

Corporate Governance Issues in Public Sector Enterprises



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Public Sector Enterprises especially Central Public Sector Enterprises have played & continue to play an important & active role in Indian economy as vehicles for industrial & regional development, creation of basic infrastructure networks & employment generation. It has to be appreciated & acknowledged that PSEs are not merely commercial enterprises but serve much larger agenda of nation building as is evident from few statistics on CPSEs enumerated below

As of March 2014, there were 290 CPSEs of which 234 were in operation & 56 under construction giving full time employment to 1.35 million workforces.

CPSEs are important capital market players. 46 CPSEs are listed & traded on stock

exchanges. Their total market capitalization in March 2014 was Rs1108307 crores accounting for nearly 15% of market capitalization of Mumbai Stock Exchange.

With total paid up capitalization of Rs 198722 crores & capital employed of Rs 1744321 crores as on 31/03/2014, these CPSEs (Only Operating) have recorded turnover of Rs 2061866 crores & overall net profit of Rs 129109 crores during FY2013-14. It is worth mentioning that contrary to public perception 163 out of 234 operating CPSEs are profit making as on 31/03/2014.

Against the above backdrop of the important role that PSEs continue to play in the Indian economy coupled with the realization that there is considerable room for further improvement in their performance, PSE reform agenda especially in the area of Corporate Governance has always been a matter of animated discussions amongst various stakeholders.

Over the decades & especially since 1991 a number of initiatives have been taken to improve PSE governance including corporate governance to bring about higher levels of efficiency, investment & economic growth. Such initiatives included categorization of CPSEs in categories of Maharatnas(7) Navratnas(17) Miniratna Category-I(56) Miniratna category-II(17) with varying degree of greater functional autonomy in decisions about investments, capital expenditure, joint ventures, mergers & acquisitions & raising of debt from capital markets subject to compliance of some preconditions.

Notwithstanding recent improvements in the performance of PSE sector as a whole & reforms initiated to improve the corporate governance of these entities, there is felt need to introduce further reforms & improve better implementation of extant guidelines to make corporate governance of these PSEs compliant with OECD guidelines on Corporate Governance of State Owned Enterprises.

A lot has been written about the governance in PSEs & our intention is not to repeat those points. Based on our experience & interactions with many present & past directors on PSE boards, we are proposing certain aspects of governance that would need the attention of the Government, administrative ministry & more particularly chairman & managing Director. But before we do that, we would like to make some general observations about the functioning of the Boards based on personal experience of the senior author of this paper and interactions with many present and former Independent directors. These are:

- 1) Most boards endeavor to comply with statutory, mandatory & regulatory requirements, To this extent, most public sector Companies have embedded governance unlike many private sector & owner driven companies.
 - 2) Most PSEs religiously adhere to conduct Board & various sub- committee meetings regularly & generally there are lesser issues in regard to Directors attendance.
 - 3) Generally Boards follow & approve the mandate of the government without much resistance even when the commercial interests of the Company may not be best served. Generally government nominees are considered "More equal than the equal" in considering the views of directors mainly because the CMD has to daily work with them.
 - 4) There is little formal induction of Independent Directors. Their compensation is inadequate and training nebulous.
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- 5) Major time of the Board is spent on mandatory agendas, project approvals, long presentations & review of various functions. In short matters related to **near term performance** always get precedence over issues related to **health** of the institution. Such issues mostly relate to soft items like strategy & vision, culture, innovations, human resources, leadership bench strength, succession planning & technology.
- 6) Some Maharatnas & Navratna Cos are severely handicapped in having capabilities in newly emerging areas & depend heavily on outside consultants with associated costs & risks.
- 7) Board processes are often business like & lack in depth analysis of issues mainly on account of inadequate familiarization of business processes & understanding of industry norms & international protocols by independent Directors. There is always a last minute urgency to approve things.
- 8) Internal bureaucracy, delays are rampant which is experienced in working with various committees. Pro-active interventions to fix accountability for delays are rare.
- 9) Promotion and appraisal processes in many cases lack rigour and there is reluctance at every level to initiate reforms in HR. In many cases, the IR situation is difficult and an atmosphere of mutual mistrust. Strategic initiatives in developing future leadership rarely forms an agenda for discussion at board level.

WAY AHEAD

Some of our Maharatna & Navratna PSEs are also not getting the valuation they deserve. Many FIIs are reluctant to look at PSEs as a class for investments. Is it because of the Government control of PSEs or the inadequate level of governance practices? We believe that perception play an important part in valuations & pitifully best of PSEs are perceived as instrumentality of the Government with little autonomy compared to commercial organizations pursuing the clear objective of creating wealth for various stakeholders. We are under no illusion about the objectives of PSEs which are always beyond commercial ones. But, the issue is to harmonize the national priorities with commercial logic.

We believe that despite the existing handicaps, Government & PSEs can do a lot to improve the perception of PSEs. We give below some ideas for action

FOR GOVERNMENT

- 1) The quality of top management has to be enhanced which requires rigour in the process of selection of whole time directors & the Chairman. Political interference in such selections can be fatal. Talent from private sector should also be encouraged and necessary changes in compensation policies should be brought about. The recent initiative by Department of financial services in opening the CEO and MD position to candidates of private sectors also is a welcome move.
- 2) Moving from functional positions to Director Role require training in strategic thinking, strategy making, policy formulation & governance. Similarly for Chairman, exposure in turnaround management & transformational leadership are very vital preferably in reputed institutions abroad to develop global perspectives in managing large sized organizations. For example, in most PSEs, Director HR are appointed from any functional area. It is desirable that such incumbents are exposed to some long duration course in HR & are socialized & inducted properly in the system.
- 3) To ensure that independent directors are identified and assigned to different Boards well in time to avoid negative market perception and performance of the Board. This is one area which requires disciplined approach from the government. Directors sitting fee and training also require attention.
- 4) Independent director's induction has to be elaborate and structured to enable them to acquire necessary knowledge about the company.

For the Chairman

- 1 The CMD has a major role in ensuring effective governance. While, he has to ensure a organic linkage between the directors and the company, he has to provide opportunities for visits to factory and project sites. He has also to provide constant learning opportunities for the directors.
 - 2 CMD has also to organize Strategy meets periodically and invite experts in various fields to interact with the Board. He has also to put strategic issues on HR, leadership development for discussion and engage the Board in laying out a clear plan of transformation.
 - 3 He has also to ensure productivity of the Board in terms of adequate allocation of time in discussing policy issues and issues about the health of the company.
 - 4 CMD has also to use special expertise of the Board and initiate studies on the subjects that can provide insights on key issues. Such insights can be received from Employee engagement surveys, customer surveys, management audits etc.
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For the Directors

- 1 Functional directors have to constantly provide insights to Board in their respective areas.
- 2 Independent Directors have to engage and continuously learn and contribute from their experience.
- 3 They must avoid “Herd Mentality” and give independent opinion on issues and problems. They must engage with issues and problems and provide guidance on critical matters.
- 4 Needless to say that all the directors need to scrupulously follow ethical standards.

It is our strong belief that Corporate Governance in PSEs needs to move beyond statutory, mandatory & regulatory requirements. Endeavors have to be made to embrace excellence in Governance by continuously reinventing the processes & introducing greater transparency openness & responsiveness in the organizations. As stated hereto before, Chairman of the Board has a very key & major role to play for these enterprises to pursue excellence in Corporate Governance. Improvement in internal governance processes, debureaucratization of the organization, responsiveness to customers, suppliers & vendors, fairness & speed in decision making & pursuing best HR practices are sine quo non for public sector enterprises to achieve global best practices in Corporate Governance. Hopefully, ideas/ suggestions outlined by us may provide some framework / mechanism to move beyond statutory & regulatory compliance of Corporate Governance & view corporate governance issues of PSEs more holistically.
