



EVALUATING THE CONSTITUTIONAL VALIDITY OF THE MODES OF ALLOCATION OF NATURAL RESOURCES IN INDIA*

INTRODUCTION

Developing countries like India have a more serious stake in optimizing the use of natural resources than the economically progressed nations. India possesses a large amount of valuable natural resources such as minerals, coal, gas etc. The mode of allocation of these resources is an issue which is politically controversial and has been long plagued by corruption and scams. Following of processes which are opaque for the allocation of such resources leads to favouritism towards those powerful and huge business concerns which have political backing. This, apart from violating various provisions of the Constitution also results in many economic disadvantages such as, monopoly, exploitation of resources, loss of livelihood to indigenous people etc.

Thus this paper aims at addressing the constitutional validity of the present modes of allocation that is followed by the government and suggesting alternatives. This is done by analysing the various judicial pronouncements on this regard and by comparing the mode of allocation followed in India with that followed around the globe.

1. Modes of Allocation of Resources

The allocation of natural resources are one of the most critical and complex decisions that are made by the government and policy makers. When the government gives away public assets, that is natural resources for private or commercial use it must make sure that the process must adhere with the three main principles;

1. Transparency
2. Equal opportunity
3. Protection of public interest

Democracy means government of the people by the people and for the people. Hence, any policy made by the government must be for the benefit of the people. Further the government must also be accountable to the people for such decisions. Transparency in case of allocation of resources is necessary in order to remove arbitrariness. Accountability, as a norm, is concerned

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with preventing abuses of power and a sense of impunity, and is one of the defining hallmarks of democracy.¹

Further under Article 39(a) and (b) of the Constitution the State has a duty to allocate such resources in such a manner as to provide equal opportunity to everyone and ensure that it does not result in concentration of resources. Thus, while such resources are allocated the interest of the people must be kept in mind primarily.

Finally, while allocating such resources it is important for the government to keep in mind the public trust doctrine.² Public trust doctrine serves a two-fold purpose: Firstly, it mandates affirmative state action for effective management of resources and secondly, empowers citizens to question ineffective management of natural resources. Thus this doctrine demands that the government doesn't allocate any of such resources for private use and the state has a duty as a trustee to protect such resources for the beneficiaries – the citizens.

Governments across the world have majorly relied upon four methods to allocate rights to private parties- **Auctions, FCFS, lottery and administrative process.**

Lotteries are allotment of rights through a randomized public drawing. They are an attractive method as they are quicker and require lower administrative costs. Many objections can be made out towards the lottery system which is used to distribute hunting or fishing licenses, alcohol dispensation etc., where this might come off as the epitome of fairness- it ensures equal opportunity but does not guarantee fair allocation. Since some may deserve a more than equal right over the resource. This can be marginally rectified by objectively weighing the probabilities of users receiving a resource. But deciding on the weighting system is hard task.

In the system of **administrative process** the problem of probabilities of users are to an extent satisfied. This method is slow and cumbersome and often the resources are undervalued. The executive settles on prior determined criteria for allocation by constituting meetings or ad hoc processes. This offers flexibility but also incentivizes the politicians to show an opaque version of the agreed dimension for selection, it increases lobbying and rent seeking behaviour and altogether fails in transparency. Lotteries and administrative processes may encourage frivolous applicants and speculators in the former case. They do not guarantee technical or technological competence³.

The **FCFS** system has the advantage of working quickly and cheaply same as lottery. It is more or less fair since applicants who are willing to sacrifice their opportunity cost (albeit low) in appropriating this resource queue up first. (The Oklahoma land rush in 1989). First users may hoard the resource which is detrimental to the later generations. The issue of transparency is another major road block in the FCFS system. As evident in the coal block allocation, the resources were given away for free and in violation of the established legislative procedures. Giving away resources at less than market price is subsidizing private corporations with the tax payers' money.

On the other hand, **Auctioning** enables the revelation of the actual market price, and costs. Since entry into industries where resources are being auctioned is easier rather than in the administrative process, it is an anti-monopoly technique. Further auction rules can be designed

¹ R Caplan, 'Who is guarding the guardians? International accountability in Bosnia and Herzegovina', International Peacekeeping, Vol. 12, No. 3 (Autumn 2005), available at, <https://www.dur.ac.uk/resources/law/LCD/Caplan--Durhamwebsite.pdf> .

² M.C. Mehta v. Kamal Nath, AIR 2002 SC 1515.

³ Joseph E. Stiglitz, Making Natural Resources into a Blessing rather than a Curse, available at, https://www0.gsb.columbia.edu/faculty/jstiglitz/download/papers/2005_Covering_Oil.pdf .

to favour the public policy. Auctioning will increase the revenue for the government, but might lead to higher prices or tariffs as companies might speculate to acquire the limited resource.

Indian Scenario:

The past few decades, India has seen an ongoing debate contemplating the most efficient or optimal mode of allocation of scarce resources.

Following the uproar over the 2G and coal block scams, the Supreme Court responded to it through the following judgments;

While deciding the case of *Centre for Public Interest Litigation v. Union of India*⁴, The Apex Court observed that natural resources are of intrinsic utility to mankind. Its value is determined by its availability and demand; albeit it belongs to the people the state legally owns them. While distributing natural resources, the State is bound to act in consonance with the principles of equality and public trust and ensure that no action is taken which may be detrimental to public interest. Article 39(b) directs the state to appropriate resources so as to sub serve the common good. The court cited the relevance of international environmental laws to determine the ownership regime of property rights of scarce natural resources. Likewise, the state is expected to act as the guardian and trustee of these resources.

The Court opined that, *a duly publicised auction conducted fairly and impartially is perhaps the best method.*

However, in the second spectrum case, that is *Natural Resources Allocation, In re, Special Reference*⁵, the contention whether the only permissible method for disposal of all natural resources across all sectors and in all circumstances is by the conduct of auctions, was clarified by the court. It was held that, the general application of auction was not meant to mandate it as the only method of alienation of natural resources but was specific to the first spectrum case because such a mandate would call into question the constitutional legitimacy of many laws enacted, which cannot all be deemed ultra vires before discussing their individual merits.

Subsequently, in the case of *Manohar Lal Sharma v. Principal Secretary*⁶, the court suggested that allocation through auction maybe the best mode only when the aim of an allocation is to maximise revenue; under Article 14, it is the only method that bears a rational nexus with an objective of revenue maximisation. However, executive may employ any other alternative method as long as it is consistent with article 14 and article 39(b).

Further the **recommendations forwarded by FICCI** to the Ashok Chawla Committee, particularly with regard to mining, were that keeping in mind the under explored resources of India, it is important to incentivize investors. FICCI said that a transparent, auction-based system similar to NELP (National Exploration Licensing Policy) can be adopted while granting license for fully explored blocks of minerals, other areas should be granted on First-Come-First-Served basis subject to competitive criteria of technical expertise, financial resources and investment proposed.⁷

Thus, among the other methods of allocation, auction has been considered as one of the best way to allocate resources. This is mainly because it is believed to be a transparent process when compared to the administrative process. Auctions urge the government to reveal

⁴ Centre for Public Interest Litigation v. Union of India, (2012) 3 SCC 1.

⁵ Natural Resources Allocation, In re, Special Reference No.1 of 2012; (2012) 10 SCC 1.

⁶ Manohar Lal Sharma v. Principal Secretary, (2014) 9 SCC 516.

⁷ Ficci's Recommendations To Ashok Chawla Committee On Allocation Of Natural Resources, Apr 30, 2011, available at <http://www.ficci.com/PressRelease/764/press-may2-chawla.pdf> .

determinant criteria prior to the bidding, auction rules and dates for the process are advertised well in advance which was not done in the 2G spectrum allocation. The openness of auction prevents the suspicion of undue influence, impropriety or even corruption that can rise if the decisions are made behind closed doors.

However, on further contemplation the social costs and other defects of auctions come to the fore front.

Problems of Auction Process:

Though auctions have been considered so far as the best mode of resource allocation, it has the following glaring issues;

Will they cure the disease that is- of resource rich countries with poor people?

Do they increase social welfare in compliance with Art 39(b)?

What will be its long term effect on the natural resource market?

The first and major defect of the auction method is that it increases the costs of production for the manufacturers and the burden is ultimately transferred to the consumers thus defeating Art 39(b) per se. If deposits like iron ore and bauxite are auctioned, commodities like steel, aluminium and cement will become costlier. This is not an efficient solution from both legal and economic perspective.

Economic logic establishes that alienation/allocation of natural resources to the highest bidder may not necessarily be the only way to sub-serve the common good, and at times, may run counter to public good. In the real world, consumers are made to pay the maximum price that they are willing to pay in order for the producers to gain more producer's surplus and deprive the consumer off their surplus. Though this may not be accepted from a welfare point of view, from economic perspective the surplus, whether enjoyed by consumers or producers both ensure allocative efficiency. However, the competitive auction method demands from the producer the maximum price that they could possibly afford to obtain the license and as a result they end up charging high prices to consumers. Hence, this result in economic inefficiency as the surplus is neither enjoyed by the producers nor the consumers.

This can be directly related to the legal perspective of the issue. According to Art 39(b) of the constitution which demands that the ownership and control of the material resources of the community should be distributed as best to sub-serve the common good is also violated here. If neither part of the community gains (neither producers nor consumer) through this method then such a method cannot be considered as one that best sub-serves the community good. Thus it can be termed as unconstitutional.

Alternative solution:

In the light of the above summarized defects the court in the second spectrum case, held that the auction process for resource allocation is not a constitutional mandate; and that revenue maximization alone cannot be the sole criterion for deciding an allocation process. It is pertinent to observe other alternative methods which are capable of setting off the defects of auction process;

1. The first come- first serve basis and the auction method are two extreme cases and there has to be an intermediary between them.

Hence, there should be a combination of methods. First the prospective companies have to be short-listed based on few important parameters and criteria and then auction should be conducted among them. This can eliminate the problem of inefficient prospects.

For industries such as mining the method cannot be completely aimed at enhancing transparency but value-addition should also be taken into consideration.

Hence, a combination of methods will lead to efficiency, transparency and maximizing revenue.

2. Another possible solution to resolve the battle between auction and other methods could be for the government to allow the recipients to resell in secondary market. In this way, the government's method of allocation matters less if it permits resale than if it doesn't. Hence, it can avoid corruption and lobbying by bureaucrats and industrialists. Additionally with respect to spectrum allocation - **Spectrum pooling**⁸ can be used as an alternative solution to combat the issue of inefficiency in the auction system. Spectrum pooling is a spectrum management strategy in which multiple radio spectrum users can coexist within a single allocation of radio spectrum space. One use of this technique is for primary users of a spectrum allocation to be able to rent out use of unused parts of their allocation to secondary users.

This method provides an incentive to the primary license holders to rent out the unused space and not retain it idly

Hence, with an open secondary market, regardless of the initial mode of allocation, the resources would eventually find its own way to reach that user who makes the best use of it, thus ensuring efficient resource utilization.

Conclusion

Natural resources are not homogeneous in nature and require different treatment in alienation. There is **no uniform policy** for the allocation of scarce natural resources, any attempt at generalizing the system of auction or the FCFS system will only be short sighted.

Hence, government should develop a combination of strategies for resource allocation which is quiet flexible so as to be fitted to various circumstances and situations. As it is rightly said that "One size cannot fit all" - one method cannot be used for all conditions and circumstances.

Hence, a combination of methods which will lead to efficiency, transparency and maximizing revenue – thereby in lines with the constitutional provisions, is the need of the hour.

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⁸ Friedrich K Jondral, Cognitive radio – A necessity for Spectrum Pooling, Feb 6, 2006, *available at*, https://www.google.co.in/url?sa=t&rct=j&q=&esrc=s&source=web&cd=9&cad=rja&uact=8&ved=0CFQQFjAI&url=http%3A%2F%2Fdigbib.ubka.uni-karlsruhe.de%2Fvolltexte%2Fdocuments%2F698872&ei=jdI4VdG7AYKfugSx4YDgCA&usq=AFQjCNGupNH Sq7jxCJht2Ed55Qvj2qZG-Q&sig2=jd8eajsIE6C_yLTTTCQE8eA&bvm=bv.91427555,d.c2E