

Conclusion and Recommendations

Conclusion

- 7.1** There is no single legislation in India providing for a systematic and cohesive system for rehabilitation and liquidation of enterprises including CPSEs. A number of legislations and regulations comprise the insolvency framework for commercial enterprises. While many financial sector laws have undergone massive transformation after the liberalisation of the Indian economy, the insolvency law remains outdated. Both, the winding up of companies under the Companies Act and rehabilitation under SICA remain cumbersome and long-drawn resulting in locking of huge national resources in these proceedings.
- 7.2** Absence of an efficient, speedy, predictable and transparent legislative framework for restructuring and revival has deprived the CPSEs from turn around and reallocation of their productive resources. BIFR was established for speedy determination of sickness and expeditious revival of potentially sick units or closure of unviable units. However, BIFR failed in achieving its objectives due to its inherent weaknesses and other reasons discussed in the report. Similarly, BRPSE was also established in December 2004 with the objective of strengthening and reviving sick CPSEs. Under BRPSE, procedural delays still persist due to consultation at multiple layers, protracted correspondence, prolonged deliberations, lack of consensus amongst different parties and lack of enforceability of the decisions. In essence, the existing legislative and operational framework was found to be inadequate to effectively address the problems of sickness in CPSEs.
- 7.3** The managements of CPSEs are heavily dependent on the GOI for taking number of key decisions. A number of approvals are required. There is a direct interaction by DPE and ownership entity with management in a number of areas. In fact, such mechanism should also provide an efficient and timely manner of responding to assistance in preparation of revival schemes, their approval and implementation. Where revival is considered not feasible an early decision will help in realizing maximum value of assets by its reallocation in economy by speedy liquidation. In order to deal with the complexity of sickness in CPSEs, there is a need for a policy framework laying down detailed guidelines on the procedure/criteria to be followed for:
- determination/ identification of loss-making/sick CPSEs including non-revivable companies;
 - revival/restructuring, disinvestment/sale/privatisation, exit/closure, etc. of sick CPSEs;
 - planning/formulation, appraisal and approval of proposals; and
 - implementation and monitoring of compliance.

7.4 There is an urgent need for strategic readjustment and restructuring of distressed and potentially sick CPSEs. Many CPSEs have failed to adapt to the new dynamics of doing business. CPSEs are prevalent in key utilities and infrastructure industries, such as railways, posts, ports, transport, defence, telecommunication, whose performance is of great importance to broad segments of population and to other parts of the business sector. Their governance is thus, critical to ensure their positive contribution to a country's overall economic efficiency and competitiveness. CPSEs can be a major contributant to the Indian economy and beneficiary to the government. In recent times there has been significant increase in the dividends and contributions made by CPSEs to state exchequer. This can multiply manifold if the CPSEs were to be governed on established corporate governance principles. This money can contribute immensely into building of infrastructure of the country easing tax pressure on citizens. It is in the governments and the public's interest that all these categories of CPSEs are professionally run and apply good governance practices. CPSEs that are potentially sick should be identified. An urgent in-depth review of the governance of CPSEs may be undertaken to prevent insolvency in potentially sick CPSEs and provide an efficient resolution of sick CPSEs. A holistic and fast-track approach should be adopted for the resolution of the problems that are causing sickness. Similarly a careful review of the sick CPSEs should also be undertaken.

7.5 As against BRPSE, the CDR framework has emerged as an effective out of court workout mechanism. CDR mechanism has worked well since inception. Its provisions were relaxed recently to enable enhanced access to the scheme. Since inception, CDR has approved 215 corporate cases for restructuring with a cumulative debt of ₹ 104299 crore. As per the statistics available on 30th June, 2010, the CDR has witnessed an increased inflow of cases seeking debt restructuring after the global and domestic economic slump.

The system has the following strengths:-

- CDR system is a voluntary mechanism which is outside intervention, judicial or otherwise but operates on the guidelines issued by Reserve Bank of India.
- There's no requirement of the borrower's account being a NPA or the borrower company being sick company under SICA or being in default for a specified period before reference to the CDR system.
- Another positive aspect of CDR mechanism for the borrowers is that the debts with high rate of interest can be transferred to lenders with a lower rate and potentially over prolonged payment terms.
- The interest of creditors under the 'doubtful' category is protected because it is not binding on such creditors to take up additional financing.
- Providers of additional finance, whether by existing creditors or new, have a preferential claim, over the providers of existing finance with respect to the cash flows out of recoveries, in respect of the additional exposure.
- CPSEs should be encouraged to participate in the CDR mechanism.

7.6 The revival scheme of ten CPSEs analysed in audit revealed that there were inordinate delays in approval of the schemes as no timeline was fixed for approval by BIFR. The delays ranged from one to 18 years. Interestingly, the revival scheme of NEPA Ltd could not be finalized even after a lapse of 14 years from its sickness. There was lack of synergy amongst various agencies involved and the financial measures and commitments of various parties could not be effectively enforced under the existing operational framework. As a result, the sick CPSEs could not reap the full benefits from the schemes. In respect of BRPSE, although there was a timeline of 8 weeks for the Administrative Ministries to obtain approval of the Cabinet on the recommendations of BRPSE, there was no timeline within which the sick CPSEs or the Administrative Ministries should submit the revival proposals for the consideration of BRPSE.

7.7 The designs of the schemes were not adequately structured as these basically involved financial restructuring only. Major portion of the funds ₹ 20,160.68 crore (about 72 percent) were marked for financial restructuring such as waiver of loans and interests, conversion of loans into equity and settlement of dues. In fact, a very small proportion ₹ 4174.03 crore (15 per cent) of the package was allocated for modernization and, diversification for long term sustainability of the operations of these CPSEs. Thus, the schemes did not address the core issues of sickness which would have yielded the sustainable revival of these companies. Further, in three CPSEs (NTC, CCI and HEC) where the revival schemes were to be financed primarily from sale of surplus land, no alternative strategies, in any eventuality, to fund the schemes were proposed.

In addition to financial restructuring more operational restructuring should be encouraged. Financial restructuring involves the evaluation of the business cash flow capabilities and determination of the optimum capital structure required to balance cash flow availability with debt service requirements. But the speed with which non performing loans (NPLs) are getting resolved has been rapidly decreasing in individual countries. Once they are resolved through out-of-court workouts or other restructuring measures, a substantial proportion of NPLs have reverted to their non-performing status, and that new non-performing loans have been generated. Operational restructuring involves increase in economic viability through methods such as merger integration, sale of divisions, rationalization of product lines and cost-cutting measures. It includes sale of non core business and assets to reduce debt levels, reduction of large employment and production capacity and changing the lines of business. Therefore, operational restructuring would lead to a better working of the debt restructuring mechanism.

7.8 Audit observed several gaps in the implementation of the schemes. Four CPSEs (NTC, CCI, ECL and HMT) suffered from time overrun up to three years. Further, though the schemes of two CPSEs (HOCL and HEC) proposed for sufficient financial arrangements and working capital, there was substantial shortfall in generating funds due to non disposal of surplus assets. In NTC and HOCL, manpower rationalisation was not carried out effectively. As a result, NTC had to bear idle wages of ₹ 32.04 crore annually and HOCL could not achieve the saving

target of ₹ 14.09 crore annually due to failure to introduce attractive VRS scheme.

7.9 Out of the nine CPSEs, targets of sales and net profit as envisaged in the revival schemes could be achieved only by four CPSEs (BCL, CCI, ECL and HEC). The remaining five CPSEs (HOCL, NTC, FACT, NPCC and HMT Machine Tools), could not achieve the targeted net profit from ordinary course of business indicating only a limited success of revival schemes in these cases. [The revival schemes in respect of nine CPSEs reviewed in audit could achieve ₹ 332.56 crore of profit as against the projected profit of ₹ 889.78 crore.](#)

7.10 However, Audit noticed that the revival schemes also did have a positive impact on the operations of four CPSEs (NPCC, BCL, HEC, ECL) which were on the path of revival. In case of two CPSEs (CCI and HOCL), though revival schemes have indicated positive impact on their operations, their performance was not at the satisfactory level and their long-term revival remains to be seen. In the remaining three CPSEs (NTC, HMT Machine Tools and FACT) the revival package had little impact on their operations, as these CPSEs could not generate operating profits. Their operating profits remained negative even after implementation of revival schemes. The net worth of NTC Ltd turned positive due to substantial inflow of funds from sale of land. The net worth of HMT Machine Tools Ltd., which was positive, eroded considerably after implementation of revival scheme mainly due to delay in implementation of capex and technological upgradation programme. The net worth of FACT was decreasing due to operating losses and it may turn negative if this trend continues.

7.11 The GoI has recently introduced Companies Bill, 2011 in the Parliament which provides for rehabilitation and liquidation of Companies under the same roof. The Bill vests the jurisdiction to deal with the rehabilitation and liquidation of companies in a neutral independent forum, NCLT with appeal to NCLAT. Even though significant improvement is expected in the corporate restructuring and liquidation regime after the Companies Bill, 2011 is passed by the Parliament, many policy gaps and legislative deficiencies remain in the restructuring and liquidation framework. It is important to address these gaps and weaknesses to capture the key objectives and provide a comprehensive insolvency framework which can function efficiently and meet needs of sick or potentially sick enterprises including CPSEs and other stakeholders operating in a fast modernizing economy. Some gaps and deficiencies are discussed in the report.

7.12 In fact, absence of a well-developed institutionalized discipline of insolvency profession has deprived the stakeholders from engagement of insolvency experts in the process. According to UNCITRAL Legislative Guide, where a jurisdiction has a well-developed cadre of insolvency professionals, who ascribe to the highest standards, together with the appropriate oversight, the insolvency system should function effectively, efficiently and in a timely manner. A competent and recognized insolvency profession can overcome gaps in the legislative framework and make the system work for the benefit of all.

Recommendations

Based on the performance audit conducted, the following recommendations are made:

- (i) GOI should consider formulating a new policy framework to address:
 - (a) Early identification of sickness in CPSEs;
 - (b) Timely formulation of proposals for revival/closure;
 - (c) Better synergy between the various national agencies involved in the revival or closure exercise; and
 - (d) Effective monitoring mechanism of scheme implementation.
- (ii) GOI may consider formulating operational modalities for reference of sick/ loss making CPSEs to the NCLT for revival/ rehabilitation.
- (iii) There is an urgent need for an appropriate mechanism with certain, predictable and transparent guidelines, operating in a timely manner, empowered with a single point decision-making authority to effectively deal with the problems of sick/loss-making CPSEs.
- (iv) There is a need to develop and institutionalize the discipline of insolvency profession. In most sophisticated economies the profession of insolvency is highly sophisticated and well-developed.
- (v) The existing framework for revival of sick CPSEs may be reviewed to ensure that formulation, approval and implementation of revival schemes are carried out in a time bound manner.
- (vi) The deficiencies identified in the Companies Bill may be suitably addressed.

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Dated : 30th March, 2012



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Dated : 30th March, 2012

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