Minimum Public Shareholding Norms In India

Is It Time For Change?

One of the big-bang proposals in the Union Budget was for the SEBI to consider increasing minimum public shareholding requirement in listed companies to 35 per cent

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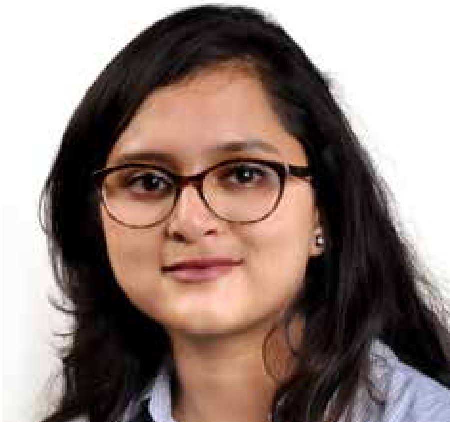
On July 5, 2019, the Indian finance minister, in her debut budget speech, announced a few big-bang proposals. One such proposal was for capital market regulator Securities and Exchange Board of India ("**SEBI**"), to consider increasing minimum public shareholding requirement in listed companies from the current threshold of 25% to 35%.

The current threshold

Many Indian listed companies are promoter-owned and controlled (promoters are generally controlling shareholders in a company). For an initial public offering to be successful and for continuous listing, the Securities Contracts (Regulation) Rules, 1957, as amended ("**SCRR**"), includes the concept of a minimum public float (public is defined to exclude promoters and the promoter group).

The minimum public shareholding requirement has been subject to change from time to time. Immediately prior to September 1993, companies seeking to list their shares were required to offer at least 60% of their capital to the public, whose threshold was subsequently reduced to 25% on September 20, 1993. In 2010, the regulation was further amended to harmonize initial and continuous listing requirements and, the current requirement of maintaining the minimum public float of 25% on a continuing basis after listing, was codified. Companies (other than public sector



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undertakings (“**PSUs**”), which are government-controlled entities) listed on or prior to June 4, 2010, were required to comply with the 25% requirement by June 3, 2013. Companies (other than PSUs), listed after June 4, 2010, were required to comply with the 25% requirement within three years from the date of listing. Listed PSUs were initially required to maintain a lower minimum public shareholding of 10%. However, the exception for PSUs was later omitted in 2014 and all listed companies (including PSUs) are currently required to maintain a public shareholding of at least 25%.

Current regulations state that if the public shareholding of a listed company falls below 25%, it is required to increase its minimum public shareholding to 25% within 12 months, subject to certain exceptions such as the implementation of a resolution plan under the Insolvency and Bankruptcy Code, 2016. If the public shareholding of a listed PSU falls below 25%, it is required to increase its public shareholding to at least 25% within two years.

The SEBI has issued various circulars from time to time prescribing the specific manner in which listed companies can increase their minimum public shareholding, including by way of issuance of new equity shares or an offer for sale by the promoter shareholders through a prospectus.

The SEBI has also issued circulars prescribing a sale of promoter equity shares through the secondary market, issuance of equity shares through selective rights or bonus issues to the public shareholders (with the promoter and promoter group shareholders foregoing their entitlement), allotment of eligible securities under a qualified institutional placement or through other means as approved by the SEBI on a case-to-case basis.

The SEBI has resisted any demands to lower the 25% threshold and companies and their promoters have been required to comply with the requirement. In its annual report for financial year 2013-2014, the SEBI noted an increase in the number of issues through an institutional placement program (a permitted means to issue fresh shares and increase the public float), most of which were completed before the June 3, 2013 deadline.

Similarly, the SEBI noted that 71 companies had used the offer for sale through stock exchange mechanism (another permitted means for a promoter to sell and meet the public float requirement) in financial year 2012-2013 as compared to 33 companies in financial year 2011-2012.

One consequence of the minimum float requirement is that the promoter shareholding in listed Indian companies has decreased. According to a recent report issued by nseinfobase.com, over a 10-year period since June 2009, promoter ownership has been steadily declined, from 61.34% on June 30, 2009, to 54.46% on June 30, 2019. However, some PSUs and other companies are still not compliant.

Consequences of non-compliance

The principal Indian regulators responsible for implementing minimum public shareholding requirements are the SEBI and the stock exchanges. The SEBI has specified procedures for stock exchanges to follow, once a company is identified as being non-compliant with the minimum public shareholding rule; such procedures include the imposition of monetary penalty on a listed company and taking steps to freeze assets of the promoter and promoter’s group until the date of compliance.

Stock exchanges could also consider compulsory delisting of the non-compliant entity in accordance with applicable regulations, including the Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009.

SEBI could also issue directions and impose penalties against non-compliant companies, their directors and promoters, including restricting relevant directors and promoters from

being associated with other listed companies. For example, in 2013, the SEBI issued an order against the promoter or promoter group and directors of 107 listed companies (including a state PSU) for non-compliance with minimum public shareholding requirements.

The Securities Appellate Tribunal (SAT) has also weighed in on a number of cases of such non-compliance and reiterated that the underlying philosophy behind minimum public requirements is the prevention of concentration of shares in the hands of a few market players.

Is there a need for a change?

The existing public shareholding requirement of 25% in Indian markets is generally consistent with norms prevailing in other sophisticated international jurisdictions. While the proposed move to increase public shareholding from 25% to 35% could be considered as raising the bar for listed companies in India, it may also be disruptive. It would be unfair to penalize companies who do not need capital and may be forced to raise funds through a fresh issue or face the consequences of non-compliance with such higher threshold. Similarly, existing promoters may not desire to sell shares as they may not need the liquidity or achieve the desired return in the currently volatile Indian and global markets. If a company has more than one promoter, these promoters may need to agree on inter-se arrangements to comply with the increase in public float requirements. Also, there are other regulations to consider, such as takeover regulations where open offer requirements are triggered if a person acquires 25% or more shares in a listed company and it is unclear if changes to such regulations need to be made. Finally, from a policy perspective and as noted above, the concentration of promoter ownership in India has declined over the past ten years.

It would perhaps be more prudent for the regulators to focus on monitoring and implementation of existing norms, including those specifically for PSUs which have periodically been provided with concessions, before opening the next chapter.

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