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The "Principal-Agent" Problem in Indian Agricultural ACT, 2020

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Review Article

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ABSTRACT

The farmer's produce trade and commerce (promotion and facilitation) bill, 2020, and the farmers (empowerment and protection) price assurance and farm services bill, 2020, were approved and notified as legislation at the end of September 2020. The proposed legislation's primary provisions were aimed to aid small scale farmers who have no way of negotiating a better deal. The agriculture bill aimed to allow farmers to sell their produce to anyone they want outside of 'mandis.' Everyone was welcome to buy their produce even at their farm gates. Despite the fact that 'mandi commission agents' and states may lose 'commissions' and 'mandi fees,' respectively. This remained the main reasons for the protests along with the neglect of MSP and the loss of commission agents' jobs. This paper attempts to study the problems in bill in light of Principal agent theory and suggests a way forwards for the farmers and government to come to a common ground.

INTRODUCTION

Recent agricultural reforms, the farm bill 2020 are three acts of the Parliament of India of September 2020 that have produced a rather astonishing result in India [1]. The bills aimed to provide several marketing outlets for farmers and provide a legal basis for, among other things, farmers to enter into pre-arranged contracts. The bills were authorized on 17

September 2020 by the Lok Sabha and on 20 September 2020 by the Rajya Sabha. Ram Nath Kovind, the President of India, gave his assent on 27 September 2020. In September 2020, protests against the acts were raised, especially in Delhi, Punjab and Haryana, where farmers were at the forefront.

Principal agent theory

In political science, supply chain management and economics (also known as the agency dilemma or the agency problem), the principal-agent issue arises when one individual or entity (the "agent") is able to make decisions and/or take action on behalf of another person or entity: the "principal" or the consequence [2]. Corporate management (agent) and shareholders (principal), elected officers (agent) and people (principal), or brokers (agent) and markets (buyers and sellers, principals) are typical examples of this relationship. When an agent works on behalf of several principals, the organization issue may be compounded. The multiple principals must agree on the goals of the agent when one agent acts on behalf of multiple principals, but face a problem of collective action in governance, as individual principals can lobby the agent or otherwise act in their individual interests rather than in the collective interest of all principals. As a consequence, in steering and monitoring, duplicate steering and monitoring, or dispute between principals, there might be free-riding, all leading to high autonomy for the agent [3]. The multiple principal problems have been coined and are a serious problem, especially in the public sector, where multiple principles are common. In the absence of salient governance, both productivity and democratic transparency are compromised. For example, this issue can arise in the governance of executive powers, ministries, departments, inter-municipal collaboration, public-private partnerships, and multi-shareholder companies.

In economics, the principal agent theory was established to analyse the problems associated with a situation where the principal recruits an agent to perform a task. The biggest obstacle in their relationship stems from the fact that the principal and agents do not have precisely matched interests, and asymmetrical information is available. Very frequently, the principal has little access to sensitive information about the agents. The theory of principal agents helps to define incentive systems and other mechanisms that reduce the asymmetric knowledge problem.

Research background

In India, agricultural markets are primarily controlled by state laws of the Agriculture Produce Marketing Committee (APMC). In order to ensure fair trade between buyers and sellers for effective price discovery of the produce of farmers, APMCs were established [4]. APMCs can: (i) regulate trade in the produce of farmers by granting licenses to buyers, commission agents and private markets; (ii) levy market fees or any other charges on such trade; and (iii) provide the infrastructure necessary to facilitate trade within their markets.

The Standing Committee on Agriculture (2018-19) noted that the laws of the APMC are not applied in their true sense and urgently need to be reformed. Issues that the Committee has found include: (i) Many APMCs have a small number of operating traders, which contributes to cartelization and decreases competition, and (ii) excessive deductions in the form of commission fees and market fees. Traders, commission agents and other functionaries are organized into partnerships that do not allow new people to enter market yards easily, stifling competition.

During 2017-18, the central government released the model APMC and contract farming Acts to allow restriction free trade of farmers' produce, promote competition through multiple marketing channels, and promote farming under pre-agreed contracts. The Standing Committee (2018-19) noted that some of the changes proposed in the model Acts have not been adopted by states. It suggested that a Committee of Ministers of Agriculture of all States be set up by the central government to find consensus and design a legal framework for agricultural marketing. In July 2019, a High-Powered

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Committee of seven Chief Ministers was formed to address, among other things: (i) the adoption and time-bound implementation by states of model acts, and (ii) Amendments to the 1955 Essential Commodities Act (which provides for regulation of the production, procurement and exchange of essential commodities) in order to encourage private investment in the marketing and infrastructure of agricultural products.

The central government promulgated three Acts on June 5, 2020: (i) the Farmers' Produce Trade and Commerce (Promotion and Facilitation) Act, 2020, (ii) the Farmers (Empowerment and Protection) Agreement on Price Assurance and Farm Services Act, 2020, and (iii) the Essential Commodities (Amendment) Act, 2020. The Acts collectively seek to (i) promote barrier-free trade in agricultural products outside the markets notified under the various state APMC laws; (ii) establish a contract farming framework; and (iii) place stock limits on agricultural products only if retail prices increase sharply. The three Acts seek to increase farmers' opportunities to enter into long-term sales contracts, increase availability of buyers [5].

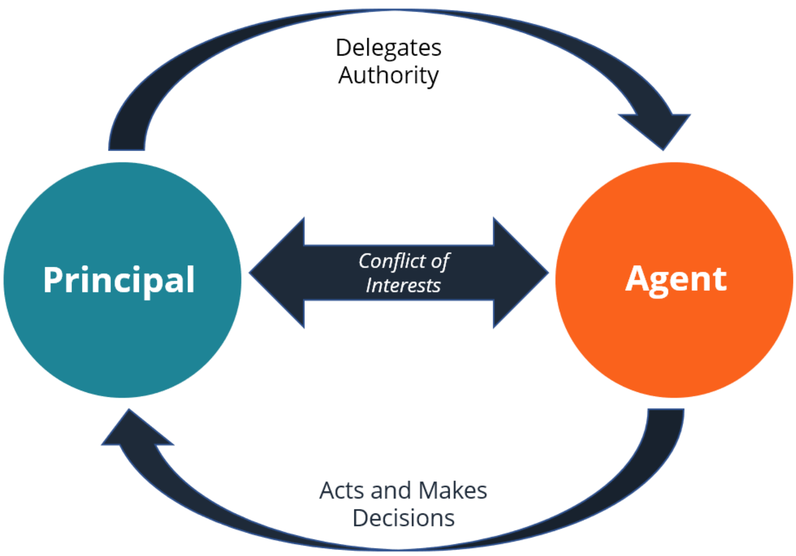
In brief, the Farmers' Produce Trade and Commerce (Promotion and Facilitation) Act allows farmers in the newly developed "traded areas" to sell produce outside the APMC (Agricultural Produce Marketing Committee) mandi yard. Any purchaser with a PAN card can buy directly from farmers in these areas without the requirement of licensing and commission fees.

The Farmers (Empowerment and Protection) Agreement on Price Assurance and Farm Services Act provides architecture for contract farming, and the Essential Commodities (Amendment) Act eliminates the restriction on the stocking, movement and export of agricultural commodities [6].

Principal agent problem: The Acts are intended to reduce the barriers in the supply chain of agriculture, liberate agriculture from the domination of Arhtiyas (intermediaries) and provide a mechanism to ensure a pre-determined price for farmers at the time of sowing and mitigate the impact of the cobweb phenomenon.

The Acts, the government (agent) says, would allow private players to invest in the agricultural sector, in particular marketing infrastructure, leading to higher productivity and farmers' prices. The Acts are intended to help create a single unified agricultural market, allowing farmers to sell their produce nationally [7].

However, the farmers (principal) call the Acts anti-farmer, saying they would result in untimely withdrawal of the government from the agriculture sector. Their key concerns are: the state will no longer support farmers *via* MSP (minimum price of support) and weaken the system of state procurement; and the farmer will be left at the mercy of large corporate buyers without an appropriate regulatory structure, who will ultimately assume monopsonic control, reducing farmers to price takers.



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In principal agent relationships, the differentiation of the "ownership" (principal) and the "control" (agent) creates the grounds for potential conflict of interests between the two parties.

LITERATURE REVIEW

No brief summary can do righteousness to the great diversity of issues and problems well-thought-out in this literature except probably this that a perfect agent for numerous reasons is pretty much impossible and in several cases a great gap exists between what the agent does and what the principal wanted him to do with any possible intervention agreement.

Higgs (2018) argues that the in genuine political representations result in The Iron law of Oligarchy. Small numbers of people make a decision which suits them and their supporters for the general public [8]. They paint their choices with philosophical tones to win the certainty of general public. The issue isn't just that the purported agents are terrible and corrupt, however they might be. It’s that the occupation they imply to do is impossible even by the best most honest conceivable delegate ever. No agent can really speak to a variated gathering of interest particularly a huge gathering whose individuals differ along numerous measurements. A few principals have their advantage apparently encouraged, others won't. The last will essentially be prospered by the power of law to submit.

György believes that the biggest issue for agents can easily be found in the public sector rather than in the private sector. Various examples of relationships marked by knowledge asymmetry present us with various points of view. The primary elements of the binomial are the principal and the agent. In the literature, the most commonly mentioned examples are: People (P)- Elected candidates (A), Taxpayers (P)- Elected officials (A), Parliament (P)- Public Authority (A), central administration (P)-Decentralised local administration (A), Public authority (P) -people working for government (A), Public authority (P)- Contractors/vendors (A).

Solutions adopted to solve principal agent problem

Gary J. Miller believes that in particular, in the infinite variety of contractual structures that can regulate transactions within organizations, rewards, supervision, and cooperation can and do play significant role in solving principal agent problems. Different solutions build very distinct types of organizations. Some organizations that rely heavily on incentives are known for a free-wheeling, risk-taking, entrepreneurial style of decision making, such as marketing giant Pepsico. Others who use monitoring more, such as manufacturing giant general motors, which means that employees are often described as "bureaucratic," by looking to hierarchical supervisors and standard operating procedures for justification of their behavior, they prefer to avoid risk-taking [9]. The observer sees high levels of cooperation and coordination in other organizations, including Southwest Airlines. Such behavioral features can be interpreted as a derivative of the various types of contracts and transactions that occur in response to various types of relationships between principal and agent. Although numerous solutions are possible, no one solution is ideal or rather, since no one solution is optimal, there are many solutions. Except in "ideal" circumstances (with zero risk-aversion and no knowledge asymmetry), with each type of attempted solution, agency costs continue. There are, however, some measures that indicate circumstances in which one form of solution might be better than others in a systematic way.

Tirole in his study shows that there are cases in which collusion (more accurately called "cooperation") can be useful than any other form of solution to the principal-agent problem.

In the principal-agent problem, cooperation seems to indicate circumstances in which both principal and agent might come

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to one common ground.

Solutions steps follwed in the farm bill 2020

Over the past 43 days, farmers' organizations have protested against the three farm laws namely, Farmers' Produce Trade and Commerce (Promotion and Facilitation) Act, Farmers (Empowerment and Protection) Agreement on Price Assurance and Farm Services Act, and the Essential Commodities (Amendment) Act. While the government has given many assurances that farmers will be 'empowered' by the laws, the protesters were firm on their demands that the laws be rolled back. Thousands of farmers, mainly from Punjab and Haryana, have been camping at several border points in Delhi, demanding the full abolition of the three agricultural laws and the legal guarantee of a minimum support price for their crops. Though adhering to their demands, farmers' leaders agreed that they were prepared to hold talks with the government as long as they debated repealing the three new farm laws before anything else. Till today's date, there have been 5 rounds of meetings between the farmers and the government. No common solution or agreement has emerged in these five rounds. Once again, the fifth round of meetings (December 5, 2020) between protesting farmers' groups and the central government failed to draw any conclusion, with farmers sticking to their stance on a full reversal of the controversial new farm laws, and the central government reiterating that it was possible to resolve all the sticking points, including reservations about the Minimum Support Price (MSP) mechanism.

Government's proposal: Documented government assurance for the continuation of the current MSP scheme

Farmers' rejection: Farmers are not only apprehensive, but fully persuaded that APMCs are being dismantled by the new agricultural rules. They therefore demand that the government should introduce a comprehensive MSP Act for the entire country and for all crops. They assume that the government is pulling its feet to put legislation on this issue and just talks of a written assurance, which is not a legal document and has no guarantee. That is why farmers ignored the government's written guarantee proposal and insisted on repealing the anti-farmers laws.

Government's proposal: State governments could register traders to control them

Farmers' rejection: There is no provision in the new farm laws to control traders. These actions grant any PAN cardholder permission to procure grains at desired prices from the markets and to engage in hoarding. The Central is attempting to pass the buck to state governments to control the traders instead of making registration arrangements to monitor the traders. The Centre is, therefore, not prepared to take any responsibility for this matter. Under pressure from farmers' organizations, this is also being proposed.

Government's proposal: Under the contract farming rule, farmers will have the option to approach the court and their land will be safe because by mortgaging it, no loan will be granted on the land of farmers and their houses.

Farmers' rejection: Farm outfits are apprehensive about the big companies taking possession of the farmers' land under the contract farming contract. The Government of the Union has put forward a proposal to mitigate the concerns of farmers by specifying that no land will be sold, rented or transferred during the contract agreement period. But the past of contract farming has several stories of businesses making different reasons for non-payment. In the case of sugar cane, where payments have been kept for several years or cases of non-procurement with low quality reasons, this has occurred. This forced the farmers into a pit of debt. Farmers are unable to repay the loans in such cases and have no other choice but to sell or lose their land. Contract farming has contributed to the displacement and devastation of farmers around the world.

Government's proposal: The private mandis can be paid fee/cess by state governments

Farmers' rejection: Together with the state-run Agriculture Produce Market Committees (APMC), the development of private mandates would drive all agricultural enterprises toward private markets. The end of government markets and intermediary

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(commission agent) systems as well as APMC systems would be the outcome. After that, only major traders and giant corporations can operate in the markets and at incidental rates can procure farm produce. The government has indicated that both the government and private markets would have a uniform tax, cost, and cessation policy. But, as in the case of paddy, the governments will purposely postpone procurement and make public markets ineffective and redundant.

Government's proposal: The 2020 Power Bill is just a draft open for debate.

Farmers' rejection: By taking the power sector from the authority of states, the government of the Union wants to regulate it. It requires farmers' subsidies to be withdrawn. The WTO has given the Indian government repeated orders to discontinue the subsidies. The Modi government, therefore, wants to place the power sector under central control. This move is being opposed by the farmers. The government proposes to remove subsidies from this bill and suggests that power subsidies would be transferred in cash to farmers, which is virtually unlikely if there are a majority of small and marginal farmers who are unable to pay their power bills first and then to benefit from subsidies.

Government's proposal: Willing to amend the NCR pollution control Act

Farmers' rejection: The Union government claims that in Delhi, stubble burning of paddy is responsible for pollution and so they have enacted a law of strict penalties and heavy fines for the suspected violators up to Rs 1 crore. Now the government is considering reforms under pressure from farmers' organizations. This law is aimed solely at intimidating poor and small farmers.

Farmers believe that the proposed reforms have little to give, and farmers' groups are ready to continue the unified war until these Acts are repealed.

Farmers in support of legislation: A coalition of 10 farmers' unions extended its support to the Central Government on 14 December for its decision to make the required reforms to the three farm laws. The community of farmers belonging to states such as Uttar Pradesh, Bihar, Haryana, Kerala, Tamil Nadu and Telangana shared their support under the banner of the All India Kisan Coordination Committee after a meeting with Narendra Singh Tomar. In support of farm legislation, 20,000 Kisan Sena members marched to Delhi on 24 December.

Perceived benefits

- **Sale option:** The bill gives farmers the long-sought freedom to sell their produce through more than one APMC channel.
- **Trade promotion:** It would also facilitate inter-state and intra-state barrier-free trade and trade outside the physical premises of markets notified under the Marketing Laws of State Agricultural Products.
- **Better prices:** It would also enable farmers in regions with surplus demand to receive better prices and lower prices for consumers in regions with shortages.
- The Bill essentially aims to build new trade opportunities outside the APMC market yards to help farmers achieve remunerative prices due to additional competition.
- **Level playing field:** New legislation would allow farmers without fear of abuse to negotiate with producers, wholesalers, aggregators, wholesalers, major retailers, exporters, etc., on a level playing field.
- **Risk transfer:** The risk of market unpredictability will be shifted from the farmer to the sponsor and will also allow the farmer to access new technology and better inputs.
- **Private sector attraction:** this legislation would serve as a catalyst to draw investment from the private sector in the development of supply chains to supply Indian farm produce to domestic and global markets and to agricultural

infrastructure.

- **Eliminate intermediaries:** Farmers can participate in direct selling, thus removing intermediaries, resulting in maximum price realisation.

Perceived loopholes

- The Farm Bills hamper the monopoly of the mandis of the APMC (Agricultural Products Market Committee), enabling the selling and purchase of crops outside those state-regulated market yards or mandis.
- MSP is not granted any legal backing by the Farmers' Produce Trade and Commerce (Promotion and Facilitation) Bill.
- MSPs for crops are declared by the government, but there has been no legislation mandating their enforcement.
- Sugarcane for which FRP is calculated is the only crop where MSP payment has any legislative enforcement. This is attributable to the Sugarcane (Control) Order, 1966, issued under the Essential Commodities Act, regulating its pricing.
- The new bills put farmers and merchants, rather than the courts, at the hands of civil servants.

Way forward: The free market can damage lakhs of unorganized small farmers without strong institutional structures, who have been remarkably efficient and have shored up the economy even during a pandemic.

DISCUSSION

- The discussion should be about how to boost farm productivity and increase the income of farmers. In order to achieve this, by supporting more farmer producer organizations and encouraging Panchayati Raj institutions to set up village marketing organizations, there is a need to expand the existing marketing infrastructure.
- Improving agricultural infrastructure to improve competition: Government should massively finance the expansion of the market system for the APMC, make efforts to eradicate trade cartels and provide good highways, scale logistics and real-time information to farmers [10].
- Empowering state farmers' commissions: Rather than opting for heavy centralization, the focus should be on empowering farmers to respond quickly to issues through the State Farmers' Commissions recommended by the National Farmers' Commission.
- Incorporation of quantity guarantee clause: Instead of MSP as a price guarantee that farmers are seeking, for a minimum duration of 5 years, government could insert a quantity guarantee clause that procurement of the production percentage of crops (currently procured) should be at least equal to the percentage of last year (with safeguards in exceptional events such as droughts, floods. This would significantly alleviate the farmers' concerns.
- Conversion of MSP to floor auction price on eNAM: The government should consider transferring the MSP to the National Agriculture Market (eNAM) floor price auction.
- Strengthening business infrastructure for APMC: Efforts must be made to improve the infrastructure of the Agricultural Produce Market Committee (APMC).
- Establishment of contract farming institutions: With the exclusive right to supervise price discovery in contract farming, the government should create a contract farming institution in India. In several countries, contract farming

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has been instrumental in providing growers with access to market-and price-stability supply chains, as well as technical assistance.

CONCLUSION

This paper attempts to study the problems in bill in light of Principal agent theory and suggests a way forwards for the farmers and government to come to a common ground.

Need for a versatile framework for KCC: Revisiting the Kisan Credit Card (KCC) standards, the SBI study indicated that it would increase farmers' monthly income by 35 percent. It is recommended that, in conjunction with the government, RBI incorporate operational flexibility into the KCC framework and direct banks to assign a specific percentage of their loans to Agri-based start-ups in particular in order to improve Agri-supply chains.

Consensus Building: The centre should reach out to critics of the bills, including farmers, clarify the need for change to them, and get them on board.

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