1

DEFINITIONS

Unit Structure

1.0 OBJECTIVES

After studying the unit, the students will be able to:

- Understand the meaning of certain concepts of Company Law.
- Know the meaning of following terms: Accounting Standards, Auditing Standards, Books of Accounts, Deposit, Financial Year.
- To understand concepts of Foreign Company, Independent director, Indian Depository Receipts, One Person Company, Small Company.

1.1 INTRODUCTION

In this unit we are going to study certain terms related to accounting of different organisations as defined in the Indian Companies Act.

1.2 MEANING OF ACCOUNTING STANDARDS

The Companies Act defines Accounting Standards in Sec. 2(2) as under:

Accounting Standards means the standards of accounting or any addendum thereto for companies or class of companies referred to in section 133.

Sec.133 of The Companies Actstates that Central Government to prescribe accounting standards: The Central Government may prescribe the standards of accounting or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949 (38 of 1949), in consultation with and after examination of the recommendations made by the National Financial Reporting Authority.

The definition of AccountingStandards is exhaustive as time-to-time Central Government can add standards as per requirements of different types of companies, on the recommendation of Institute of Chartered Accountants of India and in consultation with National Financial Reporting Authority.

In other words, Accounting Standards means authoritative standards for financial reporting. These standards specify how transactions and other events are to be recognized, measured, presented, and disclosed in financial statements.

1.3 MEANING OF AUDITING STANDARDS

The Companies Act defines Auditing Standards in Sec. 2(7) as under:

Auditing standards means the standards of auditing or any addendum thereto for companies or class of companies referred to in sub-section (10) of section 143.

Sec.143 (10) of the Companies Actprovides that: The Central Government may prescribe the standards of auditing or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949 (38 of 1949), in consultation with and after examination of the recommendations made by the National Financial Reporting Authority:

Provided that until any auditing standards are notified, any standard or standards of auditing specified by the Institute of Chartered Accountants of India shall be deemed to be the auditing standards.

Whenever an independent examination of financial information is carried out for any entity, whether the business motive is to make the profit or not, whether the size of the entity is big or small or even if the entity has any legal form, the Auditing standards as prescribed will be applicable. All Auditing standards are interlinked and have to apply in unity.

Indian Auditing Standards goes hand in hand with International Standards on Auditing formulated by (IAASB) International Auditing and Assurance Standards Board.

1.4 MEANING OF BOOKS OF ACCOUNTS:

The Companies Act defines Books of Accounts in Sec. 2(13) as under:

Books of Account includes records maintained in respect of:

(i) all sums of money received and expended by a company and matters in relation to which the receipts and expenditure take place;
(ii) all sales and purchases of goods and services by the company;
(iii) the assets and liabilities of the company; and
(iv) the items of cost as may be prescribed under section 148 in the case of a company which belongs to any class of companies specified under that section;

Books of accounts means a place where all financial information is related to a person, or a business is recorded. Books of accounts are maintained as prescribed under Income tax Act, companies Act 2013, and GST Act and for charitable organisations as per provisions of Public Trust Act.

In other words, Books of Accounts is a record maintained relating to financial transactions and is the most important document for performing further accounting procedures. Assets, liabilities, incomes, and expenses are tracked in these accounts. As a general rule, the term "book of accounts" is most commonly used to describe the general ledger in double-entry accounting systems.

1.5 MEANING OF DEPOSIT

The Companies Act defines Deposit in Sec. 2(31) as under:

Deposit includes:

- any receipt of money by way of deposit orloan or
- in any other form by a company,
- but does not include such categories of amount as may be prescribed in consultation with the Reserve Bank of India;

Indian companies may raise capital by inviting Deposits from public. When company receives deposits, it has to maintain a register with details about depositor and such register should be kept in the registered office of the company. Even application money not refunded by company can be called as Deposits by company.

Deposit includes any receipt of money in any form whether it is loan, deposit etc. but does not include such amount which is excluded from the definition of Deposit by the Reserve Bank of India.

This section must be referred along with Sections 73 to 76 of the Companies Act, 2013 and Section 2 (c) of the Companies (Acceptance of

Deposits) Rules, 2014.Following Amounts received by the company cannot be called as Deposits as per this section:

- any amount received from Central or Sate Government,
- any amount received from foreign Governments or Foreign Banks,
- Amount guaranteed by Central or State Government,
- Amount received by a Company from any other Company,
- Any amount raised by issue of bonds and debentures,
- Any amount received from its employee's non-interest security deposit,
- Any amount received in course of business,
- Loan from Public Financial Institutions

1.6 MEANING OF FINANCIAL YEAR

The Companies Act defines **Financial year** in Sec. 2(41) as under:

Financial year, in relation to any company or body corporate, means-

- the period ending on the 31st day of March every year, and
- where it has been incorporated on or after the 1st day of January of a year,
- the period ending on the 31st day of March of the following year,
- in respect whereof financial statement of the company or body corporate is made up.

A holding company or a subsidiary of a company incorporated outside India and is required to follow a different financial year for consolidation of its accounts outside India, may allow any period of one year as a financial year.

Provided further that a company or body corporate, existing on the commencement of this Act, shall, within a period of two years from such commencement, align its financial year as per the provisions of this clause.

In India, this 1-year period starts from 1st April and ends on 31st March. This period in which the income is earned is known as the Financial Year or Fiscal Year.

The Balance Sheet and Income statement of companies across the Globe are usually prepared for a period of 1 year. However, the date from which this period starts varies from country to country.

<u>For Example</u>: In case the accounts are being prepared for the year starting 1st April 2022 and ending on 31st March 2023, this period would be called as Financial Year 2022-23

And this income would be assessed to tax in the next year and this period would be called as Assessment Year 2023-24.

1.7 MEANING OF FOREIGN COMPANY

The Companies Act defines Foreign Company in Sec. 2(42) as under:

Foreign Company means any company or body corporate incorporated outside India which –

(a) Has a place of business in India whether by itself or through an agent, physically or through electronic mode; and

(b) Conducts any business activity in India in any other manner.

This definition also includes those foreign companies which are doing business in India through electronic mode via email, mobile, social media or otherwise.

To qualify to become a foreign company, one or more citizens of India or by one or more companies incorporated in Indiaholds not less than 50% of the paid-up equity or preference share capital.

For Example:

- Apple Inc.
- Microsoft Corporation
- Google
- Amazon
- Samsung
- Coca-Cola Company

1.8 MEANING OF INDEPENDENT DIRECTOR

Companies Act defines **Independent Director** in Sec. 2(47) as under:

Independent Director means an independent director referred to in sub-section (6) of section 149;

Sec149(6) of The Companies Actprovides that Company to have Board of Directors consisting of an Independent Director.

An independent director in relation to a company, means a director other than a managing director or a whole-time director or a nominee director:

(a) who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience,

(b) (i) who is or was not a promoter of the company or its holding, subsidiary, or associate company,

(ii) who is not related to promoters or directors in the company, its holding, subsidiary or associate company,

(c) who has or had no pecuniary relationship with the company, its holding, subsidiary or associate company, or their promoters, or directors, during the two immediately preceding financial years or during the current financial year,

(d) none of whose relatives has or had pecuniary relationship or transaction with the company, its holding, subsidiary or associate company, or their promoters, or directors, amounting to two per cent. or more of its gross turnover or total income or fifty lakh rupees or such higher amount as may be prescribed, whichever is lower, during the two immediately preceding financial years or during the current financial year,

(e) who, neither himself nor any of his relatives,

(i) holds or has held the position of a key managerial personnel or is or has been employee of the company or its holding, subsidiary, or associate company in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed,

(ii) is or has been an employee or proprietor or a partner, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed, of -

(A) a firm of auditors or company secretaries in practice or cost auditors of the company or its holding, subsidiary, or associate company; or

(B) any legal or a consulting firm that has or had any transaction with the company, its holding, subsidiary, or associate company amounting to ten per cent. or more of the gross turnover of such firm,

(iii) holds together with his relatives 2% or more of the total voting power of the company; or

(iv) is a Chief Executive or director, by whatever name called, of any non-profitorganisation that receives 25% or more of its receipts from the company, any of its promoters, directors, or its holding, subsidiary, or associate company or that holds 2% or more of the total voting power of the company; or

(f) who possesses such other qualifications as may be prescribed.

An Independent Director is also known as an outside director. He is a member of a board of directors who does not have a material or pecuniary relationship with company or related persons, except his remuneration.

In other words, Independent Director means a director who is not connected or associated with the Company in any manner and works only to safeguard the interest of the members/ shareholders.

We can say that an independent director is a non- executive director of a company who helps the company in improving corporate credibility and governance standards. He/ She does not have any kind of relationship with the company that may affect the independence of his/ her judgment.

1.9 MEANING OF INDIAN DEPOSITORY RECEIPTS (IDR):

Companies Act defines **Indian Depository Receipt** in Sec. 2(48) as under:

Indian Depository Receiptmeans any instrument in the form of a depository receipt created by a domestic depository in India and authorised by a company incorporated outside India making an issue of such depository receipts,

- An IDR is issued by a foreign firm that cannot go through the Indian listing process.
- An IDR is beneficial for a foreign firm that wishes to share the risk and rewards of the offering with Indian shareholders.
- IDRs are denominated in Rupees. It reflects a stake in a certain number of the Issuing Company's underlying equity shares. Deposited Shares are the name for these shares.
- These IDRs would be freely transferable and placed on Indian stock markets.
- Depositary receipts are more convenient and less expensive than purchasing stocks in foreign markets.
- Depositary receipts help international companies to raise capital globally and encourage international investment.

1.10 MEANING OF ONE PERSON COMPANY:

Companies Act defines **One Person Company** in Sec. 2(62) as under:

One Person Company means a company which has only one person as a member.

In other words, One Person Company is described as private company.

Advantages of One-Person Company:

- OPCs don't have to conduct annual general meetings.
- Cash flow statements need not be included in their financial statements.
- Directors could sign the annual returns too; a company secretary is not mandatorily required.
- Provisions regarding the independent directors are not applied to OPCs.
- Directors can take home more remuneration as compared to other companies.
- Such company when it is formed it appoints its successor by way of nomination.

- Companies Act, 2013 has not prescribed any amount as minimum paid-up capital for OPCs.
- He/she will act both as a director as well as a shareholder of the company with limited liability.

For Example:

- **Vast Online (OPC) Private Limited**
- **Evolve2achieve (OPC) Private Limited**
- **Amravati Diesel (OPC) Private Limited**
- **Bhardwaj Invention (OPC) Private Limited**

1.11 MEANING OF SMALL COMPANY:

Companies Act defines **Small Company** in Sec. 2(85) as under:

Small Companymeans a company, other than a public company,

(i) paid-up share capital of which does not exceed Rs.50 lakh or such higher amount as may be prescribed which shall not be more than Rs.5 crore; or

(ii) turnover of which as per its last profit and loss account does not exceed Rs.2 crore or such higher amount as may be prescribed which shall not be more than Rs.20 crore

Provided that nothing in this clause shall apply to:

(A) a holding company or a subsidiary company;

(B) a company registered under section 8; or

(C) a company or body corporate governed by any special Act;

A small business offers opportunities for entrepreneurship, employment, and job, and is much easier to run than a large corporation. Companies Act states that small businesses cannot be considered public entities. Their paid-up share capital does not exceed Rs. 2 crores or a larger amount that is not more than Rs. 10 crores.

A Small Company has several advantages compared with other companies regarding requirements for compliance such as:

- is not required to rotate its auditors
- lower and fewer penalties for a small company than for other public and private companies
- exempts Small Companies from filing directors' reports
- it must not prepare a report on its Annual General Meeting

A Small Company provides entrepreneurship, employment and jobs and has been made easy to run by its various advantages over medium and large companies. According to the Companies Act, Small Companies are not public companies.

1.12 SUMMARY

Accounting Statndards means authoritative standards for financial reporting.

Auditing standards are used to carry out an independent examination of financial information of any entity.

Books of Accounts is a record maintained relating to financial transactions**.**

Deposit includes any receipt of money by way of deposit orloan orin any other form by a company but does not include any amount prescribed in consultation with the Reserve Bank of India.

Year Start from 1^{st} April and ending on 31^{st} March of next year is called as **Financial Year**.

As per Accounting Standards Income earned in the financial year would be assessed to tax in the next year and this period would be called as **Assessment Year**.

Foreign companies which are doing business in India, which are incorporated outside India.

Independent Director means a director who is not connected or associated with the Company in any manner and works only to safeguard the interest of the shareholders.

Indian Depository Receipt means any instrument issued by foreign company reflected in Indian currency, traded on Indian Stock Exchanges.

One Person Company means a company which has only one person as a member.

Small Company means a company, other than a public company having paid up share capital exceeding Rs.50 lakhs or such higher amount more than Rs. 5 Crores.

1.13 UESTIONS:

I) Fill in the blanks:

a. _________ means a company which has only one person as a member.
b. _______ is a record maintained relating to financial transactions.
c. __________ means the standards of accounting or any addendum thereto for companies or class of companies referred to in section 133.
d. Financial year is the period ending on ___ every year.
e. Full form of IDR is ___________.

f. A _____company need to be incorporated outside India.

(a. One Person company, b. Books of Accounts, c. Accounting standards, d. 31st March, e. Indian Depository Receipt, f. Foreign Company)

II) True or False:

a. Unlisted private company must have independent director.
b. Accounting standards does not permit uniformity.
c. Small company cannot have share capital over Rs.50 Lakh.
d. Deposit means any amount received as loan.
e. One person company means a company which has only one employee in a company.

(a. False, b. False, c. True, d. False e. False)

III) Write Short Notes on:

a. Auditing Standards
b. Independent Director
c. Small Company
d. Deposit
e. Foreign Company

IV) Explain the Terms:

a. Accounting standards
b. One Person Company
c. Independent Director
d. Indian Depository Receipt
e. Deposit

V) Descriptive Question:

1. What is an Auditing Standards?

2. Explain the meaning of a Foreign Company.

3. What is Small Company?

4. What is financial year means under the Companies Act, 2013?

5. What do you mean by books of account in a company?

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2

INCORPORATION OF COMPANIES (Section 3 to Section 20)

Unit Structure

2.1 INTRODUCTION

Meaning: A business is a body that has been legally separated from the individuals that make up its membership. The phrase "Company has been defined as a company incorporated under this Act or under any previous company law," according to Section 2 (20) of the Companies Act, 2013. A corporate entity or firm is created via the legal procedure of incorporation. The resultant legal entity, which distinguishes the firm's assets and revenue from its owners and investors, is a corporation. Common law defines a business as a "legal person" or "legal entity" that is distinct and could endure past the lifetimes of its members.

A business is "incorporated" when it is set up in accordance with the guidelines outlined in the Companies Act of 2013.

2.1.1 Advantages of Incorporation of a Company:

1. A distinct legal identity:

When a company is incorporated, it acquires a distinct legal personality. A corporation that has been incorporated, as opposed to a partnership firm that lacks a distinct legal identity, has a legal identity that is distinct from its shareholders and members.

2. Never-ending:

Unless the business is forced to dissolve for reasons specified in the act, it will remain in existence even if all its members declare bankruptcy or pass away. The Company is independent of its members' financial situation.

3. Transferable Shares:

According to Section 82 of the Companies Act of 2013, a company's shares are assumed to be movable and transferable in the manner stipulated by the company's articles. As a result, the member can recoup his investment by selling his shares on the open market without pulling money out of the company. This ensures the stability of the company as well as the investor's liquidity. Contrarily, in a partnership, a partner cannot transfer his interest in the company's capital without the approval of the other partners.

4. Suitability:

A corporation with legal status has the authority to file lawsuits against people and other businesses on its behalf.

5. Versatility:

Every corporation is free to create rules that are appropriate for its organization, so long as they don't go against fundamental legal and ethical standards.

6. Limitation of Liability:

Members of a company are not liable for its obligations since the corporation is a separate legal entity with its own existence. The extent of the members' obligations is limited to their respective portions in the business. Nobody is required to offer more than what they have already done.

2.1.2 Disadvantage of Incorporation of a Company

Costs and documentation: The process of incorporating a business is both expensive financially and time-consuming due to the amount of documentation needed.

1) **A corporation is not a citizen:**

Despite being a legal entity, a company is not a citizen. It can only profit from those fundamental freedoms that are accorded to every "person," citizen or not. However, the nationality, domicile, and habitation of a firm do exist. A firm that was founded in a certain nation has that nation's nationality, but unlike an individual, it cannot alter its nationality.

2) **Limited access to company information:**

The employees and lower-level members of the firm have limited access to the company information and upper management, despite the elaborate legislative structure intended to promote maximum transparency and disclosure of corporate information.

3) **Control and ownership must be kept separate:**

Members of tiny shareholders have no real power to influence the actions or choices of the organisation. This occurs because there are so many employees in the organisation that no one person or even a small group of employees can have a significant impact on how the company operates. As a result, the title of "ownership" of the corporation is only a phrase with no practical meaning**.**

4) **Greater Social Responsibility:**

Hundreds of thousands of people are employed by several incorporated businesses, many of which have a net value in the billions of dollars. They have a profound effect on society, and major businesses frequently engage in charitable endeavours as part of their CSR (corporate social responsibility) programmes. These enormous corporations must abide by certain social standards and contribute to the advancement of society because of the enormous effect they have.

2.2. FORMATION OF COMPANY

As per section 3 of the Indian Company act 2013 company are being formed by following the prescribed norms:

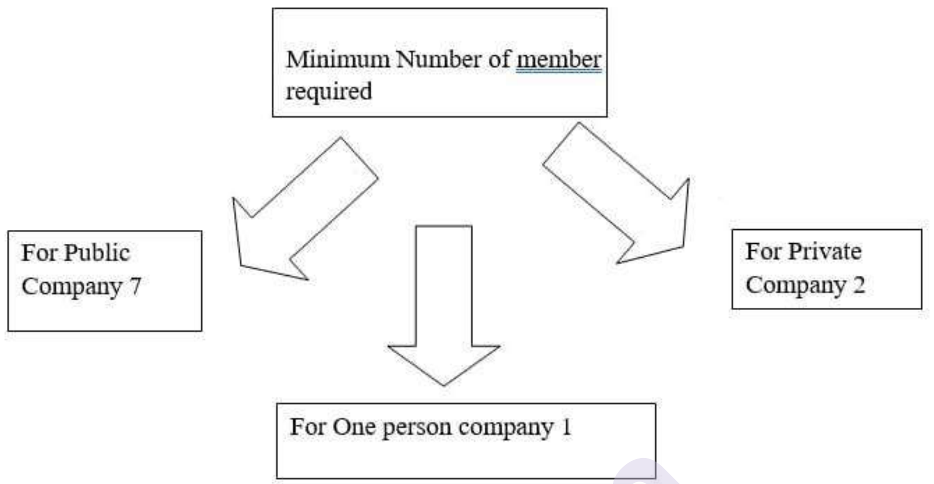
(1) (1) A company may be formed for any lawful purpose by:

(a) seven or more persons, in the case of a public company;

(b) two or more persons, in the case of a private company; or

(c) one person, in the case of a one-person company, or private company, by signing his or her name to a memorandum and complying with the registration requirements of this Act:

FORMATION OF COMPANIES



2.2.1 MEMORANDUM:

Every firm is required to create a memorandum of agreement in accordance with Section 4 of the Indian firm Act 2013 3. "Memorandum" refers to the company's memorandum as originally written at the company's establishment or as amended from time to time to carry out any action required by any other Act law. A memorandum of association enables individuals such as shareholders, creditors, investors, and other members of a company to understand the reason(s) for the formation of the organisation. They are given permission to learn about the organisation's goals and the spectrum of approved activities the company may engage in.

2.2.2. CONTENTS OF MEMORANDUM OF ASSOCIATION:

1) **Name Clause:** When creating the Memorandum of Association, the firm name must be mentioned. A firm is free to choose any name it wants, but it shouldn't be the same as another one that already exists. The business name chosen should exactly match the name approved by the Registrar of Companies as it appears in the Memorandum of Association. Both a Public Limited Company and a Private Limited Company should conclude with the words "Limited" or "Private Limited," respectively.

2) **Situation Clause:** The name of the state in which a company conducts business and information about the Registrar of Companies' jurisdiction must both be included in the firm's Memorandum of Association. The corporation must establish its registered office within 15 business days. The registered office verification must also be finished within 30 days. This process is used to determine the

company's domicile, which may or may not correspond to its operating location.

The memorandum must be changed if the registered office's location changes; the process is described below.

3) **Object Clause:** The Memorandum of Association must state the purpose for which the organisation was established. One of the most important provisions should be properly worded and include every form of business that the firm may conceivably engage in in the future. It is against the law for a firm to engage in any activity not expressly included in the object clause. The items are divided into three categories: "Main Objects," "Ancillary Objects," and "Other Objects." The objectives must be clearly articulated and clear in their nature. The items must not also be unlawful, against Act prohibitions, or against national public policy.

4) **Liability Clause:** The Memorandum of Association must expressly outline the obligations of the company's members. They might be guaranteed or limited by shares. The whole provision may be dropped in the event of an unlimited liability business.

   When a corporation is capped by shares, the members' responsibility is restricted to any outstanding debt on the shares they personally own. When a company is limited by guarantee, its members are responsible for paying the sum specified in the memorandum at the time of the firm's liquidation. In the case of limitless corporations, the members' liability, which includes personal assets, is infinite.

5) **Capital Clause:** The Memorandum of Association should specify the maximum amount of allowed capital that the company's members may create. This sum is subject to stamp duty. Although there is no legal restriction on how much money a corporation may raise, once it has been formed, it cannot increase the permitted share capital. In the case of equity and preference shares, respectively, the denomination for each of these shares must be either RS 10 or RS 100. A corporation should ensure that the allowed capital obtained is high enough to support future business development. This charter may also include any additional rights and advantages that have been agreed upon by the shareholders, creditors, investors, and other business members.

   An unlimited corporation with authorised share capital is not required to indicate it in the memorandum.

6) **Association or Subscription Clause:** The company's memorandum of association should specify the approved capital as well as the quantity of shares that each member owns. The minimum number of shares required for each subscriber to the memorandum is one. In addition to signing the memorandum in the presence of at least one witness who must authenticate the signature, each subscriber must indicate how many shares he has.

2.3 ARTICLE OF ASSOCIATION:

Sec 5 of Indian Companies act 2013 define The Articles of Association of a company are that which prescribe the rules, regulations, and the byelaws for the internal management of the company, the conduct of its business, and is a document of paramount significance in the life of a company. A business's articles, which govern the administration and authority of the company and its executives, are sometimes likened to a rule book for how the organisation should operate. It specifies a number of internal business procedures, including the way calls are made, the credentials of directors and workers, the roles and responsibilities of auditors, forfeiture of shares, and more.

In fact, a contract between the members and between the members and the firm is established by the articles of association. The defined terms of this agreement set forth the customary privileges and duties that come with being a member of the firm.

2.4 DISTINCTION BETWEEN MEMORANDUM AND ARTICLES OF ASSOCIATION

S.No.	Memorandum of Association	Articles of Association
1	Contains the essential requirements for the company's incorporation.	contain the company's internal rules and regulations.
2	intended for the general public's, creditors', and shareholders' benefit and clarity.	Regulate the interactions among the members as well as those between the firm and its customers.
3	outlines the boundaries beyond which the company's action is not permitted.	The rules for working there are laid forth in articles.
4	Memorandum specifies the conditions under which the articles must operate.	Articles give specifics within those bounds.
5	can only be changed under particular conditions and in accordance with the 2013 Companies Act's regulations. In some circumstances, the Central Government's approval is also necessary.	With the passage of a specific resolution, articles can be changed much more quickly.

6	Memorandums cannot contain clauses that violate the Companies Act. Memorandum is the Companies Act's only subsidiary.	Articles cannot contain clauses that go against the Memorandum. The Memorandum and the Companies Act are both subordinate to the Articles.
7	Any actions taken in violation of the memorandum are extra vires and cannot be approved by the shareholders either.	The shareholders may approve actions taken in contravention of the Articles so long as they do not go beyond the Memorandum.

2.5 STEPS IN INCORPORATION OF A COMPANY

The legal procedure used to establish a corporate entity, or a business is referred to as incorporation. A corporation that has been legally established is regarded as a distinct legal person in its own right. These businesses are easily recognised by the inclusion of words like "Inc." or "Limited" in their titles. It develops into a corporate legal entity that is entirely independent of its proprietors.

1. Ascertaining Availability of Name:

The selection of an acceptable name is the first stage in the establishment of any firm. A corporation can be recognised by the name it registers. In the firm's memorandum of association, the name of the company is mentioned. If the business is a private one, the name must finish in "Private Limited" or "Limited," respectively.

The promoters must submit an application in writing to the state's Registrar of Companies in order to determine whether the chosen name is accessible for adoption. Paid along with the application is 500 rupees. After the firm completes all necessary paperwork within three months, the Registrar approves the adoption of the name.

2. Preparation of Memorandum of Association and Articles of Association:

A company's memorandum of association serves as its constitution or rulebook. The memorandum outlines the company's goals, the industry in which it will operate, and the kind of business it intends to engage in. Additional divisions include five clauses.

1. **Name Clause**
2. **Registered Office Clause**
3. **Objects Clause**
4. **Liability Clause**
5. **Capital Clause**

Articles of Association are essentially a set of guidelines that the internal administration of the firm must abide by. A contract is established between the firm and its members by the article. The article discusses the members' obligations, rights, and liabilities. It binds each and every employee of the organisation equally.

3. Printing, signing, and stamping of the memorandum and articles of organization, as well as their vetting, are all tasks that the Registrar of Companies frequently assists entrepreneurs with. In particular, with promoters who have never before written a memorandum or an essay. The articles of association and memorandum of association can then be printed after they have been reviewed by the Registrar of Companies. As a result, the memos and articles are broken up into paragraphs and organised by chronological order.

Each subscriber or their authorised representative must personally sign each item in the presence of a witness for it to be legitimate.

4. Power of Attorney: The promoter may then hire an attorney who will have the ability to act on behalf of the company and its promoters to complete the legal and complicated documentation procedures of formation of a company. The attorney will have the power to modify the articles and memoranda as well as other papers that have been submitted to the registrar.

5. Additional Filed Documents with the Registrar of Companies:
The First -e-Form No. 32 - Directors' approval
The Second - Notice of Registered Address (e-Form No. 18)
The Third - e-Form No.32. - Directors' Information

6. Statutory statement in e-Form No. 1: According to this statement, "All the requirements of the Companies Act and the rules thereunder have been compiled with respect to and matters precedent and incidental thereto."

7. Payment of Registration Fees: During incorporation, a predetermined fee must be paid to the Registrar of Companies. It is based on the firms' nominal capital, which includes share capital.

8. Certificate of Incorporation: The Registrar will register the business and issue a certificate of incorporation if he is absolutely certain that all conditions have been met by the company that is being established. Therefore, the incorporation certificate issued by the Registrar is unquestionable evidence that all Act criteria have been satisfied.

2.6. FORMULATION OF COMPANIES WITH CHARITABLE OBJECTS:

Meaning: A Section 8 Company is one that is established "for promoting commerce, art, science, sports, education, research, social welfare, charity, protection of the environment or any such other object," provided that the profits, if any, or other income is applied for promoting only the objects of the company and no dividend is paid to its members. Section 8 of the

Companies Act, 2013, is where this phrase first appears. Therefore, a business incorporated under the Companies Act, 2013, for philanthropic or not-for-profit objectives is a Section 8 business or a Section 25 Company.

Creation of Companies with Charitable Objectives
(1) Where it is established to the Central Government's satisfaction that an individual or group of individuals is eligible to register as a limited company under this Act,

(a) aims to use its earnings, if any, or other revenue in advancing its purposes; (b) has as one of its objectives the promotion of trade, art, science, sports, education, research, social welfare, religion, charity, environment protection, or any other object; and c) The Central Government may, by licence issued and under such conditions as it deems appropriate, permit that person or association of persons to be registered as a limited company under this section without the addition to its name of the words "Limited" or, as the case may be, the words "Private Limited." The Registrar will then, upon application, in the form, register such person or association of persons.

(2) The company established in accordance with this section is subject to all the rights and liabilities of limited companies.

(2) A company registered in accordance with this section may include a firm as a member.

(4) (i) A business registered under this section may not change the terms of its articles or memoranda without first receiving authorisation from the Central Government. (ii) Only after meeting these requirements is a company registered under this section permitted to transform into a company of any other sort.

- Results of registration.—Section 9 of the Company Act Such subscribers to the memorandum and all other individuals who may at any time join the company will be a body corporate by the name stated in the memorandum, capable of performing all the duties of an incorporated company under this Act, having perpetual succession, and having the authority to acquire, hold, and dispose of property, both movable and immovable, tangible, and intangible.

➔ **Company's registered office:**

Any correspondence pertaining to the firm should be submitted to its registered office, which is its official address. Since it is a matter of public record, the Company receives communications from various government agencies and other organisations using the same record. At the time of the company's incorporation, the registered office is chosen. By following the method outlined in the Companies Act of 2013, we can alter the registered office of the Company at any point in the future. A business must have a registered office capable of receiving and recognising any messages and notices that may be always directed to it within thirty days of its establishment and afterwards. At the time of formation, the firm must submit the required address documentation, such as a conveyance, lease agreement, rent agreement, etc., and a copy of a utility bill (not older than two months).

CHANGE IN REGISTERED OF THE COMPANY:
Once a business is registered, its registered office may be changed at any time. Due process needs to be followed to change the registered office. After the date of the company's incorporation, notice of any change in the circumstances of the registered office must be sent to the Registrar within thirty days of the change, who must then record it. Any time a business's registered office is moved outside of a city, town, or village, a special resolution of the company must be enacted to authorise the new address. Without the Regional Director's approval, a company's registered office cannot move from the jurisdiction of one registrant to that of another registrant. Every firm must prominently display its name and registered office address in visible characters on the exterior of any office or location where it conducts business. This information must also be kept up to date.

2.7. PROCESS OF ALTERATION OF MEMORANDUM OF ASSOCIATION

The expression "alter" means to modify/ change or vary; to make or become different in some respect. As per section 2(3) of the companies act, 2013 "Alter and alteration" shall include the making of additions, omissions, and substitutions.

Step 1: Board of Directors meeting notice

Any amendment to a Memorandum of Association must first be communicated to the Board of Directors (BoD) in order to proceed. The BoD must be informed by notice at least seven days before the actual board meeting, as required by Section 173 of the Act.

A draught of the resolution and information on the proposed change must be included with the notice.

Step 2- Meeting with the Board of Directors in Step 2

The conducting of the board meeting is the second stage in amending the Memorandum of Association. The conference hears arguments about the need, benefits, and drawbacks of the suggested change. The date, place, and time of the general meeting are then set, if the BoD decides to implement such a change. Additionally, a director or another person is permitted to give notice of the general meeting to each and every company member.

Step 3: Extraordinary General Meeting Notice

The notice of the general meeting is then distributed to the company's directors, members, and auditors. The notification must be delivered at least twenty-one days before to the scheduled general meeting in accordance with Section 101 of the Act. The notice may be sent physically or electronically. The proposed meeting's actual date, time, and location should be included in the notification. It should also provide a summary of the agenda items that will be discussed during the meeting.

Step 4: General Meeting • The quorum for the meeting is first verified on the day of the general meeting. A private business requires a quorum of at least two members. (Personally present.) The quorum for a public corporation is at least five, however under Section 103 of the Act, the quorum varies depending on the number of members present.

• The existence of the business auditor is then verified. A leave of absence could be given if he or she is not present. Finally, the special resolution that was being considered for changing the Memorandum of Association was approved. A special resolution is said to have passed when it receives at least three times as many votes in support as against it. Votes may be cast in person, via mail ballot, or through a proxy.

Step 5: Submit an application to the company's registrar. Various applications must be submitted to the RoC within 30 days after passing the necessary resolution after it has been passed. As will be detailed below, the applicability change from one clause to another.

2.8 PROCEDURE FOR ALTERATION OF ARTICLES OF ASSOCIATION OF A COMPANY

Section 14 of the CA, 2013, provides for the modification of AOA. It states that certain resolutions may be used to change articles. Additionally, it has the ability to change the articles governing the transformation of a private company into a public company and a public company into a private firm. Additionally, the articles that are being suggested for change must be checked to see if they are entrenched; if so, the proper procedure for amending such provisions must be followed.

2.8.1 STEP BY STEP GUIDE TO ALTER THE AOA OF A COMPANY

1. Board Meeting:

Call a meeting of the board where pertinent information such as the-

• Take into account and approve any changes to the company's AOA.

• Next, choose the day, time, date, and agenda for the general meeting that will adopt the special resolution to put the change into effect.

• Following that, a director will be given permission to issue notice for the general meeting and a draught notice for the meeting will be created.

• Give the go-ahead for any official, including the company secretary, to notify all members by notice of the impending general meeting.

• Permit the CS, CFO, or any director to submit a copy of the special resolution to the ROC. (Registrar of Company)

2. Call a General Meeting

• To adopt a special resolution to change AOA, a general meeting must be summoned.

• A postal ballot may be used to pass a resolution.

3. Time-Bound Disclosures • In accordance with Regulations 30 and 46(3) of the SEBI (LODR) Regulations, 2015, a listed company must transmit the results of the general meeting to stock exchanges where it is listed within 24 hours of the meeting's end.

- Regulation 44 of the SEBI (LODR) Regulations, 2015 mandates that the listed company shall submit to the stock exchange within 48 hours of the conclusion of its general meeting the details regarding the voting rights in the format specified by SEBI. In addition, it should post the meeting's outcomes on the company website within two days.

4. Filing of Forms and Documents

• A copy of the special resolution and an explanation must be filed with the ROC in Form MGT-14 within 30 days of passage, together with the necessary paperwork and fees, according to Section 117 read with Rule 24 of the 2014 Companies (Management and Administration) Rules.

5. Post Compliances • It must be guaranteed that the changes to the articles are indicated in each copy of the AOA in order to be in compliance with Section 15(1).

2.8.2 COPIES OF MEMORANDUM, ARTICLES, ETC TO BE GIVEN TO MEMBERS

According to section 17 of the company act, a company must send a member who requests it a copy of each of the following documents within seven days of the request and subject to payment of any fees that may be prescribed:

- (a) the memorandum;
- (b) the articles; and
- (c) every agreement and every resolution.

- Service of documents.—A document may be served on a company or one of its officers in accordance with Section 20 of the Company Act by sending it to the company or the officer at the registered office of the company via registered mail, speed post, courier service, leaving it at the registered office, or using any other electronic or other mode that may be prescribed. As long as the securities are stored with a depository, the depository may supply the firm with the records of the beneficial ownership through electronic or other means. A document may be served on the Registrar or any member by sending it to them through mail, registered mail, speed mail, courier, delivery at their offices or addresses, or by any other prescribed electronic or other manner. This includes electronically filing papers with the Registrar. To the extent that a member requests delivery of a document via a certain method, he is responsible for paying any costs decided upon by the business at its annual general meeting.

2.9 SUMMARY

A company is a legal entity formed by individuals, shareholders, or other companies to engage in business activities. It is an organization that sells goods or services to customers, with the primary goal of generating revenue and profits

A Memorandum of Association (MOA) is a legal document that outlines the constitution of a company. It contains Name Clause, Registered Office Clause, Object Clause, Liability clause, Capital Clause.

An article of association is a legal document that outlines the purpose, functions, and structure of an organization or company. It sets forth the rules and regulations by which the organization or company will operate, including the rights and responsibilities of its members, shareholders, and board of directors.

2.10 QUESTIONS

I) Rewrite the following sentences by selecting correct option

1. What is the minimum number of members required to form a public limited company?
   a. 10 b. 2 c. 5 d. 7
2. What is known as charter of company
   a. MOA b. AOA c. Prospectusd. d. Certificate of Incorporation
3. In case o Private companies, MOA must be signed by _____ members
   a. 1 b. 2 c. 3 d. 7
4. Private company can start its business immediately after the issue of

a. certificate of commencement of business
b. certificate of incorporation
c. both
d. none of the above

5. Application for approval of name of a company is to be made to

a. SEBI b. Registrar of Companies
c. Government of India
d. Government of the State in which Company is to be registered

(Ans. 1-d , 2-a, 3-b, 4-b, 5-b)

II) State whether the following statements are true or false:

1. It is necessary to get every company incorporated, whether private or public.
2. Statement in lieu of prospectus can be filed by a public company going for a public issue.
3. A private company can commence business after incorporation.
4. Experts who help promoters in the promotion of a company are also called promoters.
5. A company can ratify preliminary contracts after incorporation.

(Ans. True – 1,2,3 False – 4,5)

III) Write a short note on:

a) Incorporation of company
b) Article of Association
c) Memorandum of Association
d) Company's registered office
e) Alteration of AOA

IV) Descriptive Question:

1. Explain Memorandum of Association? what are the Contents of Memorandum of Association?
2. Advantages and Disadvantage of Incorporation of a Company
3. Difference between Memorandum of Association and Article of Association.
4. what are the various step in Incorporation of a Company?
5. what are the process of alteration in Memorandum of Association

❖❖❖❖

3

PUBLIC OFFER
SECTION 23,25 TO 28,33,35,39

Unit Structure:

3.0 OBJECTIVE

Students will be able to:

- Elaborate various concepts like prospectus, statement in place of prospectus, and Shelf prospectus after completing the lesson.
- Describe the Prospectus's contents.
- Talk about the prospectus's legal obligations.
- Outline the penalties for making false statements and how to defend yourself against these penalties.

3.1 INTRODUCTION

Companies require money to stay afloat in the commercial world. These cash could be needed for immediate or long-term needs. Companies issue shares to meet their long-term demands.

There are three ways to issue shares:

(1) by a private placement of shares,

(2) through a public offering.

(3) Distributing the share to current investors

3.2 PUBLIC ISSUE SECTION 23 OF THE COMPANIES ACT, 2013

Mentions Public Issue as a method of public fund-raising. It refers to the marketing or sale of stock in anticipation of public subscription through the release of a prospectus. By releasing shares to the general public and becoming listed on one of India's reputable stock exchanges, public issues are important.

23 (1) A Public company may issue securities- (Bye Law)

a) to public through prospectus (herein referred to as “public offer”) by complying with the provisions of this part; or

b) 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 boards of India, 1992 and the rules and regulations made thereunder.

(2) A private company may issue securities-

a) by way of rights issue or bonus issue in accordance with provisions of this act or

b) through private placement by complying with the provisions of part II of this chapter.

An explanation of this section 23: A Public company may issue securities-

The prospectus and securities allotment rules are outlined in the Companies Act of 2013. The fundamental techniques for issuing securities by both public and private enterprises are outlined in Section 23, which is the first section under this chapter.

The following is briefly outlined in the section:

A public firm has three options for issuing securities:
1. Through public prospectus.

2. Private placement, second.
3. Bonus or rights problem.

A firm that is already publicly traded or one that plans to list its securities may issue securities in accordance with the Securities and Exchange Board of India Act, 1992, and any relevant prescribed rules.

• The term "public offer" as used in this section refers to a company's initial or subsequent public offering of securities as well as a current shareholder's public offer to sell securities through the publication of a prospectus.

• An initial public offering (IPO) occurs when a non-public corporation makes securities available to the general public for purchase, as well as when any current holder of such securities in a non-public company makes a similar offer.

• A further public offer involves a sale of securities to the public by current owners of such securities in a listed business. It also refers to an offer of securities for subscription to the public by a listed firm.

A corporation can list on a reputable stock market in India by way of a public issue, or by offering securities to the general public. As stated in Section 24 of the Act of 2013, SEBI has the authority to regulate the issuance and transfer of securities by listed and unlisted companies. As such, SEBI (Issuance of Capital and Disclosure Requirement) Regulation, 2009 and SEBI (Listing Obligations and Disclosure Requirements), Regulations, 2015, are two rules and regulations that must be adhered to when making a public offering. stocks for corporate private placements are not as regulated or as closely watched as those for publicly traded stocks.

3.3 PROSPECTUS

The Companies Act, 2013 defines a prospectus under ***section 2(70)***. Prospectus can be defined as "any document which is described or issued as a prospectus".

Any invitation to the public to subscribe for shares or debentures is included in the definition of prospectus. A prospectus is a written statement that serves as an invitation to the general public to purchase business shares or debentures. Thus, a prospectus is a document that is labelled or published as a prospectus. A prospectus includes even requests for public bids to subscribe for shares or debentures.

Type of Prospectus:

3.3.1 These are of different types. Some of them are:-

1.Red Herring

2.Shelf

3.Abridged

4.Deemed

1. Red Herring Prospectus

All of the information on the offer of securities is contained in the offer document. However, it excludes the size of the offering and the cost of the securities. Additionally, it is not the final prospectus because the company may make updates before the final release.

It is so titled because it has a para in red ink and the issuer corporation must file it with the registrar at least three days before the opening of the offer. According to that, the company is not seeking to sell the shares before SEBI has given its consent.

2. Shelf Prospectus

•The Shelf Prospectus is a single document that a company may issue several issues from, and banks and other financial institutions typically issue it.

• In this situation, the firm does not need to submit a new prospectus with each issue after filing it with the ROC. Although it has a one-year expiration date, the corporation may file an information memo requesting a modification if the situation changes.

3. Abridged Prospectus

It refers to a memorandum that highlights key elements of a prospectus and provides investors with concise information to assist them make an investment choice fast.

• In this situation, the Company must include it with each application for the acquisition of securities.

3.4 DEEMED PROSPECTUS:

Deemed prospectus has been stated under ***section 25(1) of the Companies Act, 2013.***When any company to offer securities for sale to the public, allots or agrees to allot securities, the document will be considered as a deemed prospectus through which the offer is made to the public for sale. The document is deemed to be a prospectus of a company for all purposes and all the provision of content and liabilities of a prospectus will be applied upon it.

In the case of ***SEBI v. Kunnamkulam Paper Mills Ltd.***, it was held by the court that where a rights issue is made to the existing members with a right to renounce in the favour of others, it becomes a deemed prospectus if the number of such others exceeds fifty.

3.4.1 Prospectus includes the following content:

1. **Name of the Company**
2. **Registered Address of Company**
3. **Objects of the Company**
4. **Purpose of the issue**
5. **Nature of Business**
6. **Capital structure of Company**
7. **Name and address of Signatories and no of shares subscribed by them**
8. **Qualification shares of the Directors**
9. **Particulars of Debentures and redeemable preference shares**
10. **Remuneration of Directors and Promoters**
11. **Minimum Subscription for allotment**
12. **Date of opening and closing of issue**
13. **Details of Underwriter**
14. **Underwriting Commission and Brokerage**
15. **Name and address of Auditor, Company Secretary, Banker and Trustee of Company**
16. **Particulars of material documents**
17. **Expected rate of dividend and voting rights**

3.5 VARIATION IN TERMS OF CONTRACT OR OBJECTS IN PROSPECTUS U/S 27 (BYE LAW)

(1) A company shall not, at any time, vary the terms of a contract referred to in the prospectus or objects for which the prospectus was issued, except subject to the approval of, or except subject to an authority given by the company in general meeting by way of special resolution:

Provided that the details, as may be prescribed, of the notice in respect of such resolution to shareholders, shall also be published in the newspapers (one in English and one in vernacular language) in the city where the registered office of the company is situated indicating clearly the justification for such variation:

Provided further that such company shall not use any amount raised by it through prospectus for buying, trading or otherwise dealing in equity shares of any other listed company.

(2) The dissenting shareholders being those shareholders who have not agreed to the proposal to vary the terms of contracts or objects referred to in the prospectus, shall be given an exit offer by promoters or controlling shareholders at such exit price, and in such manner and conditions as may be specified by the Securities and Exchange Board by making regulations in this behalf. **(Bye Law)**

Except by adopting a special resolution by postal vote, the firm may not modify the terms of contracts mentioned in the prospectus or the purposes for which the prospectus was issued. The notice of the proposed special resolution must include the following information:-

(a) the initial goal or purpose of the Offering;

(b) the total amount raised;

(c) the amount of money used to further the company's objectives as indicated in the prospectus;

(d) the extent of achieving the intended goals (i.e., 50%, 60%, etc.;

(e) the amount of funds that were not used from the funds generated through the prospectus,

(f) the specifics of the proposed modification to the terms of contracts referred to in the prospectus or the objectives for which the prospectus was issued;

(g) the justification for the requested modification;

(h) the proposed deadline for achieving the modified objectives;

(i) the clause-by-clause information required by sub-rule (3) of rule 3 with regard to the initially proposed objectives of the issue; and

(j) the risk factors pertaining to the proposed modification. and

(k) The additional pertinent data required for the members to make an informed choice about the proposed resolution.

(2) Form PAS-1 must be used for the advertisement of the notice for getting the resolution passed that modifies the terms of any contract mentioned in the prospectus or changes the purposes for which the prospectus was issued. This advertisement must be published at the same time as the postal ballot notices are sent to shareholders.

The notice must also be posted on the company's website, if one exists.

3.6 OFFER OF SALE OF SHARES BY CERTAIN MEMBERS OF COMPANY. (BYE LAW)

(1) Where certain members of a company propose, in consultation with the Board of Directors to offer, in accordance with the provisions of any law for the time being in force, whole or part of their holding of shares to the

public, they may do so in accordance with such procedure as may be prescribed.

(2) Any document by which the offer of sale to the public is made shall, for all purposes, be deemed to be a prospectus issued by the company and all laws and rules made thereunder as to the contents of the prospectus and as to liability in respect of mis-statements in and omission from prospectus or otherwise relating to prospectus shall apply as if this is a prospectus issued by the company.

(3) The members, whether individuals or bodies corporate or both, whose shares are proposed to be offered to the public, shall collectively authorise the company, whose shares are offered for sale to the public, to take all actions in respect of offer of sale for and on their behalf and they shall reimburse the company all expenses incurred by it on this matter. **(Bye law)**

Explanation of the Same:

Promoters of a publicly traded firm can sell their shares in a transparent manner to the general public through an offer for sale.

When specific business members want to sell all or a portion of their shares to the public, they can do so by following the established method. The Board of Directors must be consulted about this idea, and it must also follow all currently in effect laws.

Any such offer document shall be regarded to be a prospectus issued by the company, and this document shall be subject to all laws and regulations relating to prospectuses.

Collectively, these members shall provide the company its consent to act for and on their behalf in connection with the offer of sale. They will cover any costs made by the business in this regard.

3.7 ISSUE OF APPLICATION FORMS FOR SECURITIES (SECTION 33) (BYE LAW)

As per Section 33 of Indian Companies Act 2013 no form of application for the purchase of any of the securities of the company shall be issued unless such form is accompanied by an abridged prospectus. Provision in the Companies Act 2013 related to issue of application forms for Securities is as under.

(1) No form of application for the purchase of any of the securities of a company shall be issued unless such form is accompanied by an abridged prospectus:

Provided that nothing in this sub-section shall apply if it is shown that the form of application was issued

(a) in connection with a bona fide invitation to a person to enter into an underwriting agreement with respect to such securities; or

(b) in relation to securities which were not offered to the public.

(2) A copy of the prospectus shall, on a request being made by any person before the closing of the subscription list and the offer, be furnished to him.

(3) If a company makes any default in complying with the provisions of this section, it shall be liable to a penalty of fifty thousand rupees for each default.

3.8 THE LIABILITIES FOR MIS-STATEMENTS IN PROSPECTUS CAN BE COVERED UNDER THE FOLLOWING HEADS:

1. Civil Liability
2. Criminal Liability

Civil responsibility for prospectus lies (section 35)

When a prospectus contains factual errors or omissions that are intended to mislead, civil liability may result, provided that the error or omission caused the shareholder to purchase the shares in question. Every director, promoter, and other individual, such as an expert who approved the release of the prospectus, is responsible for any untruth or misrepresentation made to the person receiving the share allocation. The shareholder who bought shares on the basis of such misrepresentation has the right to sue the firm, as well as its directors, promoters, experts, etc., for any losses or damages he may have experienced.

1. Civil Liability

Whenever a person purchases a company's securities based on a misleading statement, inclusion, or omission in the prospectus and suffers loss or damage as a result of acting on that information,

- The company and everyone involved—including the person who made the misleading statement—are liable.
- The firm's director or has consented to take that position; or

• The director of the company at the time the prospectus was released:

- A professional who has been involved or interested in the establishment, management, or marketing of the firm, as well as one who is a promoter of the company, has sanctioned or allowed the release of the prospectus,
- or is a promoter of the company will be responsible for compensating any individual who has experienced such loss or harm, without affecting any penalties that may be imposed on anyone.

Exemption from Liability

No person shall be liable for misstatement if the person proves that-

1.Prior to the prospectus's release, the individual withdrew his permission. If a person who had agreed to become a director of the firm later withdraws their agreement, it would mean that the prospectus was published without their approval.

2. if a person is not consulted or informed before the prospectus is released. When a person learns that a prospectus was released without his or her knowledge or approval, and after learning of its release, the person issues a proper public notice stating that the prospectus was not issued with his or her consent.

3. Such a claim or omission was irrelevant, or

4. He had a good basis to think that the statement was accurate and that the omission or inclusion was required, and he had that belief up to the prospectus' release.

3.8.1 Penalities for misstatements in prospectus

1. Compensation: The aforementioned individual is responsible for compensating each subscriber for shares or debentures for any loss or harm he suffers as a result of any false information included therein.

2. Damages for deception or fraud: Anyone who was persuaded to invest in a firm by a prospectus that contained a misleading statement may bring a claim against the company and the person at fault for damages. Before suing the corporation for damages, the shares should be returned to it first. When a statement is made carelessly or without faith in its veracity, fraud has occurred. Fraud or deception is when a statement is made with the intent to deceive.

3. General law liability: For false representations or fraud, any person in charge of the prospectus' release may be held accountable under either general law or the Act.

4. Rescission of the Contract for Misrepresentation: Rescission of the Contract refers to a court order or a party's termination of a contract. If the assertion he used to purchase the shares is untrue or the result of deception, whether innocent or dishonest, the contract will be voided. It must not be a legal matter but a material fact. It should be highlighted that if a party had the resources to ascertain the truth with reasonable diligence, he could not assert a right to rescission of contract based on misrepresentation.

2. Criminal Liability

Section 63 of the Companies Act deals with criminal liability for mis-statements in prospectus

- Every person who authorises the release of a prospectus is liable for fraud if the prospectus contains any statement that is false or deceptive in whatever way it is presented or if any information is inserted or omitted that has the potential to deceive.

- According to Section 447, "fraud" refers to any act, omission, or concealment of any truth that is done with the intention of misleading others, obtaining an unfair advantage, or harming the interests of the firm, its shareholders, creditors, or any other person. Such a conduct does not necessarily include any unjust gain or loss. Under the provisions of this clause, misuse of position is also deemed fraud.

Penalty for mis-statement

If someone is found guilty of the crime of fraud, they will be sentenced to a term of imprisonment that must be less than six months and cannot exceed 10 years. He will also be subject to a fine, which must be less than the sum involved in the fraud and cannot be greater than three times that amount.

The sentence must be at least three years in jail if the fraud involved public interest.

3.9 ALLOTMENT OF SECURITIES BY COMPANY (SECTION 39). (Bye Law)

(1) No allotment of any securities of a company offered to the public for subscription shall be made unless the amount stated in the prospectus as the minimum amount has been subscribed and the sums payable on application for the amount so stated have been paid to and received by the company by cheque or other instrument.

(2) The amount payable on application on every security shall not be less than five per cent. of the nominal amount of the security or such other percentage or amount, as may be specified by the Securities and Exchange Board by making regulations in this behalf.

(3) If the stated minimum amount has not been subscribed and the sum payable on application is not received within a period of thirty days from the date of issue of the prospectus, or such other period as may be specified by the Securities and Exchange Board, the amount received under sub-section (1) shall be returned within such time and manner as may be prescribed.

(4) Whenever a company having a share capital makes any allotment of securities, it shall file with the Registrar a return of allotment in such manner as may be prescribed.

(5) In case of any default under sub-section (3) or sub-section (4), the company and its officer who is in default shall be liable to a penalty, for each default, of one thousand rupees for each day during which such default continues or one lakh rupees, whichever is less.

3.10 ALLOTMENT OF SECURITIES UNDER THE COMPANIES ACT, 2013

(i) Private Placement

(ii) Right Issue

(iii) Preferential Allotment

1. PRIVATE PLACEMENT: - Private placement refers to any offer of securities, invitation to subscribe for securities, or invitation to subscribe for securities made to a select group of individuals by a company (other than through a public offer) through the issuance of a private placement offer letter that complies with the requirements outlined in Section 42 of the Companies Act, 2013. Section 42 of the Companies Act of 2013 in conjunction with Rule 14 of the Companies of 2014 govern private placements of stocks.

CONDITIONS: - (i) A private placement offer may not be made to more than 200 individuals in a single financial year, with the exception of "Qualified Institutional Buyers (QIBs)" and employees of the Company who are receiving securities under a plan of employee stock options in accordance with Section 62's clause (b).

The Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009, as amended, define a qualified institutional buyer (QIB) as one who meets the requirements for capital and disclosure.

(ii) Regardless of whether payment has been received for the securities or whether the company intends to list its securities on a recognised stock exchange inside or outside of India, if a company, whether listed or unlisted, makes an offer to allot, invites subscription, allots, or enters into an agreement to allot securities to more than 200 persons, the transaction will be deemed to be an offer to the public and will be subject to Part I's rules.

No new offer or invitation under this section may be extended unless the Company has withdrawn or abandoned an earlier offer or invitation, the allotments for which have been completed, or both.

(iv)There must be a minimum of 60 days between any two such offers or invitations, and no more than four such offers or invitations may be extended in a fiscal year or more than once in a calendar quarter.

(v)The amount of the offer or invitation must be equivalent to at least Rs. 20,000 per individual in face value of the securities.

(vi) A company making an offer or invitation under this section must allot its securities within 60 days of the date it receives the application money for those securities. If it is unable to do so, it must repay the application money to the subscribers within 15 days of the completion of the sixty-day period. If it fails to do so within the aforesaid time frame, it will be responsible for repaying the application money.Additionally, the funds received as share application funds must be stored in a separate bank account at a designated bank and cannot be used for the following purposes: - For adjustments against securities allocation; - For repayment of funds in cases where the Company is unable to allocate securities.

(vii) No corporation is permitted to make an offer of securities under this section through the publication of public ads or the use of media, marketing, or distribution channels or agents.

(viii) Any invitation or offer that does not adhere to the rules of this section will be considered a public offering, and all rules under the Companies Act of 2013, the Securities Contracts (Regulation) Act of 1956, and the Securities and Exchange Board of India Act of 1992 must be followed.

2. SHARES' RIGHTS ISSUE: When new shares are issued to existing shareholders in proportion to their present holdings, this is referred to as a right issue of shares. Section 62 of the 2013 Companies Act governs the Right Issue of shares.

CONDITIONS: - In accordance with Section 62 (1), whenever a business with a share capital seeks to issue additional shares in order to enhance its subscribed capital: -

(a) by issuing a letter of offer subject to the following requirements, namely: - To people who, at the date of the offer, are holders of equity shares of the firm in proportion, as closely as circumstances permit, to the paid-up share capital on those shares.

(i)the offer shall be made by notice specifying the number of shares offered and limiting a period of time not to exceed thirty days from the date of the offer within which the offer, if not accepted by 90% of its members, shall be deemed to have been declined; (ii)unless the Articles of the Company otherwise provide, the foregoing offer shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him. And

(iii) The Board of Directors may dispose of the shares in a way that is advantageous to the shareholders and the company after the time period specified in the aforementioned notice has expired or upon receiving an earlier indication from the person to whom such notice was given that he declines to accept the shares offered.

3. PREFERENTIAL allocation OF SHARES: Section 62(1(C) of the Companies Act of 2013 and Rule 13 of the Companies (Share Capital and Debentures) Rules of 2014 govern the preferential allocation of shares.

3.11 SUMMARY

Any business needs money to be able to survive and grow. The act of 2013's Section 23 allows for the issuing of securities to the public, members, or other parties in order to meet short- or long-term financial needs. The many techniques listed in section 23 are excellent ways for a business to get funds. Although section 23 permits the use of a variety of methods for raising money, each form of issuance has its own set of criteria, procedures, and disclosure requirements. A prospectus is a crucial document for public offerings and a method of issuing securities and obtaining cash. A prospectus is crucial for an initial public offering (IPO) in particular since it informs investors about the firm. Private placement is governed by a separate provision that has undergone several amendments to ensure that there are no gaps in the law. This section, which outlines the techniques to ensure that a corporation has money and is, thus, operating, is crucial. Understanding this clause is crucial since it, together with other Act provisions and SEBI and MCA rules and regulations, aid in keeping businesses viable.

3.12 QUESTIONS

I) Rewrite the following sentences by selecting the correct option

1. How many ways are there for issuing shares

a-by a private placement of shares b-by a public offer

c-distributing the share to current investor d-all of the above

2.How many options are there available for public firm for issuing securities.
a-Public prospectus b- Private Placement
c-bonus or rights d-all of the above

3.Which of the following is not a prospectus?
a-Red herring b-Deemed
c-Shelf d-MOA

4.Prospectus includes:
a-Name of the company b-Nature of business
c-Capital of the company d-all of the above

5.Red herring prospectus excludes:
a-size of the offering b-cost of securities
c-none of the above d-all of the above

(Answers:1-d,2-d,3-d,4-d,5-d)

II) State whether the following statements are true/false

1. Red herring prospectus is a final prospectus
2. Deemed prospectus is covered under section25(1) of the companies act,2013
3. Form PAS-1 must be used for the advertisement of the notice for getting the resolution passed that modifies the terms of any contract mentioned in the prospectus or changes the purposes for which the prospectus was issued.
4. A private placement offer may not be made to more than 250 individuals in a single financial year
5. section**63** of the Companies Act deals with criminal liability for mis-statements in prospectus

(Answers:-1-false,2-true,3-true,4-false,5-true)

III) Write a short note on

a) Variation in terms of contract.
b) Offer of sale of shares
c) Exemption from the liabilities for Mis-statements in prospectus

IV) Descriptive Questions

1. Define Public offer and explain different way of issue of share by the companies?

2. Define Prospectus and what are the different type of prospects?

3. What does a prospectus includes?

4. What are the different liabilities for Mis-statements in prospectus?

5. What are the different type of allotment of securities under the companies act 2013.

❖❖❖❖

4

PRIVATE PLACEMENT

Unit Structure

4.1 INTRODUCTION

Offer or invitation for subscription of securities on private placement. **(Bye Law)--**

(1) Without prejudice to the provisions of section 26, a company may, subject to the provisions of this section, make private placement through issue of a private placement offer letter. (2) Subject to sub-section (1), the offer of securities or invitation to subscribe securities, shall be made to such number of persons not exceeding fifty or such higher number as may be prescribed, [excluding qualified institutional buyers and employees of the company being offered securities under a scheme of employees stock option as per provisions of clause (b) of sub-section (1) of section 62], in a financial year and on such conditions (including the form and manner of private placement) as may be prescribed.

Explanation:

Private placement, as defined by Section 42 of the Companies Act of 2013, is any offer or invitation by a company to subscribe for or issue securities to a chosen group of people (other than through a public offer) through a private placement offer-cum-application form that complies with the requirements outlined in Section 42 of the Companies Act of 2013.

According to Section 42 of the Companies Act of 2013, an allocation can only be made up to 200 times per year; beyond that, the issue is deemed public and the firm must follow the public issue procedure. There is no prospectus released during the private placement procedure.

4.2 TYPES OF PRIVATE PLACEMENT

1. Preferential Allotment

2. Qualified institutional placement

1.Preferential Allotment: Shares are allocated on a preferential basis to a particular group of people or businesses that express interest in them at a predetermined price. Shares or other securities offered through a public offering, a rights offering, an employee stock option plan, an employee stock purchase plan, an issue of sweat equity shares or bonus shares, depository receipts issued in a nation outside of India, or foreign securities are not included in preferential allotment. The rules for such an allocation are laid forth in SEBI (DIP) guidelines Chapter XIII. The corporation must take into account that the investors may have a lock-in period for the securities' issuance.

2. A qualified institutional placement (QIP): Fundamentally, a QIP is a method for listed firms to raise money without having to file formal documentation with market regulators. Only institutional investors may purchase shares or other securities from a listed firm. As a result, listed corporations are encouraged to raise money on the domestic market. The SEBI (DIP) guidelines' Chapter XIIIA specifies the rules regulating these placements. In India and other Southeast Asian nations, it is typical.

4.2.1.1 Preference share:

The Preference Shares are ownership interests in the Company that provide their owners the exclusive right to profit from the Company before other normal shareholders. Furthermore, in the event that the Company must shut down or fails in the future, the Preference Shareholders are entitled to a reimbursement of their capital. As a result, there is far less risk of loss.

When a business issues securities or shares to a certain group of investors, this is known as a preferred issue. The Preferential Issue is not a Right Issue or a Public Issue. The Preferential Issue of Shares is a unique means of raising money in compared to other methods. In a preferential issue of shares, the whole allocation of shares is given to a pre-identified person who may or may not already be a shareholder in the company.

4.2.1.2. Documents submitted for the preferential allocation of shares

Form	Purpose	Time Period
Form PAS-3	In order to refund the shares that were allocated.	List of allotees verified authentic copy of board resolution within 15 days after allocation date.
Form MGT-14	Fro passing a special resolution for the preferential allotment.	Within 30 days of the resolution's passage, a certified true copy of the Special resolution, as well as an explanation, must be submitted.

4.2.1.3 Advantages of Preferential Allotment

The corporation benefits from preferential allotment of shares in several ways. Preferential Allotments provide the following benefits:

1. No change on Assets:

The absence of a levy on the assets is the first benefit. Shares and convertible securities are available through preferential allocation. Unlike debentures, the shares do not place a levy on the assets. Furthermore, maintaining the assets at risk is not a requirement for preferential allocation. As a result, it is advantageous for both the company and the current shareholders.

2. Convertible securities:

The following benefit is an additional gain for shareholders and investors. Dealing in convertible securities is possible through preferential allocation. Investors and shareholders can convert their convertible assets into shares and get dividends and additional earnings if the share price rises. The predefined and fixed interest on the securities or debentures is exceeded by the dividends and earnings. For all of the current investors and stockholders, it is a fantastic opportunity.

3. No dilution of power:

The lack of a requirement for power dilution is the next benefit. Because stockholders do not get voting rights, preferential allocation does not result in a reduction in power. Investors or shareholders have a right to dividends and interest but no vote or participation in board meetings. As they won't have to share their authority with other shareholders, it is advantageous for both the firm and the directors.

4. Improve the borrowing capital:

The firm's ability to borrow money is increased via preferred allocations, which is the last benefit. It lets them make room for non-convertible debentures and loans, which lowers the debt-to-equity ratio.

4.2.1.4. Disadvantages of Preferential Allotment

1. Harm to the reputation of the firm:

Even though a corporation that fails to pay an annual or defined amount of dividend may not face legal repercussions, its reputation might suffer. First things first: an investor won't buy a business or a securities that won't generate future profits. If, for instance, Firm A generates profits and distributes dividends to its shareholders each year whereas Firm B does not, an investor may choose to invest in Firm A in order to profit. Additionally, it may have an impact on the company's reputation while borrowing money. The reason for this is that lenders won't offer money unless they are confident the firm will repay the whole amount.

2. Investors' lack of voting rights:

Shareholders who receive funds through preferential allotments do not have the same degree of ownership or voting rights as regular shareholders. Additionally, it could stop them from putting their funds into such a plan. As a result, it may have the advantage of generating a sizeable sum of money for the business' operations but may not also benefit shareholders.

3. Impact credit worthiness:

The distribution of preference shares lowers a company's creditworthiness since the shareholders have the right to the company's personal assets.

4. The allocation of shares with preference also enables certain groups to get advantages that they may not otherwise enjoy. For instance, promoters are known to have repeatedly profited personally from the benefits of these privileged shareholders. This deprives other real, otherwise interested owners of their shareholding rights and keeps them in a somewhat subordinate position to preferential shareholders. It also denies them the same rights as preferential shareholders.

4.2.2.1 How does Qualified institutional placement works:

1. The Securities and Exchange Board of India originally designated a qualified institutional placement (QIP) as a securities issuance. (SEBI). An Indian-listed firm can raise money on its home market using the QIP without having to notify any market regulators in advance of the issuance. Companies are only permitted to raise capital through the sale of securities under SEBI regulations.

2. On May 8, 2006, the SEBI announced the rules for this distinctive form of Indian funding. The main goal of creating QIPs was to prevent India from relying too much on foreign money to finance its economic expansion.

- Prior to the QIP, Indian regulators had grown increasingly concerned that domestic companies were using American depository receipts (ADRs), foreign currency convertible bonds (FCCBs), and global depository receipts (GDR) rather than Indian-based capital sources to access international funding too easily. The QIP rules were put out by the authorities to encourage Indian enterprises to seek money domestically rather than through international channels.

- QIPs are beneficial for a number of causes. Their usage saves time since they provide access to finance and QIPs far more quickly than a follow-on public offering would.(FPO). The speed is due to the fact that QIPs must adhere to far less legal laws and restrictions, which makes them considerably more economical. Additionally, there are lower legal expenses and no costs associated with listing internationally.

4.2.2.2. Regulations for a Qualified Institutional Placement (QIP)

The following are some rules and specifications that apply to businesses looking to raise capital through a QIP:

• To be listed on a stock market, the firm must fulfil the basic shareholding criteria specified in its listing agreement.

• If the issue is up to Rs 2.5 billion in size, the company should ensure that there are at least two allottees, and if the issue is beyond Rs 2.5 billion, at least five allottees;

• One allottee may not receive more than half of the total amount allotted; and

• At least 10% of the company's issued securities must go to mutual funds or allottees.

• Allottees must not be associated in any way with the issue's backers.

4.2.2.3 Who are Qualified Institutional Buyer (QIB)

Any one of the people mentioned below might be a qualified institutional buyer (QIB).

1. Foreign portfolio investor registered with the Board who is not a Category III foreign portfolio investor

2. Registered with the Board foreign venture capitalist

3. A minimum corpus of 25 crore rupees for a pension fund A mutual fund,

4. Insurance funds established and maintained by the Union of India's army, navy, or air force a commercial bank with a set schedule;

6. The National Investment Fund

7. An alternative investment fund; 8. a state industrial development company

8. A corporation that is insured and licenced by the Insurance Regulatory and Development Authority

9. A provident fund having a capital of at least 25 billion rupees.

10. A multinational and bilateral development finance institution;

11 a public financial institution as specified in Section 4A of the Companies Act of 1956;

12. A fund for venture capital

4.2.2.4. **Difference between Offer for Sale and Qualified Institutional Placement**

The following table lists the distinctions between Offer for Sale and Qualified Institutional Placement.

Offer for Sale	Qualified Institutional Placement
Promoters might lower their share and sell it to other players by using the offer for sale procedure.	A qualified institutional placement is a method by which a listed business can raise money from different QIBs for different purposes.
Offer for Sale has no plans to seek further funds. From one shareholder to another, ownership is transferred.	Qualified Institutional Placement wants to enhance the nation's capital base by raising money from QIBs.
In an Offer for Sale, the winning bidder must pay the entire sum up advance to seal the deal.	The payment is made internally in a qualified institutional placement since all transactions are made between the QIBs and the issuing firm.
In an Offer for Sale, the business establishes the price range in which offers are accepted.	In a qualified institutional placement, the business determines the starting price for the placement. The price is typically discounted.

4.3. PRIVATE PLACEMENT OFFER LETTER

➢ The rules for a company's private placement are outlined in Rule 14 of the Companies (Prospectus and Allotment of Securities) Rules, 2014 (the "Rules"). According to the Rules, a private placement offer letter in Form PAS-4 must be used by the company to offer or encourage investors to subscribe for its securities.

➢ Only those people whose names have been registered by the firm before delivering the invitation to subscribe shall get any private placement offers. The offer will be made to the individuals whose names are on file, and the corporation is required to keep a detailed record of all offers on Form PAS-5.

➢ A private placement offer letter should be sent along with an application form that is serially numbered, addressed in writing or electronically, and expressly addressed to the individual to whom the offer is being made. Within thirty days of registering the name of the particular individual, the Company must provide the Private Placement Offer Letter to such person.

➢ The offer should be accepted by the individual to whom the private placement offer letter is addressed in the application. Within thirty days of distributing the private placement offer letter, the firm must submit the full details of the offer with the Registrar of Companies (the "ROC").

4.4. MAXIMUM LIMIT OF PRIVATE PLACEMENT

The maximum number of people to whom the firm can make a private placement in a financial year shall not exceed fifty people or the larger number permitted by the rules. Qualified institutional purchasers and firm workers who receive shares throughout the fiscal year under an employee stock option plan in accordance with Section 62 of the Act are not included in the fifty-person maximum.

According to the Rules, no more than 200 people may be offered or invited to participate in a private placement over the whole fiscal year. The cap of 200 people will not apply to eligible institutional purchasers or corporate workers who received shares during the fiscal year under a plan for employee stock options in accordance with Section 62.

Each individual should be given a private placement offer or invitation for Rs. 20,000, which is equal to the face value of the securities.

The following are exempt from the maximum number of chosen individuals and private placement value restrictions:

1) **Non-banking financial institutions authorised by the 1934 Reserve Bank of India Act.**

2) **Under the National Housing Bank Act of 1987, housing financing enterprises must register with the National Housing Bank.**

4.5 PENALTY FOR NON-COMPLIANCE OF PRIVATE PLACEMENT

If a firm takes money or makes an offer in violation of the Act and Rules, the company, its directors, and its promoters may be subject to fines. If there was more money involved in the invitation or offer than that, the fine may be up to Rs. 2 crore. Additionally, the business must return all subscription fees to customers within 30 days of receiving the court judgement imposing the fine.

Following Securities are covered under Private Placement

1. Equity shares

2. Preference shares

3. Debentures

4.5.1 Equity shares:

Meaning: An equity share, sometimes referred to as an ordinary share, is a kind of fractional ownership that carries with it the greatest amount of entrepreneurial risk for a trading firm. These shareholders have the ability to cast ballots in any organisation.

4.5.1.1. Features of Equity Shares Capital

- ➔ The corporation still owns the equity share capital. Only after the business is shut down is it returned.
- ➔ Shareholders have voting rights and choose the management of the firm.
- ➔ The capacity to collect surplus capital is a requirement for the dividend rate on equity capital. However, the dividend rate on equity capital is not set.

4.5.1.2 Types of Equity Share

- Authorized Share Capital is the maximum sum that an organisation may distribute. According to the company's advice and with the assistance of a few formalities, this sum may be altered at any moment.
- Issued Share Capital – This is the authorised capital provided to investors by an organisation.
- A part of the issued capital that an investor accepts and agrees to is known as "subscribed share capital."
- Paid Up Capital – The investors provide a portion of the subscribed capital. Paid-up capital refers to the funds that a firm actually invests in running their business.
- Right Shares – These are the shares that a company issues to its current stockholders. The corporation issues shares of this sort in order to protect the old investors' proprietary rights.
- Bonus Share – When a company divides its shares among its shareholders in the form of a dividend, we refer to it as a bonus share
- Sweat Equity Share – This form of share is only given to an organisation's top managers or employees in recognition of their outstanding efforts in securing the company's intellectual property rights.

4.5.1.3. Merits of Equity Shares Capital

- Equity shares have the following benefits:

It is a continuous source of funding, and the enterprise has to repay; an exceptional case is under liquidation.

- Equity shareholders are the true owners of the company and have voting rights.
- Equity shares can be issued even without establishing any additional charges over the assets of an enterprise.
- It is a perpetual source of funding, and the enterprise has to repay.

4.5.1.4. Demerits of Equity Shares Capital

There are several drawbacks to trading on equity when only equity shares are issued. These drawbacks include:

- The enterprise cannot benefit from or take credit for trading on equity when only equity shares are issued.
- There is a risk of overcapitalization because equity capital cannot be recouped.
- The management may encounter obstacles from equity shareholders by directing them and systematising themselves.
- When the company generates higher profits, higher dividends must be paid, which increases the value of the shares in the market.

4.5.2. Preference Share:

4.5.2.1 Meaning: Preference shares, also known as preferred stock, are shares of a company's stock that pay dividends to owners ahead of payments on regular stock. Preferred investors are entitled to payment from firm assets before common stockholders in the event of bankruptcy. Common stocks often do not carry a set dividend, but the majority of preference shares do. Additionally, holders of preferred stock often do not have voting rights; holders of ordinary stock typically do.

4.5.2.2. Features of Preference Shares

The characteristics of preference shares are as follow

1.Shareholders' preferred dividend option.
2.Preference shareholders are unable to cast a ballot.
3. In the event that the firm is wound up, shareholders have the right to claim the assets.
4. Fixed dividend payments made to shareholders, regardless of earnings.
5. serves as a hybrid finance source.

4.5.2.3. Types of Preference Shares

The various types of preference share are discussed below:

1. Cumulative preference shares: These unique shares give owners the right to receive cumulative dividend payments even when a firm is not profitable. In years when the firm is not making a profit, these dividends

will be considered as arrears and paid cumulatively the following year when the company makes a profit.

2. Shares of preference that do not accumulate dividends in the form of arrears are known as non-cumulative shares. When it comes to non-cumulative preference shares, the company's current-year profits are used to pay out the dividend. If there is a year in which the firm doesn't generate any profit, then the shareholders are not given any dividends for that year and they cannot claim for dividends in any subsequent profit year.

3. Participating preference shares: These types of shares allow the shareholders to demand a portion in the surplus profit of the firm at the event of liquidation of the company after the dividends have been paid to the other shareholders. In other words, together with equity shareholders, these stockholders receive set dividends and a portion of the company's surplus earnings.

1.. Non-participating preference shares: Owners of these shares do not have the extra option of receiving dividends from the company's excess profits. The stockholders in this instance only receive the set dividend.

3. Redeemable Preference Shares: At a predetermined price and time, the issuing corporation may buy back or redeem redeemable preference shares. These kinds of shares benefit the business by acting as a buffer during inflationary periods.

2.3. Non-redeemable Preference Shares: Shares that cannot be redeemed at any moment throughout the company's existence are referred to as non-redeemable preference shares. In other words, these shares are only redeemable when the firm is being wound up.

4. Convertible Preference Shares: A form of convertible preference share permits owners to convert their preference shares into equity shares at a predetermined rate following the expiration of a defined time period as indicated in the memorandum.

5. Non-convertible Preference Shares: These shares cannot be changed into equity shares. Only fixed dividend payments will be made to these shares, and they will also get priority dividend payments in the event of a company's dissolution.

4.5.2.4. Advantage of Preference shares:

One of the most popular kinds of financing for both investors and corporations is preference shares. The benefits of preference shares are listed below:

1. Shares are thought of as a really innovative way to finance the company. This is primarily because preference shares may be issued with relative simplicity once a company has completed an IPO and has permitted share capital.

2. The firm is not required to refund the money it received from the sale of preference shares. In other words, it is possible to think of the principal that the company raises via the selling of preference shares as a long-term investment that doesn't need to be repaid in the future.

3. Investors are entitled to a predetermined quarterly (or yearly) return. This suggests that companies are well aware of the conditions for making dividend payments. It typically makes things easier for both parties because the issuer and investor are both aware of the dividend to which they are both entitled.

4. The issuing of preference shares has no impact on the ownership structure of the company that takes choices. Preference Shares have no voting rights, thus they have no say in how the company is managed. Since they still retain voting rights, it encourages the ordinary shareholders to participate.

5. Because preference shareholders receive a fixed return and the first claim upon liquidation, they are viewed as having more favorability by investors. (before common shareholders). Investors like investing because it has a reputation for being a low-risk investment.

4.5.2.5. Disadvantages of Preference Shares

Preference shares are seen as being quite popular, but from the standpoint of the issuing corporation, it is clear that they have a number of drawbacks. These drawbacks include the following:

1. Annual fixed dividends are often paid on preference shares. Regardless of the amount of profit the firm made in the particular year, this dividend must be paid to the owners.

2. Preference Shares turn out to be expensive over time. This is so because long-term investment instruments like debentures are subject to greater rates of interest than dividend charges.

3. On the stock exchange, shares may only be sold to the public by public limited businesses. As a result, only medium and large businesses that are officially listed on the Stock Exchange are permitted to use this option.

4. If the business is unable to pay dividends for a specific year, the dividend accrues and is carried over to the following year in the case of cumulative preference shares (which are the most widely used preference shares). This implies that in the years when they were unable to generate significant profits, it may be difficult for the corporation to pay the dividends.

5. Favourite In the event of a liquidation, stockholders must be compensated with top priority (before ordinary shareholders).

4.5.3. Debentures:

4.5.3.1. Meaning:

A sort of financial instrument called a debenture is one that businesses employ to finance long-term borrowing. Since the company's capital in this instance was borrowed, the holder of the debenture is a creditor of the business. The debentures are freely transferable, have an established interest rate, and are both redeemable and non-redeemable. It is unsecured and solely supported by the issuer's credibility.

4.5.3.2. Types of Debentures

1. Debenture categories based on security:

A debenture may carry security in terms of either carrying security or not. Debentures therefore here can be of two types:

a) Secured Debentures have a charge against certain assets of the issuing corporation. If the business doesn't pay back the loan, creditors will be repaid by selling off the company's assets. This debenture security may be one of two kinds: Floating or fixed charges. A fixed charge is a security that corresponds to a certain firm asset. A floating charge, on the other hand, applies to all of the company's assets collectively.

b) Unsecured Debentures: Investors should avoid these debentures at all costs. This is so that there is no charge or security against the assets of the business. Only the principal and interest on the debt are guaranteed by the corporation. If it fails to, its assets are not subject to attachment.

2. Debenture categories based on convertibility

To draw in investors, companies may make their debentures convertible. Based on convertibility, debentures can be classified into one of the two categories described below:

a) Convertible debt obligations: These debentures convert into equity or preferred shares after a defined period of time. Whether this conversion is mandatory or optional is up to the holder of the debenture. It may either be fully convertible or only partially convertible. Debentures have the option of converting into shares with a par value, a premium, a discount, or even at a different price.

b) Non-convertible debt obligations: Despite not being convertible, non-convertible debt obligations are nonetheless regarded as debentures. They are not convertible into shares.

3. Categories of debentures depending on permanency

Depending on their term and durability, debentures can be classified into the following categories:

a) A redeemable debenture is one that has a set redemption date. For instance, after a debenture's maturity period of five years has elapsed, it can be redeemed. These five years shall run from the date of issuance of the Debenture.

b) Irredeemable Debentures: Irredeemable debentures do not have a set maturity date. They persist throughout the length of an enterprise. Therefore, the company only redeems them in cases of impending liquidation.

4. Debenture categories based on negotiability

Transferability is mostly related to negotiability. Based on whether they are easily transferable or not, this criteria separates debentures. Debentures are divided according to the two following criteria:

a) Registered Debentures: As the name suggests, the corporation keeps records of the information regarding the holders of these debentures. Only the bondholders may redeem these bonds. They are therefore not transferable freely. The Companies Act of 2013 conditions must be completed in order for them to be transferred.

b) Bearer Debentures: In this case, businesses do not keep track of the details of the holders of the debentures. The cardholder does not need to have their identification confirmed in order to redeem them. This happens because the debentures are easily transferable. As a result, their owners allow anybody to buy and sell them.

5. Different Types of Debentures Based on Priority: Just like with shares, corporations prioritise debt instruments. Investors like to buy instruments first since it reduces their risk. Debentures in this case might take one of the two types indicated below:

a) initially Mortgage Debentures: As the name suggests, the companies are responsible for paying down these debentures initially. Debenture holders receive their funds before other holders in their category.

b) Second Mortgage Debentures: These bonds are only repaid upon the repayment of the first mortgage bonds.

4.6 SUMMARY

When deciding whether to issue a private placement, a corporation must take private placement into account. Some essential qualities to consider when choosing a lender or investor for a private placement are:

- Instead of being transaction-oriented, they are relationship-oriented. It is crucial that they take an interest in the organisations they support and put in the effort to comprehend their requirements and workings.
- Private placement debt is sometimes long-term, therefore it is crucial for the investor to be able to develop as a financial partner and to have

the skills and expertise necessary to guide a business through difficult times.

- They have access to important decision-makers inside their organisation and are quick to react and respond.

Throughout market cycles across the year, the private placement investor has a consistent desire for private placement debt.

4.7 QUESTIONS

I) Multiple Choice Questions

1. Bonds are only repaid upon the repayment of the first mortgage bonds
a-Second Mortgage Debentures
b-initially mortgage debentures
c-none of the above
d-all of the above

2. The companies are responsible for paying down these debentures initially.
b-initially mortgage debentures
c-none of the above
d-all of the above

3. The debentures are easily transferable.
a-bearer debentures b-registered debentures
c-none of the above d-all of the above

4. The corporation keeps records of the information regarding the holders of these debentures
a-bearer debentures b-registered debentures
c-none of the above d-all of the above

5. Debentures have a charge against certain assets of the issuing corporation.
a-secured debentures b-unsecured debentures
c-none of the above d-all of the above

Answers(1-a,2-b,3-a,4a,5-a)

I) True or False

1- Share Capital is the minimum sum that an organisation may distribute.
2-Ireedemable debentures do have a set maturity date.
3- Business must return all subscription fees to customers within 40 days of receiving the court judgement imposing the fine.
4-individual should be given a private placement offer or invitation for Rs. 25,000, which is equal to the face value of the securities.
5- In an Offer for Sale, the winning bidder must pay the certain sum up advance to seal the deal
(Answers-1-false,2-false,3-false,4-false,5-false)

III) Write Short notes on:

1. Categories of debentures depending on permanency
2. Debenture categories based on negotiability
3. Features of equity share capital
4. Types of equity share
5. Merits of preferential allotment

IV) Descriptive questions:

1-What do you mean by equity share capital .State its merits and demerits.
2-What do you mean by prefertial allotment.State its merits and demerits.
3- Who are qualified institutional buyer(QIP)
4-What do you mean by Private Placement offer letter
5-Differenc between Offer for Sale and Qualified Institutional placement

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5

SHARE CAPITAL AND DEBENTURES

Unit Structure

5.0 OBJECTIVES

After studying the unit, the students will be able to:

- Understand the meaning of Shares and Debentures.
- Know the meaning of Share Capital and its types
- To understand concepts of Sweat equity shares
- To understand provisions relating to Voting rights of members, issue of shares and alteration of share capital.

5.1 INTRODUCTION

Shares and debentures are an integral part of every company and common instruments to raise funds. The investment decision between shares and debentures depends on many factors like risk profile and returns expectations of the investors and their investment horizon. A good portfolio will have a healthy mix of shares and debentures to balance the risk and maximize investors' wealth.

Section 2(84) "Share means a share in the share capital of a company and includes stock." It is the division of the capital into smaller yet equal units. These units are then referred to as 'shares'. The people who invest and hold such shares are known as 'shareholders'.

A debenture is a debt tool – the funds raised are considered loans to the company. But shares allow you ownership in the company. It'll be good to know both to make a sensible investment choice

5.2 MEANING OF SHARES AND KINDS OF SHARE CAPITAL (SECTION 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:

Advantages of Equity shares:

1. They have the potential to generate high returns as they are high-risk investments.

2. They can vote for or against corporate policies and business

3. Limited liability of investors

4. These shares are traded on stock exchanges.
5. These shares are permanent in nature. They returned only when the company winds up.

Advantages of Preference Shares

1. Preferential dividend option for shareholders.
2. Preference shareholders do not have the right to vote.
3. Shareholders have a right to claim the assets in case of a wind up of the company.
4. Fixed dividend payout for shareholders, irrespective of profit earned.

In a company capital refers to its share capital. The memorandum of association mentions the amount of capital the company is being registered with is called the nominal capital /authorised capital or the registered capital of the company. This amount is broken up into a number of shares a company can issue. Share capital in excess of the limit specified in the memorandum of association. The entire authorised capital not to be issued. The issued capital will be in form of equity shares and preference shares. Subscribed capital means that part of the issued capital at nominal or face value which has been subscribed or taken up by the purchases of shares in the company and which has been allotted. The company may require the buyer to pay only a part of the nominal value and the balance to be collected when required the amount paid is called the paid up capital of the company.

A share also comes with certain liabilities for the shareholder if the shareholder has not fully paid the full nominal value of the share he has to pay whenever called to do so.

5.3 CERTIFICATE OF SHARES (SECTION 46)

(1) Share Certificate is a document issued by the company and is an evidence that the person named therein is the holder of specified number of shares of the company. It can be issued only in pursuance of a Board Resolution and on surrender of the letter of allotment, if issued.

Share Certificate is issued under the common seal of the company and should be signed by 2 directors or by a director and the Company Secretary. This certificate is subject to stamp duty as per the relevant stamp Act of the state in which the registered office of the company is situated.

(2) A duplicate certificate of shares may be issued, if such certificate —

(*a*) is proved to have been lost or destroyed; or

(*b*) has been defaced, mutilated or torn and is surrendered to the company.

(3) As per the provisions of Article of Association, whenever share certificate or duplicate share certificate is issued to the member, the particulars of it to be entered in the register of members and other details as prescribed in the Act.

(4) Where a share is held in depository form, the record of the depository is the prima facie evidence of the interest of the beneficial owner.

(5) If a company with intent to defraud issues a duplicate certificate of shares, the company shall be punishable with fine which shall not be less than five times the face value of the shares involved in the issue of the duplicate certificate but which may extend to ten times the face value of such shares or Rs. 10 crores, whichever is higher and every officer of the company who is in default shall be liable with imprisonment for a term which shall not be less than 6 months but which may extend to 10 years and shall also be liable to fine which shall not be less than the amount involved in the fraud, but which may extend to 3 times the amount involved in the fraud.

A share is a bundle of rights that includes the right to receive dividend attend meetings of the company receive share certificates etc whereas the share certificate is a documentary evidence of its share in the company, it is not the share in itself.

Nowadays mostly shares are issued electronically in dematerialise form. A person who owns shares is issued share certificate indicating his ownership of the shares a single certificate mentioning the share numbers of all the shares held by a person. However this will make it inconvenient for the person to sell some of the shares he owns at the same time a share certificate for each share would be equally inconvenient to be issued by the company shareholders would need to receive and store a large number of share certificate which would occupy space and volume and which is inconvenience to shareholder as well as to the company also the purpose of share certificate is to facilitate transfer therefore this should be in units convenient for trading.

Therefore, the companies act make provision for holding of shares in electronic form through the mechanism of <u>depository.</u> Depositories are like banks holding shares, debentures, bonds and units of the owners in an electronic form a depository deals with its customer only through specific agents who are called as <u>depository participants (DP).</u> A customer opens an account with a depository participant in much the same way one opens and account with a branch of a bank. The system of depository is not available in relation to shares of private companies. The depositories, depository participants, stock brokers and companies and beneficial owner are electronically connected. All the parties are regulated by the SEBI. A shareholder can get a credit of shares in his account by dematorization. The account holder applies to the depository participant for the conversion of physical certificate into electronic form. The physical shares are surrendered to the DP, the DP in communication with the company replaces the share certificate with an electronic record of membership this is this process is called as dematorization.

5.4 VOTING RIGHTS: (SECTION 47)

(a) Every equity shareholder have a right to vote on every resolution placed before the company; and

(b) his voting right on a poll shall be in proportion to his share in the paid-up equity share capital of the company.

(2) Every member of a company limited by shares and holding any preference share capital therein shall, in respect of such capital, have a right to vote only on resolutions placed before the company in proportion to his share in the paid-up preference share capital which -

(a) directly affect the rights attached to his preference shares and,

(b) any resolution for the winding up of the company or

(c) for the repayment or reduction of its equity or preference share capital

5.5 APPLICATION OF PREMIUMS RECEIVED ON ISSUE OF SHARES AND PROHIBITION ON ISSUE OF SHARES AT DISCOUNT (SECTION 52 & 53):

A company can issue shares in any denomination. However SEBI guidelines provide that share should be of denomination of Rs.1or its multiple. The allotment of shares of a company is a contract of sale of shares between the company and the subscriber. When a company issues shares for sale at the face value or nominal value of the share it is called as issue at par. For example: the face value of the share is Rs.10 and the shares are sold for Rs.10then it will be called as issue at par.

S. 53 of the companies act prohibits issuing shares at a value lower than the face value the only exception to it is for issue of sweat equity shares.

If the shares are offered for a sale at Rs.15, it would be an issue at premium. The subscribed share capital would be Rs.10and the premium would be Rs.5 the companies act does not restrict the issue of shares by a company at a premium. However the Act regulates the utilisation of the premium collected on shares the entire amount received should be treated share capital of the company the premium collected is to be taken into a separate account which is called as securities premium account.

5.6 ISSUES OF SWEAT EQUITY SHARES (SECTION 54)

A company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled, namely:—

(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.

Sweat Equity shareholders have the same rights like any other equity shareholders.

5.7 ISSUE AND REDEMPTION OF PREFERENCE SHARES (SECTION 55)

- A company limited by shares, if authorised by its articles, may issue preference shares which are liable to be redeemed within a period not exceeding 20 years from the date of their issue with such conditions as may be prescribed:

- A company may issue preference shares for a period exceeding 20 years for infrastructure projects, subject to the redemption of such percentage of shares as prescribed on an annual basis at the option of such preferential shareholders.

Redemption is subject to such conditions that:

a. not out of the profits of the company which available for dividend or

b. not out of the proceeds of a fresh issue of shares made for the purposes of such redemption;

c. no such shares shall be redeemed unless they are fully paid;

d. made out of separate amount kept in Capital Redemption Reserve Account, wherein a sum equal to the nominal amount of the shares to be redeemed, is kept as a reserve

The capital redemption reserve account may be applied by the company, in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.

5.8 TRANSFER AND TRANSMISSION OF SECURITIES (SECTION 56)

The transfer of shares is a voluntary act by the holder of shares and takes place by way of contract. Whereas, the transmission of shares takes place due to the operation of law that is on the death of the holder of shares or in an event where the holder becomes insolvent/lunatic.

Section 58 (2) of the Companies Act paves the way for the possibility of the transfer of shares in a Public Company. Such a transfer, by means of any contract or some arrangement, between two or more people, will be deemed legally enforceable as a contract. There lies no transfer of shares unless a proper instrument of transfer duly stamped, dated and executed by or on behalf of the transferor and the transferee has been delivered to the company by the transferor or transferee within a period of 60 days (listed or unlisted company) from the date of execution along with the certificate relating to the securities, or if no such certificate is in existence, then along with the related certificate or letter of allotment of securities.

Where the instrument is lost, the company may register the transfer on basis of indemnity.

This is due to the fact that transmission of share/s takes place when the shares are transferred due to the operation of law. Operation of law may include different circumstances/situations like the death of a member, member adjudicated as insolvent, lunatic, the order passed by court or arbitration award was given, etc. This process is devoid of a transfer deed or need for payment of stamp duty. Nonetheless, the liability associated with such shares persists even after transmission. Once the transmission of shares is completed, the person who receives such shares becomes the legal shareholder and may enjoy all the rights and duties (liabilities) attached to those shares.

According to Section 56(4), every company, unless prohibited by any provision of law or any order of court, tribunal or other authority, deliver the certificates of all securities allotted, transferred or transmitted, within a period of one month from the date of receipt by the company of the instrument of transfer or as the case may be of the intimation of transmission.

Section 56(4) states that where the securities are dealt with in a depository, the company shall intimate the details of allotment of securities to depository immediately on allotment of such securities.

According to section 56(5) of the Companies Act, 2013, the transfer of any security of a deceased person in a company made by his legal representative shall, even if the legal representative is not a holder thereof, be valid as if he had been the holder at the time of the execution of the instrument of transfer

According to Section 56(6), when any default is made in complying with the above provisions, the company shall be punishable with fine which shall not be less than Rs. 25,000/-but which may extend to Rs. 5 Lakh and every officer of the company who is in default shall be punishable with fine which shall not be less than Rs. 10,000/- but which may extend to Rs.1 Lakh.

Distinction between transfer and transmission of securities:

Sr. No.	Basis	Transfer of Securities	Transmission of Securities
	Nature	Transfer takes place by a voluntary act of the transferor	Transmission is the result of the operation of law.
	Instrument	An instrument of transfer is required in case of transfer	No instrument of transfer is required in case of transmission
	Circumstance	Transfer is a normal course of transferring property	Transmission takes place on death or insolvency of a holder of securities
	Consideration	Transfer of securities is generally made for some consideration	Transmission of securities is generally made without any consideration
	Stamp Duty	Stamp duty is payable on transfer of securities by a holder of securities	No stamp duty is payable on transmission of securities.

Only securities i.e. the shares, debentures, any other securities of a public limited company (listed as well as unlisted companies) have been made freely transferable. The Board of directors of such a company or the concerned depository shall not have any discretion to refuse or withhold a transfer of such security. Any other security, for example, shares or debentures of a private company or any unit of a mutual fund, or any security issued by any issuer other than a public limited company are not freely transferable and would be subject to the restrictions contained in the articles of association of the concerned issuer and terms of issue

5.9 POWER OF LIMITED COMPANY TO ALTER ITS SHARE CAPITAL (SECTION 61)

A limited company with share capital can alter its capital as provided in memorandum of association in any of the following ways provided authority to alteration is given by the articles of association.

a. It may increase its authorised capital by such amount as it things expedient.

b. Consolidate and divide the whole or any part of it share capital in to shares of large amount.

c. Convert all or any of its fully paid up shares into stock or vice versa into any denomination.

d. Sub divide the whole or any part of it share capital into shares of smaller amount.

e. Cancel the shares which have not been taken up and reduce its capital accordingly.

Any of the above things can be done by the company by passing a resolution at a general meeting, but do not required to be confirmed by the National company law tribunal. Within 30 days of alteration notice must be given to the Registrar who will record the same and make necessary alteration in the Company's memorandum and articles of association. Notice to the register has similarly to be given when redeemable preference shares have been redeemed. Similar information is also required to be sent to the resistor where the capital has been increase beyond the authorised limit or where a company being not limited by shares has increased the number of its members.

5.10 FURTHER ISSUE OF SHARE CAPITAL (SECTION 62)

A company can at any time by passing an ordinary resolution at its general meeting resolve to increase its capital by such amount as it things experience by issuing new shares the time at which and the person to whom new shares are to be allotted is an important question in the company law if the directors or the majority of shareholders are allowed to this disperse the new issue at the discretion they would naturally offer it to the nominees does adding to their own majority and reducing the strength of the minority deals with this problem.

The new issue must be offered to the existing holders of the equity shares in the proportion as nearly as the circumstances admit of the shares held by them the object of the section is that there should be an equitable distribution of the shares and the holding of shares by each shareholder should not be affected by the issue of new shares. Offer is to be made by giving a notice specifying the number of shares offered the notice must fix a time which should not be less than 15 days and not exceeding 30 days from the date of the offer within which the offer must be accepted the notice must also inform the shareholders that if the offer is not accepted within the specified time it shall be them to have been declined again the notice has to inform the shareholders that they have the right to renounce all or any of the shares of it to them in favour of their nominees the notice can be dispatched to register post Speed Post or through electronic mode at least 3 days before opening of the issue if the shareholder has neither nominated anyone or not accepted the shares himself the board of directors will get the description to dispose of the shares decline in such manner as they think beneficial to the company. Such shares can also be offered to employees under a scheme of employees' stock option it can be done under the authority of a special resolution and also subject to such condition as may be prescribed. They can also be offered to any persons if so authorised by a special resolution even if they are not within the two categories mentioned above such offer can be for a cash or for a consideration other than cash.

Power to convert loans into capital section 62 (3 to 6):

The central government has taken a new power of converting into shares any debentures issued to a loan taken from the government by a company. Where a company has issued any debentures to the government or has taken any loans from it, the central government may direct that such a ventures on loan shall be converted into shares in the company. The power is to be exercised only if such conversion appears to be necessary in the public interest. The conversion shall be on such terms and conditions as appears to the government to be reasonable in the circumstances of a particular case. If the terms and conditions proposed by the government or not acceptable to the company it may within 60 days prefer an appeal to the tribunal and the decision of the tribunal shall be final. A copy of every order proposed to be issued by the government is to be laid in draft before each house of the parliament for total period of 30 days. Where the government has converted its debentures or loans into capital, the capital of the company shall thereby stand increase by an equal amount and its memorandum altered accordingly the central government is required to send a copy of the order to the Registrar so that he may effect the necessary alteration in the companies' memorandum.

5.11 ISSUE OF BONUS SHARES (SECTION 63)

Bonus shares are additional shares allotted to the current shareholders without any additional cost, based upon the number of shares that a shareholder owns.

A company may issue fully paid-up bonus shares to its members out of—

a. its free reserves;

b. the securities premium account; or

c. the capital redemption reserve account:

Issue of bonus shares shouldnot be made by capitalising reserves created by the revaluation of assets.

Bonus shares are issued only if:

a. it is authorised by its articles

b. it has, on the recommendation of the Board, been authorised in the general meeting of the company;

c. it has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;

d. it has not defaulted in respect of the payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus;

e. the partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up;

f. it complies with such conditions as may be prescribed.

Once bonus issue is declared, it cannot be withdrawn.

The bonus shares shall not be issued in lieu of dividend.

5.12 UNLIMITED COMPANY TO PROVIDE FOR RESERVE SHARE CAPITAL ON CONVERSION INTO LIMITED COMPANY (SECTION 65)

An unlimited company having a share capital may, by a resolution for registration as a limited company under this Act, do either or both of the following things, namely—

a. increase the nominal amount of its share capital by increasing the nominal amount of each of its shares, subject to the condition that no part of the increased capital shall be capable of being called up except in the event and for the purposes of the company being wound up;

b. Provide that a specified portion of its uncalled share capital shall not be capable of being called up except in the event and for the purposes of the company being wound up.

5.13 REDUCTION OF SHARE CAPITAL (SECTION 66)

After 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 special resolution, reduce the share capital in any manner and in particular may:

1. Extinguish or reduce the liability on any of it shares in respect of the share capital not paid up or

2. Either with or without extinguishing or reducing the liability on any of it shares:

a. Cancel any paid up share capital which is lost or is unrepresented by available assets or

b. Pay off any paid up share capital which is in excess of the wants of the company,

No such reduction shall be made if the company is in arrears in the repayment of any deposits accepted by it or the interest payable thereon.

Reduction of capital of a company results in alteration of its memorandum by reducing the amount of its share capital and of its shares accordingly.

5.14 RESTRICTIONS ON PURCHASE BY COMPANY OR GIVING OF LOANS BY IT FOR PURCHASE OF ITS SHARES. SECTION 67)

(1) No company limited by shares or by guarantee and having a share capital shall have power to buy its own shares unless the consequent reduction of share capital is affected under the provisions of this Act.

(2) No public company shall give, whether directly or indirectly and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of, or in connection with, a purchase or subscription made or to be made, by any person of or for any shares in the company or in its holding company.

(3) Nothing in sub-section (2) shall apply to—

(a) the lending of money by a banking company in the ordinary course of its business;

(b) the provision by a company of money in accordance with any scheme approved by company through special resolution and in accordance with such requirements as may be prescribed, for the purchase of, or subscription for, fully paid up shares in the company or its holding company, if the purchase of, or the subscription for, the shares held by trustees for the benefit of the employees or such shares held by the employee of the company;

(c) the giving of loans by a company to persons in the employment of the company other than its directors or key managerial personnel, for an amount not exceeding their salary or wages for a period of six months with a view to enabling them to purchase or subscribe for fully paid-up shares in the company or its holding company to be held by them by way of beneficial ownership:

Provided that disclosures in respect of voting rights not exercised directly by the employees in respect of shares to which the scheme relates shall be made in the Board's report in such manner as may be prescribed.

(4) Nothing in this section shall affect the right of a company to redeem any preference shares issued by it under this Act or under any previous company law.

(5) If a company contravenes the provisions of this section, it shall be punishable with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a

term which may extend to three years and with fine which shall not be less than one lakh rupees but which may extend to twenty-five lakh rupees.

5.15 POWER OF COMPANY TO PURCHASE ITS OWN SECURITIES (SECTION 68)

Section 68 of the Companies Act 2013 allows for the buyback of own shares of a company:

a. out of its free reserves or

b. the securities premium account or

c. the process of the issue of any shares or other specified securities.

No buy back of shares or security shall be made out of the proceeds of an earlier issues of same kind of shares or securities.

5.16 TRANSFER OF CERTAIN SUMS TO CAPITAL REDEMPTION RESERVE ACCOUNT (SECTION 69)

1. Where a company purchases its own shares out of free reserves or securities premium account, a sum equal to the nominal value of the shares so purchased shall be transferred to the capital redemption reserve account and details of such transfer shall be disclosed in the balance sheet.

2. The capital redemption reserve account may be applied by the company, in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.

5.17 PROHIBITION FOR BUY-BACK IN CERTAIN CIRCUMSTANCES (SECTION 70)

No company shall directly or indirectly purchase its own shares or other specified securities—

a. through any subsidiary company including its own subsidiary companies;

b. through any investment company or group of investment companies; or

c. by making default repayment of deposits accepted and interest payment thereon, redemption of debentures or preference shares or payment of dividend to any shareholder, or repayment of any term loan or interest payable thereon to any financial institution or banking company.

Following conditions are required to be fulfilled before buy-back of securities by a company:

1. The buy-back is authorised by the AOA of the company.
2. A special resolution has been passed at a general meeting of the company authorising buy-back.
3. The ratio of the aggregate secured and unsecured debts owed by the company after buy-back is not more than twice the paid up capital and free reserves.
4. Central government may by order, specify higher ratio of debt to capital and free reserves for a class or classes of companies.
5. All the shares or other securities for buy-back are fully paid up.
6. It should be made as per SEBI guidelines.
7. The process of buy-back of securities to be completed within a period of one year from the date of passing of the special resolution.

5.18 DEBENTURES (SECTION71)

Debentures are debt tools; issued by companies to raise funds as loans from the public. It is an acknowledgement from a corporate entity that it has taken a loan from you. It is backed solely by the creditworthiness of the issuing firm. But it carries some amount of assurance.

Types of debentures

1. Secured Debentures:
Secured debentures are the debentures that are backed by an asset of the company which can be liquidated to recover the interest and redemption value.

2. Unsecured debentures :
Unsecured debentures do not have any charge on any asset of the company. So debenture holders will have to wait after the secured debenture holders to get their value of the investment at the time of liquidation.

3. Convertible debentures :
Convertible debentures are the debentures that can be converted to equity shares at the time of redemption.

4. **Non-convertible debentures**:
Non-convertible debentures cannot be converted to equity shares upon redemption.

5. Registered debentures:
Registered debentures are where the names of the debenture holders are mentioned as per the register of the company.

6. **Bearer debentures :**

In the case of bearer debentures, no name is registered under the records of the company and they can be easily transferred to any person.

Debentures can be either floating or fixed in nature. The payout on floating rate debenture varies with the market movement. But, for fixed-rate debentures, final payout remains assured.

1. A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption:
2. Provided that the issue of debentures with an option to convert such debentures into shares, wholly or partly, shall be approved by a special resolution passed at a general meeting.
3. No company shall issue any debentures carrying any voting rights.
4. Secured debentures may be issued by a company subject to such terms and conditions as may be prescribed.
5. Where debentures are issued by a company under this section, the company shall create a debenture redemption reserve account out of the profits of the company available for payment of dividend and the amount credited to such account shall not be utilised by the company except for the redemption of debentures.
6. No company shall issue a prospectus or make an offer or invitation to the public or to its members exceeding five hundred for the subscription of its debentures, unless the company has, before such issue or offer, appointed one or more debenture trustees and the conditions governing the appointment of such trustees shall be such as may be prescribed.
7. A debenture trustee shall take steps to protect the interests of the debenture-holders and redress their grievances in accordance with such rules as may be prescribed.
8. Any provision contained in a trust deed for securing the issue of debentures, or in any contract with the debenture-holders secured by a trust deed, shall be void in so far as it would have the effect of exempting a trustee thereof from, or indemnifying him against, any liability for breach of trust, where he fails to show the degree of care and due diligence required of him as a trustee, having regard to the provisions of the trust deed conferring on him any power, authority or discretion:
9. Provided that the liability of the debenture trustee shall be subject to such exemptions as may be agreed upon by a majority of debenture-holders holding not less than three-fourths in value of the total debentures at a meeting held for the purpose.

10. A company shall pay interest and redeem the debentures in accordance with the terms and conditions of their issue.

11. Where at any time the debenture trustee comes to a conclusion that the assets of the company are insufficient or are likely to become insufficient to discharge the principal amount as and when it becomes due, the debenture trustee may file a petition before the Tribunal and the Tribunal may, after hearing the company and any other person interested in the matter, by order, impose such restrictions on the incurring of any further liabilities by the company as the Tribunal may consider necessary in the interests of the debenture-holders.

12. Where a company fails to redeem the debentures on the date of their maturity or fails to pay interest on the debentures when it is due, the Tribunal may, on the application of any or all of the debenture-holders, or debenture trustee and, after hearing the parties concerned, direct, by order, the company to redeem the debentures forthwith on payment of principal and interest due thereon.

13. If any default is made in complying with the order of the Tribunal under this section, every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years or with fine which shall not be less than two lakh rupees but which may extend to five lakh rupees, or with both.

14. A contract with the company to take up and pay for any debentures of the company may be enforced by a decree for specific performance.

15. The Central Government may prescribe the procedure, for securing the issue of debentures, the form of debenture trust deed, the procedure for the debenture-holders to inspect the trust deed and to obtain copies thereof, quantum of debenture redemption reserve required to be created and such other matters.

Shares vs Debentures

Now that we have a basic understanding of what shares and debentures are, let's understand the difference between shares and debentures:

S.No.	**Basis**	**Shares**	**Debentures**
1.	Meaning	Shares are owned capital of the company.	Debentures are borrowed capital of the company.
2.	Representation	They represent owner's equity capital.	They represent debt and liabilities.

3.	Risk	Share prices are hard to predict and depend on the company's performance.	Debentures are associated with lesser risks and promise interest payments.
4.	Interest	Returns on shares fluctuate according to the market and the company's performance.	Debenture holders are entitled to a fixed interest irrespective of market conditions.
5.	Terminology	Investors holding shares are called shareholders.	Investors holding debentures are called debenture holders.
6.	Rights	Shareholders hold voting rights.	Debenture holders don't have voting rights and can't participate in annual general meetings.
7.	Trust deed	No trust deed is created when shares are issued to the public.	A trust deed is executed when debentures are issued.
8.	Repayment	In the event of winding up of the company, shareholders are paid at the very end.	Debenture holders get priority over shareholders and are thus paid off before them during the winding up of the company.
9.	Security	Shares aren't as secure as debentures. Rather, share price depends on market conditions.	Debentures are fixed-income securities and hence, are secured.
10.	Returns	Shareholders can enjoy high returns, but these returns are never fixed.	Debenture holders get low but fixed returns,

11.	Conversion	Shares can't be converted to debentures.	Some debentures can be converted into shares

5.19 POWER TO NOMINATE (SECTION 72)

- Every holder or joint holder of securities of a company may, at any time, nominate, any person to get securities transferred in his name after the death of security holder.
- The nominee enjoys all rights after the death of security holder which he was having it.
- If the nominee is a minor, security holder should appoint any other major person to hold these securities till he reaches the age of majority.

5.20 SUMMARY

- The capital with which a company is registered that is the capital mentioned in the memorandum of association is called the nominal capital/ authorised capital/ registered capital. The part of the authorised capital the company issues for raising capital is called the issued capital. The part of the issued capital which gates bought or purchased is called the subscribed capital. The contract for subscription maybe to actually pay the amount in full or partially to be subscribed capital. Fully paid up later when called for by the company the amount of the capital paid by the subscriber is called the paid up capital.
- A share certificate is only documentary evidence of the share of the person in the company it is not the right itself.
- A share in a company is a movable property it is fully transferable subject only to the existing loss and the articles of association.
- If a company decides to pay dividends preference shareholders have to be paid first in addition a preference share mentions a minimum amount of dividend either as a percentage of the face value of the share or an amount.
- All shares other than preference shares are equity shares.
- Depository is an arrangement whereby the records of shares are maintained in the electronic form in this form the physical shares are dematerialised and converted into electronic records a depository electronically integrates companies stock exchange is stock brokers and the shareholders when a share is transferred from one account to another automatic become a member in the records of the company.

- Alteration of share capital of a company means a change in the number of authorised shares of a company as authorised by the articles of association.
- Debenture is an instrument of debt executed by the company acknowledging its obligation to repay the sum at specified rate and also carrying an interest.

- The nominee enjoys all rights after the death of security holder which he was having it.

5.21 QUESTIONS

I) Fill in the blanks:

1. The part of the authorised capital the company issues for raising capital is called the___.

2. The capital with which a company is registered that is the capital mention in the memorandum of association is called____.

3. A company can issue only two kinds of shares___ and ____.

4. Only a _______ company can have it shares listed on a stock exchange.

5. Sweat equity share is authorised by a __ pass by the company.

6. Share means a share in the shape capital of company and include ______.

7. Paid up share capital means such aggregate amount of___ as paid up.

8. Preferential share capital means carries____ treatment at the time of payment of____ the company.

9. Company shall not issue shares at a ______.

10. A_______ shall takes steps to protect the interest of debenture holders.

11. ______ is an instrument of debt executed by the company acknowledging its obligation to repay the sum at specified rate and also carrying an interest.

(1. Issued Capital 2. Authorised/ Nominal/Registered capital 3. Equity and Preference shares 4. Public 5.Special resolution 6. Stocks 7. Subscribed 8. Preferential, winding up 9. Discount 10. Debenture trustee 11. Debenture)

II) True or false:

1. The memorandum of association mentions the amount of authorised and issued share capital.

2. A Equity shareholder has the right to participate in the meetings of a company.

3. In a depository the mention of a beneficial owner is the equivalent of a share certificate.

4. A preference shareholder has equal rights of participation and voting in the general body meeting like equity shareholders.

5. A private company can have its shares listed for trading on a stock exchange.

6. Share does not include stock.

7. Duplicate share certificate maybe issued even without any valid reasons.

8. Sweat equity shares issued to outsider at a discount for consideration.

9. Transfer of shares takes place during the life of the shareholders.

10. The securities premium account maybe applied by the companies towards the issue of shares of the company.

(1.False 2. True3. True 4. False 5. False 6.False 7. False 8. False 9. True 10. False)

III) Answer the following:

1. What is share and share capital?
2. Explain types of share capital
3. What is debentures of a company?
4. What is capital redemption account?
5. Explain the provisions regarding the reduction of share capital of a company?

IV) Write short notes on:

a. Issued capital
b. Share certificate
c. Preference shares
d. Debentures

V) Test your knowledge:

1. XYZ company issue shares to its employees for the value addition given to them the company gives the shares at a premium stating that the employees have been given preference over the outside us is it a valid contract? Justify.

2. ABC company could not issue shares to the public due to under subscription the directors of the company return the money to the public after 150 days of the withdrawal of the public issue has the company committed any offence can the public hold a company liable advise the shareholders.

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