

## **WOOD FOR THE TREES**

***Sebi's new guidelines on public shareholding in listed companies are welcome but some fundamental issues have not been addressed***

***The concept of 'promoter' must be replaced with 'controlling entity' to include benami holding***

**Prithvi Haldea**

SEBI has finally notified guidelines for public shareholding in listed companies. The objective is laudable -- "ensuring availability of floating stock on a continuous basis and to bring about greater transparency in respect of disclosure of shareholding pattern of companies". However, while several issues have not been addressed and some only partially addressed, the implementation too may present challenges.

Indian promoters have always had the cake and eaten it too, thanks to relaxations in policies, poor disclosure requirements and weak enforcement. A few decades ago, a company had to offer 60 per cent of its capital to get listed; that was considered minimum to obtain a public character. Over the years, pressure from corporates has brought this down to 25 per cent, and in some cases to even 10 per cent. So, the policies have hugely diluted public shareholding in listed companies.

### **Root of problems**

Lower float is the cause of several ills, including price manipulations and excessive volatility, and in recent times abnormal increase in share prices with too much money chasing too few shares. Worse, poor enforcement and ambiguity in guidelines have seen even such low public shareholding requirements being violated rampantly. This is what necessitated the new norms.

Of course, several exemptions have been given to some companies, including PSUs and top blue-chip companies (about 190 of them), thus making this guideline applicable mainly to medium and small companies. So, at the end of the day, the new guideline won't have much impact.

Though the existing reporting format of shareholding pattern has been revised, it is still deficient. Promoters hold a large amount of shares in their companies through benami /front entities. These holdings are shown in the names of innocuous individuals, relatives (such as not covered by the guidelines) and private corporate bodies and pass off as public shareholdings and therefore do not draw attention of regulators/tax authorities. Such holdings not only provide promoters the controlling rights but also, whenever opportunities arise, to make millions in the market by selling shares and not draw any attention. The new format does not attack this malaise.

### **Redefining control**

Correct public shareholding can be ascertained only if we first get the promoters' definition right, which presently is open to gross misuse. The concept of "promoters" needs to be replaced with that of "controlling entity" which would also include persons acting in concert (PACs), strategic shareholders and all such entities, except SEBI-registered QIBs, to whom preferential shares have been allotted.

To unearth promoters' holding hidden in public shareholding, we need detailed disclosure format for public shareholders which, among other things, should require addresses and names of father/directors. There should also be an upfront declaration by the promoters that they have no relationship with any of these entities, and on discovery of any ties, heavy penalties should be imposed on the promoters. Little wonder that such a format introduced by the Listing Committee and the Index Committee of the BSE last year continues to face resistance from corporates.

On another front, while dilution to reinstate minimum public shareholding was earlier allowed through public issue of fresh shares or offers for sale by the promoters, the new guidelines permit sale of shares by promoters in the secondary market. Stock exchanges will have to be vigilant to ensure this method is not misused by the promoters.

### **A step forward**

A contentious issue though has been resolved by the guidelines by not allowing GDRs/ADRs to be treated as public shareholding. While it recognises that some of such shareholding could be promoter-controlled, it ensures a minimum domestic float.

SEBI has also directed stock exchanges to monitor compliance and to report the same. Presently, most stock exchanges do not actively monitor the public shareholding requirement. So scores of companies have violated this requirement with impunity.

For non-compliance, the new guideline prescribes delisting and also liability for penal actions. In my view, the only action should be a substantive punishment for promoters. Also, a one-time penalty should be imposed on companies that have violated this norm in the past.

### **Comprehensive review**

I have another wish. Before enforcing the new guidelines, a complete review of all listed companies should have been undertaken. This would have revealed that there are thousands of companies that have no business to even remain listed any more. This would include companies that have no revenues or done any business for several years. There are companies that have zero or miniscule public shareholding; for years, Such companies have been owned fully by the promoters and have produced the penny stocks scam. Many companies have very small capital bases (what use would 25 per cent holding have if the entire listed capital of the company is just Rs 10-50 lakh). The Sebi guideline should have also prescribed a minimum amount of listed capital.

Also, many companies have been suspended from trading for violating rules or malpractices. Delistings should first take place, with necessary compensation to the retail investors, and once the system has been cleaned, new guidelines should be enforced on the remaining companies. Monitoring of fewer companies would become that much more easier.

The new guidelines also do not address the problem of thousands of companies listed only at regional exchanges. With no trading for nearly three years now, there is no benefit in asking these companies to comply with the 25 per cent public shareholding clause. The better among these companies need to be upgraded to a national trading platform while the bad ones should be delisted and compensation given to minority shareholders.