Introduction to company law

CS A Sridhar
FCS, LL.M
Practicing Company Secretary, Part-Time Faculty, PG College of Law, OU
Contact: 9989394290
asridharcs@gmail.com

Prospectus

- Section 2(70): Prospectus Means any described or issued as a prospectus and includes a red herring Prospectus or shelf Prospectus or notice, circular, advertisement or other document inviting offers from the public for the subscription of any securities of body corporate
- Matters to be stated in prospectus
    - General Information
    - Financial Information
    - Statutory Information
- Other Legal Provisions Relating to prospectus (Section 26)
    - Shall be registered with ROC
    - Not valid for more than 90 days
    - Expert Opinion Can be included
- The Public Offer Must be in Dematerialised form (Section 29)
- Shelf Prospectus
- Red herring Prospectus
- Abridged Prospectus
- Deemed Prospectus

Misstatement in Prospectus

Civil liability for mis-statements in prospectus (Sec. 35)

- **Liabilities of persons :** According to **Sec. 35(1),** where a person has subscribed for securities of a Co. acting on any statement included, or the inclusion or omission of any matter, in the prospectus which is misleading and has sustained any loss or damage as a consequence thereof, the Co. and every person who—
  - is a director of the Co. at the time of the issue of the prospectus;
  - has authorised himself to be named and is named in the prospectus as a director of the Co., or has agreed to become such director, either immediately or after an interval of time;
  - is a promoter of the Co.;
  - has authorised the issue of the prospectus; and
  - is an expert referred to in sub-Sec. (5) of Sec. 26,

shall, without prejudice to any punishment to which any person may be liable under Sec. 36, be liable to pay compensation to every person who has sustained such loss or damage.

Exceptions : No person shall be liable if he proves—

- withdrew his consent to become director before issue of prospectus
- Prospectus issued without his knowledge

Criminal liability for mis-statements in prospectus (Sec. 34)

- Where a prospectus, issued, circulated or distributed under this Chapter, includes any statement which is untrue or misleading in form or context in which it is included or where any inclusion or omission of any matter is likely to mislead, every person who authorizes the issue of such prospectus shall be liable under Sec. 447:

ACTION BY AFFECTED PERSONS [SEC. 37]

A suit may be filed or any other action may be taken under Sec. 34 or Sec. 35 or Sec. 36 by any person, group of persons or any association of persons affected by any misleading statement or the inclusion or omission of any matter in the prospectus.

Share Capital

- According to Sec. 43, broadly, there are two kinds of share capital of a Co. limited by shares:
- Equity share capital
- Preference share capital.
- The Act defines **preference share capital** as instruments which have **preferential right** to **dividend** payment (absolute/fixed or ad-valorem/%) and preferential **repayment** during winding up of the Co.
- Equity shares are further classified as plain vanilla (same voting rights) or Differential equity shares (with differences w.r.t. dividend or voting rights or otherwise)

Basic Requirements

- Physical entitlement to a particular portion of share capital is *prima facie* evidenced by way of a share certificate which has to be
- Distinctively numbered; &
- Name of Share holder
- To be issued under common seal of the Co. or signed by two directors or by a director and the Co. Secretary, wherever the Co. has appointed a Co. Secretary

PREFERENCE SHARES - ISSUE AND REDEMPTION [SEC. 55]

- No Company limited by shares shall issue any preference shares which are **irredeemable**;
- **Period for redeem of preference shares:** if authorised by its AOA, Co. can 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 prescribed under Rule 9 of the *Companies (Share Capital and Debentures) Rules, 2014*.
- **Exceptions :** A Co. may issue preference shares for a period exceeding twenty years (bot not exceeding thirty years) for **infrastructure projects** (specified in schedule VI), subject to the **redemption of 10 % of shares beginning 21st year** at the option of such preferential shareholders;
- **Shares to be redeemed out of the profits only:**
- **Redeemed shares to be fully paid:** no such shares shall be redeemed unless fully paid;
- **Proposed shares to be redeemed shall be transferred to the CRR account:**

SECURITIES ISSUED AT PREMIUM - SEC 52

Meaning: Issue of shares at a price ***higher than its Par value*** (Face Value) is called, Issue at Premium and the differential amount as premium.

- There could be several reason for issue at premium or discount like:
- To capture the play of market forces between the issuer and investor at the time of issue;
- To give effect to **fair value of underlying business** or rights linked to the securities;
- To minimise payment of stamp duty / ROC fee during incorporation of the Co. which is based on the authorised capital of the Co.
- Neither provision in the AOA is required nor Co's act 2013 does not prescribe any or restrictions regarding issue of shares at premium. I.e. no restriction on amount of Premium.
- Where Co. issue shares at premium, the premium amount has to be transferred to separate account called ***Securities premium account***.
- Issue of shares for **cash or for consideration other than cash**, Premium should be transferred to Securities Premium & it should be utilized as per the act.

Utilization of Securities Premium – SP can be utilized only for the bellow mentioned purposes

- Issuing unissued shares of the Co. ***as fully paid bonus shares*** to members.
- Writing off ***Preliminary expenses*** of Co.
- For ***Buy back*** of shares purchase of its own shares U/s 68 of Co's act 2013
- Providing for ***Premium payable on redemption*** of any redeemable Preference Shares/debentures.
- Writing of expenses, commission or discount allowed on issue of shares or debentures

FURTHER ISSUE OF SHARE CAPITAL – RIGHTS ISSUE; PREFERENTIAL ALLOTMENT [SEC. 62]

- A rights issue involves **pre-emptive subscription rights to buy additional securities** in a Co. offered to the Co.'s **existing security holders**.

As per the Sec. 62 of the Companies Act, 2013-(1) where at any time, a Co. having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered—

- **to persons who**, at the date of the offer, **are holders of equity shares** of the Co. in **proportion, to the paid-up share capital** on those shares by sending a letter of offer subject to the following conditions, namely:—
- **the offer shall be made by notice** specifying the **number of shares** offered and limiting a time **not being less than fifteen days and not exceeding thirty days** from the date of the offer within which the offer, if not accepted, shall be deemed to have been **declined**
- **to employees under a scheme of employees' stock option:** subject to **special resolution** passed by Co. and subject to the conditions as may be prescribed; or
- **to any persons, if it is authorised by a special resolution**, whether or not those persons include the persons referred to in clause (a) or clause (b), **either for cash or for a consideration other than cash**, if the price of such shares is determined by the valuation report of a registered valuer subject to such conditions as prescribed under the Rule 13 of the *Companies (Share capital and Debentures) Rules, 2014*.

ISSUE OF BONUS SHARES – SEC 63

- Bonus shares can be issued only ***to existing shareholders*** as fully paid shares at **free** of cost to them by **capitalizing the reserves**.
- AOA authorization regarding issue of bonus shares, if no provision AOA should be altered.
- BOD recommending issue of bonus shares and it is authorized by shareholders in GM by passing OR.
- it has not defaulted in payment of interest or principal in respect of fixed deposits payment of statutory dues of the employees or debt securities issued by it
- Bonus shares issued only ***in respect of fully paid up*** shares and not partly paid up shares.
- ***Bonus shares also should be fully paid up.***
- Bonus shares can be issued out of following sources:
    - *Free Reserve*
    - *Share premium received and*
    - *P/L account of credit balance and Capital redemption reserve (CRR)*
- Ensure that Bonus shares not issued ***in lieu of declared divided***
- no default in payment of statutory dues and repayment of deposits, loans etc.

REDUCTION OF SHARE CAPITAL [SEC. 66]

Company having huge Accumulated **business losses, assets of reduced or doubtful value, having Fictitious assets** or having investments with no realizable value or having paid up capital in excess of wants of the Co. could lead to the need of reducing share capital.

- **Reduction of share capital by special resolution:** Subject to **confirmation by the Tribunal** on an application by the Co.
  - <u>**extinguish or reduce the liability** on any of its shares in respect of the share capital not paid-up; or</u>
  - <u>either with or without extinguishing or reducing liability on any of its shares,—</u>
    - cancel any paid-up share capital which is **lost or is unrepresented** by available assets; or
    - pay off any paid-up share capital which is in excess of the wants of the Co., alter its MOA by reducing the amount of its share capital and of its shares accordingly:
- **<u>No reduction shall be made</u>:** Sec. further Provides that no such reduction shall be made if the Co. is in **arrears in the repayment of any deposits accepted** by it,
- **<u>Issue of Notice from the Tribunal:</u>** The Tribunal shall give notice of every application made to it under sub-Sec. (1) to the **CG, Registrar and to the SEBI**, in the case of listed companies, and the creditors of the Co. and shall take into consideration the representations, if any made within a period of **three months** from the date of receipt of the notice
- **Order of tribunal**

BUY BACK OF SHARES - SEC 68

Meaning: Buy back means Co. purchasing its own shares. re-acquisition by a Co. of its own securities. It is a way of returning money to its investors

- **Objective/purpose:** Reducing the Dilution of Control
- **Sources:** Free reserves, Securities premium & Proceeds of fresh issue out of different kind of
  - shares or other specified securities.
- **Resolution:** AOA authorization required for buy back, if no provision, AOA should be altered by passing SR.
- a. ***BR in BM*** for buyback not ***exceeding 10% of Aggregate of Paid up Capital & Free Reserves.***
- b. ***Special Resolution*** of Members if buy back ***exceeds 10% but not exceeding 25% of Paid up Capital and Free Reserves (PUC & FR)***
- Buyback in any FY shall **not exceed 25%** of PUC & FR
- Debt equity ratio should not exceed ***2 : 1*** after Buy back.
- notice of the meeting at which special resolution is proposed to be passed shall be accompanied by an **explanatory statement** stating, a full and complete disclosure of all the material facts, the necessity for the buy-back, the class of shares or securities intended to be purchased under the buy back, the amount to be invested under the buy-back;
- The buy-back under Sub-Sec. (1) may be—
- <u>from the **existing share holders** or security holders on a proportionate basis; or</u>
- <u>from the **open market**; or</u>
- <u>by purchasing the securities issued to employees of the Co. pursuant to a scheme of stock option or sweat equity</u>

- Offer of buyback should be open for a period of ***15 days & not exceeding 30 days***
- Buyback of shares can be done only in respect of ***fully paid shares***
- Whole process of Buyback shall complete within ***1 year*** from resolution date.
- Co. has to file ***Declaration of solvency*** with ROC / Stock exchange in case of listed co. stating that it will not be rendered insolvent within a period of one year of the date of declaration adopted by the Board, and signed by at least two directors of the Co., one of whom shall be the managing director
- Co. shall extinguish or ***Physically destroy shares certificates within 7 days***
- Co. shall not issue same kind of securities within ***next 6 months*** except by way of bonus shares, convertible debentures, Sweat equity shares and Employee stock option.
- Co. has to maintain proper register containing Security bought back, consideration paid, condition of buyback and list of eligible persons etc, has to specify in the notice sent to members.
- Return of Buyback should file with ROC and Stock exchange SEBI within 30 days from end of buyback.
- If buy back is from **Securities premium and Free reserves**, Nominal value of shares bought should transfer to CRR (Capital redemption Reserve) can be utilized for issue of bonus shares.
- Buy back is not permitted if Co. defaulted in payment of declared dividend, repayment of deposits and filing Annual returns with ROC. – **<u>SEC 69</u>**

DEBENTURES [SEC. 71]

- As per Sec. 2(30), debenture includes debenture stock, bonds or any other instrument of a Co. **evidencing a debt**, whether constituting a charge on the assets of the Co. or not but not includes instruments specified in III-D of RBI Act 1934 and any other instruments specified by CG win consultation with RBI.
- **Issue of debentures with an option to convert:** A Co. may issue debentures with an option to convert such debentures into shares, either **wholly or partly at the time of redemption** Provided that such issue should be approved by a special resolution in general meeting.
- No Co. shall issue any debentures carrying any **voting rights**.
- **Issue of secured debentures:** Secured debentures may be issued by a Co. subject to such terms and conditions as may be prescribed in Rule 18 of the *Companies (Share Capital and Debentures) Rules, 2014.*

SHAREHOLDERS

A company acts through two bodies of people – its shareholders and its board of directors. A shareholder, commonly referred to as a stockholder, is any individual, company, or institution that owns at least one share of a company's stock. Since shareholders are a company's owners, they receive the rewards of the company's successes in the form of increased stock valuation. For example someone who owns stock in Apple is a shareholder of Apple.

A person or corporation can become a shareholder of a company in three ways:

- By subscribing to the memorandum of the company during incorporation
- By investing in return for new shares in the company
- By obtaining shares from an existing shareholder by purchase, by gift or by will.

Meetings

The kinds of member meetings are a.

- Annual General Meeting
- Extra-ordinary general meeting
- Class meetings

ANNUAL GENERAL MEETING SEC. 96

- **Who Need to Conduct?** : Every Company shall conduct Annual General Meeting.
- **When?** Every Annual General Meeting shall be called during business hours, that is, between 9 a.m. and 6 p.m. on any day that is not a National Holiday and
- **Where?** Shall be held either at the registered office of the Company or at some other place as the Central Government may approve in this behalf
- **Other Conditions:**
- The Gap between Two AGMs shall not exceed 15 Months
- In every calendar year there shall be one AGM

EXTRA-ORDINARY GENERAL MEETING (SEC.100)

- By the Board Suo motu [Section 100 (1)]
- By Board on requisition of members [Section 100 (2)]
- By requisitionists [Section 100(4)]
- By Tribunal [Section 98]

Directors

Section 2(34): Director means a director appointed to the Board of a company

- Qualifications?? The Act has not prescribed any qualifications

<u>Disqualifications</u>

- Unsoundness of mind.
- If he is an undischarged insolvent.
- When is applied to be declared as insolvent and such application is pending.
- When he is sentenced for imprisonment for an offence involving moral turpitude for a period of a minimum of 6 months.
- If the Tribunal or court has passed an order disqualifying him for being appointed as a director.
- If he has not paid his calls in respect to any shares of the company.
- When he is convicted of an offence which deals with related party transaction.
- When he has not complied with the requirements of Director Identification Number.

Legal Position of Directors

- Directors as Agents
- Directors as Trustees
- Directors as Managing partners

Appointment and Removal of Directors

- Appointment of First Directors(Section152)
- Appointment at general Meeting (Section 152)
- Appointment by Board of Directors
    - Additional Directors
    - Filling up the casual Vacancy
    - Alternative Directors
    - Nominee Directors
- Appointment of Resident Director (Section 149)
- Appointment of Independent Directors (Section 149)
- Appointment by Tribunal (Section 242)

Removal of Directors

- Removal by Shareholders (Section 169)
- Removal by Tribunal (Section 242)
- Resignation

Powers of Directors

Powers which can be exercised by Board (Section 179)

- To make calls.
- To borrow money.
- To issue funds of the company.
- To grant loans or give guarantees.
- To approve financial statements.
- To diversify the business of the company.
- To apply for amalgamation, merger or reconstruction.
- To take over a company or to acquire a controlling interest in another company

Powers which can be Exercised only with the approval of Shareholders (Section 180)

- To sale, lease or otherwise dispose of the whole or any part of the company's undertakings.
- To invest otherwise in trust securities.
- To borrow money for the purpose of the company
- To give time or refrain the director from repayment of any debt.

Others

- To Constitute Audit Committee (Section 177)
- To Make Political Contribution (Section 182)
- Contribute to National Defence Fund (Section 183)
- Contribution to Charitable or other funds (Section181)
- CSR (Section 135)


Thank You