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Indian Chamber of Commerce

Public Sector Enterprises in India – Catalyst for Growth.

List of Abbreviations

APM: Administered Pricing Mechanism
BHEL: Bharat Heavy Electricals Limited
BPCL: Bharat Petroleum Corporation Limited
BSE: Bombay Stock Exchange
BSNL: Bharat Sanchar Nigam Limited
BU: Billion Units
CAGR: Compounded Annual Growth Rate
CDMA: Code Division Multiple Access
CIL: Coal India Limited
CNOOC: China National Offshore Oil Corporation
CNPC: China National Petroleum Corporation
CPCL: Chennai Petroleum Corporation Limited
CPSEs: Central Public Sector Enterprises
CSR: Corporate Social Responsibility
E&P: Exploration and Production
FDI: Foreign Direct Investment
GAIL: Gas Authority of India Limited
GDP: Gross Domestic Product
GHG: Green House Gas
GOI: Government of India
GSM: Global System for Mobile Communications
HPCL: Hindustan Petroleum Corporation Limited
IOC: Indian Oil Corporation
ISDN: Integrated Services Digital Network
JSPL: Jindal Steel & Power Limited
KPA: Key Performance Area
KRAs: Key Result Area
LNG: Liquefied Natural Gas
MPLS: Multiprotocol Label Switching
MT: Metric Tons
MTNL: Mahanagar Telephone Nigam Limited
NPCIL: Nuclear Power Corporation of India
NTPC: National Thermal Power Corporation
OIL: Oil India Limited
ONGC: Oil and Natural Gas Corporation
PMS: Performance Management System
RIL: Reliance Industries Limited
SAIC: Shanghai Automotive Industry Corporation
SAIL: Steel Authority of India Limited
SASAC: State-owned Assets Supervision and Administration Commission
SEZ: Special Economic Zone
SINOPEC: China Petroleum & Chemical Corporation
SOEs: State-owned enterprises
USAID: United States Agency for International Development
USDOE: United States Department of Energy
VPN: Virtual Private Network
VSAT: Very Small Aperture Terminal
VOIP: Voice over internet protocol
YoY: Year on Year

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Message

The importance of Public Sector Units (PSUs) in the Indian economy can never be over emphasized. They account for over 22 % of the country's GDP, around 6 % of the total employment in the organized sector and over 20 % of direct and indirect tax collections. A number of PSUs also serve critical functions of furthering the socio-economic objectives of the Government and ensuring stability in prices of key products and commodities.

To some, a well-performing PSU is an oxymoron. The root cause, it is argued, lies in their ownership structure. The argument goes like this: a private sector owner treats the business as his own. Thus, the private sector is efficient and performs well. Therefore, the panacea to all that troubles the public sector is privatisation.

The issues are far more complex. First, if the "ownership structure" is the root cause of all inefficiencies, then how do we explain away the performance of Singapore Airlines and SingTel, which are in effect PSUs. The second issue: most successful global corporations have dispersed ownership with no dominant owner. Third, there are numerous poor-performing private sector companies. Indeed, some of the PSUs of today were ailing private sector units of yesterday. And last, the recent financial prairie fire in the US was sparked by the private sector. Ironically, the massive rescue package came from the US government. The notion that the private sector is innately efficient and the public sector is inherently inefficient needs a second look.

Singapore Airlines is a PSU. It is profitable, efficient and well performing. The largest shareholder in Volkswagen is the state of Lower Saxony in Germany. The case of Pohang Iron and Steel Company (Posco) is even more startling. The World Bank rejected the loan application of the Korean government for setting up a steel plant in Pohang — then a fishing village. No wonder, Korea neither had deposits of iron ore nor coking coal. The Korean government took the help of a consortium of Japanese bankers and set up Posco as a State Owned Enterprise (SOE). It is now the third largest producer of steel and doubtlessly one of the most efficient. It was only in 2000 that the company was fully privatised.

Many of today's success stories in the developing world began life as SOEs. Even in the developed world — France, for instance, Renault, Alcatel, EdF, Thomson and Elf were SOEs for a long time, as were Rolls Royce and British Aerospace in the UK.

There is little difference between Singapore Airlines and Air-India in their ownership structures. The difference lies in the governance, style of management, empowerment, attitude to customer service and results produced by its leadership teams. Many family-owned businesses perform poorly compared with professionally managed companies. IBM, Unilever, Coca-Cola, Pepsi, BP, Shell have widely dispersed shareholdings but are all well performing enterprises. They have a strong set of core values and a culture that engenders innovation and success. They all have a strong brand and have been tempered by the fire of market competition for years.



Roopen Roy
Managing Director,
Deloitte & Touche Consulting
India Private Limited

Red tapes, bureaucracy, risk aversion, administered pricing systems, ineffective governance structures, inability to hire the best talent because of poor compensation, political interference, absence of objectivity in appointments of managers and corruption are among the many reasons that cause PSUs to under-perform. Privatisation may well be a short cut to uncage the PSUs and protect them from the bad behaviour of the owners. But in the long run, the root causes that afflict the PSUs must be tackled head-on.

Is it possible to preserve the ownership structure and at the same time carry out comprehensive reform? Is it feasible under our current system to change the rules of the game and have a governance structure that is transparent and independent? Is it pragmatic to believe that we can create a culture of innovation and high performance and make PSUs autonomous, merit-based and insulated from meddling by bureaucrats and politicians?

We at Deloitte Consulting think the answer is a resounding “Yes”, as has been demonstrated by various countries around the world as well as the numerous interventions which have been initiated by the Department of Public Enterprises, Government of India in partnership with the respective administrative Departments. The current compilation prepared by us highlights some of these initiatives as also the progress achieved by some of the key PSUs. We hope you will find them useful.

I would like to conclude by thanking the Indian Chamber of Commerce for providing us an opportunity to be their knowledge partners on an agenda of such significant national importance.

Message



Jayanta Roy
President
Indian Chamber of
Commerce

The Indian Public Sector has always played a dominant role in shaping the path of the country's economic development. Prior to Independence, there were only a few Public Sector Enterprises in the country with its presence primarily confined to Railways, Post & Telegraph and the Ordnance Factories. However, visionary leaders of independent India drew up a roadmap for the development of Public Sector as an instrument for self-reliant economic growth. The Public Sector provided the much-required thrust and has been instrumental in setting up a strong and diversified industrial base in the country. Over the years, PSU operations have extended to a wide range of activities including manufacturing, engineering, steel, heavy machinery, machine tools, fertilizers, drugs, textiles, pharmaceuticals, petro-chemicals, extraction and refining of crude oil; services such as telecommunication, trading, tourism and warehousing; and a range of consultancy services.

With the economy embarking on the process of Liberalization, Privatization and Globalization since the early-1990s, the role of the Indian Public Sector has subsequently undergone a rapid change. Integration of the domestic economy with global markets has thrown up a plethora of opportunities and challenges. Some of the public sector enterprises with strategic vision are actively exploring new avenues and have increased their activities to go in for mergers, acquisitions, amalgamations, takeovers and for creating new joint ventures. Acquisitions, JVs and green field projects in Petroleum Sector have already taken place and are under active consideration in Power, Coal and Mining Sectors.

Off late, disinvestment of select Central PSUs has also gathered steam to meet the government's massive social spending and bridge the economy's growing fiscal deficit. Today, both the Public and Private Sectors have become an integral part of the economy, with both the sectors complimenting each other in strengthening the nation's industrial landscape. However, the recent economic meltdown has initiated a debate about the way business and operations are being handled by the PSUs, especially against the backdrop where globally several corporates have either gone bankrupt or have marginally survived owing to state-sponsored bail-outs. In this context, it is worth noting that the Indian PSUs have emerged relatively unscathed to register reasonable growth rates.

Keeping in view the importance to address the various vital concerns of the public sector to make it even more competitive, **Indian Chamber of Commerce is organizing the Summit on India Public Sector Agenda @ 2015, in association with Department of Public Enterprises, Government of India.** I am sure this would be an ideal forum where key industry players would share their concerns with the relevant stakeholders, policy makers, service providers and vendors. I sincerely hope that this initiative would provide an opportunity to discover the best practices and alternative strategies that can be adopted by the Indian PSUs to enhance its productivity and competitiveness, which in turn will shape its agenda till 2015.

About Deloitte

Deloitte¹ is one of the world's largest audit and consulting firm, having more than 170,000 people in 140 countries. Our clients include nearly one-fifth of the world's largest corporations, including Government and public sector enterprises. Deloitte's global presence is highlighted below.

Deloitte: Global network – 140 countries; 170,000 people



The services offered by Deloitte to its clients, which are best represented in the figure below, have helped us develop an in-depth understanding of various sectors like Public Sector & Government, Healthcare and Life Sciences, Manufacturing, Aviation, Transport and Infrastructure, Energy and Resources, Consumer Business, Global Financial Services Industry (GFSI) etc.

With offices across thirteen cities in India, Deloitte is well placed to serve clients across the length & breadth of the country.

The Indian practice offers a comprehensive range of services to its clients leveraging its strength of over 14,000 professional staff comprising primarily of Engineer, MBAs and Chartered Accountants

¹ Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.com/about for a detailed description of the legal structure of Deloitte Touche Tohmatsu Limited and its member firms

About Indian Chamber of Commerce

Founded in 1925, ICC is the leading and only National Chamber of Commerce operating from Kolkata, and one of the most pro-active and forward-looking Chambers in the country today. Its membership spans some of the most prominent and major industrial groups in India. ICC is the founder member of FICCI. Set up by a group of pioneering industrialists led by Mr. G D Birla, the Indian Chamber was closely associated with the Indian Freedom Movement, as the first organised voice of indigenous Indian Industry. Several of the distinguished industry leaders in India, such as Mr. B M Birla, Sir Ardeshir Dalal, Sir Badridas Goenka, Mr. S P Jain, Lala Karamchand Thapar, Mr. Russi Mody, Mr Ashok Jain, Mr. Sanjiv Goenka, have led the ICC as its President.

ICC is the only Chamber from India to win the first prize in World Chambers Competition in Quebec, Canada.

The Chamber has a special focus upon India's trade & commerce relations with other Countries including South & South-East Asian nations, in sync with India's 'Look East' Policy, and has played a key role in building synergies between India and her Asian neighbours like Singapore, Indonesia, Vietnam, Thailand, Bangladesh, and Bhutan through Trade & Business Delegation Exchanges, and large Investment Summits.

The ICC offices Address are as follows:

Kolkata:

Indian Chamber of Commerce
ICC Towers – India Exchange
4, India Exchange Place,
Kolkata-700001
Ph: 033 22303242/3/4
Fx: 033 22313377/80
Em: ps2sg@indianchamber.net

Delhi:

Indian Chamber of Commerce
323, Ansal Chamber II
6, Bhikaji Cama Place
New Delhi – 110066
Ph: 011 4610 1431-38/ 46101439
Em: energy@indianchamber.net

Guwahati:

Indian Chamber of Commerce
No: 209, R.S.Barua Road
Guwahati – 781005
Ph: 0361 2464767/1763
Em: iccner@indianchamber.net

ICC's North-East Initiative has gained a new momentum and dynamism, and the Chamber has been hugely successful in spreading awareness about the great economic potential of the North-East at national and international levels. Trade & Investment shows on North-East in countries like Singapore, Thailand and Vietnam have created new vistas of economic co-operation between the North-East of India and South-East Asia. The North East Initiative is also engaging with the state governments in livelihood generation by promoting indigenous products of the region through export oriented projects. ICC is also recognized as Nodal Chamber for development of North East of India by Ministry of DoNER.

The Chamber also has a very strong focus upon Economic Research & Policy issues - it regularly undertakes Macro-economic Surveys/Studies, prepares State Investment Climate Reports and Sector Reports, provides necessary Policy Inputs & Budget Recommendations to Governments at State & Central levels.

The Indian Chamber headquartered in Kolkata, over the last few years has truly emerged as a national Chamber of repute, with full-fledged offices in New Delhi and Guwahati functioning efficiently, and building meaningful synergies between Industry and Government by addressing strategic issues of national significance.

Importance of PSEs in Indian Economy

Introduction

Since inception, the Central Public Sector Enterprises (CPSEs) have been the mainstay of the Indian economy and were set up with the mandate to i) serve the broad macro-economic objectives of higher economic growth, ii) achieve self-sufficiency in production of goods/ services, iii) facilitate long term equilibrium in balance of payments and iv) ensure stability in prices and create benchmarks for prices of essential items.

Historically, CPSEs assume significant importance to India's economy, both in pre and post independence period. In the pre-independence era, the public sector enterprises were confined primarily to select sectors including Railways, Posts & Telegraphs, Port Trust, Ordnance Factories, etc.

Post independence, on account of the economic status of the country being characterized by an agrarian economy with a weak industrial base, regional imbalance in economic development, low level of savings, inadequate infrastructure facilities; the development of Public sector enterprises was identified as a key driver for self-reliant economic growth in the absence of significant private capital. Consequently, the Industrial Policy Resolution, 1948 and 1956 laid emphasis on constituting public enterprises by the Central Government for industrial development in the core sectors.

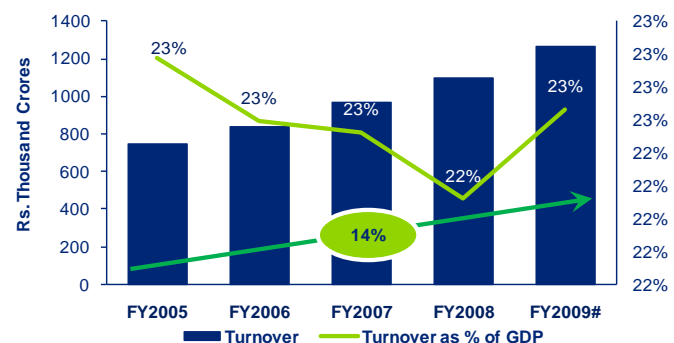
Consequent to the initiatives taken during the Five Year Plans, the role of CPSEs in terms of contribution to the Indian economy has increased manifold. Thus, the number of CPSEs² as on 31 March, 2009, was 246, with a total capital employed of nearly Rs. 5.3 lakh crores as against 5 CPSEs having a total investment of Rs. 29 crores on the eve of the first Five year plan.

With the onset of economic reforms in 1991, the Government initiated a systemic shift to a more open economy with greater reliance upon market forces and a larger role of the private sector including foreign investment. Consequently, the CPSEs were exposed to competition from domestic private sector companies as well as large multi-national corporations. Given the competitive environment, the CPSEs undertook significant initiatives for up scaling technologies and capacities in order to operate at par with the private counterparts in the liberalized economy. With continued focused efforts towards achieving excellence, several of the CPSEs have become self reliant and are playing a critical role in building the Indian economy.

Key CPSE contributions to the Indian economy

CPSE share in India's Gross Domestic Product (GDP)

- As reflected in the figure alongside, the turnover of CPSEs have increased from Rs. 7.4 lakh crores in FY 2005 to an estimated Rs.12.6 lakh crores in FY 2009 registering a CAGR of 14.1% during the FY 2005-09 period. Further, the growth in CPSEs has been in line with the overall GDP³ growth of the country, recording a CAGR of 14.5% during the same period
- Consequently, in terms of turnover, the contribution of CPSEs to the GDP has ranged between 22%- 23% during the period



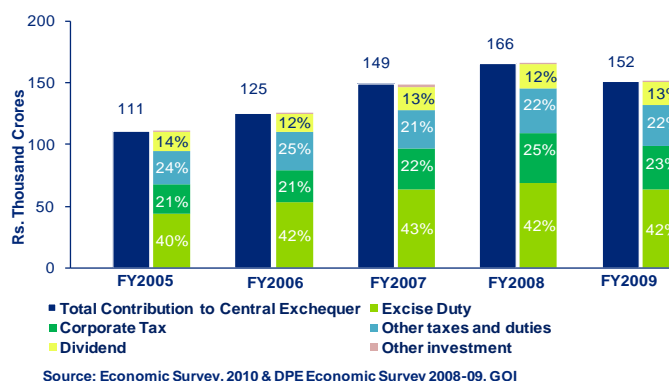
Source: Economic Survey, 2010 & DPE Economic Survey 2008-09, GOI
Quick estimate of GDP at market prices

² Excluding 7 Insurance Companies; Source: Department of Public Enterprises, Government of India

³ At market prices

Contribution to the Central Exchequer

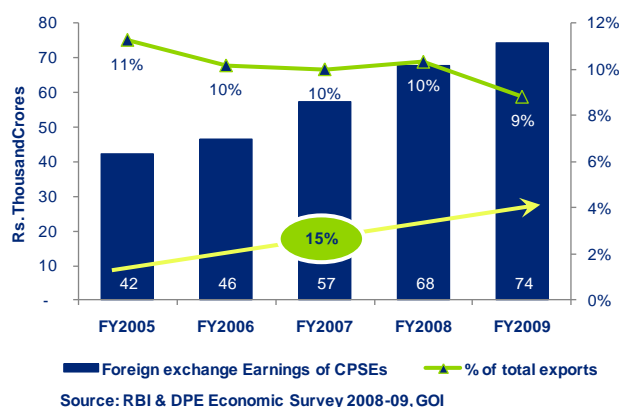
- Over the years, CPSEs have contributed significantly to the Central exchequer by way of payment of taxes (direct and indirect), duties, dividend payment and interest on Government loans. As evident from the chart alongside, the total contribution by the CPSEs has increased from Rs. 1.1 lakh crores in FY 2005 to an estimated Rs. 1.5 lakh crores in FY 2009 registering a CAGR of 8% during the FY 2005-09 period. However, there has been a YoY decline in contribution by 8.5% in FY 2009 primarily on account of reduction in contribution towards customs and excise duty



- Of the total contribution, payment towards taxes and duties accounted for over 87% on an average during FY 2005-09 period while the balance is being contributed by payments towards dividend and interest on Government loans
- It may be important to note that CPSEs contribution towards total direct and indirect tax collection in India has been significant at around 22% on an average during the FY 2007-09 period. Further, CPSEs payment towards excise duty accounted for over 50% on an average of the total excise collection while contribution to the corporate tax accounted for around 17% on an average of the total corporate tax collection during the period

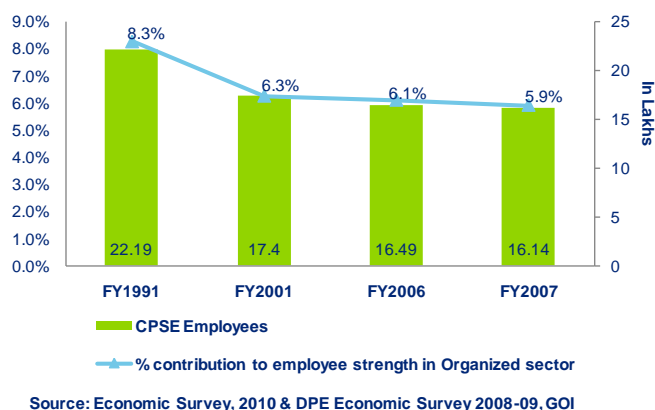
Contribution to Foreign exchange earnings

- CPSEs have contributed significantly to the overall foreign exchange earnings of the country through exports of goods and services (royalty, know-how, professional and consultancy fees) with average contribution being around 10% in the last five years
- In terms of growth trends, foreign exchange earnings by CPSEs registered a CAGR of 15.1% during the FY 2005-09 period as reflected in the chart alongside



Contribution towards employment generation in the Organized Sector

- CPSEs have made significant contribution towards employment generation in the organized sector, although there has been a steady decline over the years. During FY 2007, CPSEs employed 16.14 lakh people (excluding casual workers and contract labours) accounting for around 6% of the total employment in the organized sector. With increased automation levels across key industries in manufacturing and services, the employee strength has declined to 15.35 lakh in FY 2009. However, out of the total 246 CPSEs existing as on March 2009, around 33



CPSEs are yet to commence business implying additional scope for employment generation in future

- Although the employee strength in CPSEs has reduced over the years, aggregate emoluments have increased from Rs. 0.5 lakh crores in FY 2006 to around Rs. 0.8 lakh crores in FY 2009 with increasing salary levels.

Growth in Market Capitalization

- Based on the growth witnessed in market capitalization of the listed CPSEs, it is observed that they have emerged as major wealth creators for investors/ stakeholders. As on March 31, 2009, market capitalization of 41 listed entities accounted for 26.4% of the BSE market capitalization compared to 21.8% of the same in FY 2008
- In the backdrop of the global meltdown in FY 2009, the market capitalization of CPSEs decreased by 27% over FY 2008. Even then, the wealth erosion in CPSEs was relatively lower than the decline in overall market capitalization (around 40% in the BSE) during the same period
- With the recovery in stock markets in FY 2010, the aggregate market capitalization of 37 PSEs witnessed an increase by Rs 5 lakh crore with a 68.7% growth during January to November, 2009. Consequently, CPSEs contribution to BSE's market capitalization has increased to 30% by the end of November, 2009.

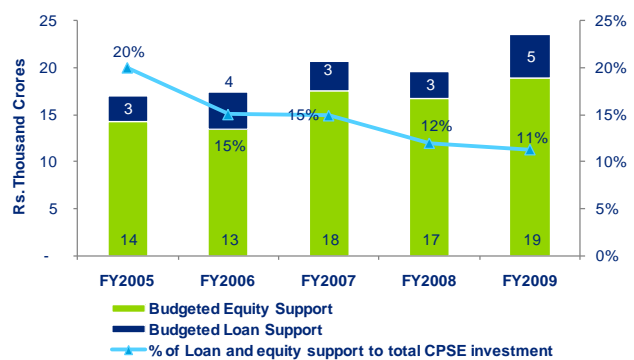
Outbound Investment

- On account of the progressive liberalization in India's overseas investment policy, FDI outflows witnessed significant increase with total outflows through investment in joint ventures/ wholly owned subsidiaries increasing from USD 6 billion in FY 2006 to around USD 18.6 billion in FY 2009.
- CPSE's contribution in outbound investment has also been significant primarily on account of investment made by ONGC Videsh Ltd. (wholly owned subsidiary of ONGC) involved in overseas Exploration & Production activities. Other key CPSEs with significant outbound investment include Indian Oil Corporation, GAIL, BHEL, NTPC, RITES etc.

In addition to significant contribution towards the growth of the Indian economy, most of the CPSEs have been able to ensure viable operations on a self sustainable basis which is evident from the decline in budgetary support in terms of loan and equity from the Government over the years as presented in the chart below:

Increase in self reliance through decline in budgetary support from the Government

- During the initial years and even during the nineties, a large number of CPSEs were dependent on budgetary support extended by the Central Government. However, the number of CPSEs in this category has gradually decreased over the years. The chart alongside shows Government budgetary support to CPSEs during the FY 2005-09 period. As shown in the chart alongside, the budgeted support (comprising equity and loan) increased from Rs. 17,000 crores in FY 2005 to around Rs. 23,500 crores in FY 2009



Source: Annual Budget documents published by GoI

- However, the budgetary support as a % of the total investment outlays in PSEs has declined from 20% in FY 2005 to around 11% in FY 2009 indicating that the CPSEs have become more self reliant and have been able to raise funds through internal accruals and borrowing from banks/ financial institutions

Key sectors for PSE operations

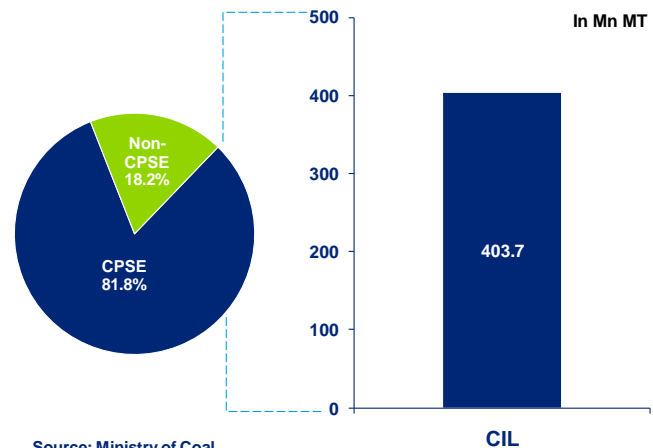
Based on the Public Enterprises (PE) Survey, 2008-09, as on March 31, 2009, 213 CPSEs out of a total of 246 CPSEs operate in five sectors/ cognate groups, namely, i) Agriculture, ii) Mining, iii) Manufacturing, iv) Electricity and v) Services.

Analysis of the market share of CPSEs further shows that, within these sectors, the key industries where CPSEs have significant/ dominant share include i) Coal and Crude Oil in the mining sector, ii) Petroleum (Refinery and Marketing) in the manufacturing / processing sector, iii) Power Generation in the electricity sector and iv) Telecommunications in the services sector.

Coal

With a view to enable investment of public funds to enhance growth in the coal industry and to optimize available coal resources, improve mining standards and working conditions, the industry was nationalized in the early 1970s. Consequently, the coal industry has been dominated by the PSEs under the Central and State Government.

- In terms of share in coal production, CPSEs contributed around 82% of the total domestic production of 492.8 Mn MT in FY 2009 with Coal India Limited (CIL) and its subsidiaries enjoying a dominant position as reflected in the chart alongside
- Among the non CPSEs accounting for the remaining share, the key players include Singareni Collieries Company Limited (SCCL), a public sector enterprise (joint venture between the State Government of Andhra Pradesh & Central Government) and Tata Steel



Source: Ministry of Coal

Coal India Limited (CIL)⁴

- CIL was incorporated in 1973 under the Coal Mines Nationalization Act, 1973 with the mandate to produce and market coal (and coal products) efficiently and economically keeping in view safety, conservation and quality. Over the years, it has emerged as the largest coal producing company in the world with coal production of 431 Mn MT in FY 2010.
- CIL is a 'Navratna' CPSE, contributing around 4% of total CPSEs turnover and accounting for nearly 25% of the total employee strength in CPSEs. In FY 2009, it was the fifth highest profit making company among all the CPSEs
- CIL has core competence in the entire coal business value chain comprising exploration, planning & design, operations, beneficiation and marketing. It currently operates 471 mines in 21 major coalfields across 8 states in India
- In terms of product mix, CIL produces both coking and non-coking coal, although bulk of the production (over 90% share) is accounted by non-coking coal. The company is highly price competitive on account of being one of the lowest cost producer globally (Cost of production from open cast mines: Rs 745 per MT in FY 2010)
- In pursuance of capitalizing on the rising demand for coal in India, CIL has been continuously focusing on enhancing production through expansion of existing mine capacities along with development of new/ abandoned mines as well as undertaking initiatives to acquire strategic international resources/ mining rights
- In October 2010, the company concluded an initial public offer (IPO) offering 63.16 crores shares, representing 10% of the paid up capital. The issue was oversubscribed 15.2 times, with the shares

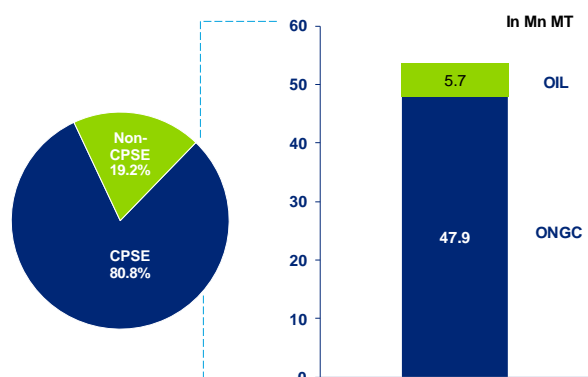
⁴ Source: Annual Report & Company website of Coal India Limited

listing on the National Stock Exchange (NSE) at a premium of 39.7% (closing price on NSE as on listing date November 04, 2010: Rs. 342.3; Issue price: Rs. 245 per share) over the issue price.

Crude Oil and Natural Gas

Crude Oil and Natural Gas is another industry within the mining sector characterized by significant presence of CPSEs. However, with the introduction of New Exploration Licensing Policy in 1999, the industry has witnessed significant change with private players gradually gaining foothold in the industry.

- In terms of share in oil and gas production, CPSEs contribute around 81 % of the total domestic production in FY 2009. Key players include Oil & Natural Gas Corporation (ONGC) and Oil India Ltd. (OIL) accounting for 89% and 11% share of the total production respectively
- Among the non CPSEs, the key players include private majors like Reliance Industries Limited, Gujarat State Petroleum Corporation, Cairn Energy India Ltd, Essar Oil Ltd, etc.



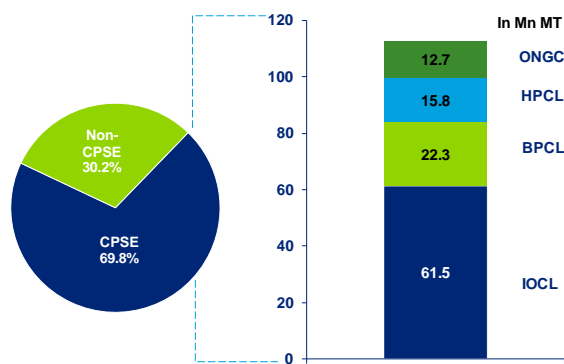
Source: Ministry of Petroleum & Natural Gas

Oil and Natural Gas Corporation Ltd. (ONGC)⁵

- ONGC was incorporated in 1993 and is engaged in exploration and production of hydrocarbons to meet the energy needs and to ensure long term energy sustainability of India. It is currently the largest Crude Oil and Gas producing company in India, contributing over 70% of the Oil and Oil Equivalent Gas (OEG) production in FY 2009
- Globally, ONGC ranks 3rd among the Oil & Gas exploration and production companies in the world and is 23rd among the leading global energy majors as per Platt's 250 Global Energy Companies List for the year 2009
- ONGC has been conferred the 'Maharatna' status and contributes nearly 5% of total CPSE turnover. Further, it ranks 1st in terms of net profit in FY 2009 among all the CPSEs with the net profit recorded at Rs. 16126 crores
- ONGC is primarily involved in Exploration and Production (E&P) activities, managed through 12 Assets for oil and gas production activities and 7 Basins for conducting exploration activities.
- In terms of production efficiency, ONGC is one of the lowest cost Exploration & Production companies, with its average lifting and finding cost being at par with best in class International peers
- With a view to insulate itself from the inherent risk of E&P activities, consequent to dismantling of APM regime, ONGC is taking initiatives to have presence across the entire hydrocarbon value chain going forward

Petroleum (Refining and Marketing)

On account of significant control on prices through Administered Pricing Mechanism (APM) by the Central Government, the CPSEs have traditionally had a strong foothold in the petroleum refining and marketing industry. However, the share of the private sector is expected to increase progressively with the commissioning of RIL's export oriented refinery at the Jamnagar Special Economic Zone (SEZ).



Source: Ministry of Petroleum & Natural Gas

⁵ Source: Annual Report & Company Website of Oil and Natural Gas Corporation Ltd

- In terms of share in petroleum refining and marketing, CPSEs contributed around 70 % of the total domestic production in FY 2009. Among the CPSEs, Indian Oil Corporation (IOC) ⁶is the market leader with 54% market share followed by Bharat Petroleum Corporation Ltd. (BPCL) ⁷with 20% market share. Other key players having significant presence include Hindustan petroleum Corporation Ltd. (HPCL) and Oil & Natural Gas Corporation (ONGC).⁸
- Among the non CPSEs, the key players include private majors like Reliance Industries Limited, Essar Oil Ltd, etc.

Indian Oil Corporation Ltd. (IOC)⁹

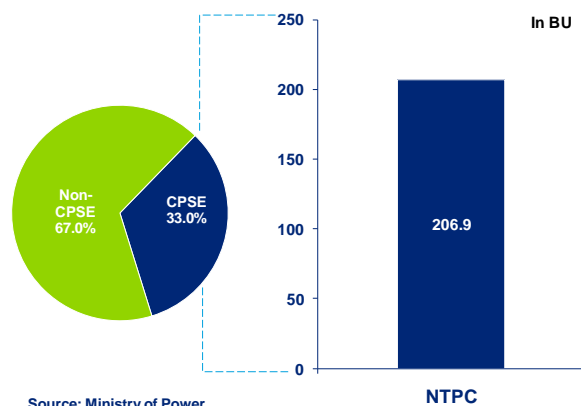
- IOC was incorporated in 1964 with the mandate to serve the national interest in Oil and related sectors and to enhance the country's self-sufficiency in Oil refining. It is currently the largest downstream company in the Oil and Gas Sector in India, accounting for around 46% market share in FY 2009
- Globally, IOC ranks 3rd among the petroleum refining and marketing company as per Platt's 250 Global Energy Companies List for the year 2009
- IOC has been conferred 'Maharatna' status and contributed nearly 21% of total CPSE turnover and around 38% of the total CPSEs contribution to the national exchequer by way of taxes and duties. Further, the company was among the ten highest profit making organizations in FY 2009 among all the CPSEs with its net profit at Rs. 2950 crores
- IOC is primarily engaged in refining and marketing of petroleum products. In addition to petroleum refining, they are involved in transportation of crude and petroleum products through its pipelines, research and development, blending and production of lubricants. The Company's operations includes 6 subsidiaries and 13 financial joint ventures (JVs) in the field of petroleum and petrochemicals
- Continuing with its pursuit of developing Green technologies, the company rolled out new technologies, during FY 2009 for deep desulphurization of gasoline and diesel streams
- In order to meet the upgraded fuel requirements as per the Auto fuel policy of the Government, IOC has embarked on fuel quality upgradation projects to ensure sustaining its leadership in the refinery and marketing sector

Power Generation

With the National Electricity Policy aiming at accelerated development of power sector in India, power generation has witnessed significant growth with total generation being 723.8 BU in FY 2009, registering a CAGR of 5.5% during FY 2005-09 period. While there has been an increased emphasis laid on diversifying the energy sources like biomass, solar, wind, etc in recent years, thermal power generation continues to dominate with over 80% contribution to the power generation in India.

Being a highly regulated sector, it has been traditionally dominated by public sector companies under the Central Government as well as individual State Governments. However, the reform initiatives undertaken by the Government in recent years, including implementation of section 63 of the Electricity Act, 2003, provision of open access & tariff framework under Tariff policy has created an enabling environment for private sector participation resulting in increasing investment by private sector.

- In terms of share of power generation, NTPC is a prominent player, accounting for around 29% of the total power generation in the country in FY



⁶ Includes subsidiary companies Chennai Petroleum Corporation Ltd and Bongaigaon Refinery & Petrochemicals Ltd

⁷ Includes subsidiary companies Numaligarh Refinery Ltd

⁸ Includes subsidiary company Mangalore Refinery and Petrochemicals Ltd

⁹ Source: Annual Report & Company Website of Indian Oil Corporation Ltd

2009

- Among the Non CPSEs, bulk of the generation is being accounted for by the state public sector companies, which contribute around 50% of the total generation while private players account for the remaining share

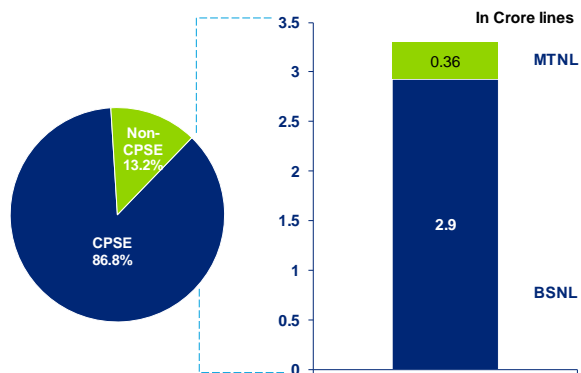
National Thermal Power Corporation Ltd. (NTPC)¹⁰

- NTPC was incorporated in 1975 with the mandate for planning, promoting and organizing integrated development of thermal power (including Associated Transmission Systems) in the country. It is currently the largest player in the power sector, generating 218.8 BU of electricity in FY 2010, accounting for 28.6% of the total power generation and 35% of the thermal power generation in India
- NTPC features in the 'Forbes Global 2000' world's largest companies for the year 2009. Globally, the company ranked 2nd among the Independent power producers in 2009, as per Platts Top 250 Global Energy Company for 2009
- NTPC has been conferred the 'Maharatna' status with its contribution to the total CPSE turnover being 3%. Further, the company was the 2nd highest profit making company in FY 2010 among all the CPSEs, with a net profit of Rs. 8728.2 crores
- NTPC is primarily engaged in construction, generation, operation & maintenance, renovation & modernization of power stations and projects, transmission, distribution, sale of power generated at Stations in India and abroad. In addition, NTPC is also responsible for planning, investigation, research, design and preparation of preliminary, feasibility and detailed project reports related to installation and commissioning of power plants
- In pursuance of continuing its leadership in the power sector, the company has embarked on new initiatives like coal mining, LNG value chain, power trading, distribution, etc to emerge as an integrated power company with presence across the entire energy value chain.
- In terms of production efficiency, the coal based thermal power stations of NTPC has operated at a PLF of 90.8% vis-à-vis national average of 77.5%
- With a view to promote sustainable energy development, the company has been progressively diversifying its fuel mix to increase the share of non-fossil fuel. In line with this objective, NTPC has entered into a joint venture agreement with Nuclear Power Corporation of India (NPCIL) to set up a nuclear power project
- In pursuit of green house gas (GHG) mitigation from existing thermal power plants, the company set up a Center for Power Efficiency and Environmental Protection in 1996 with technical assistance of USAID/ USDOE, which has resulted in significant reduction in emission levels of carbon dioxide.

Telecommunications

Telecommunication services in India, encompassing both wire line and wireless connectivity, have witnessed unparalleled growth by global standards in the last decade with the country emerging as the second largest market in the world in wireless connectivity. According to Telecom Regulatory Authority of India, the total subscriber base currently is over 650 million with wireless connectivity accounting for around 94% of the total subscriber base. While wireless connectivity is primarily dominated by the private players, the CPSEs have a strong foothold in wireline connectivity.

- In case of wire line services, the key players among CPSEs include Bharat Sanchar Nigam Limited (BSNL) and Mahanagar Telephone Nigam Ltd accounting for 77% and 9% market share respectively. The remaining share is accounted for by private players like Bharti



¹⁰ Source: Annual report and Company Website of NTPC Ltd

Source: Telecom Regulatory Authority of India

Airtel, Reliance Communications & Tata Teleservices

- Wireless segment, comprising GSM and CDMA services, is largely dominated by private players like Bharti Airtel, Reliance Communication, Vodafone, Idea Cellular, Aircel and Tata Indicom. CPSEs like BSNL and MTNL have a 12% share of the total market

Bharat Sanchar Nigam Ltd. (BSNL)¹¹

- BSNL was incorporated in 2000 with the mandate to take over the business of providing telecom services and network of the erstwhile Department of Telecommunications along with all its assets and liabilities, contractual rights and obligations. The company is a 'Miniratna - I' CPSE and currently operates under the administrative control of Ministry of Communications & Information Technology status
- Globally, BSNL is the 7th largest telecommunications company providing comprehensive range of telecom services including Wireline, CDMA mobile, GSM Mobile, Internet, Broadband, Carrier service, MPLS-VPN, VSAT, VoIP services, IN Services etc
- BSNL is a pan India service provider, having extensive reach and network penetration and provides services across the entire country except Delhi & Mumbai.
- In terms of technology initiatives, the company has set up state of the art multi-gigabit, multi-protocol convergent IP infrastructure which provides convergent services like voice, data and video through the same backbone and broadband access network
- Given the gap between the rural and urban tele-density in the country, BSNL is well positioned to capitalize on the expected demand growth in rural market in the near future, given its high network penetration in rural areas

¹¹ Source: Annual Report and Company Website of BSNL

Representative operational excellence initiatives adopted by CPSEs

As highlighted earlier, the CPSEs continue to have a dominant/ significant share in several sectors/ industries on account of their continued efforts towards achieving competitiveness and excellence to operate at par vis-à-vis their private sector counterparts. The current chapter attempts to highlight some of the key operational best practices embraced by CPSEs in their quest towards maintaining market share as well as being corporate citizens. For purpose of analysis and presentation, these initiatives have been grouped in to the following categories:

- Corporate Governance
- Organization Development / Human Resources Management
- Streamlining business processes and practices
- Environment Excellence
- Corporate Social Responsibility

Corporate Governance

Most established codes of Corporate Governance for state owned enterprises (SoE), including the OECD Guidelines on Corporate Governance of SoEs envisage a proactive role of the organization in (a) Ensuring equitable treatment of shareholders, (b) Recognizing, respecting and reporting on relations with all key stakeholders, (c) Maintaining high standards of transparency and disclosure and (d) Having requisite systems and practices for its Board of Directors to effectively discharge its role of guiding and monitoring the SoE.

Most CPSEs in India would compare favorably when it comes to adoption of the above measures, as highlighted below:

- Having an active policy for communication with all shareholders for ensuring dissemination of information on key business decisions
- Ensuring representation of minority shareholders' on the Board of Directors for assuring them that their interests are taken into consideration
- Having Internal code of business conduct and ethics for ensuring ethical and transparent process in managing the affairs of the enterprise

Illustrative examples of Corporate Governance in CPSEs

- ONGC is one of the organizations who have been following these guidelines even when it was voluntary for the companies to comply with these guidelines. As part of Corporate Governance initiatives, ONGC has inducted 4 Independent Directors on its board along with formation of various board level committees viz. Audit & Ethics Committee, Remuneration Committee, Health Safety & Environment Committee etc.
- NTPC has been following Corporate Governance guidelines issued by the Department of Public Enterprises. As part of the initiatives, it has inducted 9 Independent Directors in its Board along with formation of Audit committee, remuneration committee, shareholder grievance committee etc. The organization has also formulated policies including whistle blower policy, ethical code of conduct, succession planning etc.

Organization Development / Human Resources Management

There is an increasing realization that deployment of quality human resources is critical for sustainable performance of the CPSEs. Accordingly, in pursuance of attracting and retaining quality talent, the Government/ most of the CPSEs have taken requisite initiatives including the following:

- Adopting contractual recruitment in key management positions with market linked compensation including variable pay
- Organizing/ arranging training programs, aimed at capacity building and augmentation of skill sets of the employees
- Having a succession planning policy aimed at identifying employees with leadership potential and accordingly grooming them to fit into the envisaged leadership roles
- The Government has taken an initiative in forming a committee under Justice M Jagannadha Rao for recommending a suitable pay structure for CPSE. Key recommendations of this committee included:
 - Executive compensation package should be independent of that proposed for Government servants and should progressively be aligned with their counterparts in the private sector
 - Recommended pay package can be implemented only by profitable CPSEs and may be considered in various stages for ensuring the profitability post implementation is not significantly impacted
 - Performance linked pay can be implemented only if the enterprise has a performance management system in place, has entered into an MOU with its parent department/ ministry and have inducted Independent directors on their board
 - Annual increments can be paid based on performance of individual as determined by the performance appraisal system and the ability of the CPSE to pay

Illustrative examples of Organizational Development/ Human Resource Management

- Oil India Limited (OIL) has in place a “Performance Management System” (PMS) with the objective to achieve enhanced work standards, identify knowledge & skills required, provide feedback on performance, identify Training & Development (T&D) needs, provide objective performance evaluation for promotions, grant of incentives and inputs for succession planning. This system is used to track i) performance of its employees against Key Result Area (KRAs) linked to the overall objective of the organization and ii) identify development needs of individuals
- NTPC has a standardized and formalized KPA based performance management system. The system is designed to assess functional, managerial and potential competence in an objective and transparent manner. Further, with a view to facilitate smooth transition from incumbent leaders to their successors, NTPC has a succession policy in place wherein employees with leadership potential are identified and are suitably trained and groomed to fit into the leadership roles. The company has deployed a system that enables measurement of leadership effectiveness and gap identification against an identified set of leadership competence. Individual development plans are made based on the gaps identified to ensure that the process of development and growth is meaningful
- SAIL has organized Training programs aimed at continuously updating technologies, skills, attitudinal changes, career growth and leadership development for its employees. Further, for the transfer and absorption of advanced and new technologies, a good number of qualified technologists and specialists of SAIL plants are deputed every year for training abroad in countries like USA, Russia, Germany, UK, Japan, Austria, Australia etc

Streamlining business processes and practices

In order to ensure competitiveness vis-à-vis private sector players in terms of productivity, technological capability, cost effective operations, most of the CPSEs have taken initiatives towards streamlining the business processes and practices with focus on the following:

- Investing in state of the art technology with the objective of i) improving product quality, ii) enhancing productivity through streamlining manufacturing processes and iii) achieving cost reduction
- Adopting Integrated IT system, including ERP packages to support reengineered business processes and enhance efficiency in decision making, through real time information availability besides capturing transaction level data for MIS purposes

- Increased level of outsourcing, particularly non-core activities/ support functions, with a view to increase focus and enhance productivity in core operations together with reduction in overhead costs of the enterprises
- Increased focus on entering Public-Private Partnership (PPP) primarily with the objective of attracting funds in sectors like infrastructure, requiring significant investments, along with requisite expertise of the private player

Illustrative examples of Streamlining business processes and practices in CPSEs

- Power Grid Corporation of India (PGCIL) had been successful in adapting and efficiently implementing the state of the art Unified Load Dispatch Communication (ULDC) system, which has significantly contributed towards enhancing quality and economy in operation of power systems, besides improving data availability, visibility and transparency. This resulted in greater reliability in power supply to the users with less variations and encumbrances along with higher efficiency and cost reduction.
- With an objective of improving and integrating various processes, BHEL has implemented the SAP ERP package. BHEL had been using various disparate information architectures leading to duplication, errors and delays on account of reconciliation efforts. In order to address these drawbacks and to make the processes more efficient, BHEL decided to implement an integrated software based system for all business processes with a common database. The modules covered all its business functions including Sales & Distribution, Finance & Control, Material Management, Production Planning & Quality management. This has helped in achieving better efficiency through real time information availability.
- Realizing the importance of customer relationships in a competitive market, Bharat Sanchar Nigam Ltd (BSNL) has signed a multi-year licensing, support and maintenance contract with Convergys Corporation for a rating and billing solution in April 2008 to support its wireline subscribers. In addition to facilitating revenue growth through the delivery of new advanced services and bundled offerings, the Convergys solution has also helped BSNL lower its IT costs by consolidating and eliminating redundant systems, utilizing a distributed open-source platform, and limiting the need to pay for expensive and time-consuming custom system or application development.
- Mangalore Refinery and Petrochemicals Limited (MRPL), a subsidiary of ONGC has entered into a PPP with Kakinada Seaport Limited (KSPL), IL&FS and Andhra Pradesh Government to form a joint venture company named Kakinada SEZ limited. MRPL & KSPL are the key developers with IL&FS undertaking entire project development activities like conducting technical studies, financial structuring, bid process management, transaction advisors for financial closure.

Environment Excellence

The concept of environment and ecological balance has assumed a new dimension in the wake of increasing levels of deforestation, waste generation and environmental pollution. Most of the key CPSEs have taken a lead role towards achieving environment excellence by focusing on initiatives including:

- Having a dedicated environment department/ cell focusing on environment related initiatives
- Preventing use of or generation of toxic/ hazardous materials which may have an adverse impact on the health of the workforce, customers and overall community
- Conserving use of scarce and non-renewable resources for example - usage of recycled water, etc
- Ensuring adequate treatment of hazardous liquid waste/ solid, etc through Effluent Treatment Plant
- Preventing wasteful use and promoting conservation of resources, especially scarce and non-renewable resources

Illustrative examples towards Environment excellence initiatives in CPSEs

- Security Printing & Minting Corporation Limited (SPMCIL) engaged National Productivity Council (NPC) to conduct an energy audit of all its units and is in process of implementing the recommendations made by NPC. It has deployed "Environment Management System" at its manufacturing facilities in compliance to international standards for better environment

management.

- NALCO has established an Environment Department with presence at Head Quarter as well as plant level. The company has taken various initiatives towards environment protection through process improvement at its manufacturing locations. Further, it has carried out plantation at its manufacturing facilities and surrounding areas along with installation of hazardous waste management plant. Also, Nalco's technology associate Aluminum Pechiney (AP), France, with their experience of stringent pollution control standards in Europe, have ensured eco-friendly process technology.
- As part of the initiatives towards protecting environment and ecology, NHPC has taken several initiatives including supply of free fuel (kerosene & LPG) to construction workers to prevent use of wood as fuel & reuse of waste oils from plants. The company has taken a lead role in spreading the message of 'Green India- Clean India' and creating eco hubs by planting flowers and developing herbal parks in proximity to project sites

Corporate Social Responsibility (CSR)

The public sector in India was set up with the objective of achieving inclusive growth aimed at ensuring equity and justice to the overall community/ society. Consequently, CPSEs have been pioneers in implementing Corporate Social Responsibility (CSR) initiatives towards community growth and development while achieving their commercial mandate. Over the years, most of the CPSEs have consciously and extensively promoted corporate social activities including:

- Providing employment to the weaker and under-privileged sections of the society on a more equitable basis
- Providing all inclusive social facilities to the employees and their families, especially in the areas of education, healthcare and entertainment
- Providing assistance to social and cultural activities beneficial to employees and associated sections of the community
- Participating in or contributing to the causes and activities dealing with natural disasters

Illustrative examples of CSR initiatives by CPSEs

- ONGC has allocated around 2 % of its net profit towards CSR initiatives during FY 2010. Some of the key initiatives include i) Setting up & running five centres of Gandhi Institute of Computer Education & Information technology ii) Ashadeep "Shiksha Ki Jyot" project aimed at continued schooling of the girl students belonging to economically weaker sections of society and iii) 'Varishthajan Swasthya Sewa Abhiyan' with an objective of providing community based health services for destitute aged people
- NMDC has been actively participating in various CSR initiatives and has allocated around 2.4% of its net profit in FY 2010 towards CSR initiatives. Some of the key CSR initiatives taken by NMDC include i) Establishment of a residential school at Nagarnar in Chattishgarh ii) Mid-day meal programme for children in the surrounding villages of Donimalai Project, Karnataka covering around 10,000 children
- Neyveli Lignite Corporation has been actively involved in CSR activity with some of the key initiatives including i) Providing medical services including setting up a hospital with around 360 beds with peripheral dispensaries to provide allopathic and ayurvedic treatments to its employees, their family members and others ii) Established Neyveli Health Promotion and Social Welfare Society (NHPSWS) which offers services for the benefit of physically challenged, widows and destitute.

Empowering CPSEs with due accountability

Identifying need for empowerment of CPSEs

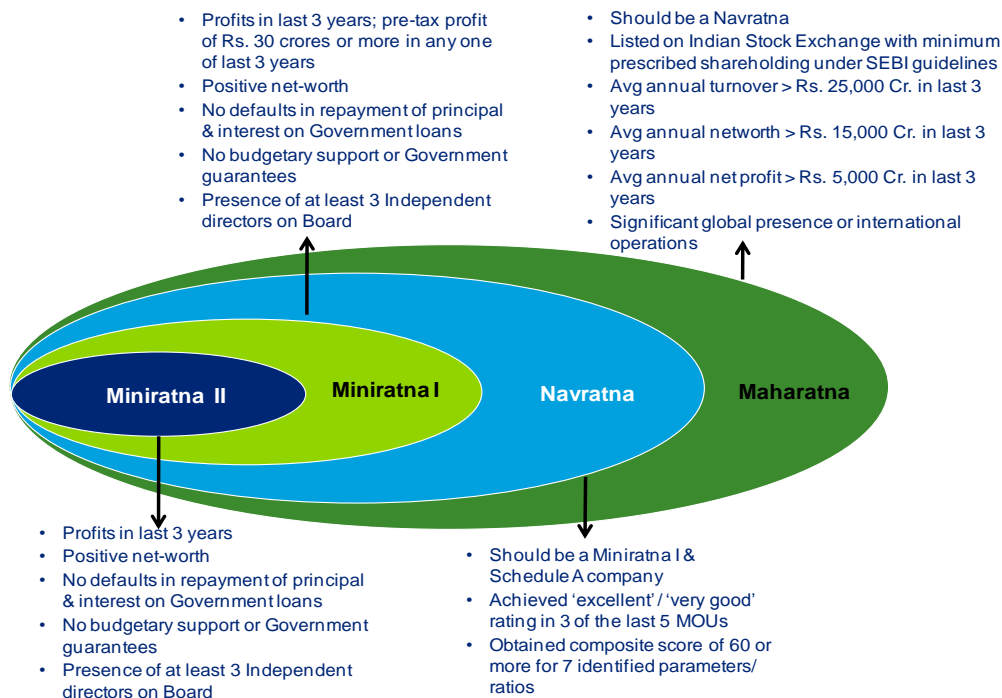
In the era of economic liberalization and globalization, the Central public sector enterprises (CPSEs) have continued to contribute significantly in building Indian economy and have demonstrated competitiveness in all aspects viz. productivity, technological capability, product quality, etc vis-à-vis their counterparts i.e. private sector players in the respective industries/ sectors. Post liberalization in 1991, the CPSEs have continuously focused their efforts in keeping pace with the competitive environment to ensure economically viable operations and long term sustainability. In the process, several CPSEs have become self reliant and have transformed into world class organizations. The stellar performance of prominent CPSEs is borne out by the fact that *“Out of the seven Indian companies selected in the Global Fortune 500 list for 2009, five were CPSEs which included one public sector bank”*.

Needless to say, such a transformation would never have been achieved by these CPSEs without the support of relevant interventions by the Central Government. In pursuance of competing with the external environment, the Government realized the need for empowering these enterprises with a view to delegate higher financial and operational powers to provide a level playing field with the private sector players (who had the competitive advantage of taking business decisions on their own).

Accordingly, the Department of Public Enterprises, Government of India, which has been the co-coordinating entity has adopted a categorization framework for grouping these enterprises into i) Navratna, ii) Miniratna I and iii) Miniratna II, in order to facilitate delegation of powers in line with their categorization. Taking a step forward in this direction, the Department of Public Enterprises, has recently introduced a new category of ‘Maharatna’ classification for empowering select CPSEs listed on stock exchanges to facilitate expansion of their operations to enable them to emerge as global giants.

Categorization Framework

The categorization framework including the eligibility criteria for classification of the CPSEs is illustrated in the figure below.



Level of Empowerment

Based on the categorization framework, as highlighted above, the level of empowerment for respective category/ classification of CPSEs are presented in the table below:

Category of PSEs	Capital Expenditure	Joint Ventures & Subsidiaries	Organization restructuring and Human resource management	Resource Mobilization	Mergers & Acquisitions
Maharatna	<ul style="list-style-type: none"> No monetary ceiling on capital investments 	<ul style="list-style-type: none"> Equity investment to establish financial joint ventures, wholly owned subsidiaries & undertake mergers & acquisitions in India or abroad, subject to a ceiling of 15% of net worth, limited to Rs. 5000 crores in one project along with an overall ceiling of 30% of net worth on all projects put together 	<ul style="list-style-type: none"> Effect organizational restructuring including creation of profit centers, etc, creation of below Board level posts upto E-9 level & abolition of all below Board level posts, delegation of powers to make all appointments, effect internal transfers & re-designation of all below board level posts, structuring and implementing schemes relating to personnel and human resource management and training 	<ul style="list-style-type: none"> Raise debt from domestic capital and international markets, the latter being subject to approval from RBI/ Department of Economic Affairs, as applicable & should be obtained through the Administrative Ministry 	<ul style="list-style-type: none"> Undertake mergers and acquisitions subject to conditions that i) it should be in line with the growth plan & in core area of the functioning of respective CPSE, ii) Cabinet Committee on Economic Affairs (CCEA) to be informed in case of investments made abroad
Navratna	<ul style="list-style-type: none"> No monetary ceiling on capital investments 	<ul style="list-style-type: none"> Equity investment to establish financial joint ventures & wholly owned subsidiaries in India or abroad, subject to a ceiling of 15% of net worth, limited to Rs. 1000 crores in one project along with an overall ceiling of 30% of net worth on all projects put together 	<ul style="list-style-type: none"> Effect organizational restructuring including creation of profit centers, etc, creation of below Board level posts upto E-6 level & abolition of all below Board level posts, delegation of powers related to human resource management (appointments, transfers, postings etc.) of below Board level executives by Board of Directors to Board sub-committees or to executives of the CPSE 	<ul style="list-style-type: none"> Raise debt from domestic capital markets and for borrowings from international market, subject to approval of RBI/ Department of Economic Affairs, as applicable & should be obtained through the administrative Ministry 	<ul style="list-style-type: none"> Undertake mergers and acquisitions subject to conditions that i) it should be in line with the growth plan & in core area of the functioning of respective CPSE, ii) conditions/ limits would be as in case of establishing joint ventures/ subsidiaries and iii) Cabinet Committee on Economic Affairs (CCEA) to be informed in case of investments made abroad
Miniratna I	<ul style="list-style-type: none"> Monetary ceiling of Rs. 500 crores or equal to net 	<ul style="list-style-type: none"> Equity investment to establish joint ventures and subsidiaries in India, 	<ul style="list-style-type: none"> Structuring & implementing schemes related to personnel and human resource management and 	N/A	<ul style="list-style-type: none"> Undertake mergers and acquisitions subject to conditions that i) it should be in line with the growth plan & in

Category of PSEs	Capital Expenditure	Joint Ventures & Subsidiaries	Organization restructuring and Human resource management	Resource Mobilization	Mergers & Acquisitions
	worth, whichever is lower	subject to a ceiling of 15% of net worth, limited to Rs. 500 crores in one project along with an overall ceiling of 30% of net worth on all projects put together	training, etc, delegation of powers related to human resources management (appointments, transfers, postings etc.) of below Board level executives by Board of Directors to Board sub-committees or to executives of the CPSE		core area of the functioning of respective CPSE, ii) conditions/ limits would be as in case of establishing joint ventures/ subsidiaries and iii) CCEA to be informed in case of investments made abroad
Miniratna II	<ul style="list-style-type: none"> Monetary ceiling of Rs. 250 crores or 50% of net worth, whichever is lower 	<ul style="list-style-type: none"> Equity investment to establish joint ventures and subsidiaries in India subject to a ceiling of 15% of net worth, limited to Rs. 250 crores in one project along with an overall ceiling of 30% of net worth on all projects put together 	<ul style="list-style-type: none"> Structuring & implementing schemes related to personnel and human resource management and training, etc, delegation of powers related to human resources management (appointments, transfers, postings etc.) of below Board level executives by Board of Directors to Board sub-committees or to executives of the CPSE 	N/A	<ul style="list-style-type: none"> Undertake mergers and acquisitions subject to conditions that i) it should be in line with the growth plan & in core area of the functioning of respective CPSE, ii) conditions/ limits would be as in case of establishing joint ventures/ subsidiaries and iii) CCEA to be informed in case of investments made abroad

Further, the above mentioned categories of CPSEs enjoy similar level of empowerment for the following activities as highlighted below:

- Technology Joint Venture and Strategic Alliances - Enter into technology joint ventures or strategic alliances and obtain by purchase or other arrangements, technology and know-how
- Creation/ Disinvestment in Subsidiaries - Holding companies can effect transfer of assets, float fresh equity and divest shareholding in subsidiaries subject to applicable guidelines
- Tours abroad of Functional Directors - Approval of business tours abroad (upto duration of 5 days) for functional directors by the CMD (for Maharatnas)/ Chief Executive (for Navratnas & Miniratnas) in emergency, under intimation to the Secretary of the administrative ministry

Accountability mechanisms in CPSEs

While the Government has empowered the CPSEs with the objective of providing a level playing field with the private sector entities, it has also instituted a mechanism in terms of adherence to Corporate Governance guidelines to ensure due accountability by these enterprises for discharging their functions. The key highlights of the guidelines include:

- To ensure independence of the Board, the CPSEs should have an optimum combination of Functional, Nominee and Independent Directors with the number of Functional Directors not exceeding 50% of the actual strength of the Board, the number of Nominee Directors appointed by Government being restricted to a maximum of two. For CPSEs listed on the stock exchange and whose Board is headed by an Executive Chairman, the number of Independent Directors should comprise at least 50% of Board Members, while for all other CPSEs (i.e. not listed CPSEs or CPSEs listed on stock exchange with non-executive Chairman), at least one-third of the Board Members will comprise Independent Directors
- The Board should meet at least once every quarter and reports on financial performance should be circulated to each Board member along with the agenda well in advance
- As part of the Board level committees, an independent Audit committee should be constituted with a minimum of 3 members with two-third of the members being Independent Directors to primarily oversee the enterprise's financial reporting process and disclosure of its financial information to ensure that the financial statements are correct, sufficient and credible
- The CPSEs shall submit quarterly progress reports on the status of compliance to Corporate Governance Guidelines, within 15 days from the close of each quarter, to respective Administrative Ministries/ Departments
- A separate section on Corporate Governance, with details of compliance, is to be published in annual accounts. The enterprise is also required to obtain a certificate from the auditor/ practicing Company Secretary regarding compliance to conditions of the Corporate Governance as stipulated in the guidelines. The certificate is to be sent to all shareholders annually and is also to be included in the annual report

In addition to adherence to the above guidelines, to ensure monitoring of overall performance of the CPSE, a Memorandum of Understanding (MoU) is signed annually between the management of the CPSE and the respective administrative department/ ministry where the enterprise management agrees on performance targets to be achieved and the respective administrative department agrees on the support to be given during the year. At the end of the financial year the achievements against targets are examined and the respective CPSEs rated. As discussed earlier, these ratings also determine the categorization of the enterprises and consequently their level of empowerment.

Best practices for managing PSEs – the global experience

Various studies have established the need for adoption of specific corporate governance practices to ensure sustained performance of PSEs / SoEs. The current chapter reviews some of the key corporate governance practices followed by developed countries in managing their SoEs and also highlights the experience of China in this area.

Corporate Governance practices in developed countries

The diagram below highlights the key dimensions which impact the relationship between Government and its PSEs. These factors have also been observed to have a significant impact on PSE performance:



Source: OECD Guidelines on Corporate Governance of State Owned Enterprises

Some of the key best practices for each dimension have been highlighted below:

Legal and regulatory framework of SOEs guaranteeing level playing field in the market

- There is a clear distinction between the government's SOE ownership function and government's market regulatory functions.
- The obligations and responsibilities that an SOE undertakes in terms of public services are clearly mandated by laws and regulations.
- SOEs are not exempted from the applicable laws and regulations applicable to the industry.
- SOEs governed by flexible legal and regulatory framework allowing necessary adjustments in capital structure for achieving company objectives.
- SOEs operate on normal commercial terms with respect to access to finance and transactions with other state owned banks and financing institutes.

Clear and consistent ownership policy of the state for ensuring transparent & accountable governance - well defined institutional structure

- Objectives of state's ownership and state's role in corporate governance of the SOEs clearly stated through an ownership policy.
- Full operational autonomy provided to the SOE management; government not involved in day-to-day management of the SOE.
- SOE board exercises its responsibilities and the government respects their independence.

- Government, as an active owner, exercises its ownership rights according to the legal structure of the companies. The prime responsibilities include:
 - Establishing well structured and transparent board nomination process
 - Developing reporting systems for regular monitoring of SOE performance, ensuring Government nominees/ representatives attends Board Meetings and General Meetings etc.
 - Maintaining continuous dialogue with external auditors and government control organizations

SOEs recognize the rights of all shareholders

- All stakeholders are treated equally.
- High degree of transparency is observed in respect of all stakeholders by ensuring access to necessary information for making informed investment decisions etc.
- SOEs formulate and operationalize policies for effective communication and consultation with all stakeholders.
- SOEs facilitate participation of minority shareholders in fundamental corporate decisions through Board representation, etc.

SOEs reports on their relationship with the stakeholders

- Stakeholder's rights recognized by the SOE and are established by laws or orders.
- SOEs communicate with investors, stakeholders and the public at large on their stakeholder policies and also provide information on their effective implementation
- Board of the SOE's develop, implement and communicate compliance programs for internal code of ethics thereby committing themselves to comply with country norms on corporate ethics, conduct and transparency

High standards of transparency

- Consistent and aggregated report on all SOEs published at least on a yearly basis.
- An internal audit function established which directly reports to the board or audit committee.
- Annual independent external audit conducted based on international standards; disclosure of financial and non-financial information in accordance to internationally recognized standards.
- Disclosures made on focus areas of significant concern for the state as owners and general public including:
 - Company objectives and their fulfillment
 - Ownership and voting structure
 - The risk factors and measures undertaken to manage such risks.
 - Financial assistances, guarantees or any financial commitments received from government

SOE Boards have necessary authority, competencies & objectivity

- SOE Board assigned a clear mandate and is responsible for the company's performance.
- SOE board carries out their functions of monitoring and providing management and strategic guidance.
- The board composition is constituted such that it can exercise objective and independent judgment. Typically, the Chairman of the board is an independent member and not the CEO. The Board has powers to appoint and remove the CEO.
- Specialized independent committees constituted, particularly with respect to Audit, Risk Management and Remuneration.
- Annual performance appraisal evaluating their own performance conducted by SOE board.

The following table provides examples of the above mentioned best practices followed by SOEs in some of the OECD member countries.

Best Practice	Australia	United Kingdom	France	Norway	New Zealand	Germany
<i>Legal and regulatory framework of SOEs guaranteeing level playing field in the market</i>	The Commonwealth Authorities and Companies Act (CAC) 1997 which applies to all SOEs replicates requirements of the Corporation Act 2001 and in some areas are more stringent. Incorporated SOEs are subject to the Corporation Act 2001 and listed SOEs are subject to the Australian Stock Exchange Listing Rules	Independent market regulators present in sectors like telecom, and electricity; General companies law apply to SOEs and other private players				General companies law apply to SOEs and other private players
<i>Clear and consistent ownership policy of the state for ensuring transparent & accountable governance – well defined institutional structure</i>	Government Business and Private Financing Advice Unit, a specialized unit with experts in financial, managerial and analytics skill sets provide oversight, management and strategic advice to SOEs	Shareholder Executive has been set up as advisory body providing advice to SOEs on shareholders role, corporate governance, formulating business plans, appointments and remuneration packages.	Agence des Participations d'Etat was created in 2004 for ensuring co-ordination of the SOE with other state agencies and reducing day-today management interventions of the government.	Centralized ownership model with most SOEs are under Ministry of Trade and Industries	Specialist advisory unit, Crown Companies Monitoring Advisory Unit (CCMAU), responsible for advising, monitoring and evaluating the SOEs; While Ministry of Finance focuses on economic efficiency and fiscal impact of SOEs, the sectoral Ministries through CCMAU are responsible for ensuring that the SOEs are successful companies.	Ministry of Finance elaborates guidelines of ownership and privatization policy; the sectoral ministries are responsible for the performance of the SOEs

Best Practice	Australia	United Kingdom	France	Norway	New Zealand	Germany
<i>SOEs recognize the rights of all shareholders</i>	The CAC Act of 1997, which applies to all SOEs, protects minority shareholders rights	General companies law apply to SOEs which protects adequately minority stakeholder rights		Government guidelines on corporate governance wrt SOEs highlighting treating all stakeholders equally the one of the most important factors; the minority stakeholders are part of the selection committee nominating board members	Minority stakeholders of listed SOEs are protected by provisions of general securities related legislation	General companies law apply to SOEs which protects adequately minority stakeholder rights
<i>SOEs reports on their relationship with the stakeholders</i>	SOEs have to be as transparent and fair to the creditors as private enterprises. SOEs have to comply with additional reporting regulations to the Treasury wrt creditors under the provisions of the CAC Act		1/3rd representatives of the board is filled by employees			SOE employees participates in decision making process
<i>High standards of transparency</i>	For enhancing ex ante accountability, the wholly owned SOEs develop a "Statement of Corporate Intent" specifying financial and non-financial targets for next three years	All SOEs (excepting trading firms) audited by external auditors; Auditor General (state) audits the trading firms; All SOEs set up under Companies Act needs to confirm UK Accounting Standards	Audit done by external auditors and Cour des Comptes (state); In France, the state audit directly reports to the executive	Audit done by external auditors as well as State Audit Office; The State Audit Office directly reports to the parliament	SOEs are required to carry out Value Based Reporting, focusing on the changes in SOE's economic value	Federal Ministry of Finance publishes German SOE Annual Report for ensuring transparency, the reports provides information on direct holding, state of privatization, etc.

Best Practice	Australia	United Kingdom	France	Norway	New Zealand	Germany
<i>SOE Boards have necessary authority, competencies & objectivity</i>	No public servant appointed to the Board; SOE Board members have absolute responsibility and are accountable for SOE performance	Specialized committees like Audit, Remuneration, Risk and Nomination committees present in all SOEs; Board members remuneration has two components – base pay and performance bonus	Rules/ regulations present providing specific guidelines on roles & responsibilities of the Board	No state representative in SOE board; Board has full authority; SOE board nominates the CEO	Structured and skill based nomination process; SOE Board nominates the CEO; Systematic evaluation of board's performance	Most/ all Board members are independent directors; SOE board nominates the CEO

The China experience

Led by a strong Government support in terms of key enablers and reforms, the State-Owned Enterprises (SOEs) have played a pivotal role in building the economy of China. Based on the information provided by Ministry of Finance, Government of China, these enterprises recorded a turnover of USD 1.8 trillion in 2009, accounting for around 36% of the country's GDP during the year.

Some of the key interventions¹² initiated by the Government for successful functioning of the SOEs include:

Formation of regulatory body - SASAC

With the objective of segregating regulation from ownership and addressing asset stripping (in case of ownership transfers through management buy-outs), the Government constituted a regulatory body called State Assets Supervision and Administration Commission (SASAC) in 2003 under the State Council with the key mandate of i) drafting laws and regulations regarding state-owned assets, ii) managing and restructuring state assets and iii) hiring and laying off the executives of central SOEs. The formation of SASAC redefined the relationship between the central government and the state owned "central enterprises". With its formation all the central SOEs were taken away from the control of various government agencies and put under one body, SASAC, with direct reporting to the State Council. The state owned 'local SOEs' are however owned and controlled by the respective local Governments.



Corporate Governance Reforms

As part of the Corporate Governance reforms, the Government has initiated the formation of 'Modern Enterprise Systems' which led to corporatization of SOEs with a view to ensure more transparency in the System. This system comprises four pillars viz. clarification of property rights, clarification of responsibilities, separation of bureaucracy and business and scientific management. The System requires the government authorities to state a clear position with respect to SOEs as their business units leading to clarification of government's role for e.g. the separation between bureaucratic role of managing macro-economy and corporate function of owning assets. The modern enterprise system led to corporatization of SOEs in which SOEs were strongly encouraged to transform themselves into corporate entity. This also led to modification of the supervisory systems in SOEs. The SOEs thus evolved from bureaucratically controlled entities to more clearly defined entities modeled on incorporated forms of ownership

Going Global Strategy

Over the years, the Chinese Government has actively pursued the 'Going Global' strategy to encourage globalization initiatives by the SOEs, as reflected from their significant outbound FDIs. The initiative towards a global footprint has helped the SOEs in i) acquiring better technology and technical know-how and ii) enhancing the corporate brand image. One of the primary reasons for such globalization has been the result of the trade barriers being imposed on Chinese exports by several countries. Consequently,

¹² Source: OECD Working Group on Privatization and Corporate Governance of State Owned Assets: State Owned Enterprises in China- Reviewing the Evidence

these enterprises embarked on setting up production facilities across various geographies. In pursuit of encouraging globalization, some of the key initiatives undertaken by the Government include:

- Facilitating economic policies in the form of regional free trade agreements, natural resource development projects like funding oil exploration abroad
- Collaboration between Ministry of Commerce and Ministry of Finance to support start-up funds for SOE investments abroad
- Creation of loan programs and streamlining of overseas investment procedures by National Development and Reform commission along with the Bank of Export and Import
- Promoting acquisition of technology from abroad through direct import of turnkey projects or through joint-venture partnerships between Chinese state-owned enterprises (SOEs) and multinational corporations (MNCs) with large tax incentives to foreign direct investors

Key highlights of the global initiatives undertaken:

- *2002 - Since 2002 GM has partnered with the state-owned Shanghai Automotive Industry Corporation (SAIC) in the South Korean venture GM Daewoo, which builds cars and sells components to GM's US operations*
 - *2003 – TCL, the large state owned enterprise acquired one of the largest TV producers in the world, the French company Thomson. It had earlier acquired German company, Schneider Electronics in 2002*
 - *2004 - Lenovo, high-tech state owned Chinese enterprise, acquired corporate brand IBM's PC Division for USD 175 million*
 - *2006 - China National Petroleum Corporation (CNPC) acquired Petro Kazakhstan, and China National Offshore Oil Corporation (CNOOC) acquired 45% of shares in a Nigerian ACPO oil well for USD 229 million. China Petroleum & Chemical Corporation (SINOPEC) acquired an Angolan oil well in 2006 for \$692 million*
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Closing Thoughts

For ensuring that the Indian economy continues to scale new heights and emerges as an economic superpower, it is imperative for the Central public sector enterprises (CPSEs) to continue to demonstrate global competitiveness and achieve market leadership. As highlighted earlier, the empowerment of these enterprises by the Government has been a key enabler which has helped them in overcoming some of the operational constraints, critical for successful functioning of these organizations. However, to make these CPSEs emerge as global leaders in their respective areas, requisite reforms/ interventions need to be fast tracked.

Experience in other countries suggests the following areas for priority intervention:

- Need to segregate ownership and governance of commercially-run CPSEs – In line with the principles of independent professional organization, there is a need for Government to progressively limit its involvement in the enterprises to that of promoter shareholder with its primary focus being on protecting and earning reasonable returns on public funds invested in such enterprises. All key strategic and operational decisions pertaining to the PSE should be delegated to the Board of Directors, which should comprise eminent professionals and have minimum representation from the Government. Simultaneously, requisite systems and processes need to be put in place for aligning the compensation structure of Board members to the long term interest of the organization and for monitoring of the Board of Directors' performance on a regular basis.
- While Government should not intervene in the day to day management of the CPSEs, in its role as promoter shareholder it should closely monitor the overall performance including creation of shareholder value in the respective enterprises. The key pre-requisites include (a) clearly defined institutional framework within Government led by a nodal agency / Department with representation from concerned Ministries / Departments which would monitor the performance of all PSUs at pre-specified intervals and be empowered to take remedial action in case of significant concerns and (b) well defined processes and templates for collection, collation and analysis of necessary information from the PSU for purposes of performance evaluation. As highlighted earlier in this report, many countries have constituted a specialist cell/ committee within Government with requisite skill sets for supporting the nodal agency in this exercise.
- For ensuring that CPSEs remain globally competitive, any obligations and responsibilities that a PSU is required to undertake in terms of public services beyond the generally accepted norms should be clearly mandated by laws and regulations. Such obligations and responsibilities should also be disclosed to the general public and related costs should be covered in a transparent manner.

While the principles underlying some of the above interventions are already reflected in the existing guidelines for managing PSUs in India, there is an urgent need for implementing them in a time bound manner so that Indian PSUs can be key beneficiaries from emerging economic opportunities both in India and globally.

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