A LEVEL-PLAYING FIELD

THE BUDGET SHOULD CLOSE THE PERPETUAL INFANCY ARGUMENTS FOR/OF PSUs AS OWNERSHIP NEUTRALITY MAKES THEM STRONGER AND THE SECURITIES MARKET HEALTHIER

Once a PSU, always a PSU

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SOME POLICIES HAVE a special trajectory of life. Gradually, after a round trip with some adventures, they come back to their original position. Still, they are treated as reforms at every turn. The Minimum Public Shareholding (MPS) rules for listed companies, a key reform of the securities market, appear to be amongst this class of reforms.

With great fanfare and after consultation for years, the Securities Contracts (Regulations) Rules, 1957 (SCRR) prescribed on June 4, 2010: "Every listed company shall maintain public shareholding of at least twenty-five percent." In about two months, by a notification on August 9, 2010, it was amended to: "Every listed company other than public sector company shall maintain public shareholding of at least twenty-five percent." PSUs were required to maintain an MPS of 10%. This created a constituency of listed/intending to be listed PSUs, who have been seeking relaxation of the MPS rule on one ground or another. Several carve-outs have been sought and made from time to time, requiring 11 amendments to this rule since its introduction.

By concerted efforts over years, all listed private sector companies and many PSUs, particularly public sector banks, fulfilled the MPS norm of 25% by 2018. The only leniency PSUs had, as provided by an amendment on August 3, 2018, was two years to bring up MPS when it falls below 25% at any time, as compared to one year for others. Being encouraged, the budget speech of 2019 sought Sebi to consider increasing MPS from 25% to 35%. However, this idea did not gain any traction.

Till 2021, the MPS rule provided a dispensation for PSUs as a class. The SCRR was amended on July 30, 2021, to empower the government, in the public interest, to exempt any PSU from MPS rule. This created classes within the class of PSUs. While broadly retaining this provision, an amendment to the SCRR on January 2, 2023, added an interesting explanation: "For the purposes of this rule, the exemption shall continue to be valid for the period specified therein, irrespective of any change in control of such listed entity subsequent to issuance of such exemption." If a PSU is granted an exemption, it would continue to enjoy the same for a period specified in the exemption notification, even if it becomes a private entity in the meantime. This extended the exemption to PSUs becoming private through divestment, creating classes among the listed entities—some entities having no exemption and others having different levels of exemption.

> **The latest carve-out of the MPS rule is reportedly for smoothening the stake sale of IDBI Bank**

The MPS rule has taken such turns mostly to accommodate an immediate need. The latest carve-out is reportedly for smoothening the stake sale of IDBI Bank. A case-by-case listing rule is too problematic for both the company and the investors. It distorts the level-playing field and creates unpredictability. If a special dispensation, whether favourable or unfavourable, is granted to an entity, it distorts the choice of stakeholders in relation to every other entity in the market and consequently misallocates resources.

In the earlier regime, the government used to play a dual role. It was doing business through its instrumentalities while making rules to govern the business. This created a perception that since the government had an interest in making sure that the PSUs performed well, any rules that it made would have an institutional bias in their favour. The market would not trust a regime where a competitor is also the rule-maker. It was this persuading logic that created the regulators at arms-length from the government to lay down ownership-neutral regulations. It is perplexing that the government makes MPS rules and exercises powers under the rules even though there is a full-fledged regulator of securities markets. For the business to have complete trust, MPS should also move to Sebi's arsenal.

Special treatment sought and given may be justifiable to address a specific issue or facilitate a specific transaction. However, it is imperative to keep in mind the rationale behind MPS. A high MPS is needed for a large free float to discover the right price, promote market integrity, and prevent potential manipulation by vested interests. Listed entities with very low public float may face considerable market turmoil as those shares may easily become victims of manipulation. The higher the MPS, the better. Further, minimum public holding is the opposite of maximum promoter holding. This makes the promoter holding practically an entitlement; whether for family-held or State-held companies. Most promoters retain the maximum possible shares with them and therefore the prosperity associated with shareholding. A higher MPS, on the other hand, promotes the sharing of prosperity amongst the larger public.

A differential MPS or any other dispensation does no good to neither the promoters of PSUs nor the investors, in the long run. It is evident from a simple fact that the BSE PSU index has grown about six times in the last two decades, while BSE Sensex grew about 18 times during the same period. Market capitalisation of a private sector company is typically a multiple of a comparable public sector company.

Listing for swimming in the shallow shores of the market does not make the company learn deep-water swimming. Rather, it can be dangerous, as a sudden, big wave may just swallow it. Listing a company is completely optional. Do it when an entity is fully ready to face the market. Let the courtesy begin at home. Let the PSUs be models for governance, rather than, like infants, perpetually seeking regulatory carve-outs, exemptions, and safe harbours. It is good for their health, growth, as well as for the health of the securities markets. Given the current confidence of the Indian economy and market, this is the right time to go for an ownership-neutral regulatory framework.