

गवर्नर  
GOVERNOR



भारतीय रिज़र्व बैंक  
केन्द्रीय कार्यालय  
बम्बई

RESERVE BANK OF INDIA  
CENTRAL OFFICE  
BOMBAY

April 20, 1993

G.B.1/ /93

Dear Dr Manmohan Singh

Kindly recall that the Government had constituted a Committee on Disinvestments of Shares in PSEs on 26th February, 1992 under the Chairmanship of Dr.V.Krishnamurthy. While some background work was done by the Committee, it had not completed the Report.

2. The Government subsequently reconstituted the Committee with me as the Chairman and Dr.Y.Venugopal Reddy, Joint Secretary (Investment) as the Member-Secretary in November 1992. The Committee was expected to submit its Report in a few days.

3. Considering the complexities involved and the need to clearly set out the recommendations consistent with economic reforms, it took longer than anticipated to complete the Report.

4. I am forwarding herewith a copy of the Report, which I hope the Government would find it useful.

5. I also take this opportunity to place on record my deep appreciation of the fullest cooperation rendered by all the Members. I must record my special appreciation of the assistance rendered by its Member-Secretary, Dr.Y.Venugopal Reddy who has brought to bear on the Report his rich background of knowledge on the privatisation process in many countries.

With kind regards,

Yours sincerely,

C R - , -

(C.Rangarajan)

Encl : as above.

Shri Manmohan Singh,  
Finance Minister,  
Government of India,  
Ministry of Finance,  
NEW DELHI.



# REPORT OF THE COMMITTEE ON DISINVESTMENT OF SHARES IN PUBLIC SECTOR ENTERPRISES

## 1. INTRODUCTION

1.1 It has been decided by the Government of India that the scheme of disinvestment of equity in public sector enterprises which commenced in 1991-92 would continue through 1992-93. In view of the above, the Ministry of Finance, Department of Economic Affairs vide their Office Memorandum No.14/1/SE/92 dated 26.2.92 had appointed a Committee with Shri V. Krishnamurthy, Member, Planning Commission as its Chairman, with Sarvashri K.P. Geetha Krishnan, Montek Singh Ahluwalia, Suresh Kumar, Ashok Desai, S.S. Nadkarni as Members and Shri Kamal Pande of Department of Economic Affairs as its Member Secretary. The terms of reference of the Committee are as follows :

- (i) To devise criteria for selection of Public Sector Enterprises for disinvestment during 1992-93;
- (ii) To advise on limits on the percentage of equity to be disinvested in respect of such Public Sector Enterprises;
- (iii) To suggest the target clientele including Mutual Funds, Financial Institutions, Banks, Employees, Resident Investors, Non-Resident Indians, Foreign Institutional Investors etc.;
- (iv) To make suggestions on the modus operandi of disinvestment, whether through public offers or private placements;
- (v) To lay down the criteria for valuation of equity shares of Public Sector Enterprises;
- (vi) To make recommendations on any other subject matter germane to the disinvestment plan.

1.2 The Committee held three meetings on March 31, 1992, April 24, 1992 and May 13, 1992. On the advice of the then Governor of Reserve Bank of India, the Committee temporarily co-opted Mr. D. Basu, Deputy Managing Director, State Bank of India, as Member because of his expert knowledge on this subject. The Committee also had the benefit of detailed analysis done by the officers of the Department of Economic Affairs and Department of Public Enterprises.

1.3 The Government reconstituted the Committee in November 1992 with Dr. C. Rangarajan, Member, Planning Commission as Chairman and Dr. Y. Venugopal Reddy as Member Secretary. The Chairman and Member Secretary held informal meetings with some members of the Committee; discussed issues with selected managers of PSUs; perused recent publications, reports of seminars, letters/suggestions received from individuals, institutions, trade union leaders at Ministry of Finance; obtained the advice of Chairman, SEBI in the light of subsequent developments; sought advice of Dr.L.C. Gupta of The Society for Capital Market Research and Development; and drew upon the research work already conducted by the Institute of Public Enterprise, Hyderabad. The Committee then met on December 31st 1992 and January 1, 1993 for detailed discussions.



1.4 In its general approach, the Committee was guided by several important factors such as :

- (a) the contributions made by the public sector in general to economic development, and entrepreneurial skills;
- (b) the institutional, technological and fiscal compulsions that have led to a review of public sector investment;
- (c) the experience gained in disinvestment in the recent past, taking into account the unusual circumstances in capital markets;
- (d) the need to enhance the competitive strength and ensure expansion of these enterprises while protecting the interests of workers; and
- (e) above all, the requirement of consistency with the ongoing economic reforms in the areas of industrial licensing, foreign trade and investment and financial sector.

## 2. CRITERIA FOR SELECTION OF PUBLIC SECTOR ENTERPRISES FOR DISINVESTMENT DURING 1992-93.

2.1 The Committee noted that the Government disinvested its shareholding in 30 Public Sector Enterprises during 1991-92. The extent of disinvestment worked out to about 8% of the Government shareholding in these enterprises and the total amount realised was Rs.3038 crores.

2.2 The present status of disinvestment during 1992-93 may be summarised as follows:

- (a) Advertisement was given inviting tenders for purchase of shares of 8 Central PSUs, namely, Steel Authority of India Limited, Bharat Petroleum Corporation Limited, Hindustan Petroleum Corporation of India Limited, Hindustan Zinc Limited, Rashtriya Chemicals and Fertilizers Limited, HMT Limited, National Aluminium Company Limited and Neyveli Lignite Corporation of India Limited. The last date for receipt of tenders was extended to 14.10.1992, to enable a wider response.
- (b) A minimum reserve price was fixed on the basis of recommendations of three merchant bankers - Industrial Credit and Investment Corporation of India, Industrial Development Bank of India and SBI Capital Markets Ltd.
- (c) Having this criterion, the bids eligible for acceptance amounted to a total sale value of Rs.681.95 crores for 12.87 crore shares in the eight companies.
- (d) Advertisement was again issued on November 28, 1992 for disinvestment of shares in 14 PSEs. The extended terminal date for reviewing the bids was December 22, 1992. The bids for 12 of these companies for a value of Rs.1183.3 crores were accepted. The average price realisation per share disinvested in the second round was substantially lower than the price realised in October 1992.
- (e) The government invited a third round of bids for sale of equity in 15 PSEs for a total of 553 million shares in March 1993. While bids were received, it was



decided to accept bids for a total of 10.1 million shares only aggregating to Rs. 46.73 crores. The referral price was fixed as earlier on the recommendations of the three agencies.

- (f) The government has also decided in principle to disinvest shares in selected companies in favour of employees during 1992-93.

2.3 The Committee further noted the following features relevant to the policy of disinvestment for the rest of the financial year:

- (a) The financial year 1992-93 is about to end.
- (b) Though listing of shares of many PSEs has been completed, there is little or no trading in most of them. In fact, many of the mutual funds and financial institutions which have acquired PSE shares have not been able to sell them in the market. This could adversely affect forthcoming tranches of disinvestment.
- (c) The weaknesses in stock markets such as low trading volumes and non-transparent trading practices have come to the fore. The Stock markets themselves have shown unusual volatility.
- (d) As of now, it has to be recognised that there is no trading history for most public enterprise shares.
- (e) The restricted tendering and handling of shares had to be resorted to in the past due to unusual circumstances but more recently, enterprise - specific bids have been invited and financial limits for bidding have also been lowered.
- (f) It is generally agreed that a public issue by way of an offer to the members of public would be the most desirable option. However, if time and market circumstances do not permit it, bid mechanisms close to a public offering should be devised.

2.4 By the time this Report was finalised and submitted, the new financial year has commenced.

### 3. LIMITS ON THE PERCENTAGE OF EQUITY TO BE DISINVESTED

3.1 The Committee recognises the need to broadly indicate the objectives that are sought to be achieved through disinvestment in public sector equity :

- a) As an immediate objective to mop up resources of non-inflationary character to meet the budgetary needs which include requirements of developmental activities and social obligations.
- b) To subserve, in the medium term, the overall fiscal objective of gradually reducing the fiscal deficit and bringing about a positive overall impact on future liabilities and income flows to Government.
- c) To improve the overall economic efficiency by bringing about a more competitive atmosphere with emphasis on the cost and quality of product and service to the customers of public enterprise sector.
- d) To enhance the efficiency of individual enterprises by imparting a new



dynamism in the management of these enterprises through diversification of ownership and control as also larger and freer access to the expanding capital markets in India.

- e) To realign the extent of ownership, control and regulation in different activities consistent with the technological needs and developments in Industrial Policy.

**3.2 The Committee, therefore, recommends that limits to the level of disinvestment should be derived from the target level of government ownership in each enterprise in the medium term. Thus :**

- (a) The target levels of ownership could be zero; 26% to ensure limited control over special resolutions brought in general body meetings of the enterprise; 51% to have effective control and 100% for full ownership.
- (b) While determining the final level of government ownership, it must be recognised that there may be group specific or enterprise-specific intermediate levels of disinvestment depending on the state of preparedness of each enterprise, stock market conditions and the requirements of government.
- (c) The desirable levels of public ownership may be reached with greater advantage to PE concerned and government by expanding the equity base through public offering than disinvestment.
- (d) The economic efficiency and financial gains to government through disinvestment in respect of each tranche in each enterprise need to be continuously assessed so that there is no compulsive disinvestment merely to reach the target levels of ownership by government.

**3.3 The Committee recommends the following considerations in determining the target level of disinvestment :**

- (a) Target level of disinvestment for the medium term (say 5 years) should be derived from desirable level of public ownership in an activity or unit consistent with Industrial Policy.
- (b) Target level of ownership should be attained through disinvestment after fully recognising the preparatory actions mentioned in para 3.6 below.
- (c) The target level of ownership in respect of all units reserved for public sector should be 51% to enable control over management. A target level of 26% of public ownership may be considered in exceptional cases. Such cases may include enterprises which currently have a dominant market share or where separate identity has to be maintained for strategic reasons. In others, it could be zero.
- (d) There should be a set of specific reasons for continued government ownership of enterprises except in sectors which are reserved for public ownership. In all other sectors, government should justify its continued holding of equity on considerations as an investor and not as owner. The government may hold more than 26% of the total equity in enterprises with outstanding prospects, but the investment would need to be justified on the basis of growth potential and the scope for larger realisation and not on the basis of desirability of government



control. The effort should, therefore, be to disinvest the holding at the best available price at the opportune time.

3.4 Arising from the above, the Committee considers that the percentage of equity to be disinvested should be generally under 49% in industries reserved for the public sector and over 74% in other industries.

3.5 In realising such target levels, no yearwise target for disinvestment need be rigidly prescribed but action plans have to be evolved as indicated in Chapter 7 of the Committee's Report.

**3.6 The Committee strongly recommends the following preparatory steps :**

- (a) Where the PSE is not in a company form, (i) determine whether it should be converted into a single or multiple companies; (ii) decide upon the capital structure differentiating between debt and equity; and (iii) evaluate whether an independent Regulatory Commission should be established for the concerned sector and, if necessary, put such a Commission in place.
- (b) Estimate firmly the ongoing investment plans for expansion or modernisation or technical collaboration.
- (c) Project the pattern of financing of such expansion through additional debt or expanded equity.
- (d) Review existing debt-equity structure including scope for bonus issue to government to capitalise accumulated reserves where the reserves are disproportionately large in relation to the paid-up capital; where loans are disproportionately high, review scope for conversion of such loans into equity or consider other ways of distributing/lowering the burden of debt so as to keep the equity base at a level attractive to the capital market.
- (e) Examine the feasibility of issuing convertible bonds as a measure of raising adequate resources for the PSEs.
- (f) Decide in the light of the above, the desirable level of equity base and the targeted level of government ownership.
- (g) Settle the modalities and accounting procedures for settlement of large arrears, if any, of dues payable/receivable between PSEs and the government, among the PSEs or between PSEs, government and financial institutions.
- (h) Appoint a merchant banker for each of the PSEs to assist in initiating some of the preparatory measures mentioned above.
- (i) Arrange to create a market-friendly image for PSEs by projecting and publicising the strong points of each PSE among the investing public in advance of the next disinvestment exercise.

**3.7 In making the above recommendations, the Committee explicitly recognised the following :**

- (a) The introduction of 'Golden Share' as in UK, where government holds a share with special voting rights amounting to veto in some matters of importance was considered. The Committee felt that there may be constitutional problems of



discrimination and did not pursue it further. Instead, 26% ownership is suggested wherever such control is necessary.

- (b) The current organisational structure of the enterprise viz., whether it is departmental or statutory corporation or company, by itself is not material for determining the target level of ownership. In fact, organisational change, where needed, is part of preparatory work for disinvestment. Similarly, the strategic importance of a unit should not be determined by the nature of the Ministry to which it is affiliated.
- (c) It is possible to visualise asset stripping (i.e. sale of either non-income generating assets or one of the production units in a multi-unit company) by a PSE. This may be one of the preparatory exercises before disinvestment in the case of some enterprises.
- (d) In some cases, it may be necessary to put a regulatory framework in place. In some other cases, the regime of administered prices may have to be altered. Further, the procedures for evaluation of bids for large value contracts by PSEs may need to be changed in some cases so as to let PSEs reap the entire benefits of any credit package for the contracts instead of government sharing such benefits. It is necessary to complete such vital actions before and not after disinvestment.
- (e) The existing status of profitability (or loss) is not material as long as it is ensured that the price realised for shares offered represents a net gain in terms of future cash flows to the government.

#### 4. MODUS OPERANDI OF DISINVESTMENT

4.1 The procedure of bundling shares, combining different public enterprises in lots and restricting the disinvestment in favour of public sector mutual funds, was adopted in 1991-92 as this was the first exercise in disinvestment. For the year 1992-93, the sale of shares was made enterprise-wise and to a wider clientele in order to get optimum benefits.

4.2 There are two acceptable and transparent processes for divestiture of government's shareholding:-

- a) Offering shares of public sector enterprises at a fixed price through a general prospectus. The offer is made to the general public through the medium of recognised market intermediaries.
- b) Sale of equity through auction of shares amongst predetermined clientele whose number could be as large as necessary or practicable. The reserve price for the public sector enterprises' equity is determined with the assistance of merchant bankers.

4.3 In addition, a third method practised worldwide for disinvestment is to transfer the controlling interest in an enterprise to a specific firm or group of persons based on a negotiated price, the entire process being finalised based on certain pre-determined objective criteria.

4.4 Two important considerations for the government in deciding the precise mode



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of disinvestment are the best means to realise the highest price and the best course which would save the highest number of jobs in the enterprise disinvested.

4.5 All the above methods have their own merits and demerits. In the first alternative of 'offer for sale', difficulties may be encountered in estimating and determining the 'fixed' price if it is offered for the first time and the shares have not actually been trading in the stock exchange. On the other hand, this method has the advantage of spreading the ownership widely amongst the general public and in a transparent manner. A pre-requisite for this method is to list the shares of enterprises in the stock exchange and establish a track record of trading. In the case of those PEs for which the first sale of equity is yet to be made, or those where the track record of trading in shares is yet to be established, the tender system would be advantageous. The last method of negotiated sale has the advantage of direct interface with potential new owners so as to specify the manner of future operation of the enterprise to achieve the best social objectives. But it has the demerit of the potential for long drawn out negotiations and allegations of favouritism.

4.6 **The Committee, in the light of experience gathered to date recommends the following modus operandi :**

- (a) Once a reasonable market price is established in a normal trading atmosphere over a reasonable period of time and a public enterprise completes the preparatory work, the fixed price method would be appropriate. In any case, for expanding the equity base through capital markets, the fixed price method has to be adopted.
- (b) In all other cases, the auction method with wide participation may be adopted.
- (c) Close and continuous involvement of public enterprises concerned and the merchant banker appointed for the purpose of devising the modus operandi is essential. In fact, disinvestment should be planned and implemented for each enterprise separately and not in groups.
- (d) PEs should have the freedom to engage merchant bankers and other intermediaries to ensure effective and efficient exploitation of market opportunities.
- (e) Where employee-takeover is involved, appropriate modus operandi would have to be devised, essentially through negotiations.
- (f) Where it is proposed to offer equity stake to existing technical collaborators in the PSEs, it needs to be ensured that such equity link-up is based on strategic considerations. The choice of partner, extent of equity stake, terms of offering, timing etc. would need to be based on objective criteria such as access to newer technology, scope for increasing export turnover and possibilities of setting up third country operations. The modus operandi would thus have to be uniquely devised.
- (g) In respect of PEs which are operating as holding company structures (for example, SAIL) or companies with multiple production units (like the Cement Corporation of India), the modus operandi could be similar but the processes have to be devised in detail and actively implemented by the PE concerned.



- (h) An enterprise-specific approach in the modus operandi, including timing of issue and choosing intermediaries, is essential to meet the needs of the government, the enterprise concerned and stock markets.
- (i) Costs of floatation have to be explicitly assessed, and reasonableness of costs ensured.

4.7 The Committee recommends that 10% of the proceeds appears a reasonable amount to be set apart by the government for lending to the PEs concerned on concessional terms to meet their expansion / rationalisation needs. The Committee recognises the need to use a part of the proceeds of disinvestment for effecting improvements in the PEs concerned in a manner similar to earmarking a part of the gross proceeds for the National Renewal Fund. Such an approach provides incentives to the PE management to augment receipts from disinvestment.

4.8 The Committee also recognised that disinvestment of government equity could be tailored to an informed process of management of external debt of the country. By allowing PEs to swap the entire or a portion of their outstanding external debt with lenders for an equity stake at negotiated prices, the twin benefit of reduction in debt service obligations to the country as well as to the enterprise concerned and a better debt equity gearing for the entity may be achieved.

4.9 The Committee, however, recognised that there are practical limitations to such an approach. Debt equity swaps have been practised as part of privatisation in certain countries with acute problems of debt overhang and servicing. Especially countries which have defaulted on external payment obligation and whose debt is traded in secondary markets at substantial discounts have resorted to this option.

4.10 The Committee concluded that the above factors are not relevant in the Indian context. There is no comparable external debt problem for India. Therefore, there is no practical utility in encouraging recourse to debt equity swaps in the context of privatisation. However, it is recommended that where an individual enterprise finds unique advantages in adopting this approach, such enterprise could be enabled to do so.

## **5. CRITERIA FOR VALUATION OF EQUITY SHARES OF PUBLIC SECTOR ENTERPRISES**

5.1 Valuation of shares in the past was generally based on the guidelines formulated by the Controller of Capital Issues. Currently, however, these are no longer in vogue. In general, three methods for valuation of shares are adopted, viz., Net Asset Value method, Profit Earning Capacity Value method and Discounted Cash Flow method. While the NAV would indicate the value of the assets, it would not be in a position to indicate the profitability or income to the investors. The profit earning capacity is generally based on the profit actually earned or anticipated. The discounted cash flow is a far more comprehensive method of reflecting the expected income flows to the investors. However, in the context of valuation of shares of public enterprises, none of the traditional methods would by themselves be adequate. The special circumstances that require to be assessed in the context of valuation of shares of public enterprises are:

- (a) In the management of the public enterprises, the focus has been on discharging



economic and social responsibilities indicated by the government rather than on projecting profitability to the investor.

- (b) In regard to valuation of some of the assets, the book value might reflect land and other facilities provided to such enterprises at lower than market cost.
- (c) The structure of the debt and equity of public enterprises had not necessarily followed commercial norms.
- (d) Many enterprises have had gains or losses in the past due to the effect of administered prices. Further, recent policy measures are also affecting immediate business prospects of some PEs (e.g. STC due to decanalisation).
- (e) A number of public enterprises have already invested heavily in projects under construction and some of them have ambitious expansion programmes.
- (f) No effort has been made to project in the public eye and in the market, the strengths of these enterprises in the past for a variety of reasons.
- (g) While in some activities such as cement, there are private enterprises whose shares are listed and traded in the market, there are certain other activities where there are no private enterprises involved in the same activity to provide appropriate basis for valuation.

5.2 The Committee wishes to record the following relevant factors in the context of valuation of shares :

- (a) Valuation is a difficult exercise, whether in the private or public sector, in India or in other countries; and more so when there are wide divergences in valuation by different merchant bankers in respect of the same public enterprise.
- (b) The price at which a share can be sold is determined more by investor perception of the worth rather than any mechanical measure of intrinsic worth. Hence the importance of information gathering and full disclosure to generate credibility and investor interest.
- (c) Rise or fall in share values of an enterprise soon after disinvestment does not by itself indicate that shares were underpriced or overpriced at the time of disinvestment.
- (d) Difficulties of valuation in a multi-unit and multi-product scenario have to be reckoned.

5.3 In assessing the intrinsic worth of a share, the Committee recommends the following :

- (a) Among the three criteria viz. net asset value, profit earning capacity value and discounted cashflow value, discounted cash flow has the greatest relevance, though it is the most difficult.
- (b) An explicit assessment of the scope and limits for selling non-income generating assets (land or buildings) and rationalising labour force (Voluntary Retirement Scheme etc.) should be made.
- (c) Government policies affecting future profitability (such as disappearance of



guaranteed offtake or guaranteed rate of return) may have to be spelt out. Such assurances wherever required may be extended only after careful assessment of the implications of such assurances on the economic efficiency rather than immediate attractiveness of the shares to investors.

- (d) The influence of social constraints in the past working of the PEs and the extent of benefit accruing due to provision of certain under-priced facilities like land should be captured and presented. Likewise, costs of projects under construction should be evaluated on a realistic basis and presented while reckoning the intrinsic worth of the PEs.

5.4 As regards investor perception, the Committee recommends the following:

- (a) Each company has to be studied carefully with the help of a merchant banking firm taking into account factors such as value of assets, its market share, potential profit earning capacity and the prevailing price in the market for shares of similar enterprises in the private sector.
- (b) It is essential that the PE and the merchant banker concerned present all positive aspects of the enterprise in the prospectus.
- (c) While fielding PEs in the capital market, the main line of activity of the PE concerned and the extent of investors' fancy for the particular industry at the material time may have to be taken into account.
- (d) In the offering memorandum and during investor presentations, the likely improvements in the efficiency of the PE concerned as a result of changed management attitudes and other relevant factors may need to be emphasised.
- (e) Wherever disinvestment is made through public issues, the offering price would need to be fixed with a close assessment of the need to project the issue as a success to pave way for subsequent offerings and at the same time avoiding any criticism of under-pricing.

## 6. TARGET CLIENTELE FOR DISINVESTMENT

6.1 The Committee adopted the following approach in determining the relative roles of target clientele :

- (a) The target clientele should include Mutual Funds, Financial Institutions, Merchant Bankers, Brokers, Employees of the respective public enterprises, Resident Investors, Non-resident Indian investors, as also Foreign Investors. In fact, there is no necessity to restrict the disinvestment among any particular groups or categories. Ideally, the purpose is best served by the shares being held by the widest cross section of the Indian public.
- (b) Ceilings may be imposed in respect of preferential allotments of shares to the employees in all production/manufacturing oriented companies. However, such preferential allotments should not exceed 200 shares for each employee subject to an overall ceiling of 5%. In the case of "consultancy" companies, preferential allotment to the employees can extend upto 20 per cent again with a ceiling per employee. In case where employee-take-over is sought by employees, the ceilings and payment arrangements could be flexible.



- (c) There can also be a ceiling for allotment if any to non-resident Indian investors or the extent of foreign holding that can be permitted. The same rules as are applicable to NRIs and foreign investors to buy the equity in private industry in India may be extended to the foreign investors to buy shares in PEs.
- (d) The question of reserving a portion of the government shareholding proposed to be disinvested in favour of Foreign Institutional Investors may be considered when the role of FIIs expands in the Indian capital markets.
- (e) It may be desirable to allow shareholding by technical collaborators in PEs on a preferential basis as part of modernisation and expansion. The new Industrial Policy allows foreign equity participation upto 51 per cent in Indian enterprises. Rather than encouraging them to set up new units for the same purpose, it should be open to the existing foreign collaborators to buy into the equity of PEs operating in such areas. The public sector will derive two advantages through this method, viz. (i) continued technological and possibly fresh managerial involvement from foreign collaborators and (ii) scope for optimising the use of existing plant and other facilities to stage a global presence with the help of the foreign collaborators.
- (f) There may be restrictions on the extent of equity sold to particular group of clients. For example, foreign investors may not be allowed to buy more than 24% of equity except on those PEs concluding strategic alliances with overseas firms on terms approved by the government.

**6.2 The Committee, therefore, recommends the following target clientele:**

- A. Where auction method or public offer is adopted, the target clientele should include:
- (i) The general public;
  - (ii) mutual funds;
  - (iii) NRIs and foreign investors on par with general principles governing their participation in the Indian equity market with no reservation for either of the categories;
  - (iv) Reservation restricted to employees who would get upto 200 shares per employee at a discount of 15% on the market price, enabling funding arrangements and a lock in period that is normally prescribed for reserved allocation of shares. While a ceiling is prescribed for each employee, where a trust or cooperative of employees is formed for the specific purpose, individual ceilings could be aggregated for the purpose;
  - (v) under special circumstances, reservation for other stakeholders such as dealers in select activities like fertilisers depending on the extent of interest of such stake-holders, upto 500 shares per applicant at market price and subject to lock-in restriction as normally prescribed for reserved allocations.
- B. In regard to technical collaborations :
- Technical collaborators may be existing or new;
  - emphasis on identification of enterprises that would benefit from conversion into joint venture;



- transparency through competitive offers (i.e. not restricting negotiations only to existing collaborator);
- expanded equity base or disinvestment by negotiated price as well as stock options subject to any SEBI regulations;
- where domestic industrial houses have synergy and offer collaboration arrangements to ensure efficiency, they should be treated at least on par with foreign technical collaborators.

C. Merchant bankers and stock brokers are essentially intermediaries and should not be treated as target-clientele. However, assistance of internationally renowned merchant bankers may be employed if the enterprise concerned expressly requests that this be done. Assistance of such foreign merchant bankers may be useful when foreign collaborations or investments have to be examined (including BIFR cases).

## 7. OTHER ISSUES

7.1 The Committee noted some important lessons of international experience in PSU disinvestment viz.

- (i) In many countries, separate apex agencies have been created to design and implement disinvestment. In some cases, such an agency was established by law, so that the concerned law overcomes existing legal impediments to PE disinvestment.
- (ii) The process of disinvestment was spread over two to three years, and where it was done in a hurry, it resulted in undesirable concentration, sometimes described as crony capitalism.
- (iii) In the case of some countries, where a rigid time-table for disinvestment was caused by prescription of donors, there was an erosion of the negotiating strength of government agencies and possible loss of revenue.
- (iv) Interested parties, including managers, bureaucracy and unions resisted such disinvestment but this was overcome with the chief executives and boards being packed with pro-changers.
- (v) Introduction of competition as part of the process of disinvestment was preferred. Consequently, to ensure competition and protection of consumers' interests, necessary policy/legal changes had to be brought about.
- (vi) Concern with equity considerations has been an important issue in striking a balance between fiscal needs, consumers' interests and workers' welfare, but often special arrangements to protect income flows, if not jobs, were put in place for workers.
- (vii) In some cases, quality of services and access of the poor to services suffered as a consequence of disinvestment but on the whole, results were positive:
- (viii) There has been virtually universal criticism of underpricing of shares wherever disinvestment has taken place. In some cases, floatation costs or gains by financial intermediaries such as underwriters and merchant bankers were considered excessive.



- (ix) Pursuance of multiple objectives blurred proper evaluation of the impact of disinvestment.

7.2 Keeping in view the international experience and our own requirements, a Standing Committee on Public Enterprise Disinvestment is recommended. The Committee may consist of both full and part time members and draw expertise from Government, Public Enterprises, Financial Sector, Professionals and academicians. The Commission's terms of reference may include:

- (a) review of public enterprises with a view to recommending enterprise-specific actions for reform, restructuring and disinvestment;
- (b) suggesting, where appropriate, parameters for selection of Chief Executives, Board of Directors to meet the requirements of reforms;
- (c) identifying the appropriate legal, institutional and procedural arrangements for protecting the interests of consumers, rural or backward areas while transforming organisational form into companies wherever needed and such arrangements may include breaking up of existing monopolies or encouraging new firms to promote competition;
- (d) proposing necessary incentives to enterprises to mobilise support for disinvestment;
- (e) applying the criteria suggested for establishing the percentage of disinvestment in regard to each enterprise;
- (f) providing guidance on modalities of disinvestment appropriate to each enterprise including share valuation;
- (g) monitoring the progress of disinvestment programme; and
- (h) arranging for independent evaluation of the progress of the disinvestment programme.

7.3 The proposed Committee would also be in a position to guide the public enterprises and the government in preparatory measures for disinvestment which include:

- (a) financial restructuring especially debt/ equity, accounting for and the settlement of dues between the government and public enterprises;
- (b) preparatory measures legally required for diversification of ownership including assistance in obtaining lenders' consent (external commercial or aid);
- (c) assessing the medium term corporate plan with special reference to the proposed equity structure;
- (d) ensuring that data is gathered by each public enterprise and prospectus is prepared with due care;
- (e) the employment of merchant bankers, timing and management of issue, listing, share transfer etc.

7.4 The Committee commends for consideration of the government, establishing the Committee mentioned in para 7.2 on a statutory basis in view of the financial



magnitudes involved, multiple ministries concerned, impact on economic reform and the need to monitor use of proceeds of such disinvestment.

7.5 The Committee further commends for consideration, use of part of proceeds of disinvestment not only for National Renewal Fund (which may include financing of retraining of workers to enable redeployment), 10% incentive for PEs, and reduction in Government debt but also for channelling resources to social sectors like literacy, health and employment generation in rural areas.

7.6 The Committee recommends that the following further measures in respect of PEs be initiated to ensure that the objectives of disinvestment are realised :

- (a) Government's expectations from the PEs as majority/dominant shareholders should be documented in the form of MOUs but the focus of these MOUs will be different viz. customers and capital markets.
- (b) With diversified ownership coming into place after disinvestment, reconstituting PEs' Boards with appropriate representation for non-Government Directors as may be necessary.
- (c) Each enterprise should be encouraged to commence work on corporate strategies and plans in alignment with ongoing reform.
- (d) Seminars and workshops could be held for the finance personnel and other senior executives of PEs on the subject of their new role in the liberalised economic environment, their relationship with the government, capital markets and their customers etc. SCOPE could take the initiative in organising such workshops/ seminars with guidance perhaps from SEBI.
- (e) A deliberate policy of 'image-building' through media and projecting performance is also necessary to ensure continuous entry into capital markets for raising resources.

**C. Rangarajan**

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New Delhi,  
April, 1993.