Working Paper No. 430

Legal and Economic Reforms in India: an Economist’s Perspective

by

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January 2011
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Abstract

The Supreme Court of India has used its constitutionally mandated task of interpreting the enforceable fundamental rights enumerated in Part III of the constitution to extend its own powers. This extension in my view poses a dangerous threat to the Constitutional democracy of India. I argue below that the situation not only impacts the spillover effects beyond each case, but the learned justices seem to be incapable of conceptualizing possible spillovers, let alone incorporating them in their decisions. They also seem to be innocent of any understanding of the intersections of the intellectual disciplines of law and economics. I think that legal and economic reforms in India are top priorities. I have organized my discussion in four related categories: Laws and Administrative Regulations, Judicial Restraint versus Activism, Economic and Fiscal Federalism in the Constitution, and Rule of Law and Judicial Reform.

Keywords: Constitution in India, Constitutional democracy, Law and economics, Economic and Fiscal Federalism, Law and Judicial reform.

JEL Classification No.: K00, K40.

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At the outset, let me caveat my comments on Mr. Desai’s wonderful presentation and what follows by saying that I am not a legal scholar, but an economist. I beg his indulgence in advance for any of my misunderstandings of the Constitutional Law in India. I was tempted to call him in the American style by addressing him as Attorney General Desai, referring to his former position as distinguished Attorney General of India. I will refrain from doing so and may be adding insult to injury by calling him Desai for brevity!

Desai’s paper sets out in clear terms that the Supreme Court of India has used its constitutionally mandated task of interpreting the enforceable fundamental rights enumerated in Part III of the constitution to extend its own powers. This extension in my view poses a dangerous threat to the Constitutional democracy of India. The Court’s arrogation of power came about in two ways. First, it read “substantial rights conferred by the constitution in a broad manner” under the doctrine “that the law must change with changing social concepts and values” (Desai, p 3). Desai illustrates how this has been done by the court’s development of the foundation of law in the constitution, namely, Article 14, on protection of life and liberty and Article 14 on right to equality before law. Second, it laid down “generous guidelines for public interest litigation (PIL) virtually waiving the rules of standing and granting reliefs beyond those on class actions”. He notes in a mild manner that “Both these have an economic impact lost in a given case.” (ibid, p 3).
I argue below that the situation in fact is far worse: not only do the impacts spill over beyond each case, but the learned justices seem to be incapable of conceptualizing possible spillovers, let alone incorporating them in their decisions. They also seem to be innocent of any understanding of the intersections of the intellectual disciplines of law and economics. The latest Chief Justice of India, Justice S.H. Kapadia seems to be aware of this deplorable state of affairs. He said in a very recent speech that he “wanted lawyers and judges to brush up their knowledge of business laws,” and went on to say, “I am reliably told that an impression is being formed that judges and lawyers in India do not even conceptually have any knowledge of business and commercial laws.” 1 Justice S.H. Kapadia cautioned against such activism in the same speech and quoted from a recent book of a British judge that, “Judicial activism beyond a point is against the law…” and added that, “If the judge is clear on concepts… he will be able to decipher the difference between judicial activism and judicial restraint” 2

I would have phrased it more generally as a lack of knowledge among lawyers and judges in India of business and economics in general and not just laws governing both. Having taught in a US university for a long time and been an observer of its academic scene, I find the contrast between India and the US very striking. In the US the discipline of law and economics is thriving in universities, and what is more, represented in the judiciary (Judge Richard Posner is an outstanding example and he is not the only one) and the bar. In India very few universities teach law and economics and, to the best

1 (http://www.thehindu.com/2010/05/03/stories/2010050352951300.htm)  
2 (http://www.thehindu.com/2010/05/03/stories/2010050352951300.htm)
of my knowledge, no expert on law and economics is on the bench. Fortunately the situation is changing. Economics is in the curricula of the newly established law schools at Bangalore, Hyderabad, Pune and elsewhere, as well as of some departments of economics at universities. Though much belated, this is welcome. Moreover Indian scholars are publishing in International Journals devoted to Law and Development. A Special Issue of the *Law and Development Review* (Volume 3, Issue 2, 2010) devoted to “New Voices from Emerging Markets” has many articles from Indian scholars. I hope these are not exceptions but part of a rapidly growing stream.

Desai traces the story of judicial activism by the Supreme Court, which in its early years decided issues of personal liberty in accordance with the statutory procedural rules. In Gopalan vs State of Madras, the “Supreme Court held that once there was some procedure established by statute, it was not assailable on the ground of violation of any fundamental right … This position has changed beyond recognition by Judicial interpretation over the ensuring years” (Desai, p. 5). Desai concludes that starting from this strict (and perhaps too narrow, in the view of activists) construction of its role, the Supreme Court has gone to the extreme position of acting “where the courts feel that the changing needs of society require liberal construction even though it might involve their straying into the realms of executive and even legislative field” (Desai, p.20). Desai views this as “a dilemma between original intent and purposive interpretation which the Supreme Court will have to reconcile in clearer manner over the years” (Desai, p. 20). In my view, it is not just a dilemma of choice between two plausible and consistent positions. It is a far more serious issue for the Indian democracy whether or not to let the Judiciary arrogate itself as the supreme arbiter of what the changing needs of the society
are, and to itself the task of how and by what means they are to be met, and commanding
the executive and/or legislative bodies elected by the people to implement them
regardless of their possible economic and non-economic social costs and benefits.

Desai’s several examples are supportive of my darker view of the Court’s arrogance. He cites its decision in 1978 the Court, in a penitential mood after having
abjectly and shamefully surrendered to the executive during the infamous national
emergency declared by Mrs. Indira Gandhi in 1975 (and the excesses of which were
punished by the people by throwing Mrs. Gandhi’s Congress Party out of power in the
General Election of 1977) declared that “Article 21 is not only a guarantee against
executive action unsupported by law, but is also a restriction on law making itself [and]
extended the concept of fair procedure to include even substantive law” (Desai, p. 6).
The Court, by interpreting the notion of equality before law of Article 14 as antithetic to
arbitrariness, has assumed “the power to strike down any executive action if it is regarded
as arbitrary” (Desai, p. 12). As he rightly notes, this not only “provides a whole new
armory for the Court to challenge state action … this invariably and inevitably brings the
value judgment of the judges concerned … As it is the concept really depends on the
view the judge takes of a given executive action … Courts now have assumed the power
to strike down a statute on the grounds of arbitrariness [whether or not there were any
actual or potential instances of potentially arbitrary executive action that its
implementation caused or could have caused]. (ibid)

The breath-taking scope of the Court’s vast expansion of its own powers by its
interpretation of the fundamental right guaranteed under Article 32 to approach the
Supreme Court can be seen in its decision in Mehta v Union of India in 1987. The Court
held that “it has all incidental and ancillary powers including the power to forge new remedies and fashion new strategies to enforce fundamental rights … In suitable cases the Courts have also given guidelines and directions the Courts have monitored the implementation of legislation and even formulated guidelines in absence of legislation” (Desai, pp 13-14).

I had written much of what follows in a note that I had sent to Desai as issues that I as an economist saw as priorities for legal and economic reforms in India. In an Appendix to it, I briefly discussed the latest book by Nobel Laureate Amartya Sen on the Idea of Justice. I had organized my discussion in four related categories: Laws and Administrative Regulations, Judicial Restraint versus Activism, Economic and Fiscal Federalism in the Constitution, and Rule of Law and Judicial Reform. In many ways, I elaborate in it aspects of Desai’s thorough presentation today. I do not propose to present my note here in detail but will briefly highlight its main points. It is appended for the interested readers.

On Laws and Regulation, my concern is about the possibility of the complex procedures involved in India going from enactment of laws by the Parliament or a state legislature to determination of rules and regulations seem to give enormous discretionary powers to both the political echelons consisting of cabinets and ministers and the bureaucracy, regulatory bodies and agencies. Much more than the laws per se, the discretionary exercise of setting rules and implementing them played a very destructive role during the heydays of the license-permit raj and still do so. Are there ways of limiting such an exercise?
On judicial activism, I supplement Desai’s incisive discussion of some examples. The founding fathers had wisely left the individual rights or more precisely entitlements mentioned in Part IV on Directive Principles of State Policy mainly as aspirational guidelines to be enforced conditionally as and when the country had developed economically and had the resources for enforcement. They had explicitly made these rights not enforceable by courts of law. Linking these conditional and non-justiciable rights to the unconditionally guaranteed and justiciable fundamental rights of Part III and in particular under Article 21, the justices circumvented through judicial interpretation the legislative process of constitutional amendment that would have been necessary to make conditional rights of Part IV or part with the unconditional rights of Part III and made them also justiciable. I have already alluded to the potential economic costs of the extraordinary judicial activism of the Supreme Court.

An issue of consequence to India’s economic and fiscal federalism as yet unresolved is the erosion over time of the role of the Finance Commission created by Article 280 with specific functions. In particular, transfers from the centre to states both from tax revenues and also grants recommended by the finance Commission have been overshadowed by transfers through Five-Year Plans by the Planning Commission The latter is a body created by a resolution of the Central Cabinet and is not mentioned anywhere in the constitution. I discuss other problems of economic federalism as well.

I conclude my presentation by highly recommending Amartya Sen’s discussion of Nyaya, Niti and other concepts of classical Indian Jurisprudence and in particular, his analysis Krishna-Arjuna Samvada in the Bhagwat Gita. It is relevant to the topic of this
session and also from the perspective of alternative philosophical approaches of deontology and consequentialism.

1. Laws and Administrative Regulations

Do our complex procedures of formal presidential assent of enacted legislations, their notification once they receive such assent in the Gazette and, finally, the formulation of rules and regulations for their implementation, give enormous discretionary powers to the executive consisting of the cabinets and the bureaucracy? These powers could be used to delay the implementation of laws, create loopholes to benefit particular vested interests, and even successfully thwart the intent of the legislature as reflected in the debates on it before enactment and in the text of the acts themselves. Attempting to challenge the outcome of this process is a time-consuming and costly legal process. What can be done to reduce the exercise of discretion and bring in more transparency and accountability? This is a very important issue for the reason that, during four decades of the unlamented License-Permit Raj, the administrative rules and regulations and their discretionary exercise have had, and continue to have, far more serious and deleterious effects on economic performance than their enabling laws per se.

2. Judicial restraint versus activism

My limited reading and understanding of the debates in the Constituent Assembly and the provisions of the Constitution is that while the Supreme Court is the final authority on the constitutionality of the legislative acts, including amendments to the Constitution, the founding fathers intended the judiciary to defer to the legislature for addressing issues that are either not explicitly addressed or explicitly made non-
justiciable in enacted laws. They were not to act on them through judicial interpretation. The justices of the Supreme Court seem to have often ignored this fundamental intention of our founding fathers, even after striking down (famously in Kesavananda Bharati v. State of Kerala in 1973) any amendment that alters the basic structure of the Constitution as unconstitutional. In my view, judicial restraint is implicit in the basic structure. Thus, justices violate the precedent of Kesavananda Bharati when they engage in judicial activism. In an activist mode, Justices have gone beyond finding that the executive has not implemented or tardily implemented provisions of legislative acts, then leaving it to the executive to remedy the failures of implementation, and prescribed particular remedies themselves, regardless of their administrative feasibility or costs to the exchequer.

Let me illustrate my concerns with a few examples. The first is the opportunity for Public Interest Litigation (PIL) opened up by Justices P.N. Bhagwati and V.R. Krishna Iyer, who vastly extended the concept of standing for ensuring justice to the poor. The right to move the court for enforcement of their fundamental rights under the Constitution by the parties hurt by their non-enforcement or violation was guaranteed by the Constitution under Article 32. Justice Bhagwati in S.P. Gupta v. Union of India in 1981 defined the concept of PIL and the need for extension of standing as follows:

“Where a legal wrong or a legal injury is caused to a person or to a determinate class of persons by reason of violation of any constitutional or legal right or any burden is imposed in contravention of any constitutional or legal provision or without authority of law or any such legal wrong or legal injury or illegal burden is threatened and such person or determinate class of persons by reasons of poverty, helplessness or disability or socially or economically disadvantaged position unable to approach the court for relief, any member of public can maintain an application for an appropriate direction, order or writ in the High Court under Article 226 and in case any breach of fundamental rights of such persons or determinate class of persons, in this court under Article 32 seeking
judicial redress for the legal wrong or legal injury caused to such person or determinate class of persons.”

This was certainly an imaginative way of addressing acts of omission or commission by government when those affected by such acts are either too poor to sue or unaware of the possibility of suing the government or both for the impact of such acts on them. I will leave aside the question whether too many “frivolous” PIL suits have since been filed, partly for the reason that frivolousness may lie largely in the eye of the beholder. Even if a PIL succeeds in its intended purpose of redressing wrongs to the poor, the PIL process enables the justices to preempt what the electoral and legislative processes are designed to do through enabling the poor to act collectively in furthering their interest and redressing wrongs.

Certain individual rights are mentioned in Part IV of the constitution relating to Directive Principles of State Policy. These were explicitly made not enforceable by any court (Article 37) but nevertheless deemed fundamental in the governance of the country. Moreover the state was to make provisions for enforcement of rights in Part IV only within limits of economic capacity and development. Thus, these were conditional and not unconditional guarantees. On the other hand the fundamental rights under Part III of the Constitution were guaranteed unconditionally. Most disturbingly, by linking the fulfillment of conditional guaranteed rights of Part IV as necessary for ensuring the unconditionally guaranteed fundamental rights of Part III, Justice Bhagwati circumvented through judicial interpretation the process of amendment of the Constitution that would have been needed to make rights of Part IV as unconditional guarantees on par with fundamental rights of Part III. This in effect also circumvented the political and legislative processes needed to get a constitutional amendment enacted.
Further, since Article 32(2) of the Constitution confers on the Supreme Court the power to issue directions or orders or writs…whichever may be necessary for the enforcement of any of the [fundamental] rights, the court can, and has, issued such directions regardless of their costs to the exchequer. The costs of implementation of judicial directions are direct charges on the Consolidated Fund of India and bypass the process of having to be included in budgets that are approved by legislatures.

The next two examples illustrate what I consider arbitrary directions of the Supreme Court. The first is the direction mandating the use of Compressed Natural Gas (CNG) in public carriers such as buses, taxis and auto-rickshaws by a specific date, without as far as I can see any serious consideration of the availability of CNG and the incidence of the costs of acquiring scarce CNG across owners of the carriers and their drivers. It turned out that the available CNG then was inadequate to demand and this resulted in long lines in front of CNG pumps by drivers of auto rickshaws in particular. They were not compensated for waiting in lines, often during late at night, for pumps to open in the early morning and then seek customers during the day. Regardless of the beneficial reduction of visual pollution by the use of CNG, the cost of enforcement clearly fell on the poorer of the groups of owners and drivers of carriers. The court could have asked but did not, to the best of my knowledge, for an assessment of the distribution of social costs and benefits of mandating the use of CNG at a particular date by inviting amicus briefs, for example. In this case, the court left the manner of implementation of the mandate to the executive. The next example shows how intrusive the Court has been by going even further.
In a November 2001 decision on a PIL petition, the Court directed all states of India to introduce cooked-midday meals in primary schools within six months. Thus the learned court directed a particular means of improving child nutrition, namely the provision of cooked-midday meals, and not simply directing the states to enforce a right to adequate nutrition and leaving it to them to choose the best means of doing so within their resources.

My interest in judicial activism versus restraint is not so much about its constitutional or philosophical justification or critique in the abstract, or from a comparative perspective of their performance in practice in India, US, Great Britain or other Commonwealth countries. My concern instead is about the economic consequences of either or both for achieving “inclusive” (another popular buzz word) growth and economic development in India.

My broader concern is that justices with little apparent knowledge or training in economics, political science or sociology, often decide on matters that cannot be decided without such knowledge. Let me illustrate again by an example. In general, though not always, judicial means are most effective and least costly from a social perspective for addressing legal problems. Using them to address political problems would not only be less effective but more costly as well. Although this proposition is fairly obvious, the more difficult question is what to do if, say, a legal problem arises and the most effective and least costly legal means are unavailable for some reason, while less effective and more costly other means (economic, social or even legal) are available. Clearly, by using the latter, some efficiency loss and higher costs would be incurred, but the legal problem would be addressed. On the other hand, not using the latter and leaving the problem
unaddressed is also socially costly. Without an analysis, based on the relevant socio-economic-political-legal system, one cannot determine which of the two actions of using political means to address the problem and not addressing it all, is socially more costly and should not be chosen. Judicial remedies and directives in such situations implicitly make such comparisons without such an analysis, but without the benefit of such analysis. I recognize that an interdisciplinary perspective from judges other than of the Supreme Court or for that matter from bureaucrats, legislators and politicians in power who make decisions affecting the welfare of the people, is too much to expect. There is in principle a channel of appeal against decisions of all the above decision makers, including, importantly, the possibility of going all the way to the Supreme Court, which, again in principle, could correct errors resulting from a lack of interdisciplinary perspective at lower levels. This can happen only if the Justices of the Court have such a perspective. Moreover, because the decisions of the Supreme Court Justices are final with no further possibility of appeal (leaving aside revision petitions), the cost to the society of their not having an interdisciplinary perspective could be high.

3. Economic and Fiscal Federalism in the Constitution

The Seventh Schedule of the Constitution assigned some tax bases exclusively to the Centre (i.e. Indian Union) in the Union List (List I) and others exclusively to the states in the States List (List II) and none in the concurrent list (List III). Part XII laid down in detail the division of responsibilities between the Centre and States with respect to Finance, Property, Contracts and Suits. The most important articles of this part, from the perspective of Fiscal Federalism, are Article 275 on grants from the Union to certain states, Article 280 mandating the appointment of a Finance Commission every five years
or at such earlier time as the President deemed necessary at Article 281 on the Recommendations of the Finance Commission (FC).

Article 280, paragraph (3) laid down the duties of the FC as to make recommendations to the President on (a) the distribution of net revenues from the divisible (between the Centre and States as a whole) pool of taxes and the shares of the individual states in the total net revenues from the divisible pool assigned to taxes as a whole, and (b) the principles that should govern the grants-in-aid to states out of the consolidated fund of India. The need to divide the revenues between centre and states arises in large part from the facts that the revenues from tax bases assigned to states were far less responsive to growth of the economy than those assigned to centre and that the states had higher expenditure responsibilities relative to the centre.

Let me set aside the facts that the states have chosen not to raise as much revenue as they could have from the tax bases assigned to them, such as, for example, allowing land revenue to become a minor source. Let me also set aside the fact that they have not exercised sufficient control over their expenditures nor spent their resources efficiently. Both these issues arise at both central and state levels in part because the assignments of tax bases and expenditure responsibilities themselves created few, if any, incentives to be efficient in raising revenue or in spending, and in fact many incentives work in the opposite direction. Let me proceed with structural problems.

To use economic terms, the assignment of tax bases and expenditures created vertical (between centre and states) and horizontal (among states) imbalances between revenues and expenditures. The revenue transfers recommended by the FC were intended to address those imbalances. Article 281 simply required that every recommendation
made by the FC and the action taken thereon by the President as head of state (basically by the central government) be laid before each House of Parliament.

In effect, the central government advises the President on the terms of reference of each FC and also informs the President as to the action it proposes to take on the recommendations of the FC. The Constitution does not require Parliamentary approval of the recommendations of FC or the government’s action thereon, except in so far as they are reflected in the annual budgets presented to and approved by the Parliament. Surprisingly, even though the duty of the FC is to recommend the shares of net revenues from the divisible pool between the centre and states and also the distribution of shares among states, and these transfers account for large shares of the total receipts of states from their own taxes and the transfers, the Constitution does not require that the recommendation of the FC and the actions taken thereon by the central government be laid before the state legislatures.

The meanings of the phrase grants-in-aid from the central government and interpretation of articles 275 and 282 of the Constitution read with article 280 that mandated the appointment of the FC and laid down its duties have been controversial. The Ninth FC appointed in 1990 had asked for their views on the scope of these articles from legal experts K.K. Venugopal, N.A. Palkhiwala and A.G. Noorani. Their opinions are available in a publication of the National Institute of Public Finance and Policy (NIPFP, 1993). Although they differed from each other on many aspects, they clearly articulated the relevant issues. They are very interesting and relevant even now. More interestingly from my perspective is the Tagore lecture of M.C. Setalvad on “Union and State Relations under the Indian Constitution” (Eastern Law House, Calcutta, 1974), from
which Noorani quoted the passage, “A general weakness of federal state financial relations, more particularly in the field of devolution, is that federal assistance tends to be discretionary in character, not necessarily on principles of uniform application. To safeguard the position of the States, our Constitution provides, therefore, that the assessment of the needs of the States as well as the measure of assistance to be afforded and the form in which this should be given, are determined by an independent Commission to be constituted at intervals of not more than five years. But this role and functions of the Finance Commission, as provided in the Constitution, can no longer be realized fully due to the emergence of the Planning Commission as an apparatus for national planning.” Noorani argues that the state of things as described by Setalvad is manifestly unconstitutional and states that there is universal agreement that the present use of Article 282 was not, and could not possibly have been within the contemplation of the Founding Fathers of the Constitution.

The present use referred to by Noorani at the time the constitutional experts submitted their opinions to the Ninth FC (sometime in the early 1990s) was the expansion of the use of grants-in-aid, a use restricted by Article 282 only for special purposes, particularly though aid for five-year plans of states as recommended by the Planning Commission and by Central Ministries for centrally sponsored schemes and many more. This expansive use continues to this day.

The FC is a constitutionally mandated body whereas the Planning Commission assuredly is not. It was established by a Resolution of the Central Cabinet in March 1950, i.e. by executive fiat. The constitution makes no reference to Planning or the Planning Commission. The Approach Paper of each Five-Year Plan and the final Plans themselves
are discussed and approved by the National Development Council, another institution not mandated by or referred to in the Constitution, in which the Central and State Governments are represented. They are placed before Parliament and state legislatures and are not voted upon. Apart from the issue of whether Articles 275 and 282 provide adequate constitutional cover for the financial transfers in support of the Plans, there is the issue of whether approval by elected members of parliamentary and state legislatures of such transfers as reflected in central and state budgets could be viewed as providing adequate means of accountability.

Even more disturbing is the excessive concentration of power in the hands of the Central Government as a consequence of the grants-in-aid and plan approval processes. It is no exaggeration to say that the state chief ministers have to present as abject supplicants before the durbar of the Deputy Chairman of the Planning Commission for the approval of their state five-year plans and plan grants. Although central planning as an economic management system lost its credibility with the collapse of the Soviet Union and its GOSPLAN, the Planning Commission survives in India by inventing new roles for itself. I am convinced that the Planning Commission has no essential role that cannot be played, and perhaps more efficiently, by other existing institutions, or by newly created ones.

The Indian Constitution debated in the Constituent Assembly and adopted in 1949, came into force on January 26, 1950. It responded to the critical situation at independence in 1947 of the trauma of partition and rehabilitation of millions of refugees, the task of interpreting princely states into the Union, conflicts with Pakistan or Kashmir, and a fear of fissiparous tendencies emerging that would break the newly independent country apart.
The felt need for a strong central government to tackle these issues firmly and effectively persuaded the founding fathers to build strong centralizing features in an otherwise federal constitution. I would argue that the centralization in the Constitution of 1950 and the subsequent strengthening of it in the economic and fiscal arenas through central planning and central transfers are unhealthy from the perspective of a vibrant democratic federal system in a very diverse and plural society. On the other hand, as the eminent founding father Dr. Ambedkar noted, the power of vested interests based on castes, for example, becomes diluted at larger levels of aggregation such as states or the nation as a whole because of greater competition from other castes, but at the level of a village individual castes or subcastes could be dominant and powerful. Thus, benefits of decentralization would depend both upon the powers decentralized and the level to which it extends. I am not sure whether short of convening a constitutional convention of existing members of state legislatures and parliament or alternatively electing a new constituent assembly to rewrite the Constitution, a most unrealistic (and in many ways undesirable) prospect, there could be legal reforms that could arrest the centralizing tendency and bring greater transparency and accountability to the legislative, executive and judicial processes, and most importantly, the electoral process.

It is well known that central and state governments by and large pursued conservative fiscal policies until the early eighties and the consolidated fiscal deficits (CFD) of the centre and states were modest. The abandonment of conservatism and the adoption of expansionary fiscal policies resulting in growing fiscal deficits financed by borrowing abroad from capital markets and, at home, were major contributing causes to the severe macroeconomic cum balance-of-payments crisis of 1990-91. On the eve of the
crisis, the CFD was around 9.6 percent of GDP. It is no surprise that fiscal consolidation and reduction of fiscal deficits were major planks of the post-crisis reform agenda. Some reduction in the CFD did take place until 1996-97 and since then it had a rising trend (with minor breaks) peaking at to 9.94 percent in 2002. It was estimated at 8.5 percent in 2008-09. All this happened despite the passing of the Fiscal Reform and Budget Management Act (FRBM) by the Parliament in 2003 and later similar FRBMs were passed by many states. The acts set time paths for deficit reductions in the near future. In my view, the reason for their not constraining deficit growth is twofold. First, the FRBMs were not politically credible in that political support for their passage and meeting their targets was at best lukewarm. Second, governments chose to deviate from FRBM targets when faced by some exigencies by postponing them (or to use the famous phrase of the former finance minister P. Chidambaram by pressing the “pause button” on them). After running a large fiscal deficit in 2009-10 ostensibly to stimulate the sagging economy due to the global financial crisis, the macroeconomic framework of the budget of 2010-11 promises to do better. Whether these are any more credible than those of the past is an open question. The facts that the terms of reference to the Thirteenth Finance Commission, which submitted its report in 2009, asked the independent Commission that is insulated from politics to recommend a fiscal consolidation programme and that it did so suggests that the Central government was trying to obtain credibility and political cover for the programme that it could not achieve through the political process.

India suffered a relatively small (compared to other countries) slow down in GDP growth and also began recovering earlier. Yet this should not lead to any complacency about the urgency of dealing with fiscal deficits and bringing down general government
debt as a proportion of GDP to a sustainable level. The current crisis in Greece is a
warning. It is true that Greece is a member of the European Union and the European
Monetary Union with the Euro as its common currency. Also it has free capital flows to
and from the rest of the world. India is not a member of any currency union, and the
exchange rate of the rupee is in principle flexible, though in fact it is managed by the RBI.
India has almost free capital inflows but outflows are restricted with residents having no
freedom to invest freely abroad. These differences are important, yet Greece’s problem as
described by its former finance minister Yannos Papantoniou: “Now we are paying the
price for the fact that we lived above our means, with amazing profligacy, and failed to
reduce the role of the state” (http://www.nytimes.com/2010/05/05/business/global/05iht-
greece.ht...) is very similar to India’s own profligacy, and the bloated public sector.
Although the profits and losses of the state-owned enterprise have implications for the
fiscal state of the central and state governments and therefore should come under the
jurisdiction of the Finance Commission, its terms of reference have not included the
operation of state-owned enterprise let alone their rationale or reform, including
divestment or complete privatization.

In my view, it is time to rethink our economic and fiscal federalism as set in the
Constitution in 1950 under a wholly different economic and political environment.
Whether this can be done without amending the Constitution substantially has to be
thought through.

4. Rule of Law and Judicial Reform

The characterization in popular discourse in the U.S. of its system of governance
is aptly summed up by the cliché: “We are ruled by law and not by men.” That the actual
functioning of the rule of law may violate this assertion, it is implied in another cliché, more widely popular than just in the U.S.: “Justice delayed is Justice denied.” The perceptions underlying all clichés including these two are partial. For example, while a society may not be governed by men of the day but by laws and rules, still contemporary laws and rules themselves were drawn up by men of the past, often distant past, some of whom may have existed only in legends and myths. In any case, one cannot hide behind rule of law in the governance of any society without examining the origins of the laws themselves and whose interests they may serve, not just among current citizens but also among those who were instrumental in enacting them. Invoking divine (e.g. “Unalienable rights endowed by our Creator”) or religious origins (e.g. Shariat) should not be used to trump such an examination. Proposals for legal reforms meant to reduce delay made without exploring (i) why the, admittedly, very long time, on an average it takes in India to resolve cases, and (ii) whether it could be in the interest (including asking for a delay as a strategy) of all parties (plaintiffs and defendants and their lawyers and the judges) to delay rather than settle, and taking into account the likely interests of all parties, are less likely to succeed in doing so. The new Chief Justice of India seems to be aware of the incentives to delay or settle when he referred to the absence in India of what he called the “settlement culture” and to the likely interest of lawyers not to settle if litigation is their only source of livelihood, in his appeal to a gathering of judges and Chief Justices to encourage litigants to resort to mediation, arbitration and conciliation for settlement of disputes, rather than to litigate endlessly without any guarantee of fair results.
His colleague, Justice Raveendran, spoke to the same gathering about the anxiety and frustration building up among the litigants because of the inherent lacunae in the present justice delivery system—the delay, uncertainty, inflexibility, cost, difficulty in enforcing decrees and the unfriendly atmosphere of courts. Echoing the Chief Justice he added “But, who will make mediation successful? The government is not going to do it. The lawyers will not do it. The litigant is not in a position to understand the benefits of mediation and reconciliation. So, it is for the judges to take the lead in making litigants understand the value of mediation” (Times of India, New Delhi, July 11, 2010. page 14).

While I am pleased that the learned justices are addressing a serious problem, I would not entirely agree with their rather simplistic characterization of litigants or with the unqualified praise of the virtues of arbitration, mediation and reconciliation. Moreover I worry whether by pushing for approaches to dispute settlement outside the formal judicial system, the learned justices may be unwittingly ensuring that any fundamental reform of the system may be further delayed, if not postponed indefinitely.

In the context of judicial reforms, I discuss in the Appendix Amartya Sen’s fascinating new book, The Idea of Justice. One does not have to agree with all the elements of Sen’s theory of justice and his penetrating analysis to be persuaded of their reach and relevance for a reasoned discussion of India’s performance (not just economic), of policy reforms, including legal reforms. Sen’s book forces us to think through whether a reform proposal is likely to advance or retreat from justice, starting from the Indian society, laws, rules and regulations as they are, rather than from what they would happen to be were India to be a “just” society.
In such a perspective, two issues call for immediate attention: namely, reform of bankruptcy and labour laws. I understand a new company law is likely to be introduced in Parliament soon and may include some provisions relating to bankruptcy. My reading of the current status is that our procedures do not facilitate opportunity, as, for example, U.S. law does, for potentially viable companies to seek protection from a bankruptcy court to relieve pressure from creditors while they undergo restructuring of their assets and liabilities, as well as their management, under the supervision of the bankruptcy court, so that they can emerge from court supervision as competitive, healthy enterprises. If a company is non-viable or if it becomes so because needed restructuring could not be brought about during court protection, the court can help in its orderly liquidation. The Indian bankruptcy process is long and complicated, in part because of the difficulty in realizing appropriate value for assets to be liquidated and in reaching agreements with creditors on writing down debt liabilities. Both difficulties also stem from other features of our legal system as well as the fact that markets for corporate debt are very thin. The fact of long delays and high costs of addressing bankruptcy, were the need for it to arise, will naturally adversely affect the market value of a company’s equity. Clearly this adverse valuation effect could reduce India’s attractiveness to portfolio investors from abroad.

The deleterious consequences of labour laws for economic efficiency and growth as well as income distribution have long been known. The late Professor Mahalanobis, the architect of India’s Development Strategy since the 1950’s until recent reforms and author of the Second Five-Year Plan, had pointed to them in 1961. He had noted that they were most protective of the interests of a small share of India’s labour force employed in
the organized sector, which together with their dependants formed less than a tenth of India’s population then, and against the interests of the rest. The situation has not changed even now. There is no doubt that the severity of our labour laws has had a lot to do not only with keeping millions of workers employed in informal sectors and low productivity primary activities, including agriculture, but also slowing the rate of poverty reduction.

Labour is in the state list in the Constitution. Political support for reform of labour law has been absent or lukewarm at best. But reforms are urgent. How do we proceed with reform of the laws in such a context?

The last two issues I want to flag without expanding on them are first, the fact that in India the legal doctrine of desuetitude, under which laws that have not been in use become inapplicable, is not practiced. The result is that a large set of laws enacted long ago under colonial rule and in different circumstances are still on the statute books. Many of them are in conflict with each other, and the circumstances and the problems some of them were meant to address no longer exist. Yet they can be invoked at any time. I suspect they contribute to delays in the final disposition of cases. Is there a way of addressing this problem?

Second, in addition to many contradictory laws in the statute books, we have created many avenues for dispute settlement ranging from Lok Adalats, Tribunals, and other ad hoc bodies. It is understandable, given the costs and delays of the general court system, that a recourse to create a special mechanism to expedite dispute settlement and lower its costs is appealing. However, since the decisions of the constituents of the special mechanisms are rarely final unless both parties to a dispute agree, and each party
has a constitutionally guaranteed right of appeal, if it is feasible and allowed by the judicial laws, all the way to the Supreme Court. I may be wrong but my impression is that no comprehensive analysis of the entire dispute settlement system, including not only the formal court system and special mechanisms but also informal means of dispute settlement, has been undertaken. I know that the Law Commission, since its creation long ago, has studied many aspects of the legal system, its functioning and issues of reforms and submitted reports. Again my impression is that few concrete actions have resulted from these studies and reports – they continue to gather dust. Perhaps if the legal profession takes to heart Justice Kapadia’s advice to teach and write articles in professional journals, the legal profession would study issues in depth and publish articles both in reputed professional journals and in the popular media, particularly in the regional languages.

References


Sen, Amartya (2009), The Idea of Justice, Cambridge, Ma., Harvard University Press.

Appendix

Amartya Sen’s latest book, The Idea of Justice, departs from the dominant feature of many theories of justice in today’s moral and political philosophy which focus almost exclusively on the nature and the establishment of “just” institutions of “perfect justice,” the characterization of “perfectly just societies.” Sen’s departure focuses on identification
of redressable injustice in actual societies and actual behaviours that emerge, rather than presuming compliance by all with ideal behaviours as in perfectly just societies. Sen justifies his departure on two grounds. First, there may be no agreement at all among reasonable individuals (i.e. who engage in reasonable discussions) even under conditions of impartiality and open-minded scrutiny (the original position under a veil of ignorance as in John Rawl’s celebrated Theory of Justice as Fairness) on the nature of the just society. Even if there is agreement on a just society it may not be a feasible alternative.

Second, there is a “need to focus on actual realization and accomplishments rather than only on the establishment of what are identified as the right institutions and rules. The contrast relates…” a general and much broader dichotomy between an arrangement-focused view of justice, and a realization-focused understanding of justice. The former line of thought proposes that justice should be conceptualized in terms of certain organizational arrangements – some institutions, some regulations, and some behavioural rules – the active presence of which would indicate justice is being done. The question to ask in this context is whether the analysis of justice must be so confined to getting the basic institutions and general rules right? Should we not have to examine what emerges in the society, including the kind of lives that people can actually lead, given the institutions and rules, but also other influences, including actual behaviour that would inescapably affect human lives?

I strongly recommend reading his Preface and Introduction for a lucid exposition of why a Theory of Justice is needed and the role of reason. He is surely right that the fact that unreason is not only prevalent but pervasive and resilient, even though it may make reason-based answers to difficult questions far less effective, is not a ground for not using
reason to the extent one can, in pursuing the idea of justice. While conceding his book
draws on lines of reasoning in the period of intellectual discontent during the European
Enlightenment, he rightly argues that this does not make the intellectual background of
his book particularly “European” and that he has made use of ideas from non-Western
societies, particularly from Indian intellectual history of a period that preceded
Enlightenment.

Sen is well known for his knowledge of Sanskrit and for having read some of the
surviving versions of Manu Smriti, Anthasastra and other classical literature in the
original. In this book he very briefly and illuminatingly discusses classical Indian
jurisprudence – in particular the distinction between “niti” and “nyaya” both of which
stand for justice in classical Sanskrit (Maybe for this reason, Niti Marg and Naya Marg in
Chanakya Puri, named appropriately enough for the suburb of embassies of New Delhi,
are close to each other and meet in a round about!). According to Sen, the “principal”
uses of the term Niti are narrowly organizational [i.e. institutional] propriety and
behavioural correctness [presumably correct behaviour denotes behaving in accordance
with rules, Dharma Sastras]. In contrast, the term Nyaya stands for a comprehensive
concept of realized justice. In that vision, the roles of institutions, rules and organizations,
important as they are, have to be assessed in the broader and more inclusive perspective
of Nyaya, which is inescapably linked with the world that actually emerges, not just the
institutions or rules we happen to have (Sen, 2009, p 20). In emphasizing this point, he
refers to “Matsyanyaya” or justice in the world of fish, where a big fish can freely devour
a small fish. Sen points out that avoiding an analogue of “Matsyanyaya” in the world of
human beings must be an essential part of justice and argues that, “the central recognition
here is that the realization of justice in the sense of nyaya is not just a matter of judging institutions and rules, but of judging the societies themselves,” (ibid).

In a footnote in the same page, Sen refers to Manu, the famous ancient Indian legal theorist as having been concerned with Nitis of the most severe kind, but adds that even Manu could not escape being into realization and Nyaya in justifying the rightness of his behavioural rules. The profound influence of Manu Smriti on the rulers and ruled all over India as far as South India in ancient days is exemplified by the many stories in Tamil literature of that era of emperors of the three Tamil kingdoms (Cholas, Cheras and Pandyas) having upheld the laws of Manu even at the cost to themselves. Among these is the apocryphal story of a Chola emperor, known by the honorific, “Manu Niti Chola” who, as the legend has it, had a bell installed in his palace that any of his subjects (human or animal) could ring to seek justice. One day, a cow rang the bell, so the story goes, to seek justice for a loss of her calf killed under the wheels of the crown prince’s chariot. The king had the prince killed to punish himself to demonstrate to all his subjects that justice will be rendered regardless of costs to anyone, including himself. I have no idea whether Sen would consider this an example of the emperor going beyond Manu’s Niti and applying the more comprehensive Nyaya!

In philosophy, a deontological approach, which emphasizes the role of duty and individual responsibility in individual action, is contrasted with a consequential approach, which evaluates actions by their realized consequences. Sen suggests philosophers who are of the deontological persuasion may fear that seeing justice in terms of nyaya instead of niti by their concentration on actual realization would tend to ignore the significance of social processes, including the exercise of individual duties and responsibilities. In Sen’s
view, this worry is misplaced since a full characterization of realizations should have room to include the exact processes through which the eventual states of affairs emerge.

Sen’s discussion of Krishna-Arjuna Samvada in the Bhagwat Geeta is fascinating. Krishna is usually perceived as a deontologist, emphasizing that Anjuna must give priority to the duty to fight on the side of justice and propriety, regardless of the consequence that many would be killed, and Arjuna as a consequentialist, whose hesitancy to go to war was precisely because he worried about its consequences. In Sen’s view, this perception, while fitting broadly with the differences between the two philosophical approaches, an examination of the totality of Arjuna’s concerns as seen not just from the last chapters of the Bhagwat Geeta but its earlier chapters and indeed from the Mahabharata as a whole, would reveal the limitations of Krishna’s emphasis on doing one’s duty regardless of consequences in the famous words: “Karmanyevamadhikaraste, ma phaleshu kadacana,” relative to Arjuna’s broader perspective. The end of the “just” Mahabharata war in Kurukshetra was utter desolation as described in Santi Parva. It vindicates Arjuna’s broader concern not just about many being killed in the war, with him leading the charge, but importantly, “that he himself would be doing a lot of the killing, often of people for whom he has affection and with whom he has personal relations, in the battle between two wings of the same family, in which others, well known to both sides, had also joined. Indeed, the actual event that Arjuna worries about goes well beyond the process independent view of consequences. An appropriate understanding of social realization – central to justice as nyaya – has to take a comprehensive form of a process-inclusive broad account” (Sen, 2009, p 24).
Equally fascinating is Sen’s discussion (Sen, 2009, pp 37-39) of the necessity of reason and in that context justly celebrated Munhall Emperor Akbar’s far reaching enquiry into the social and political values and legal and cultural practices around 1600. The path of reason and rejection of traditionalism were so brilliantly patent to him as to be above the need of argument. Akbar concluded that the “path of reason” or “the rule of the intellect” must be the basic determinant of good and just behaviour as well as an acceptable framework of legal duties and entitlements.