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ONCE A PROMOTER, ALWAYS A PROMOTER! A DISCUSSION ON THE RECENT REGULATORY CHANGE ON PROMOTER RECLASSIFICATION IN INDIA

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Abstract: *High ownership concentration in the hands of few has always been a problem in emerging economies. India, with concentrated ownership in the hands of few owner/managers (Promoters), is no exception! Such concentrated ownership structures weaken the internal governance mechanisms and increase the probability of minority shareholder expropriation. This is called Principal-Principal conflict (Promoter-Minority Shareholders), which lead to many market imperfections (illiquidity, price manipulations, illegal insider trading, etc) and keep the institutional investors at bay. To tackle such issues, Securities and Exchange Board of India (SEBI) (under the direction of Ministry of Finance) came up with an amendment in the listing regulation for both initial and continued listing in the year 2010. Publicly listed private firms in India were directed to increase their free float stocks to a minimum of 25% (10% for PSUs) within three years. Out of the 275 affected listed firms, close to 70% companies complied with the regulation by choosing the recommended methods of adherence like – sale of equity on the floor of house, further public offer, offer for sale, rights/bonus issue, and institutional private placement. While there were specific cases where certain firms tried to comply with the regulation by declassifying some promoters as public shareholders to which SEBI had raised concerns. The issue was discussed in the Securities Appellate Tribunal, which directed SEBI to come up with a detailed regulation on such re-classification. This discussion paper looks into the nuances of that regulation and tries to comment on the various merits and pitfalls which this may have in the broader scheme of the ownership structure in Indian firms. At one hand the proposed regulation is very risk averse which creates various operational complexities from the promoters' point of view while from the minority shareholders' protection perspective should prove to be mixed.*

Keywords*: Promoter shareholding, Public Shareholding, Minimum public floats regulation, Promoter re-classification regulation, ownership and control*

1. INTRODUCTION

Concentrated ownership has been observed in countries other than US and UK by many researchers, staring from La Porta, *et al.* (1999). India is no exception, which

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despite a healthy capital market still faces high ownership concentration, with a very high concentration of ownership in the hands of promoters. Since the last decade the shareholding pattern of the Indian firms, listed on the burses, has remained as high as 45-50%. And with mechanisms like differential voting rights, cross-holdings, and pyramidal structure, these firms alleviate the problem to a higher level, where the promoters have even greater cash flow rights with seemingly lesser control rights. This creates opportunities for private benefit of control by making it easier for the promoters to expropriate the minority shareholders by means of tunneling and related party transactions, giving rise to *principal-principal* problem.

Very high promoter holdings also create a problem of low *free float*[1] of the stocks in the secondary market. This in turn creates a problem of liquidity in the market which increases the chances of stock price manipulation (Imisiker & Tas, 2014) by means of informed trading. This keeps the retail investors away from such stocks which have value decreasing effect on the stocks (Bostanci & Kilic 2010). Lower public float hints at a possibility of low firm-level governance and increased chances of minority shareholder expropriation.

Government and regulators have done a lot to improve the corporate governance of the listed firms in India, by means of constantly revising the corporate and listing laws (Kumar Mangalam Birla Committee Report; Narayan Murthy Committee Report). According to the World Bank report on *Doing Business, 2010*, India ranks 41 among 183 countries surveyed for the quality of securities regulation, company laws and legal system. However, when it came to enforcing contracts, India stood at a dismal 182 among the 183 countries studied. Which certainly highlights the status of actual minority shareholder protection status of the country – although there are sound regulations but the weak enforcement makes it practically ineffective (Rajagopal & Zhang, 2008).

In view of these issues arising from the high promoter holding in some stocks, Securities and Exchange Board of India (SEBI) in consultation with the Ministry of Finance came up with a amendment in Rule 19 (2) (b) of SCR Act for mandatory regulation of Initial Public Offering and continued listing at Indian bourses, on 4th of June 2010 and 16th December respectively. According to regulation all private listed firms which had low free float should mandatorily reduce it to 25% by the end of June 2013. Similarly the minimum Public float requirement for the Public sector companies listed on the bourses was set at 10% to be complied or on before August 2013. The rationale was to improve market liquidity, check price manipulations, and improve corporate governance and foreign institutional investor participation in the market. Affected firms were given a window of three years to adhere, using five different methods – (i) Follow-on public offer, (ii) offer for sale on separate trading window, (iii) institutional private placement, (iv) rights/ bonus issuance and (v) any other approved by SEBI on case-on-case basis.

Close to 275 different firms was impacted by this regulation, of which around 60% of the firms adhered by reducing the promoter holding using one or the other methods prescribed by the regulator. 33 firms were suspended from the listing at bourses, due to no action for adherence while there were close to 35 firms which although did not comply with the regulation in the adherence window but were in the process of doing the same, and hence got an exemption from SEBI's strict action against them – like suspension.

Many firms, having very high dilution fraction (high percentage of promoter holding to be sold off to public), chose to delist by means of reverse book building, while there were a decent chunk of firms which tried to adhere with the regulation by means of re-classifying a fraction of the promoter holding stocks into non-promoter holding, by means of private placement to non-institutional players, sister firms from the same business groups or other stand-alone firms or person(s). SEBI, however, did not consider such dilution and considered these firms non-compliant. In the lack of any existing clear guidelines on the issue of reclassification of the promoter to public shareholders, Securities Appellate Tribunal (SAT) ordered the regulator to increase clarity on this issue through clarifying their stance on the same by explicitly stating the guidelines in such cases. Given this, SEBI after three rounds of discussions and consultations came up with a discussion paper for public comments for the purpose of clearly drafting the regulation on the issue of promoter re-classification.

This discussion paper looks into the nuances of that regulation and tries to comment on the various merits and pitfalls which this may have in the broader scheme of the ownership structure in Indian firms. At one hand the proposed regulation is very risk averse which creates various operational complexities from the promoters' point of view while from the minority shareholders' protection perspective should prove to be mixed.

2. REVIEW OF LITERATURE

2.1. Ownership and Governance

There has been a long list of theories from various competing streams of literature which try to explain the governance issues in firms. But when it comes to economics and finance literature the key theoretical paradigm is the agency problem which originated from the works of Berle & Means (1932) and later reintroduced in the current form by Jensen & Meckling (1976). Agency theory deals with the conflict of interest between the suppliers of the finance (the principal) and the controlling management (the agent) who are responsible for making the right use of that finance to run the corporation and provide the expected returns to the suppliers of the finance – the shareholders and debtors (Shleifer & Vishny, 1997). This conflict of interest arises because of (i) asymmetry of information between the shareholders and managers – where managers are insiders and are better informed about the prospects of the firms, and (ii) moral hazard due to managers self-serving actions – actions like empire building, unproductive expenses, etc – at the expense of the shareholders which are generally dispersed and less informed. Thus, under such circumstances, the corporate governance takes center stage to check the managerial behavior by aligning the interest of the suppliers and consumers of the fund in corporations and businesses – through internal or external control mechanism.

While historically the corporations in developed countries in the West – US & UK – have a dispersed ownership structure, while many other countries bank based economies and developing countries have a problem of concentrated ownership (La Porta et al., 1998). In India, like other Asian economies, concentrated ownership is widespread in firms. Under a concentrated ownership set-up nature of agency, problem differs from the diffused ownership firms, which have more of a Type-I agency problem between the Principal-Agent. While in concentrated ownership environment the agency problem is of Type-II in nature where the conflict is between the majority shareholder (owners/controllers of the firms) and the minority shareholders – the Principal-Principal problem, also known as the horizontal agency problem (Roe, 2004). Since the large shareholders get discretionary power of the affairs of the company by direct or indirect control over the management of the firm, they are generally seen to take advantage through minority shareholder for their private benefit with the help of tunneling, earnings management, and empire building, etc.

The scenario of minority shareholders expropriation becomes, even more, serious when there is opacity in the control and cash flow rights (Morck & Yeung, 2004). This opacity is generally created through cross-holding, and pyramidal ownership structures, which is very widespread in firms with a high concentration of family run business, like India (Sarkar & Sarkar, 2008).

However, the presence of concentrated ownership has some benefits for the firms as well, which is explained by the "alignment hypothesis" or the "convergence of interest theory" (Jensen & Meckling, 1976; Morck et al., 1988). According to the alignment hypothesis the concentrated ownership help increase the overlap between the control and ownership which in turn motivates the management to align their motives and interests with the disperse shareholders. But, in countries with weak legal and regulatory environment, the concentrated ownership becomes an issue with very high likelihood of problems of this high control translating into minority interest expropriation by the large shareholders (Gomes, 2000; La Porta *et al.,* 1999) – referred to as the promoters in the Indian context. These issues emerging out from the concentrated ownership and control is explained by many competing theories in the literature, viz – the "conflict of interest hypothesis", the "strategic alignment hypothesis" and the "entrenchment hypothesis".

Another stream of literature which talks about the presence of large block holders which are not the promoters but hold a large chunk of shareholding in the firms which have higher motivation and interest of monitoring and controlling the dominant shareholders (the promoters). However, according to researchers like Sarkar & Sarkar (2000) and Khanna & Palepu (2000), who look at the cost and benefit of the presence of large block holders and their role in improving the corporate governance of firms, find that the absence of strong legal and judicial system, along with a weak takeover markets, underdeveloped capital and bond markets, and poor information and reporting of firm performance specific parameters the effectiveness of block holders in developing markets in controlling the managerial behavior may not be as effective as they are for developed countries. Thus, the existence of highly concentrated promoter holding in firms in India is certainly an open issue in corporate governance literature which would need further empirical and theoretical investigation.

2.2. Shareholder Classification in India

Since 2006 in India the shareholders are broadly classified into two broad heads – those belonging to the promoter/ promoter groups and the rest who do not have any familiarity or formal business or bloodline relationship with the promoter/ promoter groups, better known as the public shareholders. Promoter/ Promoter groups are further classified into Indian promoters and foreign promoters. Indian promoters can be private individual/institution, a group of individuals/institutions or the government. On the other hand, public shareholders have a wider classification in place. A public shareholder can be a retail investor, a retail block holder, domestic financial institution (non-bank), domestic financial institutions (banks), foreign institutional Investors, etc.

According to the clause 2(a), (Issue of Capital and Disclosure Requirements) Regulations, 2009 of SEBI promoter is defined as (a) person or persons who are in control of the issuer; or (b) person or persons who are instrumental in the formulation of a plan or program pursuant to which specified securities are offered to public; or (c) the person or persons named in the offer document as promoters. "Promoter group" inter alia includes promoters, their immediate relatives (spouse, parents, siblings, children of the person or that of spouse) and anybody corporate in which 10% or more of the equity share capital is held by the promoter or an immediate relative of the promoter or a firm or Hindu Undivided Family (HUF) in which the promoter or any one or more of his immediate relative is a member. Those shareholders falling outside the scope of Promoter / Promoter Group definitions are considered to be public shareholders.

2.3. Definition of Promoter

Although Companies Act 1956 was silent on the definition of promoters, the first written definition was brought in by the clause 2(za) of SEBI (ICDR) Regulation, 2009 – which defined the "promoter" as:

"(i) the person or persons who are in control of the issuer;

(ii) the person or persons who are instrumental in the formulation of a plan or program pursuant to which specified securities are offered to public;

(iii) the person or persons named in the offer document as promoters."

According to the new Companies Act, 2013, the definition brought in by S. 2 (69) of the Companies Act, 2013 says that "promoter" means a person -

"(i) who has been named as such in a prospectus or is identified by the company in the annual return referred to in section 92; or

(ii) who has control over the affairs of the company, directly or indirectly whether as a shareholder, director or otherwise; or

(iii) in accordance with whose advice, directions or instructions the Board of Directors of the company is accustomed to act"

And according to the SEBI's discussion paper on the promoter reclassification is – a person either in control of company affairs, or who is instrumental in the formulation of the firm or who is named as promoter in the offer document.

Source: SEBI discussion paper on promoter reclassification

2.4. Snapshot of Promoter holding complexity in Indian firms

Firms in India are plagued with high ownership rights as majority of the firms are a family business or group affiliates. These firms are interlinked through cross holdings and pyramidal structure, which creates a wedge between the control rights and cash flow rights in these firms. This control wedge is often termed as the "opacity" of the ownership of firms, and is prevalent in firms with too many subsidiaries. Apart from the ownership wedge, due to the division of business families over time, we witness to fragmented promoter ownership where we may see even many shareholders classified as promoters but having shareholding as low as 1%. And to add to the complexity, there would be a separation of brothers/ families, marriage of daughters in some other business houses, etc. All this makes it very difficult for the common investor to understand the ownership composition of firms in India. One may refer to the works of Sarkar (2010), Chakrabarti *et al.* (2008), Kumar (2004), Rao & Guha (2006).

3. RESEARCH METHODOLOGY

A descriptive, theoretical research approach has been chosen for analyzing the genesis of the regulation, discussing its key highlights and identifying the opportunities for future research. Secondary data sources (scholarly research papers, analytics review, blogs, websites of stocks exchanges - NSE/BSE, and SEBI and company websites) have been used for collecting the data for the discussion. Three recent cases of conflict between regulator and firms on the reclassification of promoter as public shareholder have been studied and discussed and a has conceptual paper has been developed.

4. DISCUSSION AND ANALYSIS

To adhere to the Minimum Public Shareholding regulation some firms had reclassified certain promoters as public shareholders to which SEBI has raised concerns. The issue was discussed in the Securities Appellate Tribunal (SAT). After hearing to the cases SAT had instructed SEBI to come up with a more detailed and clear guidelines for promoter reclassification. The paper discusses three such cases at length below.

Gillette India Limited: When the Minimum Public Shareholding Regulation was introduced in the year 2010, Gilette had a promoter holding of 88.76%. Of these 88.76% shares, Procter & Gamble owned 75.90% shares while S K Poddar group was having close to 12.9% shares and both were official promoters of the listed entity. To adhere to the regulation of minimum of 25% free float of shares, the firm had to dilute 13.76%. According to the decision taken by the Gillette board on this issue, Poddar group was expected to transfer 4% of its holding to the parent firm (P&G) at a premium of 25%. They would then give away some of their statuary rights and privileges of the promoter in the firm and re-classify themselves as public shareholders of the firm. Then the Indian subsidiary, Gillette (India) would sell the 4.9% of its shares by Offer for Sale method to comply with the regulation.

However, SEBI had reservations with this arrangement of the firm for attaining the minimum public shareholding and did not allow the reclassification of SK Poddar group as public. The case was appealed at SAT in which SEBI's view was upheld, and Gillette had to resubmit its promoter stake dilution proposal which was conditionally accepted by SEBI for the sake of MPS adherence but wanted the

Poddar group to reduce later the shareholding to less than 5% and play no part in the firm's management and proceedings.

However the tribunal also asked SEBI to clarify the norms on re-classification of Promoter/Promoter group into public shareholder as the existing regulation was not clear and it was the duty of the regulator to lay down clear guidelines. And based on that SEBI had to undertake this regulatory change, where the motive was to lay down clear guidelines and regulation for such reclassifications.

Gokaldas Exports Limited: Similarly, in yet another foreign promoter owned Indian firm – Gokuldas Exports Ltd, in which Blackstone, a US-based private equity company, holds 57.77% stake classified under promoters. Individuals from Hinduja group were part of the Indian promoters of the firm, owning close to 20% equity in the firm. As per the regulatory requirement of minimum pubic shareholding, the firm had to dilute 13.27% of promoter holding. The company to comply with this regulation re-classified the individuals from the Hinduja group as public shareholders – was rejected by SEBI and the matter was dragged into SAT again.

Reliance Power Limited: Another case was of Reliance Power Limited. In the company's offer document, Anil Ambani did not classify his brother Mukesh as a promoter. He was re-classified as a public shareholder and the matter was controversial according to the then guidelines and definition of the promoter by SEBI.

4.1. Impact of the Proposed Change in Regulation

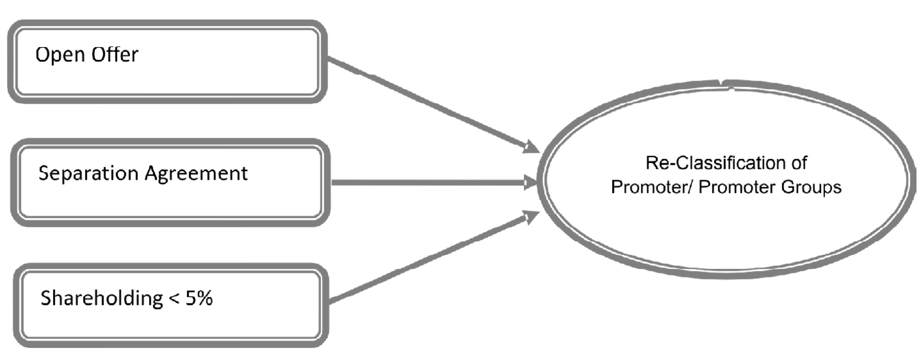
As, per SEBI guidelines, promoters of firms may reclassify themselves as public shareholders provided they fall under any of the following three general conditions:

(i) There is a change in promoter

(ii) Death of person named as promoter

(iii) When a company wishes to be professionally managed.

The central precepts of the regulation are highlighted in the annexure of the paper for reference.



We analyze all the above scenarios, the merits and caveats to understand the implications of this regulatory move closely.

When there is Change in Promoter: This scenario of change in promoter may arise in a company when another firm takes over the target firm's ownership control through acquisition of the majority stake in the firm or an open offer, in agreement with the SEBI's regulations on takeovers. However, this is a necessary but not sufficient condition for a promoter/promoter group to be eligible for getting it re-classified as a public shareholder. They would need to fulfill the following two conditions as well:

(i) The shareholding of the outgoing promoter should be less than 10%, and

(ii) The outgoing promoter would need to get approval of the company's shareholders by calling a general meeting.

However, if one analyses this carefully, he/she would realize that these two conditions imposed by SEBI are perplexing and unnecessary in this case. Since there are no barriers for any individual or entity to be named it as promoters why should there be entry barriers. Also, the exit option has cost implications in calling a general meeting and getting the shareholders' approval. The regulation does not shed any light on cases wherein the promoter having more than 10% equity ownership and manages to get shareholders' approval for reclassification. Moreover, there may be instances wherein the target firm's promoter/promoter group is having promoters' equity holding of less than 10% and was never more than 10% in their lifetime. In such cases if an acquirer acquires the equities of that particular promoter/promoter group, then in that case does the promoter again need to go for voting by calling a general meeting of the shareholders of the target firm, for converting themselves to public shareholding if the acquirer have bought the shares as part of its investments only and did not want to be part of the management? Another issue lies in the rationale for fixing a cap of 10% - does that signify anything, or solve any lacuna in the existing corporate governance framework of the Companies Act or the Clause-49 of the Listing agreement - this would certainly need further research and investigation. Secondly, if for a minor stake the outgoing promoter have to invest heavily in arranging for a general meeting for re-classifying itself into public shareholder, does this extra pain and investment de-motivates the dormant promoters from getting themselves out of the firm's promoters list which would overall reduce the promoter holding in Indian firms which currently is very high impaired to developed countries.

SEBI also imposed a condition for re-classification as a public shareholder, on the key management positions of the outgoing directors in the target company once they are classified as public. According to this condition the former promoter cannot hold the key managerial position for more than three years after the re-classification. At one hand it sounds good, as it will help resolve cases like Vijay

Mallya vs. Diageo like instances in future. On the contrary the demerits can be many – there are cases where some key management position is well managed by someone from the outgoing promoter group and the acquirer may like him/her to continue in order to manage the business well, or they may realize in the future that he could manage the business well by holding some key management position, which according to the new regulation is absolutely not possible.

Promoter by way of inheritance: In cases of inheritance caused by the death of promoter or other kinds of transmission or succession, the next inheritor shall be considered as a promoter, in all instances. This was in line with the clause 10 of the Takeover Regulation, which gives an exemption of making an open offer in such cases and the inheriting shareholder by default becomes the replacing promoter of the firm.

Re-classification when no identifiable promoter: In cases where the promoters have no intentions of control owing to any reasons what-so-ever, may choose to give the firm's control in the hands of professional managers and sit outside the board with its stake as a block holder or retail shareholder. In such cases, it has been mandated by the regulation that all the existing promoters/promoter groups must have less than 1% equity stake in the firm. However, the upper caps for institutional investors for such firm have been kept as a maximum of 10%.

The only problem with this sub-clause is the 1% cut-off for the existing promoters after offloading their promoter tag. Although a promoter may want to be out of the helm of the affairs of the company at any point in time, but would certainly like to hold some good percentage of stocks in the company which he nurtured and built over his lifetime. The less that 1% cap on promoter holding seems way too less and will discourage them from making firms professionally for businesses which are giving decent returns or having good growth prospects.

SEBI has also mandated such outgoing promoters not to be holding any key managerial positions in the firm, for more than three years from the date of exercising the declassification option. After having less than 1% stake in the firm, this does not matter much if the firm is getting managed by the erstwhile promoter or any other professional manager as her cash flow rights are so less that he would not be in a position to take any undue advantage of his position. However, another school of thought may argue that if the promoter wants to declassify as public shareholding why should she be interested to be in the helm of the firm affairs by holding key managerial position for any longer than three years.

Additional Conditions: Apart from the pre-conditions mentioned above SEBI also wants promoters to meet some additional conditions if they wish to declassify themselves as public shareholder in the firms, like:

- The outgoing promoter should not have any direct or indirect special rights in the firm though any formal or informal arrangements.

- The reclassification of promoters cannot be used by firms for adhering to the minimum public shareholding regulation of the listing agreement - Section 19A of the SCRA.

This is interesting to note that the terms of "direct or indirect" and "formal or informal" association or arrangements are very vague and subjective terms and should be clarified further. This would not only create cases of dispute between the treatments given on a case by case basis. This would also create unnecessary confusion and speculation in the market as the all the information on which SEBI's decision would be based may not be readily available in public domain. Thus, there is a need for more adding clarity and objectivity to this sub-clause to bring transparency in the system and stop unnecessary speculation in the market.

Additionally, SEBI's decision of not considering such reclassifications for adhering to the minimum public shareholding requirement for continued listing, sound little too harsh on the firms. As doing this creates a third category of neither shareholder who is neither promoters nor public shareholders, which is unfair. But this declassification holds true for only calculating the promoter shareholding for the MPS requirement but for all other practical purposes they would be considered as a public shareholder, the intent to which has to be made clear by SEBI - as this was the genesis of the whole exercise of framing the regulation for promoter reclassification.

4.2. Implications of the Regulation to Various Stakeholders

The regulation, which has genesis in another regulation which was meant for reducing the over dominance of the promoters in some firms in India, with the help of mandated promoter holding reduction to 75% for continued listing, can be seen as a step closer to an environment with better minority shareholder protection in India. This regulation would have broad implications which would not only touch the board but all the stakeholders of the firm – the shareholders, suppliers, competitors, creditors, and the employees.

To begin with, from the investors' point of view, this proposed change in regulation should be seen as an step closer to making the already complex web of ownership and control in Indian firms more transparent and informative, where these promoters who are not acting in the management decision but are only adding up to the numbers because they are labeled promoters may change their status and the actual ownership and active promoter holding of the firm will get visible to the investors – especially the dispersed shareholders.

From the promoters point of view, the proposed regulation is also seen to help those who are looking for an exit opportunity from the helm of affairs of the firm, but are not doing the same as the existing regulation is so tortuous which does not give them easy options to shed the promoter tag.

The regulation would also help some firms which wish to be professionally governed without any promoters. This at times becomes very useful for the 2nd or 3rd generation firms where the promoters want to fully concentrate on their own business initiatives and let loose the control of the old business and only be public shareholders – which not only gives them extra time to concentrate and grow their current ventures but also protects them from the fiduciary duties of the old firm, being a named promoter of the firm – even if they are actively involved in the day-to-day proceedings of the board.

4.3. Direction for Future Research

This is a unique regulatory move which will change set a change in the present composition of promoter holdings in India – especially after the introduction of Companies Act 2013 (Reference section 2(69)), which have stressed on the fiduciary duties of the promoters and made them more liable for any wrongdoings in the firm decisions. This would not only reopen fundamental research questions of understanding the composition of the ownership holdings of Indian firms, especially in the context of complex business groups and family businesses but also act as an exogenous shock to the promoter holdings. Such a unique exogenous shock can be a very lacerative to test many competing theories in the field of corporate governance, capital markets and organizational and strategic management theories. For example, if the 1st generation owner-managers/ promoters like Mr. Narayan Murthy of Infosys or the Mr. Azim Premji of WIPRO wishes to declassify themselves as promoters from their respective firms. One can look at such instances and see the impact of such declassifications of successful promoters as public shareholders on the stock returns, firm's governance and performance, etc.

Researchers may also look at researchers who do a comparative study of the impact of any such regulatory change in developed countries. They may compare and contrast the outcomes by the help of many cultural, organizational and behavioral theories.

5. CONCLUSION

This regulatory change, no matter what its genesis may be, is a welcome move from SEBI in making the ownership structure of Indian firms less complicated. Since in the lack of any existing regulations or guidelines on promoter declassification, it was tough for Promoters in India to give away their promoter tag and be part of any firm as an investor ant any given point in time. Secondly, in the Indian complex social and cultural marital set-up the previous set of regulations forced many individuals to have the promoter tag even without being at the helm of affairs even remotely. It also helps many promoters who own a very meager proportion of promoter stake that she never becomes the part of decision making in the boards or does not hold any key positions but have all the fiduciary duties of the promoters.

Prima facie, the regulation has many positive implications for the investors, firms and promoters. Though very expensive and tortuous to implement, the regulation, at least, opens up the doors for some more formal promoter exit options in which the control of the firms may not always change, but the promoter holdings would change which would have information of unique type. How does the market react to such moves? Does that make the existing complex web of ownership control more transparent in Indian firms? Does that help setting up more professionally run businesses in India? Does the regulation help in decreasing the concentrated ownership and control in a family run and business group firms? These are few questions from the plethora of research questions which it will set open for inquiry and further empirical investigations in the days to come. However, amendments are needed at many places to make the regulation lucid, more objective and precise for promoters if the intent of SEBI is to reduce the high promoter holding from the firms in India.

Note

1. Free-floating share is a percentage of the total capital of a company that is available for trading in the stock market or part of a company's shares that are tradable without limitation. And it is a figure that is obtained from deduction of non-tradable shares from the total number of shares of the company. This definition was first presented by Salmon (1989).

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ANNEXURE

The Regulation

Disclosure of Class of shareholders and Conditions for Reclassification

"31A. (1) All entities falling under promoter and promoter group shall be disclosed separately in the shareholding pattern appearing on the website of all stock exchanges having nationwide trading terminals where the specified securities of the entity are listed, in accordance with the formats specified by SEBI.

(2) The stock exchange, specified in sub-regulation (1), shall allow modification or reclassification of the status of the shareholders, only upon receipt of a request from the concerned listed entity or the concerned shareholders along with all relevant evidence and on being satisfied with the compliance of conditions mentioned in this regulation.

(3) In case of entities listed on more than one stock exchange, the concerned stock exchanges shall jointly decide on the application of the entity/ shareholders, as specified in sub-regulation(2).

(4) In case of transmission/succession/inheritance, the inheritor shall be classified as promoter.

(5) When a new promoter replaces the previous promoter subsequent to an open offer or in any other manner, re-classification may be permitted subject to approval of shareholders in the general meeting and compliance of the following conditions:

(a) Such promoter along with the promoter group and the Persons Acting in Concert shall not hold more than ten per cent of the paid-up equity capital of the entity.

(b) Such promoter shall not continue to have any special rights through formal or informal arrangements. All shareholding agreements granting special rights to such entities shall be terminated.

(c) Such promoters and their relatives shall not act as key managerial person for a period of more than three years from the date of shareholders' approval: Provided that the resolution of the said shareholders' meeting must specifically grant approval for such promoter to act as key managerial person.

(6) Where an entity becomes professionally managed and does not have any identifiable promoter the existing promoters may be re-classified as public shareholders subject to approval of the shareholders in a general meeting. Explanation.- For the purposes of this sub-regulation an entity may be considered as professionally managed, if

(i) No person or group along with persons acting in concert taken together shall hold more than one per cent paid-up equity capital of the entity including any holding of convertibles/outstanding warrants/ Depository Receipts:

Provided that any mutual fund, bank, insurance company, financial institution, foreign portfolio investor may individually hold up to ten per cent paid-up equity capital of the entity including any holding of convertibles/outstanding warrants/ Depository Receipts.

(ii) The promoters seeking reclassification and their relatives may act as key managerial personnel in the entity only subject to shareholders' approval and for a period not exceeding three years from the date of shareholders' approval.

(iii) The promoter seeking reclassification along with his promoter group entities and the persons acting in concert shall not have any special right through formal or informal arrangements. All shareholding agreements granting special rights to such outgoing entities shall be terminated.

(7) Without prejudice to sub-regulations (5) and (6), re-classification of promoter as public shareholders shall be subject to the following conditions:

(a) Such promoter shall not, directly or indirectly, exercise control, over the affairs of the entity.

(b) Increase in the level of public shareholding pursuant to re-classification of promoter shall not be counted towards achieving compliance with minimum public shareholding requirement under rule 19A of the Securities Contracts (Regulation) Rules, 1957, and the provisions of these regulations.

(c) The event of re-classification shall be disclosed to the stock exchanges as a material event in accordance with the provisions of these regulations.

(d) Board may relax any condition for re-classification in specific cases, if it is satisfied about non-exercise of control by the outgoing promoter or its persons acting in concert.

(8) If any public shareholder seeks to re-classify itself as promoter, it shall be required to make an open offer in accordance with the provisions of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011."