

# A STUDY ON REGULATORY REQUIREMENT AND IMPACT FACTORS OF SICK UNITS IN INDIA

<sup>1</sup>Mr A.ABDUL KHADAR, <sup>2</sup>Dr.A. ABDHUL RAHIM

<sup>1</sup> REG.NO 10217, Scott Christian College (Autonomous), Nagercoil

Affiliated to Manomanian Sundarnar University, Abishekapatti, Tirunelveli-627012 Tamilnadu, India

<sup>2</sup> Assistant Professor, Department of Commerce, Alagappa Govt Arts College, karaikudi.

Email - nasihakadhar@gmail.com

**Abstract:** *Sickness in Industries has become very sensitive problem in India. It is creating adverse problem to industrial health and the economy as well. Rapid industrialization gives positive as well as negative impact on the economy. Sickness covers all types of units in small, medium and large sectors in all over the world. It is a matter of crore of rupees concern directly and indirectly to the nations. It is also a phenomenon shows adverse effect on employment, availability of goods and services and the price of those things soaring up. The investors lose their earning and creditors lose their future returns and the business become weak. The Government, Financial Institutions and Management should focus on prevention of sickness, to save the business world. However, before discussing the measures of industrial sickness, regulatory requirement of sick industries and the most important piece of legislation dealing with industrial sickness was the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA).*

**Key Words:** SICA, BIFR, NPA, NCLT, and AAIFR .

## 1. INTRODUCTION:

### Sick Industrial Companies Act (SICA)

According to Companies (Second Amendment) Act, 2002 Sick Industrial Company means an industrial company which has i) The Accumulated losses in any financial year equal to 50 per cent or more of its average net worth during four years immediately preceding such financial year or ii) Failed to repay its debts within any three consecutive quarters on demand made in writing for its repayment by a creditor or creditors of such company.

Sick industrial unit is defined as a unit or a company (having been in existence for not less than five years) which is found at the end of any financial year to have incurred accumulated losses equal to or exceeding its entire net worth. The net worth is calculated as sum total of paid up capital and free reserves of a company less the provisions and expenses, as may be prescribed. An industrial unit is also regarded as potentially sick or weak unit if at the end of any financial year, it has accumulated losses equal to or exceeding 50 per cent of its average net worth in the immediately preceding four financial years and has failed to repay debts to its creditor(s) in three consecutive quarters on demand made in writing for such repayment.

When an entrepreneur is unable to profitably grow and expand the business on a sustained basis, he/she may have to take a decision of either restructuring its organization or closing it. Thus, he/she may either revive the company if it is potentially viable or ensure the closure of a nonviable unit so as to release the investments locked up in such units for productive use elsewhere.

In order to wind up or close a business organization, an entrepreneur must take into account the interests of its employees, creditors, shareholders, etc. Hence he/she must follow the basic regulatory requirements of the country.

The most important regulation relates to sick industries in India. Sick industries are those industries which make losses that are more or less permanent and are not likely to be eliminated easily. In the normal course, such units would close down or would undergo extensive restructuring to eliminate the operations or activities that are particularly unprofitable. To deal with such a problem, SICA or Sick Industrial Companies (Special Provisions) Act, 1985 was enacted. It aimed to detect industrial sickness and provide for speedy remedial measures. Hence, a quasi-judicial body called Board for Industrial and Financial Reconstruction (BIFR) was set up which expedited the process of revival of potentially viable units or closure of nonviable units. This Act was repealed and replaced by Sick Industrial Companies (Special Provisions) Repeal Act, 2003, which made the whole process more transparent and simpler by setting up of National Company Law Tribunal (NCLT) in place of BIFR.

As a part of the continuous reforms process, the Government has been making efforts to bring more flexibility in the process of winding up of an industrial unit through a practicable exit policy.

## 2. OBJECTIVES OF THE STUDY:

- To understand the concepts, measurements and regulatory requirement of sick units

- To identify the what are factors results in sick units in India.
- To create awareness about the SICA to business unit

### 3. RESEARCH METHODOLOGY:

The study is based on secondary data. The data is collected from various sources newspapers, magazines and websites. Data was collected from its inception till 31.08.2018. For presentation, the table is used and for analysis percentage method used.

### 4. FACTORS RESULTS IN SICK UNITS IN INDIA:

#### (A) Internal factors are those which arise within an organization. They include:

- Mismanagement in various functional areas of a company like finance, production, marketing and personnel;
- Wrong location of a unit;
- Overestimation of demand and wrong dividend policy;
- Poor implementation of projects which may be due to improper planning or managerial inefficiency;
- Poor inventory management in respect of finished goods as well as inputs;
- Unwarranted expansion and diversion of resources such as personal extravagances, excessive overheads, acquisition of unproductive fixed assets, etc.;
- Failure to modernize the productive apparatus, change the product mix and other elements of marketing mix to suit the changing environment;
- Poor labour-management relationship and associated low workers' morale and low productivity, strikes, lockouts, etc.

#### (B) External factors are those which take place outside an organization. They include:-

- Energy crisis arising out of power cuts or shortage of coal or oil;
- Failure to achieve optimum capacity due to shortage of raw materials as a result of production set-backs in the supply industries, poor agricultural output because of natural reasons, changes in the import conditions, etc.
- Infrastructural problems like transport bottlenecks;
- Credit squeeze;
- Situations like market recession, changes in technology, etc;
- International pressures or circumstances, etc.

#### (C) Industrial sickness may be caused by a combination of all such factors.

It has several adverse consequences on the economy as a whole. Some of which may be enumerated as follows:-

- It leads to loss of substantial revenue to the Government and enhances its public expenditure;
- It locks up necessary resources and funds in the sick unit. This also increases the non-performing assets (NPAs) of banks and financial institutions;
- It leads to loss of production and productivity in the economy;
- It aggravates the problem of unemployment in the economy;
- It vitiates the industrial atmosphere and leads to worker-management disputes, strikes, lock-outs, etc;
- It undermines the public confidence in the functioning of the organized sector in the country which in turn affects the overall investment climate of the economy.
- In the light of the above consequences of sickness and its growing incidence by size, region and industry followed by its far-reaching adverse social-economic effects, the Government has been taking many steps and remedial measures in order to tackle this problem in India. The most significant measure has been the enactment of the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA).

### 5. REGULATORY REQUIREMENT OF SICA

#### Sick Industrial Companies (Special Provisions) Act, 1985

The most important piece of legislation dealing with industrial sickness was the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA). It applies to industrial undertakings both in the public and private sectors. SICA pertains to the industries specified in the First Schedule to the Industries (Development and Regulation) Act, 1951, (IDR Act) subject to the exceptions specified in the Act. SICA, including any rules or schemes made there under, had overriding provisions over other laws except the provisions of the Foreign Exchange Regulation Act, 1973 and the Urban Land (Ceiling and Regulation) Act, 1976.

The basic rationale of enacting SICA was to determine sickness in the industrial units. It also aimed at expediting the revival of potentially viable units so as to make the investments in such units profitable. At the same time, to

ensure the closure of unviable units so as to release the investments locked up in such units for productive use elsewhere.

**Thus, the broad objectives of SICA were:-**

- Timely detection of sick and potentially sick companies.
- Speedy determination by a body of experts of the preventive, ameliorative, remedial and other measures which need to be taken with respect to such companies.
- The expeditious enforcement of the measures so determined and for all matters connected therewith or incidental thereto.

**The important provisions of SICA were:-**

It provided for the constitution of two quasi-judicial bodies, that is, Board for Industrial and Financial Reconstruction (BIFR) and Appellate Authority for Industrial and Financial Reconstruction (AAIFR). BIFR was set up as an apex board to tackle industrial sickness and was entrusted with the work of taking appropriate measures for revival and rehabilitation of potentially sick undertakings and for liquidation of non-viable companies. While, AAIFR was constituted for hearing the appeals against the orders of the BIFR

**BIFR would make an inquiry as it may deem fit for determining whether any industrial company had become sick, under the following conditions:-**

If the Board of Directors of a sick industrial company made a reference to the BIFR for determination of the remedial measures with respect to their company, Such reference was to be made within sixty days from the date of finalization of the duly audited accounts of the company for the financial year at the end of which the company had become sick. For filing the reference, the Board of Directors must have sufficient reasons to form the opinion that the company had become sick; or

On receiving such information (reference) with respect to a sick company or upon its own knowledge as to the financial condition of a company, Such a reference to the board may be made by:- (i) The Central Government; (ii) The Reserve Bank of India; (iii) State Governments; (iv) Public financial institutions; (v) State level institutions; or (vi) Scheduled banks.

However, such a reference shall not be made in respect of any industrial company by :- (i) the Government of any State, unless all or any of the industrial undertakings (belonging to such a company) were situated in that State; (ii) a public financial institution or a State level institution or a scheduled bank, unless it had, by reason of any financial assistance or obligation rendered by it or undertaken by it, interest in such a company.

**The Board may order any operating agency to enquire into the matter and complete the inquiry as expeditiously as possible.**

If the Board deems it fit to make an inquiry or to cause an inquiry to be made into any industrial company, it may appoint one or more persons as special director(s) of the company for safeguarding the financial and other interests of the company. The appointment of a special director shall be valid and effective notwithstanding anything to the contrary contained in the Companies Act, 1956 or in any other law for the time being in force or in the memorandum and articles of association or any other instrument relating to the industrial company.

**Any special director so appointed shall :-** (i) hold office during the pleasure of the Board and may be removed or substituted by any person by order in writing by the Board; (ii) not incur any obligation or liability by reason only of his being a director or for anything done or omitted to be done in good faith in the discharge of his duties as a director or anything in relation thereto; (iii) not be liable to retirement by rotation and shall not be taken into account for computing the number of directors liable to such retirement; (iv) not be liable to be prosecuted under any law for anything, done or omitted to be done in good faith in the discharge of his duties in relation to the sick industrial company.

If after making an inquiry, the Board is satisfied that the company has become sick, it shall, after considering all the relevant facts and circumstances of the case, may take either of the following decisions:-

If the Board decides that it is practicable, it shall, by order in writing and subject to such restrictions or conditions as may be specified in the order, give such time to the company as it may deem fit to make its net worth exceed the accumulated losses.

**The measures may include:-**

- The financial reconstruction of the sick industrial company;
- The proper management of the sick industrial company by change in or take over of the management of the company;

- The amalgamation of the sick industrial company with any other company (transferee company), or any other company with the sick industrial company (transferee company);
- The sale or lease of a part or whole of the sick industrial company;
- Such other preventive, ameliorative and remedial measures as may be appropriate;
- Such incidental, consequential or supplemental measures as may be necessary or expedient in connection with or for the purposes of the measures specified above.

If the Board is of the opinion that the sick industrial company is not likely to make its net worth exceed the accumulated losses within a reasonable time while meeting all its financial obligations and that the company as a result thereof is not likely to become viable in future and that it is just and equitable that the company should be wound up, it may record and forward its opinion to the concerned High Court. The High Court shall, on the basis of the opinion of the Board, order winding-up of the sick industrial company in accordance with the provisions of the Companies Act, 1956.

Where in respect of an industrial company, an inquiry is pending, or any scheme referred is under preparation or consideration or a sanctioned scheme is under implementation, then no proceedings for the winding-up of the industrial company or for execution, distress or the like against any of the properties of the industrial company shall be made. Also, no suit for the recovery of money or for the enforcement of any security against the industrial company or of any guarantee in respect of any loans, or advance granted to the industrial company shall lie or be proceeded with further, except with the consent of the Board or, as the case may be, the Appellate Authority.

Also with respect to the above conditions, the Board may by order declare with respect to the sick industrial company concerned that the operation of all or any of the contracts, assurances of property, agreements, settlements, awards, standing orders or other instruments in force, to which such sick industrial company is a party or which may be applicable to such sick industrial company immediately before the date of such order, shall remain suspended or that all or any of the rights, privileges, obligations and liabilities accruing or arising there under before the said date, shall remain suspended or shall be enforceable with such adaptations and in such manner as may be specified by the Board.

However, such declaration shall not be made for a period exceeding two years, which may be extended by one year at a time so that the total period shall not exceed seven years in the aggregate.

Under the Act, whosoever violates its provisions or any scheme or any order of the Board or of the Appellate Authority, shall be punishable with imprisonment for a term which may extend to three years and shall also be liable to a fine. No court shall take cognizance of any offence mentioned except on a complaint in writing of the secretary or any such other officer of the Board or the Appellate Authority or any such officer of an operating agency as may be authorised in this behalf by the Board or the Appellate Authority.

Sick Industrial Companies (Special Provisions) Act, 1985 (SICA) was repealed and replaced by Sick Industrial Companies (Special Provisions) Repeal Act, 2003. The new Act diluted some of the provisions of SICA and plugged certain loopholes. It aimed not only to combat industrial sickness but also to reduce the same by ensuring that companies do not view declaration of sickness as an escapist route from legal provisions after the failure of the project or similar other reasons and thereby gain access to various benefits or concessions from financial institutions. Under it, the Board for Industrial and Financial Reconstruction (BIFR) and Appellate Authority for Industrial and Financial Reconstruction (AAIFR) were dissolved and replaced by National Company Law Tribunal (NCLT) and National Law Appellate Tribunal (NCLAT) respectively.

## 6. CONCLUSION:

Sick industries are those industries which make losses that are more or less permanent and are not likely to be eliminated easily. In the normal course, such units would close down or would undergo extensive restructuring to eliminate the operations or activities that are particularly unprofitable. To deal with such a problem, SICA or Sick Industrial Companies (Special Provisions) Act, 1985 was enacted. It aimed to detect industrial sickness and provide for speedy remedial measures. Hence, a quasi-judicial body called Board for Industrial and Financial Reconstruction (BIFR) was set up which expedited the process of revival of potentially viable units or closure of nonviable units. This Act was repealed and replaced by Sick Industrial Companies (Special Provisions) Repeal Act, 2003, which made the whole process more transparent and simpler by setting up of National Company Law Tribunal (NCLT) in place of BIFR. As a part of the continuous reforms process, the Government has been making efforts to bring more flexibility in the process of winding up of an industrial unit through a practicable exit policy.

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