



## Company Law Refresher Course

Broad Overview of provisions pertaining to Capital Structures,  
Rights, Private placements and public offerings



**Janak Bathiya**

# An ever changing law



	2018	2017	2016	2015	2014	2013	Total
Rules	49	23	33	28	40	0	<u>172</u>
Circulars	11	14	16	16	44	4	<u>105</u>
Notifications	32	19	32	15	17	2	<u>117</u>
Orders	3	3	7	3	8	1	<u>25</u>
	<u>95</u>						<u>419</u>

- 30<sup>th</sup> March, 2015 deposit relief
- 5<sup>th</sup> June, 2015 exemption notifications (13<sup>th</sup> June, 2017 amendment)
- Companies Amendment Act, 2015
- Insolvency and Bankruptcy Code 2016
- Companies Amendment Act, 2017 implemented in parts starting 2018
- Companies Amendment Ordinance 2018 (approved by loksabha) re-promulgated as Companies Amendment Ordinance 2019

*Legal stability and predictability are a fundamental part of “what people mean by the Rule of Law” (Schwarzschild 2007, 686). In the absence of stability and predictability in law, citizens have difficulty managing their affairs effectively (Eskridge and Frickey 1994).*

## ***Net no. of sections in the CA, 2013***

<b>Total no. of sections in the Companies Act, 2013</b>	<b>470</b>
<b>Number of sections omitted by:</b>	
The Companies (Amendment) Act, 2015	1
The Insolvency and Bankruptcy Code, 2016	39
The Companies (Amendment) Act, 2017	3
<b>Number of new sections inserted by:</b>	
The Companies (Amendment) Act, 2015	1
The Finance Act, 2017	1
The Companies (Amendment) Act, 2017	3
The Companies (Amendment) Ordinance, 2018	2
<b>Net no. of sections</b>	<b>434</b>

# Key Take-Aways



• Kinds of share issues- Private Placement and Public Offer



• Provisions in relation to Demat of Shares



• Kinds of Share capital

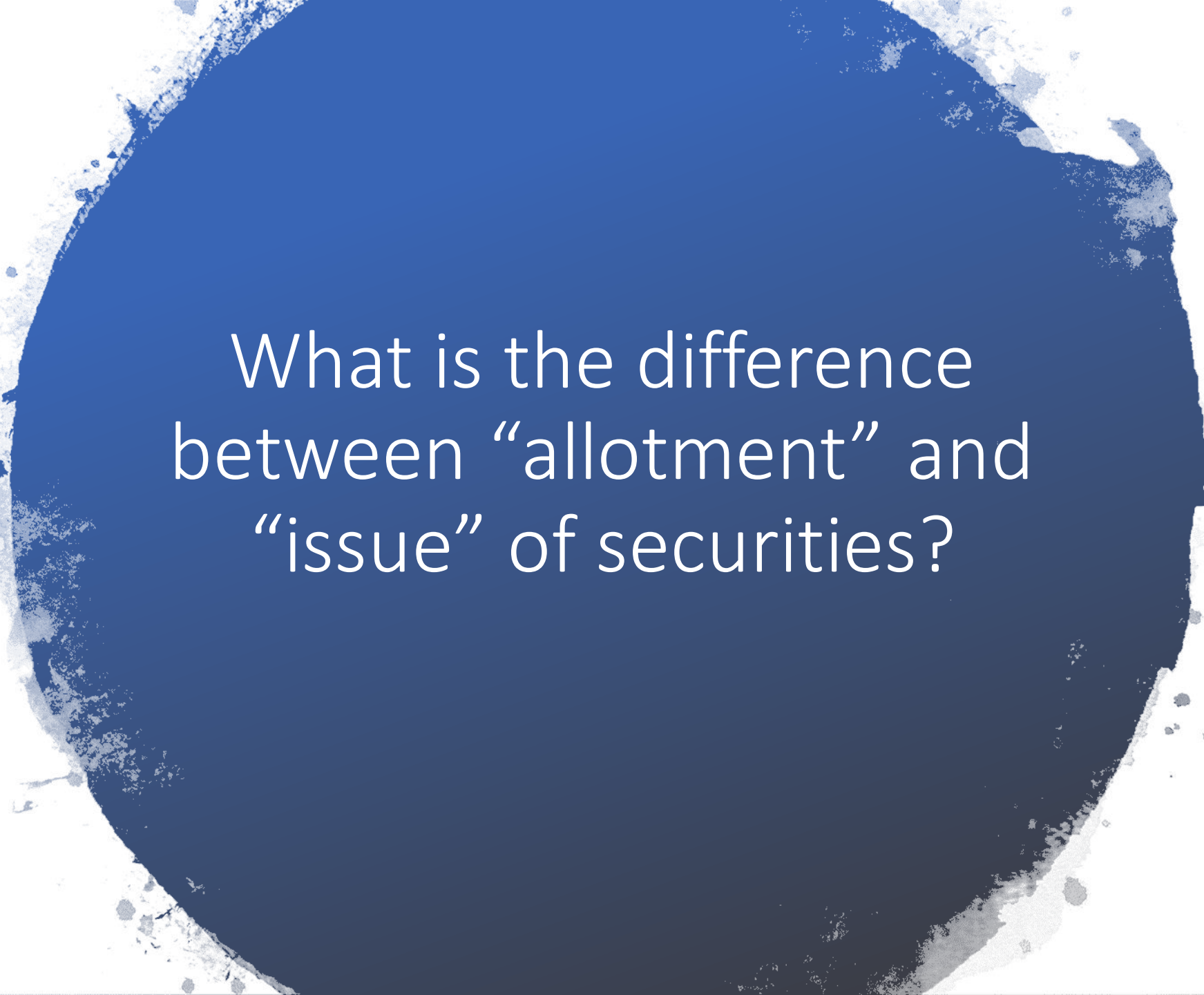


• Rights, Preferential Offer



• Sweat, ESOP and others

# Kinds of Share Issues



What is the difference  
between “allotment” and  
“issue” of securities?

# Creation vs Issue vs allotment of shares

Creation- Authorised Capital

Issue- Passing of Resolution by shareholders or board as the case may be

Allotment- Follows issue of shares and is the last step

There is a difference between “creation”, “issue” and “allotment” of shares. A share in a company comes into existence on the evolution of a process which begins with the creation of a share and ends with its allotment. The intermediary step is that of “issue” of shares.

*-Supreme court in Shree Gopal Jalan vs. Calcutta stock exchange association limited [1963] 33 Comp Cas 862: AIR 1964 SC 250*

# Section 23- Public Offer and Private Placement

**23.** (1) A public company may issue securities—

- (a) to public through prospectus (herein referred to as "public offer") by complying with the provisions of this Part I of chapter III; or
- (b) through private placement by complying with the provisions of Part II of this Chapter; or
- (c) through a **rights issue** or a **bonus issue** in accordance with the provisions of this Act and in case of a listed company or a company which intends to get its securities listed also with the provisions of the Securities and Exchange Board of India Act, 1992 (15 of 1992) and the rules and regulations made thereunder.

*Explanation.*—For the purposes of this Chapter, "public offer" includes initial public offer or further public offer of securities to the public by a company, or an offer for sale of securities to the public by an existing shareholder, through issue of a prospectus.



# Section 23

(2) A private company may issue securities—

(a) by way of **rights issue** or **bonus issue** in accordance with the provisions of this Act; or

(b) through **private placement** by complying with the provisions of **Part II** of this Chapter.

# Scope of SEBI under Companies Act

24. (1) The provisions contained in this Chapter III, Chapter IV and in section 127 shall,—

(a) in so far as they relate to—

- |     |                                       |      |                          |
|-----|---------------------------------------|------|--------------------------|
| (i) | issue and transfer of securities; and | (ii) | non-payment of dividend, |
|-----|---------------------------------------|------|--------------------------|

**by listed companies** or those companies which intend to get their securities listed on any recognised stock exchange in India, except as provided under this Act, **be administered by the Securities and Exchange Board by making regulations in this behalf;**

# Public Offer

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Details Information and Reports to be stated in the prospectus omitted from CA 2013 and to be governed by SEBI Regulations

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Section 27 Variation of terms of contract or objects in prospectus possible only after special resolution as long as money remains unutilized

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Other important provisions in the law but no change, Red herring prospectus, shelf prospectus, offer for sale by members

## Private Placement - Definition

Sec 42(3) Explanation I. — "Private placement" means any offer or invitation to subscribe or issue of securities **to a select group of persons** by a company (other than by way of public offer) through private placement offer-cum-application, which satisfies the conditions specified in this section.

## Private Placement- Section 42 replaced

42(2) A private placement shall be made only to a **select group of persons** who have been **identified by the Board** (herein referred to as "identified persons"), whose number shall not exceed fifty or such higher number as may be prescribed excluding the qualified institutional buyers and employees of the company being offered securities under a **scheme of employees stock option in terms of provisions of clause (b) of sub-section (1) of section 62**, in a financial year subject to such conditions as may be prescribed

42 (4) Every identified person willing to subscribe to the private placement issue shall apply in the private placement and application issued to such person along with subscription money paid either by cheque or demand draft or other banking channel and **not by cash**:

**Provided** that a company **shall not utilise monies** raised through private placement **unless allotment is made and the return of allotment is filed** with the Registrar in accordance with sub-section (8).

# PAS 3 filing period reduced to fifteen days

42 (8) A company making any allotment of securities under this section, shall file with the Registrar a return of allotment **within fifteen days from the date of the allotment** in such manner as may be prescribed, including a complete list of all allottees, with their full names, addresses, number of securities allotted and such other relevant information as may be prescribed

1000 Rs. Per day liability of promoters and directors in case of default in filing of return of allotment

**PAS 4 and PAS 5 filing with ROC has been eliminated and is now no longer required.**

# Approvals under private placement

42(2) A private placement shall be made only to a select group of persons who have been identified by the board ("**identified persons**")

Rule 14(1) – Company shall not make an offer or invitation **unless** proposal has been previously **approved by the shareholders by a special resolution**

Provided further that this sub-rule shall not apply in case of offer or invitation for **non-convertible debentures**, where the **proposed amount to be raised through such offer or invitation does not exceed the limit as specified in clause (c) of sub-section (1) of section 180** and in such cases relevant Board resolution under clause (c) of sub-section (3) of section 179 would be adequate:

# Bank payments and Other than cash



(5) The payment to be made for subscription to securities shall be made **from the bank account of the person subscribing** to such securities and the **company shall keep the record of the bank account** from where such payment for subscription has been received:



Provided that monies payable on subscription to securities to be held by **joint holders shall be paid from the bank account of the person whose name appears first** in the application:



Provided further that the provisions of this sub-rule **shall not apply in case of issue of shares for consideration other than cash.**



# Issue of offer only after filing with ROC

Rule 14 (8) A company shall issue private placement offer cum application letter only after the relevant special resolution or Board resolution **has been filed in the Registry:**

Provided that private companies shall file with the Registry copy of the Board resolution or special resolution with respect to approval under clause (c) of sub section (3) of section 179.

Issue in demat form for **unlisted**  
public limited companies

Issue of securities in dematerialised form by unlisted public companies –  
Rule 9A of PAS rules – Effective 2<sup>nd</sup> October, 2018

(1) Every unlisted public company shall -

- (a) **issue** the securities only in dematerialised form; and
- (b) **facilitate** dematerialisation of all its existing securities

*(2) Every unlisted public company **making any offer** for issue of any securities or buyback of securities or issue of bonus shares or rights offer shall ensure that **before making such offer, entire holding** of securities of its **promoters, directors, key managerial personnel** has been dematerialised in accordance with provisions of the Depositories Act, 1996 and regulations made thereunder.*

## Rule 9A Transfer and subscription of securities by holder of securities to be in demat form

(3) Every holder of securities of an unlisted public company,-

(a) **who intends to transfer** such securities on or after 2nd October, 2018, shall **get such securities dematerialised before** the transfer; or

(b) who **subscribes** to any securities of an unlisted public company (whether by way of private placement or bonus shares or rights offer) on or after 2nd October, 2018 shall ensure that **all his existing securities are held in dematerialized form** before such subscription.

# Rule 9A (continued)

(4) Every unlisted public company shall facilitate dematerialisation of all its existing securities by making necessary application to a depository as defined in clause (e) of sub-section (1) of section 2 of the Depositories Act, 1996 and **shall secure International Security Identification Number (ISIN) for each type of security and shall inform all its existing security holders about such facility.**

(5) Every unlisted public company shall **ensure** that -

(a) it makes **timely payment of fees** (admission as well as annual) to the depository and registrar to an issue and share transfer agent in accordance with the agreement executed between the parties;

(b) it **maintains security deposit, at all times, of not less than two years' fees** with the depository and registrar to an issue and share transfer agent, in such form as may be agreed between the parties; and

(c) it complies with the regulations or directions or guidelines or circulars, if any, issued by the Securities and Exchange Board or Depository from time to time with respect to dematerialisation of shares of unlisted public companies and matters incidental or related thereto.

(6) **No unlisted public company** which has defaulted in sub-rule (5) shall make offer of any securities or buyback its securities or issue any bonus or right **shares till the payments to depositories or registrar to an issue and share transfer agent are made.**

# PAS 6

## Reconciliation of Share Capital – Half Yearly

### *PAS Rules- Rule 9A (8)*

Every **unlisted public company** governed by this rule shall submit Form PAS-6 to the Registrar with such fee as provided in Companies (Registration Offices and Fees) Rules, 2014 **within sixty days** from the **conclusion of each half year** duly certified by a **company secretary in practice** or **chartered accountant in practice**.

*(8A) The company shall immediately bring to the notice of the depositories any difference observed in its issued capital and the capital held in dematerialised form.*

*(9) The grievances, if any, of security holders of unlisted public companies under this rule shall be filed before the Investor Education and Protection Fund Authority.*

*(10) The Investor Education and Protection Fund Authority shall initiate any action against a depository or participant or registrar to an issue and share transfer agent after prior consultation with the Securities and Exchange Board of India.*

# Non-Applicability of PAS 6

(11) This rule shall not apply to an unlisted public company which is:—

- (a) a Nidhi;
- (b) a Government company or
- (c) **a wholly owned subsidiary**



PAS 6.pdf

# Kinds of share capital



# Kinds of share capital

43 The share capital of a company limited by shares shall be of two kinds, namely:—

(a) equity share capital—

(i) with voting rights; or

(ii) with **differential rights** as to dividend, voting **or otherwise** in accordance with such rules as may be prescribed; and

(b) preference share capital:

# Special preferences of preference shareholders

Section 43 Explanation (iii) capital shall be deemed to be preference capital, notwithstanding that it is entitled to either or both of the following rights, namely:—

(a) **that in respect of dividends**, in addition to the preferential rights to the amounts specified in sub-clause (a) of clause (ii), it **has a right to participate**, whether fully or to a limited extent, **with capital not entitled to the preferential right aforesaid**;

(b) **that in respect of capital**, in addition to the preferential right to the repayment, on a winding up, of the amounts specified in sub-clause (b) of clause (ii), it has a **right to participate**, whether fully or to a limited extent, **with capital not entitled to that preferential right in any surplus** which may remain **after the entire capital has been repaid**.

Preference Shares may have voting rights after two years in certain circumstances

Section 47 (2) – Second Proviso\*

**Provided further** that where the dividend in respect of a class of preference shares has not been paid **for a period of two years** or more, such class of preference shareholders **shall have a right to vote on all the resolutions placed before the company.**

Two years means two consecutive years?

Whether cumulative or non cumulative is relevant for the second proviso to section 47?

Whether subsequent payment would make good the voting rights?

Whether it is possible to redeem preference shares at a time dependent upon happening of a particular event and not based on fixed number of years?

# Redemption of Preference Shares

## SCD Rules- Rule 9

(6) A company may redeem its preference shares only on the terms on which they were issued or as varied after due approval of preference shareholders under section 48 of the Act **and the preference shares may be redeemed:—**

- (a) at a fixed time or **on the happening of a particular event;**
- (b) any time at the company's option; or
- (c) any time at the shareholder's option.



Whether redemption of preference shares is possible by “reduction of capital” in the absence of profits?

Whether redemption of preference shares is possible by “reduction of capital” in the absence of profits?

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Re Birla Global Finance  
Limited [2005] 126 Comp Cas  
647 (Bom)

The redemption of  
preference shares is nothing  
but paying back to  
shareholders their preference  
share capital and amounts to  
reduction of share capital.

# Reduction of share capital

66. (1) Subject to confirmation by the Tribunal on an application by the company, a company limited by shares or limited by guarantee and having a share capital may, by a **special resolution**, reduce the share capital **in any manner** and in particular, may—

- (a) extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up;  
or
- (b) either with or **without extinguishing or reducing liability on any of its shares**,—
  - (i) cancel any paid-up share capital which is lost or is unrepresented by available assets; or
  - (ii) **pay off any paid-up share capital which is in excess of the wants of the company, alter its memorandum by reducing the amount of its share capital and of its shares accordingly:**



## Selective Reduction

Non-Promoter shareholders were being paid a fair value for their shares and an overwhelming majority of non-promoter shareholders had voted in favour of the resolution. There was no justification for withholding sanction of the resolution.

-Sandvik Asia Limited v. Bharat Kumar Padamsi and others  
[2009] 151 Comp Cas 251 (Bom)

# Shares with differential voting rights- key conditions\*

SCD Rule 4(1)(b) the issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders:

SCD Rule 4(1)(c) the shares with differential rights shall not exceed **twenty-six per cent** of the total post-issue paid up equity share capital including equity shares with differential rights issued at any point of time;

SCD Rule 4(1)(d) the company having consistent **track record of distributable profits for the last three years**;

SCD Rule 4(3) The company **shall not convert** its existing equity share capital with voting rights into equity share capital carrying differential voting rights and vice versa.

# Rights Issue and Preferential offer

# Rights issue

62. (1) Where at any time, a company having a share capital proposes to increase its subscribed capital by the **issue of further shares, such shares** shall be offered—

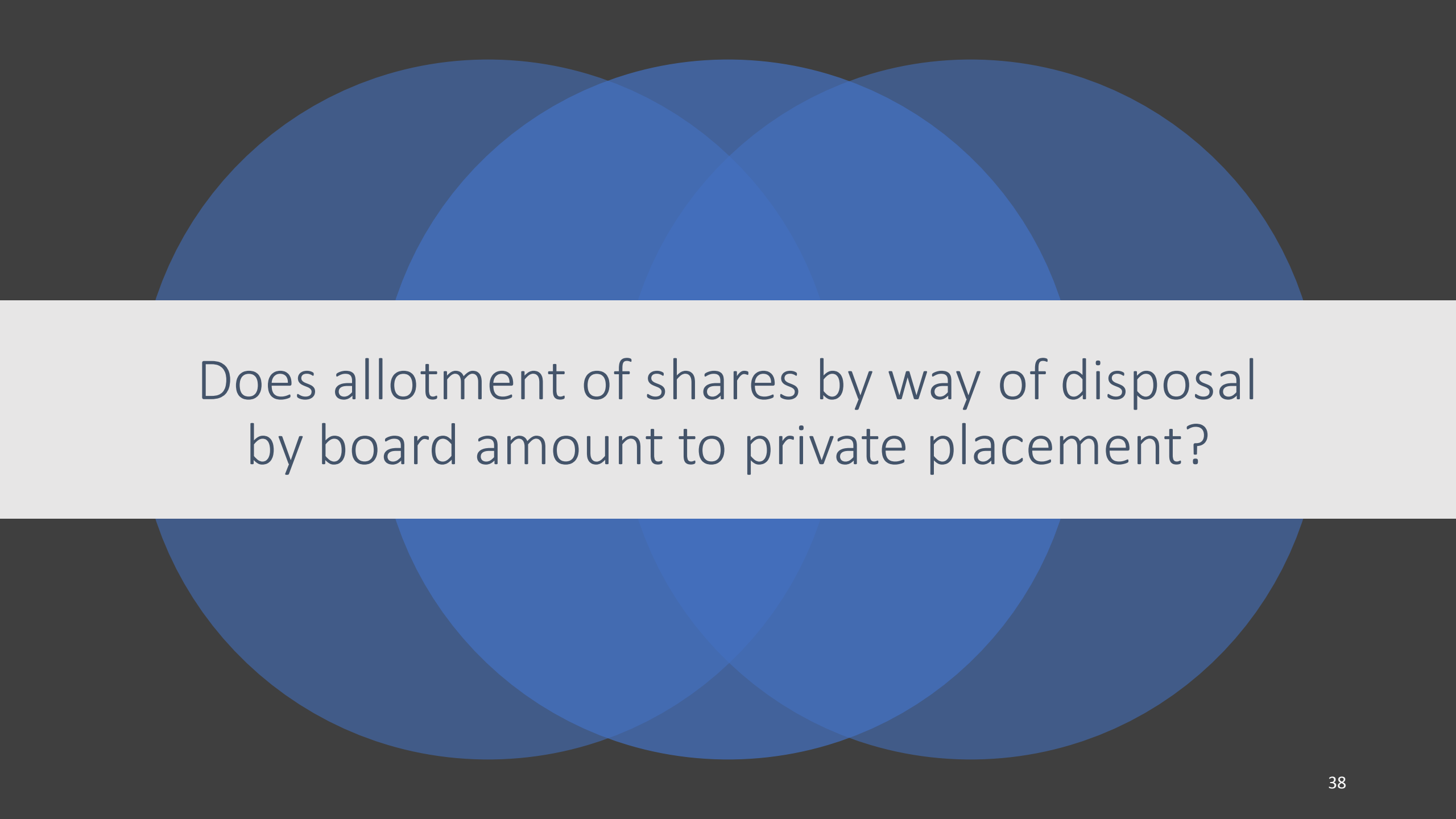
(a) to persons who, at the date of the offer, **are holders of equity shares** of the company **in proportion, as nearly as circumstances admit**, to the paid-up share capital on those shares by sending a letter of offer subject to the following conditions, namely:—

(i) the offer shall be made by notice specifying the number of shares offered and limiting a time **not being less than fifteen days and not exceeding thirty days** from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined;

(ii) unless the articles of the company otherwise provide, the offer aforesaid shall be deemed to include a right exercisable by the person **concerned to renounce the shares offered to him** or any of them in favour of any other person; and the notice referred to in clause (i) shall contain a statement of this right;

(iii) after the expiry of the time specified in the notice aforesaid, or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered, **the Board of Directors may dispose of them in such manner which is not dis-advantageous to the shareholders and the company;**<sup>36</sup>

Whether rights issue  
with a right to renounce  
can be considered as a  
public issue?



Does allotment of shares by way of disposal  
by board amount to private placement?

# Preferential Offer Definition

61(2)(c) to **any persons**, if it is authorised by a **special resolution**, whether or not those persons include the persons referred to in clause (a) or clause (b), either for cash or for a consideration other than cash, if the price of such shares **is determined by the valuation report** of a registered valuer, subject to the compliance with the applicable provisions of Chapter III and any other conditions as may be prescribed

## *Rule 13 of SCD rules*

*Explanation.*—For the purposes of this rule, (i) the expression 'Preferential Offer' means an **issue of shares or other securities**, by a company to any **select person or group of persons** on a preferential basis **and does not include shares or other securities offered through** a public issue, rights issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities;

(ii) the expression, "**shares or other securities**" means equity shares, fully convertible debentures, partly convertible debentures or any other securities, **which would be convertible into or exchanged with equity shares at a later date.**

# SCD Rule 13

## Issue of shares on preferential basis

“13. (1) For the purposes of clause (c) of sub-section (1) of section 62, if authorized by a **special resolution** passed in a general meeting, shares may be issued by any company in **any manner whatsoever including by way of a preferential offer**, to any persons whether or not those persons include the persons referred to in clause (a) or clause (b) of sub-section (1) of section 62 and such issue on preferential basis **should also comply with conditions laid down in section 42 of the Act:**”

**In case of any preferential offer made by a company to one or more existing members only, PAS 4 – PP Offer Letter will not be required to be prepared**



# Disclosures in explanatory statement in preferential offer

...

(ix) the **names** of the proposed allottees and the percentage of post preferential offer capital that may be held by them;

...

# Rule 13 – Preferential Offer- other conditions

(h) where convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the **price of the resultant shares** pursuant to conversion shall be determined—

(i) either upfront at the time when the offer of convertible securities is made, on the basis of valuation report of the registered valuer given at the stage of such offer, or

(ii) at the time, which shall **not be earlier than thirty days to the date when the holder of convertible security becomes entitled to apply** for shares, on the basis of valuation report of the registered valuer given not earlier than sixty days of the date when the holder of convertible security becomes entitled to apply for shares:

Provided that the company shall take a decision on sub-clauses (i) or (ii) at the time of offer of convertible security itself and make such disclosure under sub-clause (v) of clause (d) of sub-rule (2) of this rule.

# Sweat and ESOPs

# Section 54 Issue of Sweat Equity Shares

A company may issue sweat equity shares **of a class of shares already issued** if

- (a) the issue is authorised by a **special resolution** passed by the company;
- (b) the resolution specifies the number of shares, the current market price, consideration, if any, and the **class or classes of directors or employees** to whom such equity shares are to be issued;
- ~~(c) not less than one year has, at the date of such issue, elapsed since the date on which the company had commenced business; and~~
- (d) where the equity shares of the company are listed on a recognised stock exchange, the sweat equity shares are issued in accordance with the regulations made by the Securities and Exchange Board in this behalf and if they are not so listed, the sweat equity shares are issued in accordance with such rules as may be prescribed

2(88) "sweat equity shares" means such equity shares as are issued by a company to its **directors or employees** at a discount or **for consideration, other than cash**, for providing their know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called;

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## Sweat Equity Shares

# Extent of permissible issue of Sweat Equity

Rule 8 (4) The company shall not issue sweat equity shares **for more than fifteen per cent** of the existing paid up equity share capital in a year **or** shares of the issue **value of rupees five crores**, whichever is higher:

Provided that the issuance of sweat equity shares in the Company **shall not exceed twenty five per cent**, of the paid up equity capital of the Company at any time:

Provided further that a **start up company**, ... may issue sweat equity shares **not exceeding fifty per cent of its paid up capital up to five years from the date of its incorporation** or registration.

# Compulsory Lock In and Valuation

Rule 8 (5) The sweat equity shares issued to directors or employees shall be **locked in/non-transferable for a period of three years** from the date of allotment and the fact that the share certificates are under lock-in and the period of expiry of lock-in shall be stamped in bold or mentioned in any other prominent manner on the share certificate.

(7) **The valuation of intellectual property rights or of know how or value additions for which sweat equity shares are to be issued, shall be carried out by a registered valuer**, who shall provide a proper report addressed to the Board of directors with justification for such valuation.

# Accounting for Sweat Equity shares

Rule (9) Where sweat equity shares are issued for a non-cash consideration on the basis of a valuation report in respect thereof obtained from the registered valuer, such non-cash consideration shall be treated in the following manner in the books of account of the company—

- (a) where the non-cash consideration takes the form of a depreciable or amortizable asset, it shall be carried to the balance sheet of the company in accordance with the accounting standards; or
- (b) where clause (a) is not applicable, it shall be expensed as provided in the accounting standards.



# ESOP Ineligibility

62(1) (b) to employees under a scheme of employees' stock option, subject to **special resolution (ordinary resolution for private limited)** passed by company and subject to such conditions as may be prescribed

Rule 12: Explanation :For the purposes of clause (b) of sub-section (1) of section 62 and this rule "Employee" means—

...

but does not include—

- (i) an employee who is a promoter or a person belonging to the promoter group; or
- (ii) a director who either himself or through his relative or through any body corporate, directly or indirectly, holds more than ten per cent of the outstanding equity shares of the company:

**Provided that in case of a startup company, as defined in notification number GSR 180(E), dated 17th February, 2016 issued by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry Government of India, the conditions mentioned in sub-clauses (i) and (ii) shall not apply up to five years from the date of its incorporation or registration.**

## ESOPs situations requiring separate resolution

(4) The approval of shareholders by way of **separate resolution** shall be obtained by the company in case of—

(a) grant of option to employees of **subsidiary or holding company**; or

(b) grant of option to identified employees, **during any one year**, equal to or **exceeding one per cent of the issued capital** (excluding outstanding warrants and conversions) of the company at the time of grant of option.

# Other related provisions

# Issue of Bonus Shares

63. (1) A company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of—

(i) its free **reserves**;

(ii) the securities premium account; or

(iii) the capital redemption reserve account:

**Provided that no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets.**

2(43) "free reserves" means **such reserves** which, as per the latest audited balance sheet of a company, are available for distribution as dividend

# Buyback

Whether non-cash buy back is permissible?

# Non cash buy back is not permissible

Rule 17 (9) The company shall within seven days of the time specified in sub-rule (7) —

- (a) make **payment of consideration in cash** to those shareholders or security holders whose securities have been accepted; or
- (b) return the share certificates to the shareholders or security holders whose securities have not been accepted at all or the balance of securities in case of part acceptance.

Payment of  
dividend in  
proportion to  
amount paid-  
up.

51. A company may, if so authorised by its articles, **pay dividends in proportion to the amount paid-up on each share.**

## Prohibition on issue of shares at discount

Section 53 (2) Any share issued by a company at a **[discount]** shall be void.

(2A) Notwithstanding anything contained in sub-sections (1) and (2), a company **may issue shares at a discount to its creditors when its debt is converted into shares** in pursuance of any **statutory resolution plan or debt restructuring scheme**.



# Variation of shareholders' rights

48. (1) Where a share capital of the company is divided into different classes of shares, the rights attached to the shares of any class may be varied with the consent in writing of the holders of **not less than three-fourths of the issued shares of that class** or by means of a **special resolution** passed at a **separate meeting** of the holders of the issued shares of that class,—

(a) if provision with respect to such variation is contained in the memorandum or articles of the company; or

(b) in the absence of any such provision in the memorandum or articles, if such variation is not prohibited by the terms of issue of the shares of that class:

Provided that if variation by one class of shareholders affects the rights of any other class of shareholders, the **consent of three-fourths of such other class of shareholders** shall also be obtained and the provisions of this section shall apply to such variation.

# Application of Securities premium

52 (2) Notwithstanding anything contained in sub-section (1), the securities premium account may be applied by the company—

- (a) towards the issue of unissued shares of the company to the members of the company as fully paid bonus shares;
- (b) in writing off the preliminary expenses of the company;
- (c) in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company;
- (d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company; or
- (e) for the purchase of its own shares or other securities under section 68.

# Key Take-Aways



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- Provisions in relation to Demat of Shares



- Kinds of Share capital



- Rights, Preferential Offer



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Thank You



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