requires transparency, prevention of unfair trade practices and increasing the level of Indian markets to the International standards. All three of these factors were being stalled by the unnecessary rules and regulations provided by the legislature and hence not allowing the potential growth of the financial system in India which remained stagnant till 1990’s.

**1.4 Banking Sector in India:**

India’s Independence marked the end of a regime of laissez faire for the Indian banking as the government started taking active role in the economic life of the country. The major step to regulate the Banking sector was the nationalization of the Reserve Bank of India by passing the Reserve Bank of India (Transfer to Public Ownership) Act, 1948. Another act to regulate the Banks was the enactment of the Banking Regulation Act, 1949 which empowered the RBI to regulate, control, and inspect the banks in India[[47]](#footnote-47).

Being the Central Bank of India RBI plays a key role in a highly regulated economy. It is the Banker to the Central Government and has the obligation[[48]](#footnote-48) and a right[[49]](#footnote-49) to manage public debt, transact government businesses, the right to issue bank notes[[50]](#footnote-50) and such other conventional Central banking tasks. Though private banks were allowed to practice in the 50’s and the 60’s they were heavily regulated and controlled by the RBI and the Banking Regulations Act, 1949. The private banks were never comfortable with the ruling ideology of the time of centralization and socialism and therefore could not function properly. Major changes occurred in the banking sector, in 1969 when the Central Government promulgated the Bank Nationalization Ordinance, nationalizing 14 largest commercial banks, after the issuance of the ordinance the parliament passed the Banking Companies (Acquisition and Transfer of Undertakings) Bill and hence the Banking sector was nationalized in the 70’s. With this the muscle of the state was also brought into the banking sector, as a result majority of lending was done at a subsidized interest rates. This in relation with poor credit appraisal procedures, poor accounting norms for sub-standard assets led to an increase in non- performing assets. Due to the change in the labor laws the bargaining power of trade unions increased and they started raising unreasonable demands, they showed resistance to mechanization and computerization. As protection from discretion and equality in matters of promotion and transfer plus heavy reservations for the lower castes in India was provided in the Constitution of India, the emoluments and the incentives of the staff were not in relation to their productivity and profitability. This was a major cause of lack in efficiency, red tapism, incompetence etc. in the banking sector. Moreover administered rates created restrictions on earning capacity which leads to poor profitability and efficiency in the Banking system. Therefore the banking sector in India could not develop and could not compete with the international Banking Market as it was regulated.

Even the Supreme Court did not show any respite to the private sector and in Akadashi Pradhan vs. State of Orissa[[51]](#footnote-51) it upheld the creation of monopolies as not violative of the fundamental right to carry on trade, profession and business, on the basis that the Indian Constitution has chosen the doctrinaire version of Socialism in which nationalization is a matter of principle and its justification is the general notion of social welfare and hence all important and nation-building industries should come under the control of the State. According to the legislature, law relating to the creation of state monopoly should be presumed to be in the interest of general public. The fundamental right to freedom of trade and business can be restricted under the ambit of public interest. Therefore many Public Sector Undertakings and Public Corporations were formed through the process of nationalization. Air transport was nationalized in 1953 by passing the Air Corporations Act, 1953; the Life Insurance Sector was taken over by the passing of Life Corporation Act, 1956. The entire [general insurance](http://en.wikipedia.org/wiki/General_insurance) business in India was nationalized by the General Insurance Business (Nationalization) Act, 1972. The [Government of India](http://en.wikipedia.org/wiki/Government_of_India), through Nationalization took over the shares of 55 Indian insurance companies and the undertakings of 52 insurers carrying on general insurance business. The Coking Coal Mines (Emergency Provisions) Act, 1971 provided for taking over of the management of Coking Coal Mines and Coke Oven Plants in the Public Interest, this was then followed by the Coking Coal Mines (Nationalization) Act, 1972 nationalizing the Coking coal mines and the coke oven plants and created a new central government undertaking. Another law was passed in 1973 Coal Mines (Nationalization) Act, 1973 which was made the central piece of legislation determining the eligibility of coal mining in India. Apart from these posts, telegraphs, railways, power, communication sectors were also under the control of the Government. Moreover just to protect the jobs of the workers the government took over many units from private hands as they were about to close down. Public money was used in protecting jobs of workers rather than creating new opportunities for more jobs.

**1.5 Law Governing the Private Economic Activity**

The freedom and liberty of private sector was circumscribed in many ways by number of rules, regulations and restrictions. The state was regulating almost all the spheres of private business it had wide ranging powers for “regulating or prohibiting the production, treatment, storage, movement, transport, distribution, disposal, acquisition, use of or consumption of articles or things whatsoever. Besides these the state regulated the use and control of foreign exchange, the pricing and distribution of essential commodities by way of different acts and establishing agencies and instrumentalities of the state. The Industrial (Development and Regulation) Act, 1951 was enacted to undertake the development and regulation of the industries and activities by bringing them under the control of the state and many new industries have been added under its ambit. A study of the World Bank in 1987[[52]](#footnote-52) pointed out that between 1981 and 1985 43% of license applications were rejected on the ground of adequate capacity and the allocation of licenses were subject to substantial delays. Entrepreneurship was killed at its birth and hence entire private sector became incumbent. It was believed that if the state would intervene in the economic sphere and regulate it with legislations the interest of the people at large would be taken care of, market regulations was seen in the interest of the public welfare as there was distrust of free markets in the political thought of that time.

In matters relating to Insolvency and Bankruptcy colonial outdated laws still governed this area in India. There was clear law on bankruptcy and in fact there was significant confusion in the meaning of the terms bankruptcy, insolvency, liquidation and dissolution till the parliament enacted the Insolvency and Bankruptcy Code 2016. In a survey[[53]](#footnote-53), it was found that an insolvency petition took more than a decade to complete its proceedings. Such huge delays occurring in completing the procedure for insolvency are unacceptable for a growing economy. Companies could be wound up under the Companies Act, 1956 in which the procedural requirements were too many causing delays in winding up of the companies. The main reasons for the delay as showed in the Development Discussion Paper[[54]](#footnote-54) in insolvency cases are inexperienced judges; direct handling of the insolvents property by the court through ad-hoc appointments; absence of skill oriented training available to judicial officers as well as receivers; complexities due to varied nature of claim and preferences and the evidential system in an adversarial jurisprudence.

Under section-433(e) of the companies Act, the court has the power to issue winding up proceedings if the company is unable to pay its debts. But security of the secured creditor is subject to a pari passu charge in favor of the workmen to the extent of his portion therein. In this case to protect the workmen’s right the winding up procedure could be stopped as it would be against the public interest of the workmen. Section-25(O) of the Industrial Disputes Act, 1947 provides that no industry can be closed without the prior approval of the state government concerned. Hence winding up of a company was also not an easy task in India considering the legal requirements and the delays in the court procedure.

**1.6 Exchange Control:**

To limit the use of foreign exchange Foreign Exchange Controls Act, 1973 was enacted. Like most of the contemporary acts it also created a regime of prohibitions, permissions, licenses and exemptions in relation to activities dealing with foreign exchange. The act prohibits all private transactions in foreign exchange unless approved by the RBI. The act contains many restrictions and regulations in relation to activities or transactions affecting foreign exchange. The act prohibits all exports if the value of the goods being exported is not equal to the market value of that good. The RBI can also withhold the shipping documents till the payment is corrected according to the market value. The transaction relating to goods is completely contractual in nature yet the RBI has been given enough powers to interfere as national interest is at stake. Permission is required for taking or sending of a security outside India, issuing, creating or transferring an interest to any person outside India of securities registered in India. The act prohibits persons residing outside India to acquire, hold, transfer or dispose any immovable property in India. Restrictions have been laid down if any foreign company wanted to do business in India. Due to all these regulations foreign investment was severely damaged, foreign investments which could have provided an inflow of capital, funds, increase in transfer of skills, technology and job opportunities as well as local productivity growth was deprived from the citizens of the country only in the name of public interest.

**1.7 The Road to Serfdom:**

An erroneous model of development can betray the aspirations of the young generation; they suppressed growth and jobs and denied their people to rise above poverty. The worst indictment of Indian Socialism is that in the end it did very little for the poor. There are many reasons for this; India adopted an inward looking, import substitution path rather than outward looking export-promoting path denying itself its share in world trade and the prosperity it could have brought. Two, the set-up of massive monopolistic public sector to which it denied autonomy of working; hence the public investments were not productive and India had a poor capital output ratio. Three, overregulation of private enterprise with the most controls in the world, diminished competition completely from the market; besides the merchant-businessman were not tinkerers and were slow to innovate. Four, it discouraged foreign capital and denied itself the benefits of technology and world-class competition. Five, it pampered organized labor to the point where it had extremely low productivity. Six, it ignored the education of majority of the children, especially of girls.

Hence, India’s per-capita income remained $450, which placed it 162nd out of 206 countries in the World Development Report for 2000-20001. In 1960 it was higher than china’s, but reduced to its half. Although by purchasing power parity India’s income rose to $2,149, which lifts its global rank only marginally, to 153rd. Half the Indian people are poor by the international poverty line of one dollar per person per day, and a third of world’s poor are Indian. An Indian’s life expectancy is 63 years, lower than that in many poor countries. As many as 65 out of a thousand infants die; two-thirds of the children suffer from malnutrition and are underweight.

Seventy-one percent cannot access sanitation. Four out of ten Indian’s are illiterate. Therefore India is ranked 134th out of 174 countries on the United Nations Development Programs Human Development Index.

The Nationalized industries proved to be ineffective and generated huge losses hence the illusion of nationalization increasing productive efficiency was washed away. There was widespread dissatisfaction with the welfare activities as they showed disappointing results. The welfare program turned into a mess saturated with fraud and corruption. The failure of the well intentioned programs is not because of the mistakes in execution but because of the use of bad means to achieve good objectives. High inflation, high unemployment, opposition to taxes, emigration of some of the talented people, stagnation in productivity and real income have been the outcomes of the welfare state. It became the holy cow which no politician could question. The central economic planning which was seen as dawn of a world of plenty shared by many turned into tyranny and misery in India. Suspension of the price mechanism and replacement of the market by a centrally directed economy was a major obstacle to growth and development in the Indian economy.

The root of the evil is thus the unlimited power of the legislature in India which passed many regulatory legislations restricting and prohibiting the development of the private sector. John Locke in “Classical Theorists of Representative Government” said that “in a free state even the power of the legislative body should be limited in a definitive manner, namely to the passing of laws in the specific sense of general rules of just conduct equally applicable to all citizens.” This was the fundamental belief of the classical liberalism; coercion should be limited to the enforcement of general rules of just conduct. F.A.Hayek in New studies in philosophy, politics, economics and the history of Ideas said that “differences in wealth, education, tradition, religion, language or race may today become the cause of differential treatment on the pretext of a pretended principle of Social Justice or of public necessity. Once such discrimination is recognized as legitimate, all the safeguards of individual freedom of the liberal tradition are gone.” This is what had happened, individual freedom in the name of social justice, welfare state and public necessities have been subjugated and the people of India have been kept deprived of those rights and freedoms as the individual rights come secondary to the state. Social or Distributive Justice is achieved only at the cost of Individual Justice. It requires the society to be just rather than the individual in determining the shares of the individuals in the social product and to achieve a just distribution it is imperative for the government to decide and direct the individual in what he must do rather than allowing him to act in his own volition. This is what has been termed as the “mirage of social justice”.

Jeremy Bentham had said that “Every law is an evil for every law is an infraction of Liberty”. French Declaration of Man and of Citizens, 1789 says “Any society in which rights are not securely guaranteed, and the separation of powers is not determined, has no constitution”. The problem is not Democracy but unlimited Democracy, the Government has to be ‘under the law’ and it cannot act above law. The rule of law is a necessary safeguard for individual freedom and against as it lays down restriction on the Government and permits coercion only to enforce obedience to general rules of individual conduct applicable equally to all. The triumphant claim of the parliament to have become sovereign to such an extent that it can govern under no restrictions has been the death knell of democracy and individual freedom specially during the period from independence when plethora of legislations to divulge into all spheres of the economic activities of the State. What is to be achieved is the division between government and the legislative assembly and restrictions have to be brought to restrain the government from interfering in matters relating to individual freedom and liberty. The Supreme Court has tried to restrain the government from changing the basic Structure of the Constitution and the Constitution also puts the legislature under some restrictions but the problem lies in not realizing the individual freedoms and liberties of the citizens in achieving their pursuit of happiness under that basic structure of the Constitution which the legislatures cannot alter. India initiated a proliferation of restrictions on what to buy and sell, from whom to buy and where to sell on what terms, whom to employ and whom to work for, where to eat how much to eat and what to drink, how much to earn by guiding private industry through central planning became ineffective and misleading and destructed the competitive market, free enterprise turning to a totalitarian Socialist Statism resulting into disastrous loss of personal freedom.

**Chapter 2: The Legal Structure post Liberalization:**

As the post-Independence era was one of shattered dreams and unfulfilled promises which the Preamble of the Constitution had shown, we had certainly led the founding fathers of our constitution down by taking the wrong road to development. The economic policies had certainly failed and India was at the verge of defaulting on its foreign exchange obligations and the International Community was not ready to bail out the country without a commitment to vacate it’s over occupied space in the economy and allow the market forces to manage the economic problems. Hence India had no other option but to break away from its past and be replaced by the phenomenon of globalization, liberalization, deregulation and privatization. The birth of the New Economic Policy in India can be understood by twofold explanation. If one looks at the global perspective and the New World Oder of the 1990’s emerging due to the collapse of USSR and the European Socialist Countries at the end of the Cold War the entire world was moving towards a free market system. Globalization of the Indian Economy and its integration with this new world system had become imperative as India did not want to be left behind and marginalize itself from the new global political and economic situations. Another reason is the obvious State-led development of India arriving at a dead end. The state-regulated economy had become completely dysfunctional and the state sector instead of acting as an engine of growth became responsible for the deep crisis of the economy. An eminent Indian economist said that “History has its unforeseen ironies. The post-war period, now spanning four decades through the 1980’s, began with both a strong economic performance and western empathy and approbation of India’s development efforts and ideas. It ended with an economy in serious difficulty and, worse, the perception that India had not merely chosen the wrong economic path but had also marginalized herself in world economic affairs in consequence”[[55]](#footnote-55). Hence began the reforms of 1991 liberalizing India from its past.

**2.1 The 1991 Financial Crisis: State Failure**

One of the main reasons for the crisis of 1991 was inflation caused by expansionary monetary and fiscal policy which hindered the exports to a great extent and led to consistent trade deficits. The Soviet Model of foreign trade followed by the Indian Government viewed exports as an evil whose sole purpose was to earn foreign currency with which to purchase foreign goods which could not be produced at home. Because of this reason the government did not encourage exports and led to an inward- looking import substitution policy. Hence due to inadequate incentives on exports the Indian Economy missed out the gains from comparative advantage exports could have brought to the country. India’s Balance of Payment problems began from 1985 onwards, it had consistent current account deficits as imports continuously increased and so did the interest payments. Because of the Gulf War there was a drastic rise in the oil price which increased the burden on imports in India. According to the RBI Bulletin of 1991 the trade deficit in India in 1990 was US $9.44 billion and the current account deficit was US $9.7 billion, foreign currency assets fell to US $1.2 billion[[56]](#footnote-56). These factors destablished an already unstable economic situation brought by inflation and debt. India was left with no other option but to liberalize its economy and break away with its past to join hands with the New World Order.

**2.2 People must operate and the Government must cooperate**

The New Economic Policy aimed at shifting the State-centered and state-led development to export-led industrialization with great encouragement to foreign investment and technology. The fiscal deficit in India had to be curbed, limited and eliminated by way of the structural adjustment model provided by the IMF and the World Bank. Which means that the public institutions and the public investments will have to be displaced by the market determined investments and production decisions. The pre-requisite for the foreign borrowing in the financial crisis was the macro-economic stabilization, structural adjustment and fiscal reforms. Deregulation of the Indian Economy and allowing the free-play of market forces to determine the economic decisions, international trade, international finance and international investment which would act as new engines of growth for the country was imperative.

Liberalization and globalization are two interrelated pillars of the new journey which India undertook. The challenge to the liberalization of market in an Indian context is to consider the policies for poverty elevation, improved nutrition, higher employment, better living standards etc. Professor Amartya Sen opined that “the removal of barriers to using markets can significantly enhance opportunities, the practicable usability of these opportunities requires the sharing of certain basic capabilities including those associated particularly with literacy and education, basic health, social security, gender equality, land rights, local democracy and related matters”[[57]](#footnote-57). This shows that there are some important areas where the government would still have to play an important role. The free market advocates would want the state to become invisible and the government to have no role in the market economy, which is the ultimate goal of liberalization of markets. This viewpoint has gained great respectability after the collapse of Socialism in USSR, Eastern Europe and the economic reforms and the structural changes that were taken by these countries have tried to create free markets by destroying the state owned enterprises.

 The founders of the Liberal Constitutionalism had hoped to protect individual liberty by providing with separation of powers between the executives, legislatures and the judiciary. It is also the basic feature of the constitution of India. Coercion could only be permissible for the enforcement of universal rules of individual conduct sanctioned by the legislature. The essence of the free society is that the private individual is not one of the resources which the government administers and that a free person can count on using a known domain of such resources on the basis of his knowledge and for his purpose. This is the characteristic of free markets where the individual is allowed to use the resources for his own purpose on the knowledge he possesses. By removing the restriction on the economic sphere the state has to take a back seat and allow the markets to be free from its interference and allow the free flow of information in the market to create a spontaneous order that benefits all the players in the market. A truly free market society is one which primarily relies on voluntary exchange through the market to organize their economic activity and in which government is limited to the three main duties as specified by Adam Smith for a laissez faire economy viz. the duty of protecting the society from the violence and invasion of other independent societies, duty of protecting every member of society from the injustice or oppression of every other member of it, or duty of establishing an exact administration of justice, and the duty of erecting and maintaining certain public works and public institutions for the good of the great society. A society where there would be the highest standard of living, no restraints on international trade, and no government directions on economic activities would be a modern example of a free market economy and would be the imaginary utopia every society wanting to achieve.

**2.3 Eight Five Year Plan in India 1992: From Serfdom to Freedom**

The planning commission in India also recognized that development could be ensured by freeing the economic activities from unnecessary controls and regulation and withdrawing the states intervention from the economy. The 8th five year plan was launched in 1992 which aimed at providing much greater impetus to private initiative in industrial development and to withdraw the public sector from its myriad activities and making it selective. It aimed at rolling back the public sector investments from those sectors of the economy where the private sector could be moved and the state can increase its investments in the social sector. This plan laid more importance on “performance improvement, quality consciousness, and competitiveness, efficiency of operation and completion of projects on time rather than concentrating on its allocative role and giving out central directions[[58]](#footnote-58)”.

The plan also criticizes the public sector performance, it recognizes that the public sector was assigned authoritative heights in the economic scene and it was expected to create the “basic infrastructure for development, be a pace setter in taking risk and nurturing entrepreneurship, take care of the social needs, help the poor and the weak and create an environment of equal opportunities and social justice[[59]](#footnote-59)”. The public sector expanded considerably and in such a manner that it touched every aspect of life. In this process, it had made the people take public sector for granted, oblivious of certain crucial factors like efficiency, productivity and competitive ability. This eroded the public sectors own sense of responsibility and initiative and many of these enterprises became slow moving, inefficient giants. A certain amount of complacency had set in which was not conducive for growth and it was the 8th plan that took up the task of reorientation of the public sector. The plan also undertook a re-examination of the role of government as well as the process of planning in the economic development. This required the working out of ways and means of involving people in the development task and social evolution. Hence planning was to be made more indicative it would have to create a culture of high productivity and cost efficiency in the government both at the Centre and the State. The emphasis was on autonomy and efficiency induced by competition. In order to achieve what was set forth in the objectives it was necessary to shed off some of the practices and precepts of the past which had outlived their utility and to adopt new practices and precepts, in the light of the experience gained by India and by other nations. The plan also accepted the failures of the previous development plans and policies. It accepted that vested interests had got established in the regulatory framework and they often gained through the system at the cost of the consumer and the common man.

 The distribution of assets were sought to be pursued in an equitable manner, but this failed as land reforms could not be implemented effectively. The land reforms were necessary to tackle the problem of poverty through growth, which itself was slow over a long period of time. The plan suggested that “the imperatives of growth in the face of these challenges required an innovative approach to development which was based on a re-examination and re-orientation of the role of government, the harnessing of the latent energies of the people through peoples involvement in the process of nation building and the creation of an environment which encourages and builds up peoples initiative rather than their dependence on the government and which sets free the forces of growth and modernization. The state is required to play a facilitating role and has to concentrate on protecting the interest of the poor and the underprivileged[[60]](#footnote-60)”. Systems of control and regulation, developed for good reasons in the past had outlived their utility and they stood in the way of further progress. Such dysfunctional system had to be overhauled in the light of emerging realities. The industrial regulatory environment of the past had led to certain unintended results which in turn had contributed to the weaknesses in the industry. Domestic competition had often been restricted, leading to lack of quality and cost consciousness in segments of industry. The level of protection offered to Indian industry, by way of quantitative import restrictions and tariffs, had been too high leading to high costs of production and inadequate technological dynamism. These weaknesses had to be removed in the context of global economic trends which require a high degree of competitiveness. Indian industry was ready to face the full pressure of domestic competition and had to prepare itself to face international competition.

The public sector was made more selective in covering activities and making investments. The main changes made by the planning commission for the public sector were as follows:

1. “The public sector should make investments only in those areas where investment is of an infrastructural nature which is necessary for facilitating growth and development as a whole and where private sector participation is not likely to come forth to an adequate extent within a reasonable time perspective;
2. The public sector may also withdraw from areas where no public purpose is served by its presence. The public sector should come in where the investment is essentially for preservation and augmentation of basic resources of the country, like land, forest, water and ecology, science and technology or for running key infrastructural activities. The public sector will have responsibility for meeting social needs or for regulating long-term interests of the society like population control, health, education, etc.
3. In large parts of public sector operations where commodities or services are produced and distributed, unless it is necesary for protecting the poorest in the society, the principle of market economy should be accepted as the main operative principle. It means charging as per cost and costing with full efficiency in operations”[[61]](#footnote-61).

This clearly shows that the main emphasis of the 8th five year plan was to withdraw the State from interfering too much in the economic activities and the principles of market economy were accepted in the future dealings of the economy. This shows that there was a clear shift from the previous ideologies and they were given up and India was now ready to march ahead with the ambition of creating a freer market with less interference from the State for its people.

**2.4 Major Economic Reforms:**

As India was going through a major crisis, the reforms were carried out in two main areas, first being the macro-economic reforms for crisis management dealing with the balance of payment and fiscal deficits and meeting its external debt liabilities and second structural sector-specific reforms in trade and external sector policies, Industrial policies, Infrastructure, Privatization, financial sector to open India’s market to international competition by way of De-regulation, De-reservation and Dis-investment. Macro-economic stabilization was necessary to keep the high inflation in control; it would provide a strong foundation for the structural economic reforms and increase the growth in a sustained manner. The main focus of these reforms were to remove the distortions created by controls and administered prices and improve the quality of Indian goods and services in international markets.

Most important thing for reforms in that time was to bring the fiscal deficit in control, this was sought to be done by reducing subsidies in certain sectors and by reducing the expenditures in public investment and on social welfare services. Another sector where reforms were necessary was taxation. The tax reforms tried to focus on reducing “direct taxes for individual and corporations; abolishing export subsidies; lowering import duties; rationalizing direct and indirect taxes by removing unnecessary exemptions; tax incentive for infrastructure and export oriented sectors; setting up of Special Economic Zones for encouraging Foreign Direct Investment; computerization of the entire tax system for efficient administration. The main intention of the structural sector specific reforms in all the sectors had been to open India’s markets to “international competition, remove exchange rate controls, encourage private investment and participation in industry and, in the finance markets, to liberalize access to foreign capital and to ensure that foreign investment is not penalized merely for being foreign”[[62]](#footnote-62).

**2.5 Sector-Specific Structural Reforms:**

In the process of deregulation the major statutes which restricted and regulated the system like Industrial (Development and Regulation) Act, 1951, Monopoly Regulation and Trade Practices Act, 1969, Foreign Exchange Regulation Act, 1973, Capital Issues Control Act, 1947 had to be repealed, changed or amended to make it more market friendly. This was done through launching the Statement of Industrial Policy, 1991[[63]](#footnote-63) also known as the New Industrial Policy, which abolished the Industrial Licensing System which was developed under the Industrial Development and Regulation Act, 1951, it also removed restrictions on large industrial houses under the Monopolies Regulation and Trade Practices, 1969 and did away with the ceiling of 40% on foreign equity under the Foreign Exchange Regulations Act, 1973, this act was later changed to Foreign Exchange Management Act, 1999 which did away with many of the restrictive practices of the previous act and was much more market friendly.

The Capital Issues Control Act, 1947 was repealed which meant that Government control over the issue of capital, pricing of the issue, fixing of the interest rates on debentures and meddling with the functioning of the free flow of information in the market had come to an end and the markets were allowed to allocate resources to competing uses. In place of the Capital Issue Comptroller the Securities Exchange Board of India was created by passing of the Securities Exchange Board of India Act, 1992. The Act established a statutory autonomous agency called SEBI, the main responsibilities assigned to it were to protect the interest of the investors in securities, to promote the development of securities market and to regulate the securities market[[64]](#footnote-64). This Act ensures minimum standards of quality and enhances the confidence of people in the markets. It aims at identifying market imperfections and work towards prevention of market failure. It replaces the previous set of restrictive regime created by the Capital Issues Control Act, 1947 with a more liberal and market oriented regime allowing full freedom to economic players and at the same time prescribing necessary restrictions on carrying out their activities. This minimized the risk of systemic failures which the markets are prone to and lets the market operate in an efficient and fair manner. In contrast to its predecessor the Securities under the Securities Exchange Board of India Act, 1992 were to be issued at the market determined rates. Another feature of this act has been the risk management so that the participants are safe, customers protected and the integrity of the markets safeguarded. Securities Control and Regulation Act, 1956 was amended in 1995 to lift the ban on ‘options’ in securities market. It was further amended in 1999 to include ‘derivatives’ in the definition of Securities so that the derivatives market could be brought under the framework of the act and hence the three-decade ban on the forward trading was withdrawn from the financial markets. These reforms were the major initiatives taken by the government towards liberalization of the financial sector.

Reforms were brought by decreasing the activities of public sector, the areas which were reserved under Schedule-A of the Industrial Policy Resolution of 1956 were then reduced from 17 to just 4 which were Defense Equipment, Atomic Energy, Some associated Minerals and Railway Transport were highly important for the State to develop these sectors. In Schedule-B in which Public Sector had to play a major role was completely dispensed with and private sector was given absolute freedom to participate and compete with the Public Sector Enterprises. The Narasimhan Committee Report of 1991 was the blue-print for the Banking Sector Reforms. The committee recommended that the Statutory Liquidity Ratio and the Cash Reserve Ratio should be reduced as they cause great hindrance in the productivity as the Banks had to lock their resources for government purposes. It suggested stopping of Directed Credit Program as it compelled the Banks to provide resources to the poor at concessional rates of Interest and this reduced the profit making capacity of the Banks and hence needed to be dispensed with the program. For the Free Market System to function the determination of Interest Rate should be done by the market forces on demand and supply mechanism. Hence elimination of governmental controls was a necessary requirement. The committee further recommended that Public Sector Banks were reduced and private and foreign banks be allowed liberal entry without many restrictions and regulations. As the proportion of bad debts and non-performing assets were very high the committee recommended establishment of Asset Reconstruction Fund so that to help the banks get rid of their bad debts. The control of the Banking Division of the Ministry of Finance was done away with and Reserve Bank of India was made the only agency regulating the Banks. The Public Sector was also made free and autonomous in order to pursue competition and efficiency.

The Financial Sector had undergone important transformation; changes had been made to permit entry of private Banks and Mutual Funds which was restricted in the earlier regime. The Public Sector Financial Institutions were allowed to set up commercial Banks. The Mutual Funds segment attracted many foreign fund operators. The Government introduced the Insurance Regulation and Development Authority Act, 1999, de-regulating the Insurance Sector and allowing the private companies to operate in the previous nationalized insurance sector. Foreign investors were allowed with a cap of 26% holding in the Insurance Companies. Apart from these areas the sectors in which private sector was allowed to participate were Iron and Steel, Heavy Casting Industries, Electrical Plants, Aircrafts, Air Transport, Shipbuilding, Telephone and Telephone Cables, Telegraphs and Wireless Apparatus, Generation and Distribution of Energy etc. Hence a wide area of activities were made open for the private sector and since then many private companies have started doing business in these areas and have flourished along with the Indian Economy.

Another process of privatization used in that time was Disinvestment; the transfer of Public Sector Enterprises to private sector was made possible by Disinvestment of Government held Equities, Joint Venture for further expansion, Transfer of certain existing units or operations, entering into management contracts[[65]](#footnote-65). The main reasons for disinvestment were to bring more market discipline, increase resources and encourage wider public participation in management of the public sector enterprises. By 1992, 31 public sector enterprises were disinvested by the Department of Public Enterprise[[66]](#footnote-66). Hence great advancement had been made in the area of privatization by the New Industrial Policy despite of great resentment, opposition and controversies by different interest groups. The Sick Industrial Companies Act was passed in 1984 and the act allowed the closing down of the sick Public Sector Enterprises which could not be revived or reconstructed. The Board of Industrial and Financial Reconstruction was established through the Act to revive the sick public sector enterprises and to formulate a revival package for its survival. The Foreign Exchange Regulations Act, 1973 was replaced with a more market friendly act Foreign Exchange Management Act, 2000. The New economic Policies for the foreign Investment gave automatic approval of equity in the high priority Industries up to 51%. It allows majority for the equity holdings up to 51% for trading companies in export activities so that the domestic companies can have easy access to international markets. Banks and Financial Institutions Act, 1993 for the effective recovery of debts due to banks established the Debt Recovery Tribunal and framed the Debt Recovery Procedure Rules, 1993 to speed up the process of security realization.

Hence these are some of the changes which were brought into the Legislation and this is how through the process of Law the earlier economic system was changed which transformed the Indian economy by taking a different road to development. Therefore the role of law and the Legal Institution are very important for the economic development of the country and it is through the process of law that the country shapes its economic future according to the economic policies it shapes its law and the Institution. It is through the Legislations that the entire economic sector of India is being governed and we can see how the entire legal structure from State/discretionary law based had changed to Market/rule based. From the initial phase of centrally planned State led development to the more and more market led development we can see a change in the role of legal institutions as well as the administrative system. Initially there were regulatory institutions lead by the bureaucratic regime where the decision making power given to them by the state and the law was completely discretionary. They decided on the basis of their whims and fancies and this led to a widespread corruption in the bureaucratic regime. Later after liberalization the management was taken over by the private sector and the role and the responsibilities of the state changed along with the role of the legal institutions. It reduced the power of the bureaucracy and led to more organized and rule based system. Hence after the process of liberalization the legal system has also changed into a more market/rule based system.

**2.6 Role played by the Supreme Court in the Process of Liberalization and the challenges to the Constitution posed by the New Economic Policies:**

The role of the State had decreased in the Economic sector which was something not foreseen by the founding fathers of the Constitution of India. The role and responsibilities of the State as laid down by the Directive Principles of the State Policy did not intend that the role of the state would slowly diminish and the responsibilities would be shared by any other sector than the public sector. The directive principles of the state policy which plays a fundamental part in the governance of the country are without any doubt Socialistic. The words used in the preamble to the Constitution such as ‘Social’ and ‘Economic’ Justice means justice to the weaker and the poorer sections of the society, to “secure Equality of status and opportunity” means to minimize inequalities of income, eliminate the inequalities of status and provide opportunities without discrimination. The preamble of the constitution which is also part of the basic structure of the constitution directed towards the creation of a socialistic society. But the word Socialism was not included anywhere in the Original Constitution when it was drafted as Pandit Nehru the first Prime Minister of India strongly opposed it as he thought this was likely to be interpreted differently by different people[[67]](#footnote-67). The path of development taken by the Indian Economy was not based on Strictly Socialistic pattern as even private sector was allowed to function in the economy. Hence it was trying to create a Mixed Economy rather than a completely Socialistic Economy. But in the year 1977 an amendment was brought to the Constitution of India and the word Socialist[[68]](#footnote-68) was added in the Preamble. Therefore the preamble now aims at making India a sovereign, socialist, secular, democratic republic. The amendment was brought so that the means of production, control and distribution of national productive wealth could be brought under the ownership of the state for the benefit and use of the community and the rejection of a system of misuse of its resources for selfish ends[[69]](#footnote-69). The Supreme Court in the case of Akadasi Pradhan vs. State of Orissa said that the word Socialism is related to State Ownership and Social Welfare of the people and nationalization was the means to secure the goals enshrined in the constitution and the social, economic and the political rights of the people[[70]](#footnote-70). The economic policies post-independence were in line with the socialistic ideals enshrined in the constitution but the problem arises with the issue of Socialism vis-à-vis the present policy of privatization. This issue was considered by the Supreme Court in the case of Excel Wear vs. Union of India[[71]](#footnote-71), the court tried to strike a balance between the competing claims of nationalization on one hand and privatization on the other. The court stated “that the concept of socialism or socialist state has undergone changes from time to time, from country to country and from thinker to thinkers. But some basic concepts still hold the field. The amendment made to Article 19(6) shows that, a law relating to the creation of state monopoly should be presumed to be in the interest of the general public.”[[72]](#footnote-72) Hence the Supreme Court was also of the view that the process of nationalization was in the interest of the general public. But since 1991 there was a paradigm shift in the ideology from nationalization we were now moving towards privatization. What is interesting to note is how the courts have reacted and tried to adapt and interpret the changes. In State of Punjab vs. Modern Breweries, the Supreme Court stated that process of globalization has brought radical changes in the economic and social landscape of this country and that the policy of liberalization has a significant impact on it[[73]](#footnote-73). In a series of judgments[[74]](#footnote-74) the Court have said that the policies of liberalization is not violative of any part of the Constitution and that matters of economic policy are not subject to judicial review. In the BALCO case the court held that disinvestment policy cannot be challenged as the executives were the best judge in the matters of economic policies, they further stated that the courts are not intended to conduct the administration of the country and that should be left to the executives and the legislatures. Hence the court has accepted the policies of liberalization irrespective of whether it is against the constitutional mandate of socialism. Hence the essence of socialism seems to be lost with deferential approach of the courts. The era of socialism in practice has gone and it just remains in the preamble of the constitution. The State with the changing needs of the society has changed its policies and ideologies and has moved away with the past. The Constitution is indeed a living document and hence has to be interpreted with the changing needs of the time. If the objectives with which the word socialism was introduced in the constitution were being achieved through privatization then this does not mean that constitutional goals are demolished. It is high time that policies are judged by the results it achieves rather than the objectives with which it is introduced. The Supreme Court has rightly dealt with this issue of nationalization vs. privatization and allowed the development of the country without creating any hindrance to it.

**3. Conclusion:**

Jawaharlal Nehru in his famous speech said that “A moment comes, which comes but rarely in history, when we step out from the old to the new, when an age ends, and when the soul of a nation, long suppressed, finds utterance”. This moment came twice for India, once during the Independence in 1947 and the second during the Economic Independence in 1991. The soul of the nation long suppressed by the highly centralized bureaucratic inward looking regime of controls and regulations had found utterance in the New Economic Policy which completely changed the course of development and India stepped out from the old to the new methods of development, the age of socialism ended and the era of privatization began. The winds of change brought the change in the attitude of the state towards the industrial society, change from centrally planned economy to market led economy, change from excessive government intervention to minimal intervention, change from nationalization to privatization, change from subsidization to withdrawal of subsidy.

Through the reforms India did overcome its worst economic crisis that too in a very short span of two years. The Balance of Payment crisis was over by 1994 and its foreign exchange reserves had increased to US $15.07 billion, the current account deficit was nearly eliminated[[75]](#footnote-75). Hence the macro-economic stabilization reforms proved to be quite successful in India. The foreign exchange in March, 2003 reached US $70 billion and the current account recorded a surplus of 0.3% of GDP in 2001-2002[[76]](#footnote-76). India’s trade rose from 13.1% in 1990 to 20.3% in 2000. This is an incredible increase in the export rate. The middle class in India is ever growing with a much better standard of living then before; it provides a huge market for foreign corporations as all the quantitative restrictions on imports have been lifted since 2003. The reduction in poverty has been substantial; the poverty ratio as estimated by the planning commission came down to 26.1% in 1999-2000 from 36% in 1993-94. The flow of Foreign Direct Investment and the Foreign Institutional Investor has increased tremendously in the infrastructural sectors like power and telecommunications. India’s economic reforms have contributed to great improvements in technological and managerial innovations. The reforms have also benefited the consumers as they now have better quality products at much lower prices.

The performance of the Indian economy after reforms has been quite impressive on some fronts, satisfactory at other fronts and inadequate in certain respects. The most notable weakness has been the failure of government to control the growing revenue deficits and reducing the fiscal deficits. It certainly needs to maintain fiscal discipline for achieving sustainable high growth rate. The compulsions of democratic politics have certainly delayed the pace of implementation of the reforms. There are many political obstacles in way of reducing the subsidies and downsizing the government at all levels. This is the main reason behind the poor fiscal reforms. Another problem with re-organizing government finances is right-sizing the government by allowing the expenditures of the government in those areas where investment is of an infrastructural nature necessary for facilitating growth and development and where the private sector participation is not likely to come to an adequate extent. This has not been allowed to be achieved by the political pressure from different interest groups. India has been ranked 119 in the Human Development Index[[77]](#footnote-77) by the United Nations which shows that it has long way to go in terms of Social Development of its people. Hence there is a need to increase the spending on social services as the private sector would not have any incentive to enter in this sector. The state has to focus on social development as it acts as a precondition for the acceleration of growth.

Another weakness in the reform sector has been the lack of labor law reforms. The rigid labor laws have restricted the growth in the organized manufacturing sector. Because of the inflexibility in the labor laws the economic reforms despite of accelerated growth have not been able to generate adequate employment. The labor laws needs to be changed or amended and needs to be made more flexible for the private sector. Privatization on the other hand has seen a reduction of workforce as the new managements have opted for modernization and automation. Privatization of public sector enterprises has resulted into the replacement of better paid jobs with low wage unorganized casual labor jobs. Another area which also faces similar situation is the Land Reforms. Property rights are very important rights for a developing country like India. It is facing huge crisis because of poor property rights for the citizens and hence property rights should be brought under the ambit of the Fundamental Rights of the Constitution.

Last but not the least there has been a growing disparity between the rich and the poor. Within India most state governments are not well prepared to the challenges posed by the globalization. The farming sector and the small scale industries are vulnerable to global competition. The policies and reforms have not touched upon all these areas effectively and hence there still is a need for further changes in the policies and amendments to law. India still needs a second generation of reforms in bringing good governance, developing fiscal prudence, re-engineering the role of government, agricultural sector reform, Industrial restructuring, labor sector reforms and financial sector reforms. Finally to conclude, freer Markets can exist if Law would allow it to exist.

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13. As per the amended Art.31 (2). This particular change was brought in through the Fourth Amendment in

1955,after the Supreme Court had in various cases nullified laws on the ground that the compensation fixed was

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