Chapter-3

PROCEDURE FOLLOWED

IN PREPARATION OF

THE REPORT

&

STUDIES UNDERTAKEN

3.1. PROCEDURE FOLLOWED

3.1.1 The PRC held Thirty Nine sittings **(Annex - 3.1).** The first meeting of the PRC was held on 13th December, 2006 at New Delhi where, among other deliberations, the strategy to be adopted for studying the existing market scenario and issues related to compensation packages for the PSEs executives, were discussed.

3.1.2 The approach adopted included analysis of the existing compensation packages in the CPSEs/Relevant Private Sector Companies etc by obtaining feedback in a structured manner through a questionnaire **(Annex - 3.2)** from Management as well as Officers' Associations of CPSEs, administrative Ministries/Departments, eminent individuals/consultants Association with CPSEs, special organizations like BIFR, PESB, 6th Central Pay Commission, Employers' organizations and Professional Bodies such as SCOPE etc. Key issues covered in the Questionnaire are; Role of the Government, Scales of Pay & Uniformity in pay packages, Recruitment, Promotion, Flight of Talent, Composition of the package, Performance Related Payments, Increments, Issues of relativity and comparison with Government/Private sector/International – criteria for determination of emoluments/compensation packages, Issue of resources, Central Dearness Allowance (CDA)/IDA related issues, Pay revision in Sick/BIFR referred CPSEs, number of Holidays, Voluntary Retirement Scheme, City Compensatory Allowance, Performance Appraisal etc.

3.1.3 The Committee also decided to take the opportunity of meeting the management of CPSEs belonging to different sectors and their Officers' Associations to gather their views on the compensation related issues. In the process, 30 CPSEs, 38 Officers' Associations and 20 other Agencies/Department have made presentations before the PRC **(Annex - 3.3).**

3.1.4 The Committee also had a meeting with the Sixth Central Pay Commission, wherein issues of common interest were discussed.

3.1.5 In addition, Institute of Public Enterprises, Hyderabad has also been engaged to conduct a study of current market trends in the Private sector as well as CPSEs of few leading countries, where CPSEs exist along with thriving Private sector companies.

3.1.6 The Committee also identified few compensation related issues and desired that thematic studies on these issues need to be carried out. Thereafter, approach papers can be presented with a futuristic view. The issues identified were:

- **(i)** IDA/CDA Pattern
- **(ii)** Entry Level Compensation
- **(iii)** Performance Related Payments
- **(iv)** Employee Stock Option Plans [ESOP]
- **(v)** Voluntary Retirement Scheme
- **(vi)** Retirement Benefits

3.1.7 The Committee also took note of the studies conducted by SCOPE through M/s Mercer Consultants and the one commissioned by oil companies through M/s Hewitt Associates.

3.1.8 The Committee was also assisted by number of Executives from various CPSEs. The detailed list is at **Annexe- 3.4.**

3.2. RESPONSES TO QUESTIONNAIRE

3.2.1 The PRC undertook the exercise of collecting and assimilating the primary source of information pertaining to existing compensation and benefits from various agencies so that the views of the stakeholders, who are likely to be affected by the decisions taken by the PRC are made available. Based on the replies received from 184 different agencies (**Annex.-3.5)** including 111 CPSEs and their subsidiaries, 44 Officers' Associations; 19 Ministries/Departments and 10 Consultants/Task Force members, a detailed analysis has been done on each of the question and is given at **Annex.- 3.6**. However, a brief summary of the replies has been prepared and is as under:

a. On the role of the Government as owner in the current context, 44% CPSEs have favoured for complete autonomy in the pay structure, while nearly 66% of the CPSEs felt that there should be broad guidelines for pay structure but the issue of finalization of perquisites may be left to the individual organization.

b. Regarding the Scales of Pay & uniformity in pay packages, majority i.e. 82% of the CPSEs, are against the uniformity of the pay scales in all CPSEs though uniformity within one schedule is welcomed.

c. On composition of the compensation package, it should be structured in such a manner so that the tax liability on the part of employee is reduced. 55% organizations are of the view that present system of Fixed Pay + Perks may continue. Further, another 65 % have advocated for the fixed and variable components of Salary.

d. Regarding incentive to the Members of the Board of Directors, 88 % advocated for payment of incentive (Profit sharing). Overall, 40% wanted that the incentive to Members of the Board to be decided by the concerned CPSE.

e. Most CPSEs are inclined towards open-ended scales, whereas others have suggested the ratio ranging from 1:15 to 1:20.

f. Most of the respondents have asked for parity with the private sector / market or freedom for CPSEs to structure their compensation packages with only broad guidelines being issued by the Government. Majority of Officers' Associations have also sought parity in compensation with the private sector / market

g. 75 % of the organisations were in favour of Performance Related Payments and have set the Organisations Performance, Groups Performance (Performance of Business Unit), Productivity and Profit as the Criteria for such payments.

h. The relativity in remuneration between the top management & workmen, as recommended by CPSEs, is maximum at 35:1. So far as Officers' Associations are concerned, they recommended a maximum of 25:1.

i. Regarding fair comparison between the salaries available in the public sector vis-à-vis the private sector taking into account benefits like security of tenure, promotional avenues, retirement packages, housing etc., 30 % of CPSEs are of the opinion that the afore-mentioned benefits are available in the private sector also. 24% felt that Cost to Company (CTC) concept should be adopted to compare compensation in the public sector with the private sector. Most felt that focus has shifted from employment to employability. Officers' Associations are of the view that comparison of emoluments in the public sector with that existing in comparable private sector companies is fair as benefits like security of tenure, promotional avenues, retirement packages, housing etc are available in comparable private sector companies also and CTC in competing private companies is in fact higher.

3.2.2 Thus, it can be seen that CPSEs, particularly profit-making ones, are seeking closer relationship with the private sector for compensation issues. Another notable feature is the acceptance of increased role of Performance related payments and more thrust on variable pay as compared to fixed pay. The competitive spirit of CPSEs is also visible for attraction and retention of talent in the open market scenario through innovative use of pay, benefits, growth & development opportunities etc.

3.3. INTERACTIONS HELD

The Committee, held meetings with around 30 CPSEs, 38 Officers' Associations and 19 other bodies. The committee also met the Public Enterprises Selection Board [PESB]. The Sixth Central Pay Commission constituted for pay revision of central government employees, Board of Industrial & Financial Restructuring (BIFR) etc. Managements of CPSEs, which included Navaratna, Miniratna, Profit-making, loss-making as well as Sick units, their Officers` Associations, Federations were also given opportunity to express their views and related concerns before the Pay Committee.

During the process, elaborate presentations were made by the CPSEs/Associations and deliberations on significant factors for designing an appropriate compensation packages matching industry specific requirements were held. Interactions with the Sixth Central Pay Commission and PESB also gave an enlightened insight to some of the key issues that need to be addressed and incorporated in the compensation strategy for CPSEs. A broad spectrum of issues which came up during such deliberations as well as during discussions with a select population of CPSEs executives and need to be considered are being summarized below.

3.3.1 Certain Views Considered

During the deliberations of the Committee, different views were expressed in regard to the proposed classifications, in regard to parity with Salaries in Government and also as regards the proposal of different remunerations to different categories. The Committee considered all these views while making its recommendations, in the long term interest of CPSEs, keeping in view the specific mandate in the terms of reference of the Committee.

3.3.2 Meetings/Discussions with Management of CPSEs : The broad suggestions came out of these meetings are:

(i) Capacity to pay should be the principle with full autonomy to Board of Directors for taking need based decisions.

(ii) 50% IDA should be merged with Basic Pay w.e.f 1.1.05, the date on which IDA crossed 50%.

(iii) Open ended pay scales in order to avoid stagnation.

(iv) Rate of increment should be on percentage of Basic Pay and Promotional Benefit at the rate of double the proposed Rate of Increment.

(v) Government should provide broad guidelines for Salary Revision.

(vi) Introduction of Contributory Pension Scheme, Comprehensive Medical Coverage to employee and Spouse.

(vii) Uniformity of retirement age across all CPSEs, Enhancement of retirement age may be considered up to 62 years.

(viii) Periodicity of Pay revision to be in the range of 3-5 years.

(ix) Autonomy to be given to CPSEs to design their own VR schemes as per their requirements.

(x) Existing ESOPs guidelines issued by the DPE need to be modified to make it attractive and popular.

(xi) Boards should be allowed to function as per the provisions of Companies Act, 1956 and be empowered to decide as per prevailing circumstances exclusive to respective CPSEs.

3.3.3 Some CPSEs undertook separate studies through independent consultants on their own initiative. SCOPE undertook a study through **M/s Mercer Human Resource Consultant** and presented the findings before the Committee. The study while elaborating in detail the current scenario in which CPSEs are being encouraged to look for business growth in global markets, seek opportunities for expansion through mergers and acquisitions, seek Finance from open markets to fund their business plans, all with little support from the Government, calls for a paradigm shift of the basis for determining salaries and benefits policies in CPSEs and emphasizes that the rationale or foundation that forms the basis for establishing pay practices in CPSEs requires a serious rethink.

(i) In an environment, where CPSEs are competing head to head for business and growth opportunities in the open market with other employers, where the public sector is seeking to attract and retain employees that form a part of the same talent pool, determining the basis for pay should be based on an appropriate mix of the following factors such as Affordability or Capacity to pay; Job content; Cost of living; Market benchmarks for Pay and Benefits in comparable companies; Individual performance; Qualifications and Competencies. Need to set wages, organization wise, treating each CPSE as an individual entity with due regard to productivity has emerged as an important outcome of this study.

(ii) Other interesting outcome of the study is that Government should only articulate the ground rules or guidelines for companies to manage their own employee costs, concept of Remuneration Committee, Total Reward Strategy or Cost To Company

(CTC) Concept, Performance based compensation, periodicity of salary reviews, Provision of Retirement Benefits. Details of the studies are placed at **Annex.-3.7.**

3.3.4 Similarly, the Oil Sector CPSEs undertook study through **M/s Hewitt Associates** as 'Compensation and Benefits Benchmarking'. The study points out the need to adopt such remuneration strategies, which shall facilitate in enabling the CPSEs to compete with the global competitors attract and retain talents from among the common pool available and linkages with market salaries etc. Total Guaranteed Cash Compensation; autonomy in managing perks & allowances; sharing of profits; aggressive pay for performance even where profits are inadequate; a higher percentage of basic pay as performance based pay; introduction of an Employee Stock Option Plan (ESOP); Benchmarking Compensation once in at least 2 years; and differential increments based on performance in percentage terms are some of the key factors, which this study intends to take into consideration, while designing the overall pay package in CPSEs. Details of the studies are placed at **Annex.- 3.8.**

3.3.5 Meetings/Discussions with Officers' Associations of CPSEs : Major issues that were highlighted during these discussions were:

(i) Merger of 50% IDA with Basic Pay.

(ii) Interim Relief of minimum 15% of Basic Pay plus DA w.e.f. 1.1.2007 till finalization of salary revision.

(iii) CPSE employees to be treated at par with Central Government employees for housing perquisites.

(iv) Revised scales should take into account the increase effected in the last salary revision and incremental growth over the years.

(v) Rate of increment demanded ranges from 3% to 10% of Basic Pay and Promotional Benefit at double the proposed rate of increment.

(vi) Substantial increase in all perks and benefits applicable to executives.

(vii) Enhancement in the allowances linked to Basic Pay such as HRA/CCA/NPA etc.

(viii) Fitment in revised scales should be made on point to point basis for ensuring seniority.

(ix) Removal of 50% ceiling on perks and allowances.

(x) Enhancement in the existing limit of 5% of distributable profits to 10%.

(xi) Removal of existing limit of Rs 3.5 lakhs , Gratuity to be paid on actual basis.

(xii) Periodicity of Pay Revision to be 5 years as was the case before 1997 Pay Revision.

(xiii) Provisions should be made to extend more number of non-taxable perquisites and benefits to executives.

3.3.6 Public Enterprises Selection Board (PESB):

(i) PESB pointed out that the Terms of Reference of the PRC provides that the recommendations of the 6th Central Pay Commission has to be taken into account by the PRC. Therefore, it may not be possible, to de-link the pay scales of CPSEs from the Central Government pay structure. This also poses the question "how to attract and retain talent in CPSEs". There will be continuous need to interact with the Government and there can be no escape from being under its control and linkage with the Government pay scales. PRC may consider granting flexibility to the Board of CPSEs to be liberal in payment of performance related incentives, profit sharing benefit, Gratuity, Bonus, pension (as in the case of Coal Industry), Post Retirement medical benefits etc, while having pay structure more or less on line with the Central Government pay scales. Chairman, PESB also stated that despite all constraints, there are definite advantages like freedom of decision making, status etc. in CPSEs as compared to private sector.

(ii) PESB also reminded that so long as the concept of owner and management relationship is implied between the Government and CPSEs, it would be difficult to completely de-link the pay structure of CPSEs from the Government. The problem of attracting students from IITs, IIMs etc, at the entry level will continue to remain and solutions have to be found out by giving leverage to the CPSEs to decide the extent of performance related payments (PRP), profit sharing benefit, liberalized bonus, Gratuity etc, or finding out other avenues.

(iii) PESB impressed on the need to consider salary revision as also uniform age of retirement to the sick CPSEs as well, as much as such a step will motivate the executives to make all efforts to come out of the red.

3.3.7 Board for Industrial and Financial Restructuring (BIFR):

(i) During the interaction with members of BIFR, the concerns of BIFR referred companies especially for their revival were foremost. However, to retain and motivate employees, implementation of revised pay scales was also discussed with Government budgetary support.

(ii) The presence of a large number of sick companies and employees engaged in these companies make it imperative that their key concerns are taken into account in the recommendations of the PRC.

(iii) The thriving economy provides greater opportunities for these companies to make smart recovery and become profitable.

3.4. STUDIES ON COMPENSATION & BENEFITS

With the appointment of the Second Pay Revision Committee to review the salaries and benefits for supervisory and managerial executives of CPSEs, there is an opportunity to revisit the basis and principles used to establish the executive salary levels in CPSEs. In order to develop an overall understanding of current trends in compensation strategies as well as their widespread impact on the performance and growth of the individual organizations, need was felt to conduct studies on the subject. The objective was to study different components of pay package with special emphasis on fixed and variable proportions, performance related components, short as well as long term rewards, and their linkages with the performance at individual and organization level. Accordingly, different studies were conducted on the subject which deserve mention here. A study was conducted by Department of Public Enterprises through the Institute of Public Enterprises, Hyderabad (IPE). The task included studying the current compensation trends in the market and to suggest appropriate methods for incorporating them, while deciding the pay structure in CPSEs with an intent of retaining and attracting suitable talent. A brief summary, highlighting the key issues/findings/recommendations are provided as under.

3.4.1 STUDY REPORT ON COMPENSATION IN PUBLIC, PRIVATE AND OTHER SECTORS WITHIN AND OUTSIDE INDIA BY IPE, HYDERABAD.

The Study covers about 84% population of Executives in CPSEs and takes into account key comparisons such as inter and intra group among CPSEs, with respect to the Central Government employees; MNCs as well as domestic private sector. The study has also attempted to ascertain the practices being followed in other countries, where CPSEs concept is still in vogue with a relationship in compensation with government and private sector.

Certain other issues such as Accountability, Reward system, Affordability and Sustainability in Private sector & MNCs vis-à-vis' CPSEs have also been taken into consideration apart from having a broad view of pay packages in few similarly placed organizations abroad.

The study indicates some of the basic parameters and constraints that need to be given due considerations in view of the emerged competitive business environment in which the CPSEs are required to perform. Some of the concerns that mainly emerge out of the study are - need to explore the feasibility of Board driven pay packages; based on capacity to pay; inclusion of a higher variable component taking into account factors for local working conditions; improving quality of working environment, avenues for growth and development and empowerment to inculcate a sense of ownership; and a dynamic compensation structure. Details of the studies are placed at **Annex.- 3.9.**

3.4.1.1 General Feedback

i. The feedback obtained during the one to one interactions, IPE had with several senior executives of CPSEs can be summarized as under:

- Decisions related to employee compensation should be Board driven and shall be linked to market conditions, and the affordability and sustainability of the pay hikes as determined by the profitability of the CPSE.
- The elements of the executive compensation can be broadly divided into four parts :
    - ➢ The basic salary and allowances which can be fitted into some frame work of standardization and structure, linked again to the paying capacity of the CPSE.
    - ➢ Allowances, suitably formulated to make the compensation packages industry specific for increased conformity to industry standards.
    - ➢ Variable and performance based pay related to the organization's profitability and individual performance.
    - ➢ Compensation suitably designed to offset/alleviate the occupational hazards and difficulties in working conditions.

ii. Based on the responses received to the PRC's questionnaire, and various presentations given by the officers Associations, the following observations could be made.

- Compensation is an important tool for attracting and retaining talent and the same has to conform to market trends for performing CPSEs.
- The pay scales of the CPSEs within the Schedule should be uniform. Separate pay scales may be decided for performing / non-performing CPSEs.
- The number of pay scales may remain the same as at present, but the existing pay scales should be replaced by open ended pay scales.
- More emphasis be laid on variable components of pay, which will help Managements to liberally bring about variations in the pay structure to retain talent at individual or group level.
- The decisions regarding the perquisites should be left to the individual CPSEs to be decided depending upon their capacity to pay, their productivity and profit.

- The desirable ratio of pay between top level and entry level executives may be kept at 1: 6 or more; and the ratio of pay between the lowest workmen and CEO to be 1:10 or more.
- The desirable ratio of minimum and the maximum of any pay scale should be 1:2. However, it depends on the periodicity of pay revision. Sufficient care is to be taken that employees do not stagnate at the maximum of the scale.
- A better pay package may not always be the sole factor for migration of talent. The general working environment, work culture, job satisfaction, area of operations, personnel policies are some of the intangible factors, which people take into consideration before moving to another organization.
- The individual CPSEs will have to ensure that the quality of working environment, avenues for growth and development, and empowerment to facilitate, inculcating a sense of ownership amongst the executives, are taken care of, to retain the talent in the organization.
- One of the measures to retain talent could be to revise the pay scales every five years since the economic/industry scenario changes drastically over a long period of 10 years, thus, rendering the exercise of pay revision ineffective.

3.4.1.2 Limitations

i. Information related to remuneration and compensation is kept extremely confidential in the private sector companies and MNCs.

ii. The reluctance to part with information is not limited to private companies and MNCs alone. Even the CPSEs have not been forthcoming in responding to the requests for information from IPE. A total of only 84 responses have been received by IPE despite several requests and reminders from IPE and DPE. Due to incomplete information available in some cases, some assumptions had to be made in the compilation of the CPSE related data.

3.5. THEMATIC PAPERS

Based on preliminary interactions within the Pay Committee members and with some of the CPSE managements and Associations, some key issues of significance constituting the pay package of an employee were identified and it was decided to have detailed approach papers on the issues. Specific issues were assigned to some leading CPSEs, who volunteered for contributing. The salient outcomes are being reproduced here.

3.5.1 IDA/CDA PATTERN

This paper was attempted by National Textiles Corporation and supplemented by DPE. Broadly stating, Central/State Govt. employees are getting Central Dearness Allowance (CDA) & Employees of CPSEs are getting Industrial Dearness Allowance (IDA). However, there are certain CPSEs, where both CDA & IDA pattern are being followed. The difference between the two patterns remains because the reference dates for calculation is different (CDA/1.1.96; IDA/1.1.97).

(i) The study paper has brought out that as against 13.6 lakh IDA employees; there were about 2.0 lakhs CDA employees in CPSEs. CDA employees are further reducing due to Promotions, Retirements & adopting IDA scales voluntarily. Vide DPE Guidelines dated 12.6.90, all fresh appointments in CPSEs on or after 1.1.89 will have to be in IDA scales only.

(ii) There are still 58 CPSEs, which have both CDA and IDA pattern of pay scales. Some of these are incurring losses, are referred to BIFR and are unable to revise their pay scales. They are, therefore, in the pre-revised scale of 1992 or even 1987. But in these CPSEs, who are in CDA pattern of pay scales have the revised 1996 pay scales as recommended by the 5th CPC. This has lead to an anomalous situation, where in the same CPSE, some employees are enjoying revised CDA scales, whereas others are still in pre-revised IDA scales. The Committee took cognizance of the court directions that those, who are following CDA pattern prior to the court order may continue to be in CDA pattern of pay scales and any change made in the Central Government shall ipso-facto be applicable to the employees of CPSEs following CDA pattern. The option to switch over to IDA pay scale is voluntary. On the other hand, the Supreme Court held in the case of A.K.Bindal vs UOI (2003) that the economic viability or the financial capacity of the employer is an important factor, which cannot be ignored, while fixing the wage structure, otherwise the unit itself may not be able to function and may have to be closed down, which will inevitably have disastrous consequences for the employees themselves. The Committee also took note of the Supreme Court direction that the employees appointed on or after January 1st 1989 will be governed by IDA pay scales.

(iii) The PRC observed that continuing indefinitely with CDA pay scales in CPSEs is leading to anomalous situation leading to litigations. The courts are also of the opinion to have one set of pay scales as seen from some judgments. It is, therefore, felt that the solution lies in the employees under CDA pattern pay scales opting for IDA pay scales forthwith. Those who continue on CDA pay scales to be entitled only to the perks and allowances as applicable to Central Government employees and not as applicable to CPSEs, till they switch over to IDA pay scales. These employees cannot take advantage of CDA pay scales on the one hand and the benefit of better perks and allowances available for IDA employees on the other.

3.5.2 PERFORMANCE RELATED PAYMENTS

This paper was prepared by NTPC. This is the variable pay based on a combination of the organization's/unit's and the individual officer's performance. The individual performance should have a significant weightage to ensure differentiation. This amount should be based on performance on the job. There is persistent demand to have higher performance based pay as a percentage of Basic pay for the higher grades.

(i) In some of the CPSEs, the Performance Related Payments are already being made within the limit of 5% distributable profits, which has been made based on the Memorandum of Understanding reached between ASTO and Management. The Performance Related Employee Incentive Scheme (PREIS) provides for payment for Individual performance, Unit based performance and Overall

Company performance. In some CPSEs, based on composite score of individual employees, percentage of incentive in relation to Basic Pay will be determined. A Remuneration Committee of the Board determines the incentive payable to the fulltime Directors & CMD. In IOCL, total Productivity Incentive Bonus for 100 marks is 15% of basic pay plus DA. Accordingly, computation of Productivity Linked Incentive bonus for each location would be as per the formula given below:

Productivity Linked Incentive Bonus (%) = Actual Points scored / 100 * 15

Additionally, IOC has also recently introduced some payment linked to individual performance. Total performance related payments (Monthly & Annual Performance Linked Incentive payments and Ex-Gratia / Bonus) in a financial year shall be limited to ceiling specified by DPE from time to time.

(ii) There is greater stress on variable compensation all over the world. In private sector, the variable component is lesser (as % of total income) at lower levels and increases at higher levels. In Public Sector, the variable component is very small and is mostly linked to performance of the organization and not individual.

(iii) There is a need for a robust and transparent Performance Appraisal System based on pre-determined Key Performance Areas. Once such a system is in place, the CPSEs can go for Performance Related Payments.

3.5.3 EMPLOYEE STOCK OPTIONS PLAN (ESOPs)

This paper was submitted by IOC. These options are to encourage a sense of involvement among the employees, create a mutuality of interest and reward employees for long term performance. ESOP to employees has to be within the guidelines of SEBI, DPE & CBDT. The study conducted on ESOPs brought out the various options & models for ESOPs. They have also given the criterion for Eligibility, Terms, Frequency, Exercise Price, Vested Period & Exercise period for ESOPs.

(i) There is a wide range of financial participation schemes and these can be classified into the following broad categories. Each of the above option is described in brief.

I. Profit sharing

a. Cash-based profit sharing
b. Deferred profit sharing
c. Asset accumulation and savings plans

II. Stock options

a. Employee stock options plans (ESOP)
b. Employee stock purchase plan (ESPP)
c. Stock indexed plans
   - Stock appreciation rights (SAR)
   - Phantom stocks

I. Profit sharing

Profit sharing, in the strict sense, means the sharing of profits between providers of capital and providers of labour, by giving employees, in addition to a fixed wage, a variable part of income directly linked to profits or some other measures of enterprise results. Profit sharing is a collective scheme applied to all or to a large group of employees.

a. Cash-based profit sharing (CPS)

The reward under a cash based profit sharing plan is paid immediately in the year of performance. Ordinarily, this would be expected to increase the incentive value of the payment, but it also means that the amount received in the year is taxable. There is another variant of cash-based profit sharing, known as gain-sharing. Gain sharing is usually considered as a productivity improving or cost reducing activity, not directly related to company profit levels. It also provides for payments to participants much sooner to the performance that is being rewarded and is often organized on a unit-wise basis. Cash-based profit sharing, in contrast is usually company-wide. Gain-sharing is thus closer to a true incentive plan than cash-based profit sharing, and is certainly closer than deferred profit sharing, savings or employee share ownership.

b. Deferred profit sharing (DPS)

It is a form of deferred compensations under which the allocated profit share is held, most commonly, in trust and is not immediately available to the employee. Usually, a DPS scheme allocates certain percentage of profits to enterprise funds, which are then invested in the name of employee. Investment can be made in the employees company, but other assets can also be developed. Alternatively, the amount can be allocated to the employee's account, with a certain minimum retention period, before it is available to the employee.

DPS plans, generally, have minimal value as employee motivators. The employee receives nothing more than a periodic statement of the amount accumulated in his or her account and a projection of prospective savings of income. While the employee is receiving some future financial security, immediate incentive value is minimal.

c. Asset accumulation and savings plans

Asset accumulation and savings plan provide for employees to set aside a portion of their pay, and to receive contribution from their employer, in an account that is, in most cases, invested in stock, bonds or other investment choices for a period of time before being made available to the employee. Although, usually intended as a long term savings programme, plans may allow for withdrawals or loans.

Savings plans are designed mainly to encourage employees to save, while entailing little risk for them, and to attract a committed work-force. There is virtually no direct incentive that might influence immediate performance.

II. Stock options

Stock options provide for employee participation in enterprise results in an indirect way (on the basis of participation in ownership), either by receiving dividends or by the appreciation of employee owned capital, or a combination of both. Such schemes are not directly related to company profits but to company profitability and so enable participants to gain directly from the company's added value. Share ownerships can be both individual and collective. Shares can be in the company where the employee works or in other companies or in both. Employee share ownership can take many different forms.

a. Employee stock option plan (ESOP)

Employee stock option plans are the most commonly used form for employee ownership. The rising use of ESOP comes in part from a tightening labour market for knowledge workers. The principle message conveyed to the employees through ESOP is that, if they stay long enough till vesting, they stand to gain significantly through exercising the options. ESOPs are generally offered by offering fresh equity resulting in dilution of stake-holder shares and an alteration in the company equity structure. The other method for offering ESOPs relates to formation of a trust, which buys company's equity from the open market for offering options to the employees as per the company policy.

b. Employee stock purchase plan (ESPP)

Under an employee stock purchase plan, stock is transferred to employees, usually at a discount to the market price. Under this scheme, full rights may be conditional and predicated on the occurrence of certain events e.g. continued employment and/ or achievement of certain business measures. During the restricted period, the employee enjoys full share-holder rights, except for the right to sell or transfer the shares.

c. Stock indexed plan (SIP)

Stock based incentive plans do not involve actual purchase and acquisition of stock to link employee rewards to the value of the company stock. The expenses incurred under this plan, have to be borne by the company. Consequently, it is treated as tax-deductible compensation expense in the books. These plans have three features that make them tremendously appealing to the shareholders. First, they only reward managers, who out perform the market. If a company uses these options, there is no risk that mediocre or even poor managers will be over compensated as a result of bull market. Second, because the strike price is not fixed and tends to rise every year, an indexed plan will transfer less value than a conventional stock option plan. Third, indexed plans have lower strike prices and higher values even in bad times making it easier to retain valuable employees just when they are needed most.

- **Stock appreciation rights (SAR)**

  Although, SARs are not technically employee stock options, companies often use them in a like manner. SARs provide employees with cash payments equal to the appreciation of the company's stock over a specified duration. Thus, unlike other options, SARs provide employees with equity upside without exposure to any downside. Also, options, SARs result in periodic payments of cash to the employees over the SARs life. These are subject to same accounting treatment as index options and, therefore, are avoided by managers.

- **Phantom stocks**

  Phantom stock is a form of long-term deferred compensation using the company stock as the measuring device for calculating the value of the deferred compensation. It simulates the company stocks in everything except that does not represent true ownership. The company simply credits these phantom shares on its books and as the value of the company stock rises and falls, so does the value of the phantom stock.

While the employee is benefited under all the above schemes, ownership, in varying degrees, is possible only through the stock options because under the profit sharing schemes, the 'employee' (us) vs. 'employer' (they) feeling remains. In view of this, various stock options have been compared on four major dimensions i.e. (i) company liability, (ii) dilution of stake of major shareholders (changes in the equity structure), (iii) benefits to the employee and (iv) ownership (engagement levels).

(ii) Considering all these options/variations, it is felt that ESOP is the most appropriate option for CPSEs as it is not expected to increase financial burden on the enterprise and the employees stand to gain significantly, in the long run, if they continue to be with the company.

(iii) The extent of dilution has to be considered since the major shareholders interest would be affected to that extent and this should not have any significant change in the equity structure.

(iv) Considering competitiveness of an organization being dependent more on availability of talent, stock options as a piece of ownership and commitment towards organization, are a necessity.

3.5.4 VOLUNTARY RETIREMENT SCHEMES

This paper was prepared by MMTC. It is a Social Security Scheme by Government/CPSEs for their employees by way of an option for voluntary retirement from service on personal grounds. It also helps CPSEs to rationalize their excessive manpower. The catch is to have a VR scheme attractive enough to encourage employees to quit and yet enable CPSEs to retain the necessary talent. Existing VR schemes prevailing in different forms and shapes suiting to the specific industry and in line with DPE guidelines or with certain modifications reveal that over the years, the significance and utility of the same has gone down considerably and there is a need to go for exploring other better options to make VR schemes attractive in future. Some of the alternative schemes suggested were as follows;

(i) Option A – ex gratia benefit of 90 days for each completed year of service. 45 days salary to be paid in lump sum and with the balance purchase annuity from LIC or wages/salary for the residual months of service whichever is less.

(ii) Option-B –

- Ex-gratia @ 60 days salary for each completed year of service or the balance months of service, whichever is less.
- Pension by way of LIC annuity @ 50% of last drawn salary till the date of attaining the age of superannuation.

(iii) Option-C – Under this option, no change in the ex-gratia is proposed. However, to make the scheme more attractive, it is suggested that Income Tax on ex-gratia amount be totally withdrawn.

(iv) Option-D – Autonomy may be given to consistently profit making and financially sound CPSEs to devise their own Voluntary Early Retirement (VER) Scheme according to their organizational requirements.

(v) National Renewal Fund (NRF) option – NRF assistance to be given to only such CPSEs that have carried out scientific manpower planning study.

(vi) Compulsory Retirement Scheme (CRS)- The performance of inefficient employees be evaluated on the basis of Performance Appraisal System for one year and if the rating is found to be 'Poor' or 'Fair' during the first year, the employee should be counseled, and if required can be deployed to some other area of work and imparted training accordingly. His performance for the next (2nd) year should be assessed and if performance doesn't improve, he should be cautioned with the warning that if his performance does not improve during the next assessment year then he may be compulsorily retired. In the 3rd year, if the performance has still not improved, then the employee should be retired under the CRS with certain benefits.

(vii) The essential requirement is to make the organization lean so that it becomes competitive. Public Sector enterprises have to compete with private sector and MNCs, which are run much more efficiently. To survive, Public Sector Enterprises will have to right size their manpower.

3.5.5 POST RETIREMENT BENEFITS

This paper was submitted by NALCO. Post retirement benefits include provident fund, leave encashment gratuity, pension post retrial medical facilities, etc.

(i) Retired employees of many CPSEs are left with little or no economic support as most CPSEs do not have any post retirement benefit schemes. As a measure of social security and also considering the fact that retiring employees have contributed to the company some schemes need to be put in place, which will provide regular income or support after retirement. This will give a sense of pride and independence, which these employees would have enjoyed, when they were regular employees. Whether it is a pension scheme better than EPS95 or enhanced gratuity or post retrial medical facility, etc. should be in the form of annuity purchased from LIC or any similar agency. Depending on the capacity of the company, the expenses could be shared between the company and the employee during the course of employment. Better performing CPSEs could share a larger proportion and in those CPSEs that are not doing well, the major portion could be from the employees themselves. The company is anyhow bound to contribute the statutory requirement towards PF, EPS 95 and gratuity.

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