

Management of Agency Problem through Performance Contracts – Case of Public Sector Enterprises

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1. Introduction

The inevitable role of incentives offered to a manager or an employee in the success of the management of an organization was never underestimated in the discipline of organizational studies. Incentivizing a manager to contribute his best to the performance of the organization is central to the agency theory perspective which views organization as a nexus of principal-agent contracts. The current endeavor attempts to understand how the management of public enterprises as units of interest could be incentivized to work by putting their maximum effort in the direction of the objectives set forth by the government as the owner. By bringing principal-agent theory in context, we see how performance contracts in the form of MoU contracts between PSEs and administrative ministries operates to incentivize the agents (management of PSEs) to work in line with the objectives of the principal(Government). Given this brief introduction of the theme, let us bring clarity on the broad agenda of this exercise which is to study the following:-

1. How to ensure alignment of goals of the agent through performance contract?
2. How incentive based performance contracts could be improved through operations and design?

1. Public Sector Enterprises - Organizations and their Environment

What we are interested is in the agency relationship between the Government as the owner (the principal) and the management (the agent) of a Public Sector Enterprise(PSE). This relationship is central to the issue of governance and management of such enterprises as this may be based upon exercise of authority or use of incentives or mix of both. We are in a lookout for mechanisms which improves the dynamics in which the principal (the Government) as owner incentivizes the management of PSEs as their agents to work towards achieving the economic and social objectives envisaged by the principal. Given this agenda, it would be conducive at the outset to explain the rationale of choosing to study PSEs as the units of observation. Here we would be looking into the characteristics of these organizations which make them interesting organizational units to study.

¹ Authors register their gratitude towards Dr. Sharat Kumar, the Economic Adviser at Department of Public Enterprises(DoPE) of Government of India for his valuable inputs to the paper and to and Ms. Rachna Chopra, the Joint Adviser at DoPE for the help extended.

Public Sector Enterprises attract the attention of an Organizational Studies expert as hybrid organizations whose understanding requires a multidisciplinary perspective. As an "enterprise" it sells its output, is subject to market pressures and hence performs functions that concerns management specialists and economists. As a "public" organization, it is owned and/or controlled by the government or its agent and is subject to direct and indirect pressures from bureaucrats, politicians, and the public, hence concern of public policy (Jones, 1982). As hybrids, PSEs share characteristics of traditional government units and private business enterprises. Public enterprises differ from traditional government units in being subject to the pressures of the markets in which they buy and sell, but they also differ from large private organizations in being subject to *direct*, or internal, government control. Governments, of course, can influence private managers *indirectly*, or externally, by passing laws, imposing taxes, and jawboning, but this is quite different from public enterprises where government has the power to hire and fire the manager, although this process is cumbersome. For a private manager, on the other hand, the discipline imposed by the capital market is typically the major determinant of his tenure. The conflict between public and private goals and procedures is thus central in a public enterprise but tangential in private enterprises (Jones, 1982).

Given this understanding of hybrid nature of these organizations of interest, a quick exposure of political economy of PSEs would give us a better idea of the structural contingencies or more so of the changing external environment within which these organizations operate. The State in the planned economy enjoyed the commanding heights of the economy and owned the lion's share of business enterprises. The state in its role of the owner of these enterprises or what we may call as 'the State in Business' dominated most of the segments of economy. This phase continued till the reforms when State started distancing itself from the role of the owner and identified itself with the role of regulator and later facilitator. In the current era, the State tries to achieve the desired macro-economic and sector wise objectives by indirectly controlling the activities of the enterprises through its legal regulations and stipulations and through taxes and subsidies as against the direct control which earlier exercised by operating nationalized industries in the planned economy context (Williamson 2003). But in spite of this withdrawal of State from the domain of businesses, interest in managing Public Sector Enterprises continue being vital to the Indian Economy and they remain inevitable forces not to be ignored. They share a significant part of the national output, are big players in the markets and offer employment to large sections of the populations. But the new external environment is different. Today we find that PSEs are facing new circumstances in terms of a competitive business environment and a different policy environment. Many PSEs are today players in certain markets with strong competition from private players and hence face questions of

sustainable growth and survival while others which are monopolies faces inefficiencies, economic non-viable circumstances and strong competition from substitutes.

2. Changing Environment - Organizational Adaptations and Policy Reforms

Thus today the State had transformed from being a Provider to a Regulator and from being a Controller of the Private Sector to being a Facilitator of the Private Sector. In their respective markets, PSEs are no longer the “blue-eyed boys” of the State as monopolies or dominant players or government backed player in the markets in the era of “commanding heights, but just yet another player in competitive market segments (always facing the threat of new entrants) or monopolies of markets with strong threat of substitutes even leading to unviable performance indices. Hence PSEs as organizations faces strong threat in the new business environment which makes case for changes within and in the policy concerning these entities. Thus when the public policy shows more interest in the survival and growth of these organizations and start viewing it role as their owner more sincerely and seriously, we make here a case for a renewed interest in PSEs. Hence we find that these organizations and its governing authorities are responding to the new contingencies by adopting organizational adaptations and policy reforms. It did not take long for the Government to make appropriate policy responses identifying the need of adjusting itself as the owner and the PSEs as the enterprises facing different realities.

Such reforms in the Public Policy with respect to Public Sector Enterprises Marriage believed in a more sustainable marriage between exercise of both incentives and authority. The government thought about use of the carrot and stick and well beyond it. Firstly it was the empowerment of these PSEs through offer of Ratna Status and consequent devolution of autonomy to exercise discretion in making strategic decisions related to mergers and acquisitions, international expansion, capital investments, etc. Then we found bringing these PSEs to the coverage of the corporate governance guidelines which made them closer to their private counterparts. More importantly, the implementation of a performance contract called Memorandum of Understanding (MoU) system was crucial policy reform which tried putting in place “the right incentives” for the PSE management to perform better and envisaged a symbiosis of the owner and manager based on offer of autonomy in return of accountability. Our paper looks at the latter policy reform more closely. The setting up of institutions and organizational set ups like Bureau of Public Enterprises(BPE) and Public Sector Enterprises Selection Board(PESB) and enabling the functioning of an umbrella group in the form of Standing Conference of Public Enterprises(SCOPE) was a step forward. Identifying the vital role formation of Board of Directors for PSEs as a step towards efficient monitoring mechanisms to tackle agency problems and making them functionally competent was another step. To add to this, interest in

policy reforms with respect to PSEs be could understood from the various recent policy decisions like,

1. Cabinet Committee on Economic Affairs recently devolving more autonomy and powers to blue-chip PSUs for taking the final call on M&As and also empowering them to decide on investment limits up to Rs 300 crore
2. Government planning to set up a Board for Reconstruction of PSEs broadly mandated to devise ways and means to strengthen the public sector and
3. Government stressing on giving a 'big push' to the corporate governance of the public sector.

3. Aspects of Organizational Behaviour- Dual Identities of PSEs

Having spoken about the external environment of these organizations, let us dwell more upon their internal environment. To start with, the defining characteristic of a PSE is its dual identity. It is at the same time a corporate entity and a public entity. PSEs seem to have two faces, one being of a public entity as implied within the definition of state and the other being of a corporate entity. As companies, CPSEs publish their annual accounts as per the Companies Act (1956) and as corporate entities, they have to comply with all legal and regulatory processes as any private corporate entity. The additional issues of oversight arise because of their being public entities. CPSEs are considered an instrumentality or an agency of the State under Article 12 of the constitution. They are accountable to Parliament, Parliament Committees, constitutional authorities, Line Ministries, CVC, CAG, Ministry of Finance, and Ministry of Corporate Affairs etc. As PSEs has to managing both these identities, we need a different perspective on management and governance when it comes to the case of PSEs. (KPMG 2011, Jones 1982).

Emanating from its dual identity existence, the following organizational characteristics of the PSEs emerge, namely,

1. goal conflicts between owners and managers (and between managers at different levels and between those of different units);
2. complex, hierarchical bureaucratic decision structures;
3. information impactedness;
4. difficulty of measuring and rewarding individual performances in joint-product endeavors

All these organizational characteristics leave significant implications on the governance of PSEs. Consequent of these dual entity status and mainly public entity, we find that PSEs reeling under agency issues, problem of multiple principals, principal without agent, perverse incentive system,

poor monitoring, etc. The many-principal situation leads to a situation of over- governance which makes day to day management cumbersome for PSEs. The Roongta Expert Panel on PSEs has cited ‘over governance’ as one of the major issues affecting the performance of Public Sector and thereby its competitiveness. The problem of over governance arises because of ambiguities in the roles of various stakeholders. Compliance to summons from various quarters comes at a heavy cost of time and money. Over governance, in turn, promotes conservative, cautious and risk averse organizational culture, with procedures being paramount and outcomes becoming secondary. The issue of ‘over governance’, therefore, needs to be tackled within the performance related accountability so that CPSEs become more proactive and result oriented. Or in contrary, we can find that too many principals leading to a situation of under-governance, as too many cooks can spoil the broth even by passing on the responsibilities to each other and never owning up for the affairs of the entity under their supervision.

4. Agency Problems in Managing Public Enterprises

The aforesaid problems related to governance of PSEs could be brought to context if one could analyze this problem through a simple analytical lens offered by principal agent theory. Let us see the relationship of the government-owner and management of the PSE under this light. Whenever a party whom we call as principal wants another party (agent) to do a task of the former’s interest in lieu of a payment, we find a context to understand principal-agent interactions. Often it is difficult to align the interests of the agent in line with objectives of the principal. The principal expects only certain optimal output levels and hence certain levels of effort from the agent and the agent expects, at a bare minimum, certain threshold utility so as to take up the task. Thus there is a need of such a payment incentive mechanism which creates incentives for the agent to put in the required levels of effort in the work so as to produce the optimal levels of output which the principal desires. Contracts are hence designed to create incentives and payment mechanisms subject to these incentive compatibility and participation constraints so to induce the agent to put in the expected levels of effort. Principal –Agent problem within the context of the management and governance of Public Sector Enterprises could be articulated in the following fashion:

For this, we assume a model involving a single principal and an agent(PSE). Principal wants the agent to do certain work. The agent puts in an effort ‘x’ and such an effort ‘x’ brings out an output ‘y’ such that $y = f(x)$. The agent has to bear the cost $c(x)$ commensurate with the ‘x’ effort he has expended (Varian 2001).

Now the principal is ready to pay a payment $S(y)$ according to the output 'y' he gets from the work done by the agent. Now we need to identify the objective functions of both the parties. The principal wishes to maximize his profit function Π and the agent his utility 'U', where,

$$\Pi = p \cdot y - s(y) = p \cdot f(x) - s(f(x))$$

For sake of simplicity, let us assume price of the output to be 1. So profit function becomes

$$\Pi = y - s(y) = f(x) - s(f(x))$$

Now consider the utility function U of the Agent which he wishes to maximize.

$$U = S(y) - c(x) = S(f(x)) - c(x)$$

Firstly, we need to consider the conditions under which agent would be interested to take part in the activity. The agent would have derived some minimal utility ' \bar{U} ' by doing some other activity or even remaining idle. That minimal utility ' \bar{U} ' would decide the decision of agent to participate or rather in our case, work for the principal.

So the participation constraint stipulates that the agent should be able to derive utility at least as much as \bar{U}

$$\text{Or } U = s(f(x)) - c(x) > \bar{U}$$

But the objective function we wish to maximize would be the profit function of the principal which would entail an optimization problem as

$$\text{Maximize (in } x) \Pi = f(x) - s(f(x))$$

, subject to

$$U = s(f(x)) - c(x) > \bar{U} \text{ (Participation Constraint from above)}$$

The practice of such a participation constraint would be tantamount to the specification of to

a minimum level of salary assured for a bureaucrat, Thus the principal can prescribe a minimum output for the salary to the agent and this would be in line with the HR practices and compensation mechanisms in the public sector and the fashion in which bureaucracy works.

Now we can proceed to derive an unconstrained maximization problem by bringing the constraint within the objective function such that, our objective function becomes

$$\text{Maximize } \Pi' = f(x) - s(f(x)) - (s(f(x)) - c(x) -$$

$$\bar{U}) \text{ Or Maximize } \Pi' = f(x) - c(x) + \bar{U}$$

This optimization problem would arrive at some effort level x^* such that

$$\text{MP}(x^*) = \text{MC}(x^*)$$

So all the effort levels x^* at which the marginal product of the effort $\text{MP} = \partial f(x) / \partial x$ would be equal to marginal cost of the effort $\text{MC} = \partial c(x) / \partial x$ would qualify for the optimal effort levels expected from agent. Thus the principal expects from the agent an effort of x^* in an optimization problem which took into account of latter's participation constraint. From this, we can articulate that constraint which will speak about the payment mechanism which will incentivize the agent

to work for the principal and bring out x^* effort. This could be found by bringing in the optimal effort level x^* into the participation constraint.

Thus the incentive compatibility constraint is

$$s(f(x^*)) - c(x^*) > s(f(x)) - c(x) \quad \text{for all } x$$

which simply says that the utility to the worker from choosing x^* must be greater than utility of any other choice of effort . So any incentive scheme in a principal agent situation should be able to give a total utility to the agent which is more than \bar{U} and it must make the marginal product of effort equal to the marginal cost of effort.

1. The principal (Government) has certain objectives to be achieved. And this needs to be neatly and clearly articulated (and communicated to other) as they would decide the levels of effort expected from the agent (PSE management).
2. The level of effort x^* which could be in any parameter, call it financial, static or dynamic has to be arrived at either through the above optimization or a bargaining process between the principal and agent.
3. These bargaining or mutual negotiations would bring out a participation condition from the agent (PSE management). PSE management would not be ready to work for the Government or, in other words, ready for negotiations unless and until a minimal utility (which could be a minimum compensation or payment) is assured to them through the process. So the payment (or the Performance Related Pay) should assure a participation constraint.
4. More importantly, the payment incentive scheme should be so designed such that the utilities of the agents from the payments made for achieving the target levels of effort (expected under various heads of financial and non-financial parameters as per the negotiations) are better than utilities received from other levels of effort. That is, the managers of PSE should find it in their own interest to work for achieving the targeted levels than any other level of effort and prefer to work for achieving these levels than for any other sub-optimal levels.

Till now, we had seen the issue based on the consensus that the government is the principal and the management of PSE is the agent. That is, we were making an implicit assumption that this is a situation where a single principal interacts with a single agent. But as we saw already, one could find that this is a too simplifying assumption for understanding the reality of PSEs which operates in a complex environment with too many stakeholders and interests.

The dominant school which tries to explain the problem of over governance associated with PSEs is that there are too many principals. And in certain cases, this many-principal phenomena and same set of reasons could be put forth to explain the under-governance of PSEs. This is realistic as we find the PSEs being answerable to too many organizations within government and presence of too many political interests in the governance of them which strictly constrains the space of strategy formation and decision making of PSEs. It is in this context that, as per the

OECD guidelines for SOEs, we see the demand for a single coordinating body. In our case, we see that we simply try to handle this many-principal problem in Indian context by entrusting the administrative department / machinery as the single reporting authority authorized to engage in the MoU deliberations with the PSE. Thus PSE ,as an agent, interacts only with that ministry/ department as the single principal during MoU formation. After the formation of draft MoU, for a period of one year, none of these principals including this ministry/department are expected to interfere in the activities of the management of PSEs(Aharoni,1982).

Another major school of thought is that the principal is not identifiable. This would lead to a problem of not being able to identify the agent costs clearly. Then all types of agency costs - distinct managers' interests, monitoring and detection costs, replacement costs - as well as such environmental variables as uncertainty about strategy are likely to apply to SOEs. Another view is that the notion that the government or the minister is the principal and that the enterprise is the agent is in fact misleading. Rather, the populace as a whole is the principal, with a variety of agents acting on its behalf. These agents include various government ministers, members of parliament, managers of firms, and so on. All these agents are in fact a coalition - a group working together who share *some*, but not all, goals. PSE shares are not traded in the market, and the populace does not have an effective voice in their direction and control. As state ownership does not necessarily imply social ownership, the mechanism of goal formulation is an important one. To add to this discussion, there is a view that places the management of PSE in a higher pedestal compared to that of private sector and empowers it to higher powers and responsibilities. Here we are speaking about the management of PSE gaining characteristics of a principal. Thus the PSE management has as legitimate a claim to the participation in the goal formulation on behalf of the principal as do the other agents. The multiple and often ill-defined objectives make performance measurement almost impossible. As a result, the market may police PSE managers much less than in the case of private enterprise (Aharoni,1982).

5. Managing Agency Problems through Contractual Solutions

A digression about the many principal and other scenarios in PSE Management could be validated as this would elucidate on how complicated the reality is. But as our interest is in looking at improvising incentive based contractual solutions for better governance of PSEs, we

would return to understand such contracts. To start with, Memorandum of Understanding (MoU) as applicable to public sector enterprises is a negotiated document between the government and the management of the enterprise specifying clearly the objectives of the agreement and the obligations of both the parties. Operationally, such an 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. This setup ensures monitoring of overall performance of the CPSE. The targets are set out in conformity with the long term mission and vision of the enterprise. At the end of the financial year the achievements against targets are examined and the respective CPSEs rated. Also these ratings also determine the categorization of the enterprises and consequently their level of empowerment. Thus this MoU system is based on the twin objectives of 'autonomy' and 'accountability'. While 'autonomy' is necessary for good performance, the 'accountability' of managements is measured through performance evaluation. (Sharatkumar 2008)

Thus MoU aims at providing greater autonomy to the PSEs vis-à-vis the control of government. And the 'Management' of the enterprise is made accountable to the government through the promise of a 'performance contract'. Nevertheless, the government continues to exercise control as the principal shareholder over these PSEs through a priori supervision, i.e., in setting MoU targets, and through a posteriori 'performance evaluation' during and at the end of the year. The performance evaluation at the end of the year indicated the extent to which the mutually agreed targets and objectives are achieved. To conduct the negotiations associated with administering the performance contract between the agent (the PSE management) and the principal (owner ministry), to arrive at the targets, to see to it that these targets are meaningful, to evaluate the performance of the contract signing PSEs and to finally arrive at final composite score and rating for CPSEs, there should be a central coordinating entity. The Department of Public Enterprises (DoPE) serves this purpose. DoPE solves the problem of translating the assumption of single principal to reality by making the administrative ministry do that role and keep other interferences at bay. The operation of MoU system is summarized in the Fig 1.

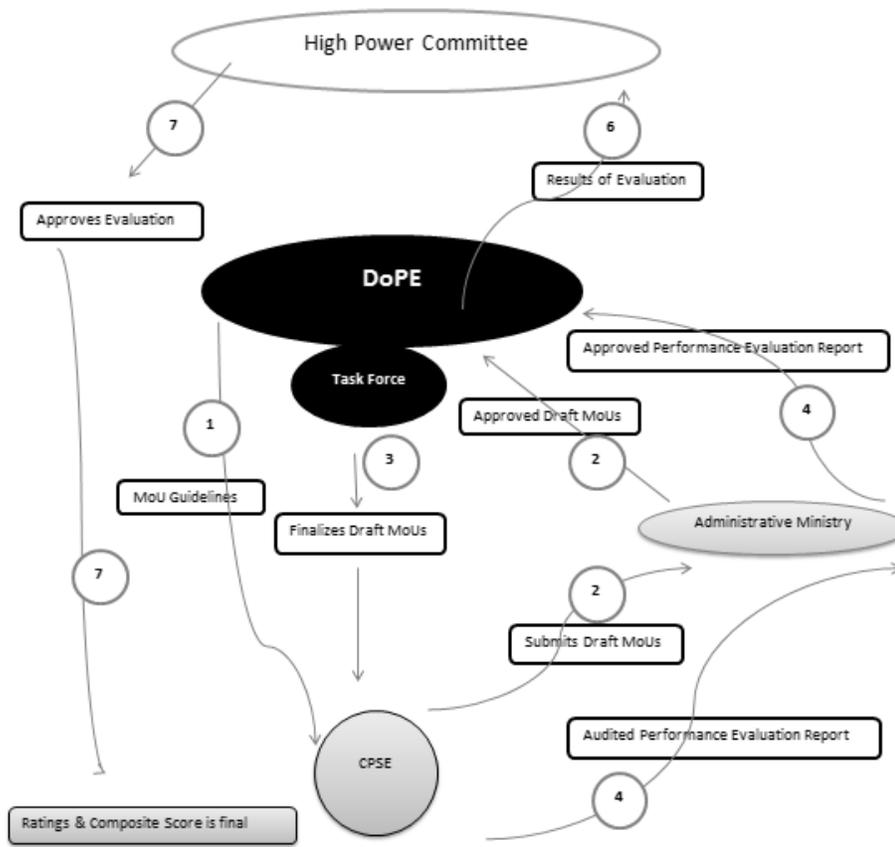


Figure 1

An MoU system is not a perfect or fool-proof system. It has its own pros and cons. The contract approach is potentially an important mechanism by which Governments can exercise control in a functional way. The possible advantages of a contract system are as follows;

- (1) When the contract is truly debated and agreed upon by managers and bureaucrats it becomes reverent and therefore important on that score
- (2) The agreed upon targets can be made difficult enough to realize significant gains in performance, and yet not too difficult to be de-motivating. Indeed the clarity can contribute to motivation independently of the (known) rewards and punishments which quite obviously prod the top management towards task orientation. Feedback is well recognized as a vital element in motivation by organization theorists

(3) Management of change across large organizations becomes possible in the flexibility of a periodically negotiated contract: During the tenure of the contract it shields the organization from the buffeting of the environment, yet the signals from the environment can also be incorporated as the content of the contract changes periodically. In other words a well institutionalized process of contracting by goal oriented governments, with their PSEs, has the potential to translate and carry its goals (which may have been derived from a Plan or a certain ideology) effectively down to the productive units. And in bringing about this purposiveness can greatly enhance the performance of the system as a whole (Morris, 2005).

On the other hand, there could be problems with the contract approach. Such an approach presumes that there are adequate skills, knowledge and information available with both parties, so that one cannot confuse the other; and the costs of ensuring this can be quite large. Moving on, the more important problem with contract approach emerges from the very nature of government in most societies. There is rarely the extreme consensus to agree upon a distinct role for public enterprise, or to interpret and accept the signals from a changing environment in a particular way. These are necessary for a truly dynamically functional contract. Government can differ within itself or may choose to avoid clarifying statements, thereby diluting its commitment to the contract. Operationally there have been complaints of arbitrariness in fixing targets. The PSEs and their umbrella organization SCOPE complains of unrealistically high targets while there is a strong speculation that the MoU Task forces (the third part supervising the formation and practice of MoUs) or DoPE and the PSEs could collude and set too low targets easy to achieve.

Nevertheless, MoU system as of now serves as the best available option for us in the domain. An exploration of various possibilities of improving the system and to see what would work better could be always a great a good domain of enquiry. Streamlining the operational dynamics of the system by rationalizing the processes, ensuring the independence and autonomy of DoPE task force and high power committee as third parties in the operation and bringing more transparency by making MoUs public are on agenda of such a move.

If one attempts to answer few of the above questions, the solutions suggested could be

1. Tightening the target, so that problem of self-defeating wide margins is ruled out.

2. Fine-tuning the matrices of the MoU contracts
3. Increased weightage on aspects like innovation
4. Keeping tab on the tradeoff between accountability and performance in terms of not allowing the reins of accountability constrain the PSE from achieving higher levels of outcome/outcomes or pooling in higher amounts of inputs.
5. Completing the loop by assuring the earnest participation of every stakeholder involved. This would involve that committee involved makes unbiased coordination and is professional in its exercise, the evaluating framework is fool proof, the evaluation is made with respect to actual case and the consequences are effective and binding upon the agent.

But the questions of who will *guard the guardians* thus remain incompletely explored. Would the coordinating entity see to it that these MoU contracts are effective and aid in augmenting the performance of PSEs remains within the efficacy at which they carry out this mandate. Today we have Results Framework Documents which are applicable to every ministry of Government of India. which includes Department of Public Enterprises. Such performance scoring systems would be an attempt to keep these *guardians* in watch and prevent such monitoring mechanisms from becoming ineffective.

6. Measuring Effectiveness of Contractual Solutions- An Exploration

One explores the effectiveness of a performance contract like MoU by evaluating how much it has achieved in terms of achieving the objectives set in the contract. Every incentive contract in a principal-agent relationship is a case of constrained maximization of the objective of the principal. This in our case is the objective of the Government which could be parameters like profits and turnover or even social objectives. So an MoU could be evaluated based on how much the PSE achieve in terms of the objective dictated to it by the Government. The fact is that multitude of PSEs try to further many economic and social objectives. But for the argument sake, let us assume that profit is the universally accepted objective of interest for the Central PSEs. Then one can embark on an exploratory analysis based on this assumption.

The MOU system was introduced on an experimental basis in 1986 on the basis of the report and

was medium term based. But from 1989-90 it became based on annual targets agreed upon between the government and the CPSEs. One could treat 1990 as the starting days of its operation, but the practice of the system in its full-fledged manner took off in 2000s as the design and operations of the system got revamped after the NCAER study. It is in this period that MoU was started to be observed seriously and compliance to targets agreed upon made a necessary condition for PSEs to stay within the fold. Thus when one looks out for broad indices to gauge the effectiveness of MoU contracts, exploring key parameters during the period of 2003-04 to 2011-12 helps to understand whether there was a correlation if not causation between the tightening of MoU System and performance of PSEs. We do understand the fact that there were other explanatory factors especially the ones related to general performance of the Indian economy as a whole. But an indication of coincidence between well performing PSEs and increased compliance to MoU targets during this period would be a good starting point for measuring their effectiveness.

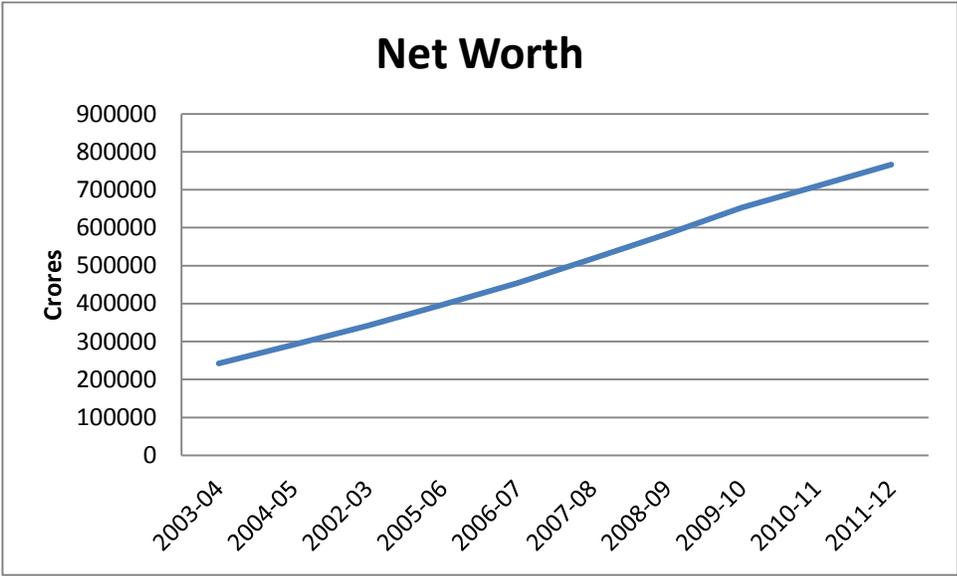


Figure 2 Net Worth of PSEs (2003-04-2011-12) (Source : PSE Survey 2011-12)

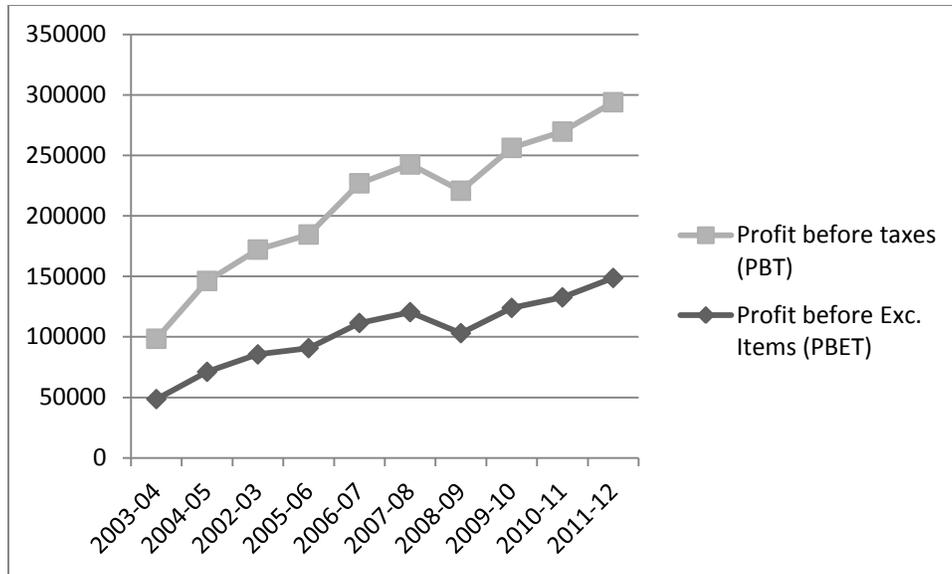


Figure 3 PBT and PBET of PSES during 2003-04-2011-12(Source : PSE Survey 2011-12)

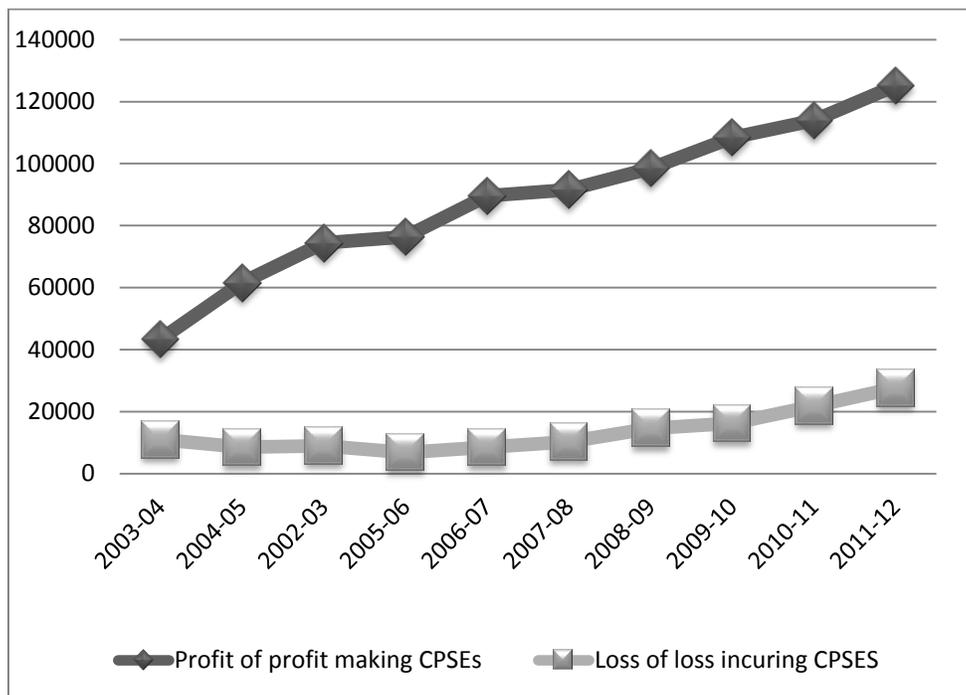


Figure 4 Profit/ Loss of Profit making/ Loss incurring PSEs during 2003-04-2011-12(Source : PSE Survey 2011-12)

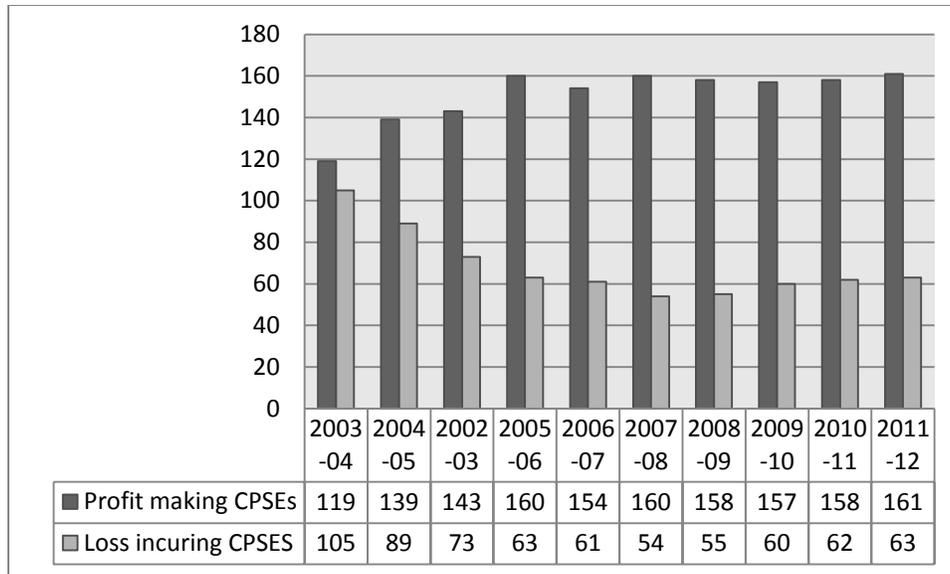


Figure 5 Number of Profit making and Loss incurring PSEs during 2003-04-2011-12(Source : PSE Survey 2011-12)

Looking at the Figures 1-4, one could make few claims about the effectiveness of MoU contracts albeit unsubstantiated and supported by weak assumptions. There is a strong upward trend in total net worth of all PSEs as shown by Fig.1 and same is the case with total PBT and PEET as indicated by Fig.2. A more interesting pattern unveils when one divides the population into profit making and loss incurring PSEs. Fig.4. shows that there has been a steady increase in the number of profit making CPSEs from 119 in 2003-04 to 161 in 2011-12 (out of a total 225 operating PSEs) , while there is a steady fall in the number of loss making PSEs from 105 to 63. Fig.3. shows another interesting pattern within these two categories of PSEs. Here there is a significant and steady increase in profits of the ones which make profits , but there is almost a stagnation in the loss of the PSEs incurring loss. Let us reiterate the fact that one can only assume that this improved performance of PSEs in terms of Net Worth, PBT and PEET, fall in the number of loss incurring PSEs , increase in the number of profit making PSEs, etc. could only at best be treated as an indication towards a possible causation between operation of an effective performance contract system and performance. One could only bring out explicitly a causal link between an effective contractual solution to managing agency problems in PSEs and their performance only if we examine and take into account other changes in internal and external environments of these organizations and the validity and compliance of PSEs to the MoUs they sign.

7. Conclusion

The agenda of the paper is clear in its ambition to invite a renewed academic interest in public enterprises management in India and emphasizes on the need to cater to the special needs of PSEs. On a deeper note, it tries to elucidate on the role of incentives in public enterprises. These hybrid organizations are at the interface of markets and bureaucracy and needs a different treatment when it comes to the issue of governance. Historically, there has been a dominance of the exercise of authority over use of incentives in these organizations and hence need has arisen to change the skewed mix of authority and incentives in managing such organizations. By a quick case study of performance contracts called as MoUs, we try to see how contractual solutions could be found for principal agent problems in the PSEs. So a deeper understanding of the existing performance system and recognition of the different set of constraints and incentives which a public manager faces would help us to look for better mechanisms which incentivize the managers of such hybrid organizations at the interface of market and bureaucracy to perform better

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