**UNIT 4: Share Capital and Debenture**

Semester- II (UG)

Subject- Company Law

Topic-Issue and Redemption of Preference Shares, various regulations relating to issue of bonus shares, Further issue of Capital

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Lecture no-4

***(D) Issue and Redemption of Preference Shares***

According to section 55 of the Act, company limited by shares cannot issue any preference shares which are irredeemable. However a company limited by shares may, if so authorised by its articles, issue preference shares which are liable to be redeemed within a period not exceeding twenty years from the date of their issue subject to such conditions as may be prescribed.

According to the Rules a company having a share capital may, if so authorised by its articles, may issue preference shares subject to the following conditions, namely:-

1. The issue of such shares has been authorized by passing a special resolution in the general meeting of the company.
2. The company, at the time of such issue of preference shares, has no subsisting default in the redemption of preference shares issued either before or after the commencement of this Act or in payment of dividend due on any preference shares.

Under the rules a company issuing preference shares shall set out in the resolution, following

1. The priority with respect to payment of dividend or repayment of capital vis-a-vis equity shares
2. The participation in surplus fund ;
3. the participation in surplus assets and profits, on winding up which may remain after the entire capital has been repaid.
4. The payment of dividend on cumulative or non-cumulative basis.
5. The conversion of preference shares into equity shares;
6. The voting rights
7. The redemption of preference shares.

The explanatory statement to be annexed to the notice of the general meeting pursuant to section 102 shall, inter-alia, provide the complete material facts concerned with and relevant to the issue of such shares, including-

1. The size of the issue and number of preference shares to be issued and nominal value of each share
2. The nature of such shares i.e. cumulative or non - cumulative, participating or non - participating , convertible or non - convertible;
3. The objectives of the issue;
4. The manner of issue of shares;
5. The price at which such shares are proposed to be issued.
6. The basis on which the price has been arrived at.
7. The terms of issue, including terms and rate of dividend on each share, etc.
8. The terms of redemption, including the tenure of redemption, redemption of shares at premium and if the preference shares are convertible, the terms of conversion.
9. The manner and modes of redemption.
10. The current shareholding pattern of the company.
11. The expected dilution in equity share capital upon conversion of preference shares.

The company issuing preference shares shall incorporate the particulars in respect of such preference share holder(s) in the Register of Members maintained under section

**88.** Further a company intending to list its preference shares on a recognized stock exchange shall issue such shares in accordance with the regulations made by the Securities and Exchange Board of India in this behalf.

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

(a) At a fixed time or on the happening of a particular event;

(b) Any time at the company’s option; or

(c) Any time at the shareholder’s option.

Issue and redemption of preference shares by company in infrastructural projects.- A company engaged in the setting up and dealing with of infrastructural projects may issue preference shares for a period exceeding twenty years but not exceeding thirty years, subject to the redemption of a minimum ten percent of such preference shares per year from the twenty first year onwards or earlier, on proportionate basis, at the option of the preference shareholders.“Infrastructure Projects” have been covered defined under Schedule VI of the Act.

***Conditions for redemption***

Preference shares can be redeemed under following conditions:

* Redemption can be made in any of the two procedures i.e. either out of the profits of the company which would otherwise be available for dividend; or; out of the proceeds of a fresh issue of shares made for the purposes of such redemption.
* Preference shares shall be redeemed only when they are fully paid up.
* In case the company proposes redemption of shares out of the profits of the company, there shall, out of such profits, be transferred, a sum equal to the nominal amount of the shares to be redeemed, to a reserve, to be called the Capital Redemption Reserve Account, and the provisions of this Act relating to reduction of share capital of a company shall, except as provided in this section, apply as if the Capital Redemption Reserve Account were paid-up share capital of the company. 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.
* Certain class of companies as may be prescribed and whose financial statements comply with the accounting standards prescribed under section 133, for such class of companies, the premium, if any, payable on redemption shall be provided for out of the profits of the company, before the shares are redeemed. For other companies the premium, if any, payable on redemption shall be provided for out of the profits of the company or out of the company’s securities premium account, before such shares are redeemed.

***(E) Issue of Bonus Shares***

Section 63 of the Act a company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of—

(i) Its free reserves;

(ii) The securities premium account; or

(iii) The capital redemption reserve account: The section specifically clarifies that no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets. The bonus shares shall not be issued in lieu of dividend.

***Conditions for issue*:** No company shall issue fully paid-up bonus shares unless—

1. It is authorised by its articles;
2. It has, on the recommendation of the Board, been authorised in the general meeting of the company;
3. It has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;
4. It has not defaulted in respect of the payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus;
5. The partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up;
6. It complies with such conditions as may be prescribed. Under the rules no company which has once announced the decision of its Board recommending a bonus issue, can subsequently withdraw the same.

***(F) Further Issue of Capital***

***Eligibility*:** According to section 62(1) of the Act where at any time a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered to the following:

(a) persons who, at the date of the offer, are holders of equity shares of the company in proportion, as nearly as circumstances admit, to the paid-up share capital on those shares by sending a letter of offer. The offer shall be made by notice specifying the number of shares offered. The offer shall be open for a period not being less than fifteen days and not exceeding thirty days from the date of the offer. If the offer is not accepted within the period it shall be deemed to have been declined.

Further, unless the articles of the company otherwise provide, the offer aforesaid shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him or any of them in favour of any other person; and the notice shall contain a statement of this right. Hence a company may restrict the right of renunciation by its Articles. It has been clarified that after the expiry of the time specified in the notice aforesaid, or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered, the Board of Directors may dispose of them in such manner which is not disadvantageous to the shareholders and the company The notice mentioned aforesaid shall be despatched through registered post or speed post or through electronic mode to all the existing shareholders at least three days before the opening of the issue.

(b) Employees under a scheme of employees’ stock option, subject to special resolution passed by company and subject to such conditions as may be prescribed.

(c) Any persons, if it is authorised by a special resolution, whether or not those persons include the persons referred to in clause (a) or clause (b), either for cash or for a consideration other than cash, if the price of such shares is determined by the valuation report of a registered valuer subject to such conditions as may be prescribed.

Under the rules a company may if authorized by a special resolution passed in a general meeting, issue shares in any manner whatsoever including by way of a preferential offer, to any persons whether or not those persons include the persons referred to in clause (a) or clause (b) of sub-section (1) of section 62. Such issue on preferential basis should also comply with conditions laid down in section 42 of the **Act (private placement):**

The price of shares to be issued on a preferential basis by a listed company shall not be required to be determined by the valuation report of a registered valuer.

Under the rules ‘Preferential Offer’ means an issue of shares or other securities, by a company to any select person or group of persons on a preferential basis and does not include shares or other securities offered through a public issue, rights issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities.

“Shares or other securities” means equity shares, fully convertible debentures, partly convertible debentures or any other securities, which would be convertible into or exchanged with equity shares at a later date.

Where the preferential offer of shares or other securities is made by a company whose share or other securities are listed on a recognized stock exchange, such preferential offer shall be made in accordance with the provisions of the Act and regulations made by the SEBI, and if they are not listed, the preferential offer shall be made in accordance with the provisions of the Act and rules made hereunder and subject to compliance with the following requirements:-

(a) The issue is authorized by its articles of association;

(b) The issue has been authorized by a special resolution of the members;

(c) Securities allotted by way of preferential offer shall be made fully paid up at the time of their allotment. The company shall make the following disclosures in the explanatory statement to be annexed to the notice of the general meeting pursuant to section 102 of the Act:

1. The objects of the issue;
2. The total number of shares or other securities to be issued;
3. The price or price band at/within which the allotment is proposed;
4. Basis on which the price has been arrived at along with report of the registered valuer;
5. Relevant date with reference to which the price has been arrived at;
6. The class or classes of persons to whom the allotment is proposed to be made;
7. Intention of promoters, directors or key managerial personnel to subscribe to the offer;
8. The proposed time within which the allotment shall be completed;
9. The names of the proposed allottees and the percentage of post preferential offer capital that may be held by them;
10. The change in control, if any, in the company that would occur consequent to the preferential offer;
11. The number of persons to whom allotment on preferential basis have already been made during the year, in terms of number of securities as well as price;
12. The justification for the allotment proposed to be made for consideration other than cash together with valuation report of the registered valuer.
13. Pre issue and post issue shareholding pattern of the company in the format specified in the Rules.

***Completion Period*:** the allotment of securities on a preferential basis made pursuant to the special resolution passed are required to be completed within a period of twelve months from the date of passing of the special resolution. Where the allotment of securities is not completed within twelve months from the date of passing of the special resolution, another special resolution shall be passed for the company to complete such allotment thereafter.

***Rights of Convertible Securities*:** The section provides that nothing in this section (Section 62) shall apply to the increase of the subscribed capital of a company caused by the exercise of an option as a term attached to the debentures issued or loan raised by the company to convert such debentures or loans into shares in the company. It is essential that the terms of issue of such debentures or loan containing such an option have been approved before the issue of such debentures or the raising of loan by a special resolution passed by the company in general meeting. As per Section 62 (4)\* Where any debentures have been issued, or loan has been obtained from any Government by a company, and if that Government considers it necessary in the public interest so to do, it may, by order, direct that such debentures or loans or any part thereof shall be converted into shares in the company on such terms and conditions as appear to the Government to be reasonable in the circumstances of the case even if terms of the issue of such debentures or the raising of such loans do not include a term for providing for an option for such conversion. In terms of proviso, where the terms and conditions of such conversion are not acceptable to the company, it may, within sixty days from the date of communication of such order, appeal to the Tribunal which shall after hearing the company and the Government pass such order as it deems fit. In terms of Section 62(5)\*, in all the circumstances the Government shall have due regard to the financial position of the company, the terms of issue of debentures or loans, as the case may be, the rate of interest payable on such debentures or loans and such other matters as it may consider necessary. In terms of Section 62(6)\*, where the Government has, by an order directed that any debenture or loan or any part thereof shall be converted into shares in a company and where no appeal has been preferred to the Tribunal or where such appeal has been dismissed, the memorandum of such company shall, where such order has the effect of increasing the authorised share capital of the company, stand altered and the authorised share capital of such company shall stand increased by an amount equal to the amount of the value of shares which such debentures or loans or part thereof has been converted into.

***Determination of Price*:** the price of the shares or other securities to be issued on a preferential basis, either for cash or for consideration other than cash, shall be determined on the basis of valuation report of a registered valuer. Where convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares shall be determined beforehand on the basis of a valuation report of a registered valuer and also complied with the provisions of section 62 of the Act.

Further where shares or other securities are to be allotted for consideration other than cash, the valuation of such consideration shall be done by a registered valuer who shall submit a valuation report to the company giving justification for the valuation; The preferential offer of shares made for a non-cash consideration, such non-cash consideration shall be treated in the following manner in the books of account of the company-

(i) where the non-cash consideration takes the form of a depreciable or amortizable asset, it shall be carried to the balance sheet of the company in accordance with the accounting standards; or

(ii) where clause (i) is not applicable, it shall be expensed as provided in the accounting standards.

**Reference:**

1. “ **Share Capital and Debentures**”, Companies Act 2013 published by **The Institute of Company Secretaries of India.**