

# Economic Controls During World War II And Their Continuance

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The Second World War had a devastating effect on economic life in India. While India had been spared the material destruction that had befallen on many other countries, she had suffered in full measure and in some areas in greater measure than others, the economic consequences of war. Between 1939-45 the economy was subject to enormous strains, leaving fundamental imbalances in many areas lasting long after the war.

The purpose of this paper is to examine why the economic controls which were implemented as emergency measures during World War II continued after the war in India. We shall focus on some of these controls.

## Controls Regarding Procurement and Distribution of Food

### Reason For Implementation

During the Second World War there was a drastic decline in imports. Moreover, industrial production was allowed to expand only in those industries that supplied the war. Thus there was an acute shortage of consumer goods and thus fewer goods were available for the civilian population. This led to a savage increase in the prices of consumer goods especially food.

Thus to resurrect the situation the appropriate economic controls were placed such as the

- Imposition of ration schemes
- Price controls

### The Rationing Scheme, 1939

The food crisis emerged during the war—a basic ration of 16 oz. of grains per day in the city of Bombay in 1943 and the system extended later also. Poor harvest in 1946 (for millets) and in 1947 (for wheat) made the supply situation worse, and the basic food ration was reduced to 12 oz. (equivalent to 1200 calories). By 1946, as many as 771 cities and about 150 million people were covered by rationing arrangements of some kinds.

### Procedure of Rationing

A system of official procurement was now in place. Theoretically it implied the compulsory purchase of the farmer's entire surplus, in practice only about one-sixth of the surplus was extracted in this way over the country as a whole. Thus two-third of rations were procured in this manner, the rest coming from imports<sup>1</sup>. Now after the winter of 1947 the threat of starvation receded, only to be replaced by the problem of pricing the procured grain. This arose due to the uncertain harvests and inflationary conditions operating in the economy. We shall now discuss the system of price control

### Price Control

In 1944, the Government of India had agreed ceiling and floor prices at which it would purchase wheat and millets from the provinces. The basic problem with this system was that it was inflexible and was not responsive to the changes occurring in the economy at the time. For instance, in 1945, the food situation improved and thus the statutory price of rice was reduced. But in 1946, due to harvest difficulties and the existing inflationary conditions, there was a widespread demand of

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<sup>1</sup> *Foundations of Indian Political Economy*, pp 278-79, Sage Publications India Private Limited.

increase in prices. In 1946, the government admitted in the central legislature, "That grain was sold in some markets at 2.5 times the control price, but still opposed any increase in the procurement prices, arguing that the grain prices were already high enough to serve the interests of the farmers."<sup>2</sup>

### Analysis

There was no need for continuance of these controls as there was no longer a shortage of food grains. Moreover, the existing controls hampered the existing situation by creating artificial scarcity through the procurement system. Ironically people covered under the system suffered immensely.

This was because inflationary conditions created a seller's market for grain in the winter of 1946-47. Administrative inflexibility meant the procurement price of grain did not rise even when the supply was weak and the demand was strong. This led to leakages to the black market which acquired a larger part of the farmer's surplus thereby reducing the ration scale leading to extreme scarcity among the people under the rationing system. The advocates of decontrol took the view that removing restrictions would discourage hoarding, and only lead to a modest rise in prices, no higher than that already existed in the black market.

Fortunately, some enlightened individuals of the Indian government in power like C Rajagopalachari realised the need of the hour and opposed the control of food grains by the government. Thus in his capacity of the minister of industries and supply, Rajaji, towards the end of 1947, abolished all controls of grain supply, price and distribution.

### Rent Control

Besides economic controls on procurement and distribution of goods, rent controls were also imposed during the war. Inexplicably these rent controls have been prevalent ever since, even though it was initiated as an emergency provision. We shall attempt to study this aspect in detail.

#### **Rationale for Rent Control**

The National Commission on Urbanisation (NCU) traces the origins of the rent control legislation in India in its Interim Report, January 1987, pp 26-27.

The beginning of the Second World War brought a dual pressure to bear on the urban housing stock in India. The demands of the military increased the pressure on existing housing and wartime shortages prevented an increase in supply. Purely as a temporary measure, therefore, the British government introduced laws relating to the control of rent and accommodation. But since then various state governments extended the rent regulations to deal with the special situation first arising out of migrations triggered by partition of India, and then that influenced by industrialisation. So though intended to deal with special conditions, rent control became a permanent feature

#### **Features of the Rent Control Acts**

Broadly speaking, with state variations, the Rent Acts imposed during the Second World War and the decade that followed have the following provisions:

- Control of letting and leasing of vacant buildings,
- Fixation of fair or standard rent,
- Protection of tenants from arbitrary eviction,
- The obligation of owners regarding up-keep and maintenance,
- The rights of owners in case of misuse, non-payment of rent, and
- The procedure whereby owners can regain possession of premises.

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<sup>2</sup> *Foundations of Indian Political Economy*, p 280, Sage Publications India Private Limited.

In their original form, these laws brought all urban properties within the purview of a rent controller who could both allot vacant premises and fix the fair rent thereof. Gradually these laws have become permanent and their focus has shifted away from allotment of vacant premises by a public authority to a freezing of rent at existing levels and the protection of the tenancy rights of the occupants.

### Case Study—Bombay Rent Controls

The genesis of the present rent dispute in Bombay goes back to the outbreak of World War II. It was initiated by the Bombay RENT Control Act, 1940.

#### **Bombay Rent Act, 1940**

This Act applicable only to private premises provides that rent in excess of the standard rent is illegal except where an agreement entered into before September 1, 1940 provides for periodic increases. However, it does permit rent increases subject to certain conditions in the case of premises that receive the benefit of improvements or special additions, and premises that are subjected to special or heavy repairs<sup>3</sup>. In other words, standard rent is the maximum legally permissible rent a landlord can collect, and under the Act this amount was pegged as the rent as on September 1, 1940. For buildings constructed after that date the standard rent would be the first rent paid when the property was let out. These norms were extended under the Bombay Rents, Hotel Rates and Lodging House Rates (Control) Act, 1944 and the Bombay Rent Control Act 1947. The primary bone of contention has been the concept of standard rent, which is condemned to be highly unreasonable.

The Supreme Court judgment cited the hypothetical case, presented by counsel for the appellants, of a landlord who was getting a rent of Rs 1,200 a year, exclusive of municipal taxes, on September 1, 1940. According to the counsel's calculations, this landlord would receive only Rs 800 a year in 1996 or 1997 and, as the value of the rupee in 1996 or 1997 was only 1/66th of what it was in 1940, in real terms the annual accrual to the landlord would have fallen from Rs 1,200 to Rs 12.12.

Thus on the premise of this act the state froze rents in the city at the 1940 levels. The courts decided then that property rents would not be increased. The 1940 Act was extended 20 times in the past 50 years, with no government willing to anger the powerful tenants' lobby. Increases in the cost of living, the cost of building materials and imposition of additional levies and property taxes by the local authorities have burdened the landlords. This led to the paradoxical situation that certain apartments in Bombay, considered the world's most expensive real estate, are today rented out for as little as Rs 200 per month (the 1940 price) whereas the market rate is Rs 15,000 per month!

The landlords contend that they have been given a raw deal under the Bombay Rent Control Act. They say that while it allows them to pass on the municipal taxes to the tenant, a similar provision does not exist for society charges. With most buildings being owned by cooperative societies, they end up paying society charges that exceed the rent.

According to experts the landlords are angry at the fact that while the rents have remained the same, the municipal taxes have increased from 18 per cent of the rateable value in 1940 to 242 per cent (for commercial premises) and 150 per cent (for residential premises). Similarly, the repair cess that was 25 per cent in 1970 has now jumped to more than 1,170 per cent (commercial) and 575 per cent (residential). Due to the prevailing low rents till date, there was reluctance on the part of the landlords to rent out their premises. As a result, around three to four lac flats are lying vacant in the city, say industry experts.

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<sup>3</sup> Accessed at <http://www.indialawinfo.com/bareacts/mrca.html>

**At \$10,000, Bombay rents are untouchable<sup>4</sup>**

Bombay may be a poor third world city in the underdeveloped world, but its real estate prices tower above anything in Paris, Tokyo or Manhattan. Even modest one-bedroom apartments in the center of this Indian city can top \$10,000, leading Bombay's press to dub it "the most expensive slum in the world." But don't blame landlords for the sky-high rents—the real culprits are a triple-whammy of outdated rent laws that prompt would-be tenants, high-flying multinationals among them, to flee.

We shall now attempt to summarise the adverse effects of rent control on the real estate investment.

## Effects of Rent Control

- The outmoded rent legislation has an adverse impact not only on investment in new housing stock but also on the maintenance, upkeep, up gradation and extension of the old stock. As emphasised by NCU, the foremost and most visible effect of the Rent Acts has been the almost universal deterioration in the condition of old buildings throughout our cities. Because rents are frozen, the owners increasingly find it difficult to keep the buildings in a state of good repair. Whilst the Rent Acts have protected the tenants in terms of the amount that they have to pay and security of tenancy, they have directly contributed to their insecurity in terms of the quality of the building in which they reside.
- Another effect of the Rent Control Act brought out by the NCU is a very substantial reduction in residential construction for rent. All new residential development is invariably for sale, so much so that even state housing boards no longer construct any rental housing. There is also evidence of houses being kept out of the rental market even where the owner does not himself occupy the property. It is the perception of most house owners that once the house is given on rent, it will never be available to the owner. There is the emergence of the parallel economy in which there are lump sum advance payments of rent, partial payment of rent without receipts, etc. The rental market is thus highly distorted.
- Housing Shortage: Reference must also be made to the growing gap between the demand and supply of housing stock for which, among other factors, Rent Act is responsible in no small measure.

## The Present Scenario

However, in December 2001, the Supreme Court, in a historic judgment, declared the 1940 Rent Act outdated, and ordered the state to implement the new rent act from the first week of April 1998, the new Maharashtra Rent Control Act, in force since March 31, 2000. Under the new Act, the landlords are permitted to increase the rent by five per cent every year. Some of the major provisions of this act are as follows:

### Definitions (Section 7)<sup>5</sup>:

#### Provisions regarding Standard Rent

- Standard Rent means Standard Rent fixed by the Court plus an increase of 5%; or the rent at which the premises were first let on or after October 10, 1987.

<sup>4</sup> Accessed at <http://www.nextcity.com/main/town/1planners.htm>

<sup>5</sup> Accessed at <http://www.indialawinfo.com/bareacts/mrca.html>

- Tenant includes deemed tenant, sub-tenant, heir, legal representative, and assignee. Transmission of tenancy shall not be restricted to the death of the original tenant, but shall apply even on the death of any subsequent tenant.
- Rent in excess of Standard Rent is illegal; any contravention punishable with imprisonment up to three months or fine up to Rs 5,000 or with both.
- Increase in rent (Section 11): 4% per annum from the date of the commencement of the Act; 15% per annum for improvements and alterations other than tenantable repairs which the landlord is required to carry out, provided 70% of the tenants consent in writing; 25% per annum for special or structural repairs, exclusive of any repairs, exclusive of any repairs carried out under the MHADA Act; due to any increase in taxes; to the extent of increase.

### Recovery of Possession

No eviction suit can be filed on the ground of arrears until the expiration of 90 days next after notice of demand served upon the tenant.

- No decree for eviction shall be passed in an eviction suit on the ground of arrears, if the tenants pays up within 90 days from the date of service of the summons of the suit, the arrears of rent with 15% interest and continues to pay the standard rent and permitted increases till the suit is finally decided and also pays the costs of the suit.
- Landlord entitled to recover possession from licensee: On expiry of license; in default can apply to the competent authority. Such licensee liable to pay damages at double the rate of the license fee—an arrangement of license in writing shall be conclusive evidence of the fact stated therein.
- Time Limit for disposal of suits/appeals: For suits it is twelve months from the date of service of summons and for appeals, it is six months.

### Right of Tenant and Landlord to receive lawful charges (Sec 56) (i.e., PUGDI)

- It is lawful for the tenant to receive any *pugdi* as a condition of relinquishment, transfer, assignment of his tenancy;
- It is lawful for the landlord to receive any *pugdi* for grant or renewal of a tenancy or for giving his consent to transfer the tenancy to any other person.

Note that the *pugdi* system, under which a landlord receives a lump sum payment (which is related to the market value of his premises) every time there is a transfer of tenancy, is prevalent in Mumbai. The system exists in buildings constructed before 1940, wherein the tenants while leaving the premises had to pay one third of the money received from the new tenant to the owner as *pugdi*.

While exploring the concept of *pugdi* or *pugree* it is interesting to note that the system flourished as a consequence of the frozen rents and a shortage of fresh housing. Generally stating, *pugdi* is nothing but a premium on rent. As the rent itself is not high enough to induce the landlord to let it out, the tenant gives a non-refundable amount based on the market rate of the property to acquire this property. This system evidently originated because there was a ceiling on the rent rates that were miserably low. This practice was in place illegally earlier and none of the parties involved complained as it served needs of both. Astoundingly, instead of removing the abolishing the rent controls the state has decided to legalise *pugdi*. They obviously find it appropriate to rectify the effects of a policy and ignore its inherent causes.

### Conclusion

Thus it is evident that although rent control was initially implemented as a measure to counter scarcity of housing facilities, its continuance has created an antagonising artificial scarcity due to faulty legislation and unnecessary government intervention in spheres of economic activity. The above analysis brings out the seriousness of the issues and their continued neglect over decades. Proliferation of slums in all towns and cities is a direct fall out of these shortsighted policies. All available evidence shows that persons belonging to even lower middle class and middle class families

have to stay in slums for want of suitable rented accommodation. Instead of addressing the root cause of the problem, the government of Maharashtra, for example, has announced populist policies of providing free accommodation to all slum-dwellers. The disastrous experience of the scheme in Mumbai shows the futility of dealing with issues in this irrational manner.