Scope and modalities of restructuring state owned enterprises in India

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Abstract

State Owned Enterprises (SoEs) play a prominent role in the industrial and overall economic development of a developing country. India opted for mixed economy framework soon after the independence, which provided space for both the SoEs and the private sector. The private sector was, however, not as matured and vibrant at the time of Independence as today. SoEs had therefore, to step-in for a quick catch-up with the developed countries. From hindsight, it is apt to agree that the SoEs in India played the historic role in the economic development of the country.

The present paper tries to discuss the role of SoEs in promoting economic development, reasons for their failure, restructuring mechanisms, policies for reviving and key challenges faced by these enterprises.

SoEs and Economic Development

State Owned Enterprises (SoEs) were set up to serve the broad macro-economic objectives of higher economic growth including self- sufficiency in production of goods and services, long-term equilibrium in balance of payments and low and stable prices meeting certain socio-economic obligations. During the first five-year plan there were only five enterprises with an investment of Rs 29 crore. SoEs were established in dominant sectors such as petroleum, coal, steel, mining and transport & logistical services. Constantly the number and the investment in these enterprises increased to 339 enterprises with Rs 13.73 lac crore[1]. Several greenfield projects were initiated which were categorized as essential goods and services. These enterprises were under pressure to meet the competition and to achieve goals. The gross revenue from operations of SoEs has increased by 10 per cent recording their contribution of around nine per cent to GDP during 2017-18[2].

SoEs had their heyday between 1960s and 1990s during which period they had an astronomical growth not only in terms of numbers but also in terms of investments. As on April 1, 1961 there were 47 SoEs with an investment of Rs. 948 crores. There has been multifold increase in the number of SoEs, their paid-up capital, contribution to GDP, gross value added, etc. The SoEs stood at 339 with an investment of Rs 2.49 lakh crore showing an increase of 7.68 per cent during 2017-18. SoEs contribution to economic development is determined by the number of enterprises, sectoral presence, investments, contribution exchequer, market capitalization, employment generation, net value addition, foreign exchange earnings, etc. There has been an increasing trend that has been recorded in terms of investment by 10.24 per cent, total income by 11.61 per cent and capital employed by 6.87 per cent. Table 1 depicts the growth of investment from 2011-12 to 2017-18.

Table 1: Growth in Financial Investment

Particulars	Total Investment (Rs. in crore)	Increase over previous year (%)	Enterprises (Nos.)
2011-12	7,29,298	-	260
2012-13	8,45,334	15.91	277

[1]Public Enterprise Survey, Department of Public Enterprise, Government of India, Volume 1, 2017-18 pg 1
[2]Public Enterprise Survey, Department of Public Enterprise, Government of India, Volume 1, 2017-18 pg 7

2013-14	9,92,095	17.36	290
2014-15	10,95,554	10.43	298
2015-16	11,61,018	05.98	320
2016-17	12,45,819	07.30	331
2017-18	13,73,412	10.24	339

SoEs contributes to the Central Exchequer by way of dividend payments, interest on government loans and payment of taxes and duties. Table 2 depicts SoEs contribution to the exchequer from 20014-15 to 2017-18. It is evident that there has been an increase in the dividends paid, interest earned, and taxes paid in the form of excise duty, custom duty, corporate tax, service tax including GST.

Table 2: Contribution to Central Exchequer

(Rs.in crore)

Sr. No.	Particulars	2017-2018	2016-2017	2015-2016
1	Interest on Central Government Loans	391	477	7,483
2	Dividend on Central Government Equity	42,312	45,196	42,027
3	Central Sales Tax	1,182	4,743	3,663
4	Central Excise	1,77,843	1,90,622	1,39,602
5	Customs Duty	13,624	12,196	9,952
6	Corporate Tax (incl. Fringe Benefit Tax)	51,364	52,957	42,827
7	Dividend Tax	13,586	14,221	11,398
8	Other Taxes and Duties	17,521	30,409	11,869
9	Service Tax	2,527	9,992	7,019
10	Non-Tax Revenue	2,099	-	-
11	Goods and Services Tax (CGST+IGST)	27,604	-	-
	Total	3,50,052	3,60,815	2,75,840

Internationalisation has encouraged SoEs to earn foreign exchange. SoEs has a gross foreign exchange earnings of more than 1000 crore. Out the 15 SoEs, 13 have shown an increase in years over the last year. SoEs provided employment opportunity to more than 14,66,694 people as on 31.03.2018. Employment in SoEs is spread across managerial/executive, supervisory and non-executives in corporation, the offrole include casual and daily employees and contract. The on-role employees are 10,88,140 employees with a share of 74 percent in the total employees in SoEs. The unorganized sector with off role employment is occupied by 26 percent in the total employees of SoEs. Table 3 depicts the employment details of SoEs in India.

Table 3: Break-up of Total Employment

Category	Sub-Category	No. of employees		%Change
		31.03.17	31.03.2018	
Managerial/Executives		265484	266478	0.37
Supervisors	Unionised	76931	79096	2.81
	Non-Unionised	28063	29629	5.58
Workers	Skilled	566505	521778	(7.89)
	Unskilled	198692	191159	(3.79)
Casual/Daily Rated Workers		30638	40060	(30.75)
Contract Workers/Employees		336780	338494	0.51
Total		1503093	1466694	(2.42)

The Net value addition by SoEs increased from Rs 6.92 lakh crore in 2016-17 to Rs 7.17 lakh crore. The share of net value addition to GDP stood at 4.28 per cent during the same year. The Table 4 details the component of NVA in CPSEs (Rs in crore).

Table 4: NVA in SoEs

Sl. No	Net Value Addition	2017-18
1	Profit Before Tax (PBT)	187697
2	Interest	53303
3	Indirect Taxes and Duties	305997
4	Salaries and Wages	157621
5	Rent and Royalty	12626
	Total	717244

Review of related studies

The phenomenal increase in the number of SoE reform programmes in both developed and developing economies has generated a lot of research interest. The bulk of the research efforts, however, are intuitive, mainly theoretical and country specific. They address many questions and majority ones being: why governments have opted for reforms, how reforms were implemented, the degree of implementation and the problems encountered (Onis, 1991; Ramandaham, 1989). While many of these studies are useful to policy makers to carry out successful state enterprise reform, they do not address how privatization and reforms have affected the performance of divested firms and they do not highlight the outcomes. Very few studies analyse the impact of public enterprise reform on profitability, productivity, exports, budgetary impacts, etc. In a study, Bishop and Kay (1988) compared the performance of a number of privatized firms in the United Kingdom (shipping, airline, gas, telecom, oil and automobile industry) with another set of firms under state control (in rail, steel and postal sector) using several indicators, including revenue, employment, profit margin and total factor productivity. The World Bank (1996) conducted a very innovative study on the political economy of state enterprise reform and investigated the economic problems that arise when governments own and operate enterprises that could be managed by the private sector and the political obstacles to reforms. Barnett (2000) investigated the relationship between macroeconomic parameters and privatisation of SoEs. According to the study the reforming SoEs through privatisation, transferring the proceedings of privatised SoEs to budget would help in domestic financing. This would help the economy to overcome large fiscal deficit. Balbuena (2014) in the OECD working paper discussed the SoEs governance reforms and challenges across Southern African Developing Community region. The report provided facts and figures aiming to improve corporate governance of SoEs. These studies throw light on reforming of SoEs including revival, restructuring, and privatization. These are relevant for developing and developed economies.

Reasons for failure of SOEs

Sickness is a universal phenomenon. Sickness is a symptom of ailment and not an ailment. During 1970, there were 22,500 sick units in India which grew some ten times over a decade. Many financial institutions resources are locked up in sick units, large, medium and small. The incidence of sickness, quite understandably, has been a cause of considerable concern to the government, financial institutions and banks.

Sickness in SoEs has been a continuing concern of the Government. The reason for sickness varies from enterprise to enterprise. In some cases, the cause of sickness is inception, historical, economical, market conditions, etc. Due to these reasons some SoEs have been incurring losses continuously for the last several years. The problem of sickness in SoEs is addressed by the administrative Ministries/ Departments in the Government by evolving appropriate need-based strategy concerning these enterprises. The accumulated losses in these sick enterprises have surpassed their net worth. The various reviews identified the two reasons for sickness are financial and operational. The financial and operations reasons include higher that prudent level of leveraging for the industry, project cost overrun, funds diversion out of the project, funding of long term assets with short term funds, bunching debt servicing obligations, new project coinciding with a downturn in the industry, operating profits insufficient to serve debt, very high level of receivables, inadequate debtor recoveries

It is interesting to mention that as a part of restructuring exercise and to fight for successful existence in the global market, the merge of Air India and Indian Airlines, Rashtriya Ispat Nigam Ltd and Steel Authority of India Ltd and Oil Group Companies were considered. The Indian Post is an excellent

example of undergoing restructuring to come back with a big bang to take on private sector couriers and couriers from abroad such as DHL. The Indian Railways are not lagging and giving a tough fight to the private sector Airlines.

The following matrix categorizes the SoEs basing on the type of sickness, causes of sickness and response strategies:

Type of sickness	Diagnostic status	Basic Cause (s)	Response strategy
Genetic	Decision Failure	Varied technologies, economics or management related issues	Restructuring with heavy or critical inputs
Structural	Intrinsic	Decisions on location feed stock, technology product	Restructuring or management interventions
Operational	Acquired	Management failure, lack of leadership faculty HRM,	Needs management interventions
Policy Linked	Based on parameters	Conditions imposed by policy decisions	Policy change or adjustments
Environmental / Exogenous	External Factors	Industry, location	Needs management and policy interventions

Restructuring of SoEs

Restructuring is the modern mantra for survival of SoEs. This is an approved strategy to revive the operations of an entity and make it profitable once again or decide to close in case it can't be revived. The other techniques that have been adopted by most of the enterprises is mergers or acquisitions. Organizations need to adopt a result-oriented approach that not only keeps the organization on the move but also enables it to target a new destination or higher goals. Hence restructuring is a continuous process driven by the corporate vision. Corporate restructuring is the act of partially dismantling or otherwise reorganizing a company for the purpose of making it more efficient; more profitable; attain greater efficiency; adapt to new markets; liquidating projects obsolete and unviable in some areas; redirecting assets to other existing or new areas. SoEs are going for diverse type of restructuring such as manpower, operations, strategic, financial and organizational restructuring including setting up of joint ventures.

The Reserve Bank of India was constantly monitoring the industrial sickness in the country. During the year 1975 RBI has appointed a study group. The Government of India has constituted an Experts Committee during 1981 to examine the industrial scenario in the country and recommend suitable remedies, therefore. Based on the recommendations of the Committee, the Government of India enacted a special legislation known as the Sick Industrial Companies (Special Provisions) Act (SICA), 1985.

The SICA[3]1985 was amended in the year 1991 bringing industrial public sector enterprises under its purview. SICA defined sick enterprise, '*if at the end of any financial year, it has accumulated losses equal to or exceeding its entire net worth*'. The main objective of SICA is to determine sickness and expedite the revival of potentially viable units or closure of unviable units. It was expected that by revival, idle investments in sick units will become productive and by closure, the locked-up investments in unviable units would get released for productive use elsewhere. Such companies are required to be referred to the Board for Industrial and Financial Reconstruction (BIFR) for formulation of rehabilitation/ revival plan. As per Department of Public Enterprises Resolution dated 6th December, 2004, a company will be considered 'sick' if it has accumulated losses in any financial year equal to 50% or more of its average net worth during 4 years immediately preceding such financial year and a company which is a sick company within the meaning of Sick Industrial Companies (Special Provisions) Act, 1985 (SICA).

According to Companies Act 2002, a sick company is defined as one *"which has accumulated losses in any financial year equal to 50 per cent"*. An enterprise remains healthy if it operates in reasonably favorable environment and has an efficient management. When these conditions are not satisfied the enterprise is likely to become sick. Sickness is caused by unfavorable external environment and managerial deficiencies.

Change in fiscal and government policies to face new challenges and meet new financial requirements due to deregulation, decontrol, withdrawal of government patronage, competition is the main reason for reforms in the public enterprise system. Due to liberalization, privatization and

[3]Muralidharan, S. (1993), Handbook of Industrial Sickness, Vidhi Publications, New Delhi

globalization the expanded markets have given highly competitive environment to these enterprise to 'perform' or 'perish'. Technology revolution has become lifeline for all corporate resulting in more investments in IT and related infrastructure and making people familiarize in the latest. Customer delights bringing to the fore a new concept as to how to understand and fulfil the needs and expectation of the customer. SoEs were segregated into high priority and non-priority enterprise basing on the model for restructuring. Box 1 describes the business model classifies SoEs into high and non-priority enterprises.

Box 1: Revival Mechanism	
High Priority SoEs	Non-priority SoEs
Strategic objectives, national interest and economically viable	Short and medium plan for sustenance
Business model for government policy convergence	Performance efficiency benchmark operations, technology adoption, business strategy
Strategic disinvestment and joint ventures	Desirable short and medium market share

The BIFR was set up in January 1987 and functional with effect from 15th May 1987. The Appellate Authority for Industrial and Financial Reconstruction (AAIRFR) was constituted in April 1987. Government companies were brought under the purview of SICA in 1999, the SoEs whose accumulated losses are equal to or have exceeded their net worth may be referred to BIFR. BIFR grants immunity from legal sanctions to the company arising from proceedings from executive of decree against property, recovery, etc. BIFR sanctions suitable revival / rehabilitation schemes for revival, closure, partial closure, etc. Table 3 depicts the SoEs registered with BIFR. It is evident that for the last twenty-four years i.e. from 1992-2007, 65 SoEs have been referred to BIFR and there were no references from 2008-2016. BIFR disposed more than 50 cases through sanctioning revival schemes, declaring 'no longer sick, dismissing the cases as non-maintainable de-registration and recommended for winding up.

Table 3: Year-wise Registrations of SoEs with BIFR

Year	No. of CPSEs	Year	No. of CPSEs	Year	No. of CPSEs
1992	31	1998	2	2005	2
1993	2	1999	3	2006	1
1994	4	2000	1	2004	4
1995	2	2001	1	2007	1
1996	2	2002	2	2008 - 16	0
1997	4	2003	1	Total	65

Table 4 depicts the status of SoEs which were registered with BIFR under various categories of revival. Out of the 65, 18 SoEs were recommended to windup/ closely followed by revival of 13. It is interesting to note that ten SoEs showed growth rate.

Table 4: Status of SoEs registered with BIFR (as on 31.03.2016)

Sl No.	Particulars	Number
1	Winding up recommended and closed	18
2	Revival Scheme sanctioned by BIFR	13
3	Draft Rehabilitation Scheme (DRS) awaited	12
4	Declared no longer sick	5
5	Dropped on net worth becoming positive	5
6	Winding up recommended	4
7	Dismissed as non-maintainable	3
8	Deregistered with BIFR/Others	2
9	Stay by AAIFR	1
10	Remanded by AAIFR	1
11	Pending determination of sickness	1
	Total	65

It is evident from the above table (Table 4), 65 SoEs were referred to BIFR of which 40 were in operation. The accumulated losses of sick operating SoEs during 2007-08 to 2015-16 is Rs 51,670 crore. Andrew Yule, Hindustan Insecticides, Project & Development India, Scooters India Ltd and Vignyan

Industries Ltd does not have accumulated losses. Table 5 shows the no of operating sick SoEs registered with BIFR, year-wise accumulated losses, total number of loss making SoEs and aggregate loss.

Table 5: Sick and Loss making operating SoEs

Year	No. of operating sick SoEs registered with BIFR	Accumulated losses of sick operating SoEs (Rs in crore)	No. of loss making SoEs, during the year	Aggregate loss, (Rs. in crore)
2007-08	46	72820	54	10303
2008-09	46	68577	55	14621
2009-10	46	62828	60	16231
2010-11	45	65146	62	21817
2011-12	45	65642	64	27683
2012-13	45	70918	79	28562
2013-14	44	55507	70	21341
2014-15	39	56065	76	27498
2015-16	40	51670	78	28756

(Source: Public Enterprise Survey 20015-16, Vol 1, Department of Public Enterprise, GoI)

The streamlining the mechanism for revival / restructuring of SoEs for winding / closure, etc was intended to facilitate multiple mechanisms exist for restructuring / revival of SoEs. Government has taken steps to make the mechanism and process for revival/restructuring of SoEs time bound, comprehensive, performance driven and efficient. The Government decided to remove the multiple layers in decision making to ensure timely revival/restructuring of sick SoEs, revival/restructuring of sick/incipient sick enterprise is to be merit based, considering strategic, national and business concerns of the SoEs.

The Companies Act, 2013, Chapter XIX refers to Revival and Rehabilitation of Sick Companies whereas Chapter XX refers to Winding up. The decision whether a company has become a sick company would be taken by the National Company Law Tribunal. The administrative Ministries/ Departments must keep track of the debts of SoEs and take advance action to avoid a situation where the SoEs may be considered fit to be declared sick entity as per provisions of the Companies Act, 2013. The concerned Administrative Ministries /Departments are responsible to monitor sickness of SoEs functioning under them and take timely redressal measures with the approval of the Competent Authority. The administrative ministry analyses the performance of the enterprise within six months from the closure of annual accounts. The enterprise is considered weak or sub optimal performing basing on criteria discussed in Box 2.

Box 2: Criteria for declaring SoE as Weak / sub-optimal Performer
Turnover or operational profit has declined by an average of 10 per cent in the last three years
Profit before tax is less than income from the other sources
Trade receivables and inventories are more than 50 per cent of net worth
Claims against the company, not acknowledged as debts, are more than its net worth

The administrative Ministry would put the weak enterprise under 'observation and intensive review' to arrest the early sign of weakness. The Ministry would also nominate an independent member on the board to review and undertake corrective measure to improve financial performance of the enterprise. The administrative Ministry would inform Ministry of Finance on the revival / restructuring mechanisms of the enterprise. The Ministry of Finance would consider the enterprise for the revival / restructuring mechanisms. The Ministry decides keeping the public interest in making the process, time bound and performance driven.

Conclusion

Reforms and Restructuring has been fuelled by variety of forces like global competition, technological breakthroughs, managerial innovations, regulatory changes, transformation and formerly centrally planned socialistic economies and expansion of international trade. It has led to dramatic improvement in corporate performance. The strategic movers of turnaround management are touched in the context of complex sick organizations in general and transport undertakings in specific. Key insights are drawn from functional as well as operational point of view to explain the complete process and develop insights specific to the context. The move contributes to devise, develop and implement

turnaround strategies for organisations especially in the Indian scenario. SoEs are expected to run on commercial lines, the financial appraisal continues to be an important yardstick to measure the performance of these enterprises. An analysis of financial performance of these enterprises with reference to some important ratios such as profit before interest and tax to capital employed, sales to capital employed, etc has been attempted. Because the SoEs must discharge a number of socio-economic obligations, generate employment opportunities, public exchequer, management development, development of backward regions, employment generation, employee's welfare measures, foreign exchange earnings, there is a need to revive them.

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