

TUESDAY, DECEMBER 31, 1996

In the public interest

It is illogical for FIs to express inability to arrange for competent nominee directors, says Uttam Gupta

FINANCIAL irregularities in some of the leading corporate entities have brought to the centrestage the issue of corporate governance. The government and the industry are on the lookout for a set of rules or code which management could adopt to prevent their recurrence.

Almost all the companies in India are run mainly with public money. While the public sector undertakings (PSUs) are either owned entirely or predominantly by the GOI or state governments, in private companies too, the bulk of the capital is contributed by government-controlled financial institutions (FIs). The public thus, has a fundamental interest in ensuring that the funds are put to productive use.

One would wish the government and industry good luck, if they think that adopting a code, by itself, could protect the interests of the shareholders or public; for, the problem is not so much due to lack of knowledge about good conduct rules, but mainly because of lacking commitment to subserving public interest.

In the public sector, presently, more than 100 PSUs do not have a full-time chief executive (CE). In many PSUs, the second line of command does not exist, as there is no post of director. Even where it exists, it is invariably bypassed and the slot is filled by the official from the concerned administrative ministry.

A person trained to do administrative work, and having spent bulk of the time on such functions, is inherently not competent to manage and run a business enterprises. Moreover, having to continue his ministry's work simultaneously, there is very little time he can devote to the PSU. The situation is much worse if the same official is given charge of more than one PSU.

Even PSUs which are lucky to always have full-time CEs, the selection process raises doubts about the quality of the management. Until 1987, ACC (the appointing authority) was bound by the recommendations of the PESB. This is no longer the case. This means that the political bosses have a free hand in picking the candidate of their choice.

Against this backdrop, the CE cannot be guided only by the need to run the enterprise efficiently and profitably. Even if he is keen to act

in the best interests of the undertaking, he is not free to do, as under the rules for virtually every important decision he has to seek the nod of the politicians and bureaucrats.

Despite much bravado, no serious attempt has been made to do away with the system in 1992, and induct professionals as the government's nominee directors on PSU boards. This too remains unimplemented.

Thus, the PSUs continue to suffer due to widespread controls which are often justified in the name of accountability. A series of scams — securities scam, urea scam etc, in-

companies. In this situation, the possibility of any one company getting neglected and its financial interest sacrificed is not entirely ruled out.

Second, during the so-called reform era of the 90s, the promoters have mobilised huge funds by way of premium. This was a rare thing in the past, and even in such limited cases, the premium amount used to be small. Premium is virtually free money in the hands of the promoters and constitutes a sizeable chunk of the funds employed in the business. That gives enough leverage to do things which may not be in the wider

encing the crucial decisions.

While one may see their active involvement when it comes to Indian and foreign companies vying for control, the FIs hardly act when it is a question of looking after the interests of the shareholders. The indifferent or passive attitude was at its climax recently, when some of them even argued that the FIs' interests can be protected even without the presence of their nominees on the company board.

The role of the FIs is much bigger than simply ensuring safety of their capital, and its timely and proper servicing. However, even from this limited angle, it does not make sense to stay away. There are several instances of the FIs and banks losing money in a company going sick, because the assets cannot fully pay for the value of the loan.

In every corporate entity, public or private, the need for effective and proper management cannot be overstressed. For the public sector, the government, as the custodian of tax payers' money, should ensure that the funds are used productively and they generate reasonable returns. This is possible only if the PSUs are allowed to be run as professional entities.

A truly autonomous management, free from government control and accountable only for the overall financial health of the PSU, can deliver the goods. This applies equally to government-owned FIs, mutual funds and commercial banks. If the rule book comes in the way, that should be changed and if need be, even dismantled. Stability and continuity of the management should be ensured through timely action. The CE's slot should not remain vacant even for a day.

In private companies, the FIs should play a proactive role instead of merely acting as fence-sitters, as at present. The emphasis has to be on intelligent tracking of key moves and decisions to prevent unhealthy situations.

Some FIs have expressed inability to arrange for competent professionals to act as nominee directors for the numerous companies to which they have exposure. This is illogical. The FIs need to visualise their role in the much broader context of ensuring proper use of funds and prevent losses. Indeed, this would more than pay for the expenses on professionals.



volving banks and PSUs have occurred under the watchful eyes of the government. Given this background, it is unlikely that adoption of a new code would be of any help. Far from that, this will lead to further tightening of controls on the management.

In private companies, having invested his own money, the promoter is likely to have an inherent interest in ensuring the company runs well. The shareholders may, thus, have some reason to feel safe especially in the hands of promoters with good track record. In recent years, this natural convergence of interests has been substantially eroded.

First, the promoter having diversified his business empire, has stake in a number of companies, i e group

interests of the shareholders.

Third, there is the factor of division within the family of the promoters, leading to major restructuring of business. Even as efforts are made to satisfy each member of the family, interests of millions of shareholders are sacrificed. At times, protracted differences within the family lead to total neglect of management, making the company sick.

Fourth, despite having pumped huge public money, whether by way of equity or loans, the FIs have behaved like lame ducks. The presence of their nominees on the boards of companies is just a ritual. Rarely do the nominees keep track of the way the company is working, much less meaningfully participating and influ-