

Tackling industrial sickness

Radical attitudinal changes are needed in institutions which have to deal with reviving sick units, says Uttam Gupta

AS reported recently, Modi Carpets, a company of the Modi group, was ordered to be wound up by the BIFR in 1993 as it had failed to identify a workable option for its rehabilitation. The BIFR had suggested that the Modi's revive their carpet unit by bringing the requisite funds from other cash-rich companies of the group. This was rejected by the management on the ground that the latter being a limited liability company, funds cannot be infused from outside.

The offer of the Modis instead to allow amalgamation of Modi Carpet with Modi Rubber was rejected by the BIFR. The Board viewed the proposal as a subterfuge for diluting the profits of the latter with the accumulated loss of the former and consequently save on tax rather than as an earnest of rehabilitating the ailing company.

The liquidation is a disaster for commercial banks and FIs with huge funds locked up in the sick industry. For example, the Modi Carpet owes Rs 40 crore to the Punjab National Bank alone. With an accumulated loss of about Rs 50 crores, the company is simply in no position to repay. Although, the PNB has filed a suit with the Recovery Tribunal in Delhi recently, it is impossible for the bank to recover the entire sum. The problem for the bank is compounded because it has a claim only on the floating, and not on the fixed, assets. With the former having been almost completely eroded by the losses, it is a foregone conclusion that almost the entire sum due from the company is a bad debt.

The Modi carpet episode is not an isolated phenomenon. According to available estimate, in 1989 a staggering Rs 3,387 crore of bank money was locked in the sick companies which, by now, would have further increased manifold. The banks know that it is impossible for them to recover the loans through recourse to legal procedures. Consequently, they have fallen back on negotiating directly with the promoters to realise even a small fraction of the outstanding dues. The RBI, too, has given them necessary authorisation to enter into such arrangements. The amount remaining unrecovered is simply written off.

In a fundamental sense, such a position in the private sector is no

different from the sick enterprises in the public sector. The only difference is that in the latter the accumulating losses are supported by increasing budgetary support from the government. Whereas in the former, these represent predominantly the corresponding loss of the banks and the FIs.

In either case, the money comes from the national exchequer. It may be recalled that during 1993-94 and 1994-95 more than Rs 10,000 crores was provided from the Union budget to enable the commercial banks meet the prescribed capital adequacy norms

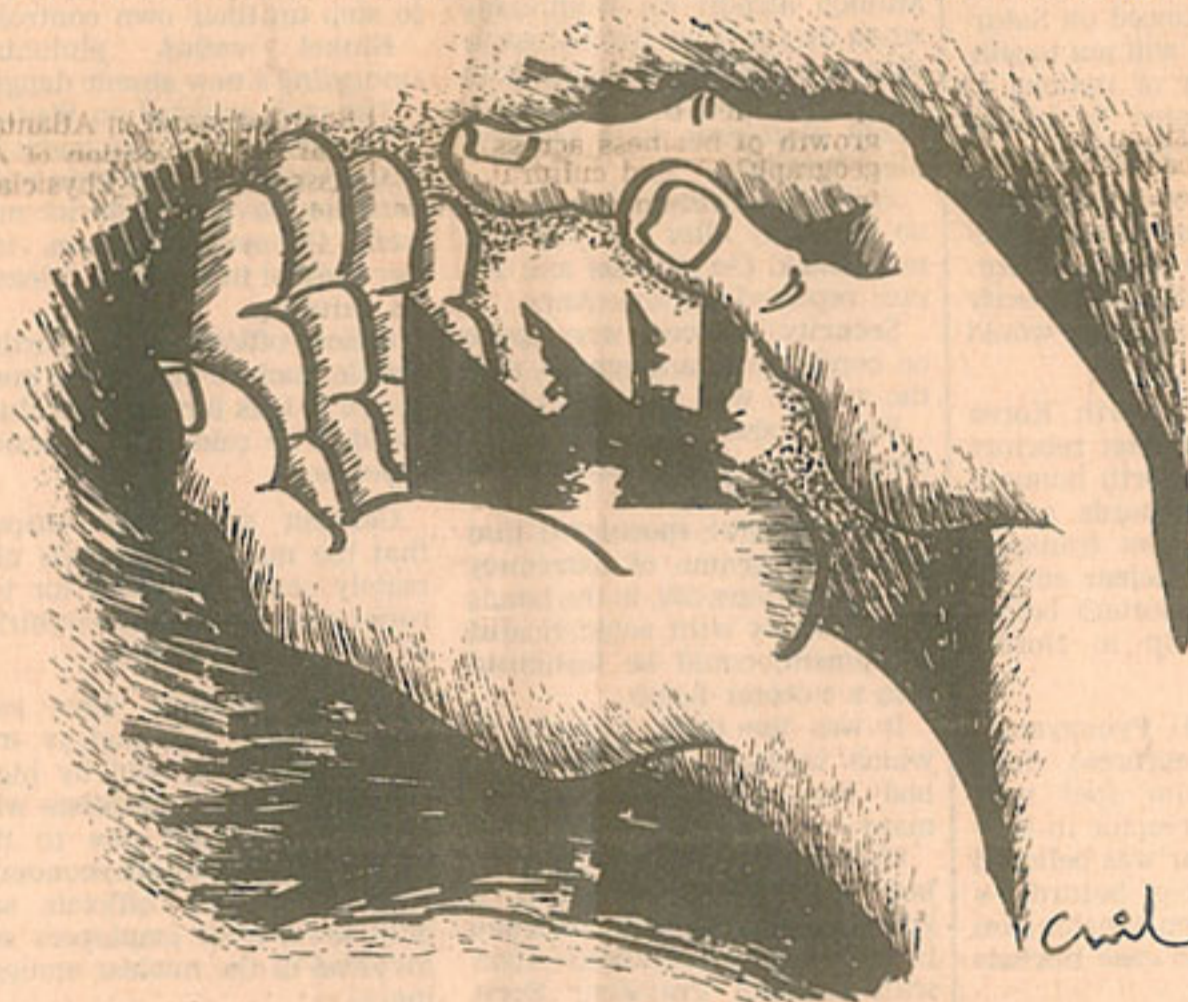
after making necessary provision for losses and bad debts.

BIFR is certainly not the answer to these problems, although one might get the impression that something is being done. Notwithstanding this, the BIFR needs maximum cooperation from the promoter in evolving a package for rehabilitation. After all, he cannot exonerate himself from the responsibility of having turned the company sick, even though some damage might have been caused by external policy impulses or changing overall business environment within the country or outside. Unfortunately, and as various hearings before the BIFR amply bear out, the promoter is the least interested party.

Amongst the lucky cases for which

a package is evolved, it is invariably the government agencies i.e. commercial banks/FIs or the revenue authorities (excise & customs) who are made to bear the brunt. The former for giving more loans and the latter for waiving the tax dues. Implementation of these packages too remains a big question mark as either the designated banks refuse to lend more or, even if they decide to do so, it means still greater burden on the sick company as by further raising the debt-equity ratio, chances of turning around are further dampened.

Creation of a corpus fund and an



autonomous body that does not report to the usual administrative machinery as recommended by Union commerce minister Pranab Mukherjee in a recent meeting with the CEOs of the PSUs, is also no solution to the problems of the sick companies. If inadequacy of working capital alone is the problem of ailing units, as opined by the commerce minister, that can be arranged within the existing dispensation without having to create additional monoliths. Moreover, if BIFR can't get the units the necessary funds for their running, what is the guarantee that a new institution will succeed?

The problem is of a structural nature and cannot be addressed merely within the framework of building new institutions or expanding the

paraphernalia of existing ones. A radical approach has to be thought of which requires attitudinal changes.

First, the Banks and FIs have to take the lead. They must realise that it is their money that is at stake if the company goes bankrupt. Consequently, they should develop a vested interest in ensuring that companies in which they have deployed funds remain healthy. Merely making a man sit as nominee director on the company's board will not be enough. Continuous monitoring of the financial and physical parameters, which the banks and the FIs have a right to ask for, would help them detect the signs of incipient sickness as also initiate timely remedial action. In cases where a company with good track record gets into trouble because of sudden change in the policy environment, the FIs/Bank should take a proactive role in dialogue/consultation with the government to facilitate an appropriate solution.

Second, necessary amendments in the Companies Act need to be made to facilitate regular disclosures and make operation of the company transparent. Strict enforcement of the disclosure norms is another requirement. Non-compliance should attract heavy punishment, not merely by way of payment of fine but even imprisonment. Supplementary efforts through the visual and print media aimed at involving even the small shareholders on the working of various companies can also augment accountability by keeping the company managements on their toes.

Finally, the government should not give a clean chit to the ailing company either by readily agreeing to provide budgetary support as in the case of PSU or writing off of the bad debts of the banks. Instead, it should work for strengthening the legal and administrative machinery so that once a sick company is allowed to be wound up, all its creditors/liabilities i.e. workers, suppliers, banks/FIs and government dues are recovered from the sale of assets.

If necessary, funds from the other companies of the group should be used to settle all dues from the unit under liquidation. The directors of such companies should be blacklisted and the banks and FIs warned that no financial assistance be given to new companies/existing companies with which these directors are associated.