

## 7. ALLOTMENT OF SECURITIES AND PRIVATE PLACEMENT

### QUESTION WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC AND CA INTER

Q.NO.	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)	M-19 (O)	M-19 (N)	N-19 (O)	N-19 (N)	N-20 (O)	N-20 (N)
1	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3	-	-	4	-	-	-	-	-	-	4	-	-	4	-	-	-	-
4	8	-	4	-	-	-	-	-	6	-	-	-	-	-	-	-	-
5	-	-	-	-	-	-	-	-	-	-	5	-	-	-	-	-	-

### PRACTICAL QUESTION WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC AND CA INTER

Q.NO.	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)	M-19 (O)	M-19 (N)	N-19 (O)	N-19 (N)	N-20 (O)	N-20 (N)
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### CHAPTER OVERVIEW

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### SECTION 1: THEORY FOR CLASSROOM DISCUSSION

Q.No.1. What are the requisites of a valid allotment of securities by the Company. When Company is liable to refund the application money? (A) (NEW SM, OLD SM)

#### ALLOTMENT OF SECURITIES BY COMPANY:

- 1) "Allotment of Securities" means an act of appropriation
  - a) out of previously un-appropriated capital of a Company
  - b) by the Board of Directors of the company
  - c) to the persons who have made applications for securities.
- 2) Shares come into existence once allotment is made.

#### GENERAL PRINCIPLES REGARDING ALLOTMENT:

- 1) Proper authority: Allotment must be made by proper authority. The proper authority is

- a) Board of Directors, or  
 b) Any committee authorised to allot securities on behalf of the Board.
- 2) **Communication of allotment to the applicants:**  
 a) It must be communicated in writing. Generally it is communicated through post.  
 b) Posting of allotment letter will be taken as a valid communication even if the allotment letter is lost in transit or delayed in transit.
- 3) **Reasonable time:** It must be made within a reasonable time. If the allotment is made after a long time then the applicant may refuse to take securities.
- 4) **Absolute and unconditional:** It must be absolute and in accordance with the terms and conditions of the application. Otherwise the applicant may reject the allotment.
- NOTE:** However in the event of over-subscription, the company will make pro-rata allotment (i.e. the applicant may accept a lesser number of shares).

### STATUTORY PROVISIONS REGARDING ALLOTMENT (SEC 39 & 40):

- 1) **Prohibition on allotment of securities [Sec.39(1)]:** Company cannot make allotment of securities unless the following 2 conditions are satisfied:  
 a) **Minimum subscription:** The amount stated in the prospectus as minimum subscription has been subscribed (*as per SEBI, min. subscription is 90%*) and  
 b) **Minimum amount payable on application [Sec.39(2)]:** The amounts payable on application on every security shall be –  
 i) not less than 5% of nominal amount (FV) of the security; or  
 ii) Such other percentage or amount as may be specified by SEBI by making regulations in this behalf  
 iii) Company has to receive application money either by cheque or through any banking channel.
- 2) **Repay all application monies if minimum subscription is not received [Sec 39(3)]:**  
 a) If amount of minimum subscription is not received within 30 days from the prospectus date (*or any other period prescribed by SEBI*) then the amount received shall be returned within 15 days from the date of closure of issue.  
 b) If the amount is not so paid, the directors of the company, who are in default, shall be jointly and severally liable to repay that money along with interest of 15% p.a.
- 3) **Filing of return of allotment [Sec 39(4)]:** Whenever a Company having share capital makes allotment of securities, it shall file with ROC a return of allotment (*Form PAS-3*) within 30 days of allotment.
- 4) **Consequences of default u/s 39(3) & 39(4):**

Who is Punishable	Punishment
Company	<ul style="list-style-type: none"> <li><b>Minimum:</b> Rs 1,000 for each day during which such default <u>continues</u></li> <li>or</li> <li><b>Maximum:</b> Rs.1 lakh for each default.</li> </ul>
Officers in Default	

### SIMILAR QUESTION:

1. M/s Super Communications Ltd recently went for further public offer for an amount of Rs.100 crores (10 crore shares of face value Rs.10 each). The company received applications for 8 crore shares. The company intends to allot the securities to the applicants. As a lawman advise the company whether it can allot securities or not? If allotted then what are the consequences?  
 A. Hint: No. Company has to refund the money as Minimum subscription is not received.
2. What are the statutory restrictions on allotment of securities u/s 39 of the Companies Act, 2013?  
 A. Hint: Minimum subscription and Minimum Application Money.
3. What are the requisites of a valid allotment of securities by the Company? When the Company is liable to refund the application money? Can share application money be deposited in any bank? (N13 - 5M)  
 A. Refer above answer

Section 40 (3) provides for the deposit of the application moneys received from the public for subscription to the securities offered, in a separate bank account in a scheduled bank and shall not be utilized for any purpose other than adjusting the same against the allotment of securities or refunding the same in case allotment is not made for any reason.

4. A applied for the purchase of shares in a public company. The letter of allotment was signed by B. an accountant of the company, and was posted to A. However, the accountant was not authorised to sign the Letter of allotment on behalf of the company. Is the allotment Valid?
  - A. In this case, the allotment of shares is not valid, and thus A will not become the shareholder on the basis of this allotment letter. Generally, such powers are not given to the accountants.
5. A applied for the purchase of certain shares in a public company. The letter of allotment was properly posted by the company. However, the letter of allotment never reached A. Is the allotment properly done?
  - A. Posting of allotment letter will be taken as a valid communication even if the allotment letter is lost in transit or delayed in transit. A became the shareholder in the company, and was liable to pay the balance of amount due on the shares.
6. A applied for the purchase of certain shares in a public company. The application by A was made in December, A heard nothing till August next year when he received the letter of acceptance (i.e., allotment). He refused to take shares and pay the amount due on them. Is it a Proper allotment?
  - A. Allotment must be made within a reasonable time. If the allotment is made after a long time then the applicant may refuse to take securities. A was entitled to refuse to take the shares, as the allotment was too late and was invalid.
7. "If a company does not receive minimum subscription, it should refund money received from applicants within such time as may be prescribed". Explain the above statement with suitable comments.
  - A. Refer above answer

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 1, 2)

**Q.No.2. What are the provisions relating to listing of securities on stock exchange and consequences of failure to get the securities listed? (A) (NEW SM, OLD SM)**

**PROVISIONS FOR LISTING OF SECURITIES ON STOCK EXCHANGE: (SEC 40)**

- 1) **Filing of an application with recognized stock exchange [Sec 40(1)]:** Before making a public offer, every company shall
  - a) make an application to one or more recognized stock exchange or exchanges and
  - b) obtain permission for the securities to be dealt with in such stock exchange or exchanges.
- 2) **Prospectus to state name(s) of stock exchange(s):** The prospectus shall state
  - a) that an application has been made to a recognized stock exchange; and
  - b) the name or names of the stock exchanges in which the securities shall be dealt with.
- 3) **To maintain separate bank account:**  
 All monies received on application, from the public, for subscription to the securities, shall be
  - a) kept in a separate bank A/c in a scheduled bank and
  - b) utilized for the following purposes only -
    - i) for adjustment against Allotment of securities (When permission is granted by stock exchanges with which we filed application for listing).
    - ii) for repayment of monies to the applicants (when company is unable to allot securities for any reason)
- 4) **Condition purporting to waive compliance shall be void:** Any condition, which requires any applicant of securities, to wave compliance with any of the requirements of this section, shall be void.
- 5) **Penalty for default u/s 40:** If a default is made in complying with the provisions of this sec, then

Who is held liable	Punishment
Company	<b>Fine: Minimum: Rs.5,00,000; Maximum: Rs. 50,00,000</b>
Officer in Default	<b>Imprisonment: Term which may extend up to 1 year; or Fine: Minimum: Rs.50,000; Maximum: Rs.3 lakhs; or Both</b>

**SIMILAR QUESTIONS:**

1. A Company which went for a public issue could not raise the 'Minimum subscription' as stated in the prospectus. Also the company fails to obtain listing permission from one of the stock exchanges where the shares proposed to be listed. Can the Company allot shares to its applicants? Advise the company as to the course of action
  - A. No. The company cannot make allotment.
 

Reasons:

    - a) Company failed to raise minimum subscription and
    - b) It failed to obtain approval from all the stock exchanges to whom application for listing is filed.
2. M/s Beta Limited collected money from public by issue of prospectus. The money was kept in a separate bank account. Company fails to obtain permission of listing from one of the recognized stock exchange. Meanwhile Company allotted its securities to the applicants. As a lawman advice whether action taken by company is in order. What are the consequences of such allotment? (or)  
Explain the consequences of failure to get the shares listed in stock exchange(s) named in the prospectus by a Public Company.
  - A. If company fails to obtain permission for listing of securities from the stock exchange (s) then the company is liable to repay all the application monies within the time specified by SEBI.  
Failure to do so will attract Punishment u/s 40. (Refer Point e)

**(IMMEDIATELY REFER PRACTICAL QUESTION CRD 4)**

**Q.No.3. When is Allotment of Shares treated as irregular allotment? State the effects of irregular allotment. (A) (NEW SM-TYK, OLD PM, N15 - 4M)**

**IRREGULAR ALLOTMENT<sup>1</sup>:** An allotment is deemed to be irregular when it is made in contravention of Sec. 23, 26, 39 and 40.

**IRREGULAR ALLOTMENT ARISES IN THE FOLLOWING INSTANCES:**

- 1) Company does not issue a prospectus in a public issue as required *u/s* 23.
- 2) Prospectus does not include all matters required to be included therein under section 26 (1), or the information given is misleading, faulty and incorrect.
- 3) Prospectus not filed with ROC for registration *u/s* 26.
- 4) Minimum subscription as specified in the prospectus not received *u/s* 39.
- 5) Received application money less than 5% of nominal value or the amount prescribed by SEBI *u/s* 39.
- 6) In case of public issue, approval for listing has not been obtained from recognized stock exchange *u/s* 40.

**EFFECTS OF IRREGULAR ALLOTMENT:** It depends on the nature of irregularity (*section violated*). There are only penalty provisions under respective sections apart from refund of application money.

- 1) If a prospectus is issued in contravention of the provisions of Sec 26 then Section 26(9)<sup>2</sup> shall apply.
- 2) In case the Company has not received either minimum application money or minimum subscription within 30 days of the date of issue of prospectus then
  - a) It must refund the application money received by it within the stipulated time.
  - b) Or else the allotment is treated as void and the defaulting Company & officers will be liable to further punishment as provided in Sec.39(5).
- 3) In case of a public issue, if company fails to obtain approval for listing of securities in one or more recognized stock exchange then
  - a) It must refund the application money received by it within stipulated time
  - b) Or else the allotment is treated as void and the defaulting Company & its officers will be liable to further punishment under section 40(5)<sup>3</sup>.

1) The Companies Act, 2013 does not separately provide for the term "Irregular Allotment"

2) The company shall be punishable with a Fine: Amount not less than Rs.50,000 but extend to Rs.3 Lakhs. And Every officer who is in default shall be liable for Imprisonment: Term which may extend upto 3 year; or Fine: Amount shall not be less than Rs.50,000 which may extend to Rs.3 lakhs; or Both.

**SIMILAR QUESTIONS:**

1. MPN Limited allotted shares to the public without issuing a prospectus. Discuss the validity of such allotment and list out any five circumstances when allotment is deemed to be irregular. (N18 (O) - 4M)
- A. Refer above answer.
2. How irregular allotment has been defined under Companies Act 2013?
- A. Companies Act, 2013 does not define the term irregular Allotment. It contains the essential requirements of valid allotment. An allotment of shares which does not satisfy the requirements of valid allotment is referred to as irregular allotment.

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 3)

**Q.No.4. Define the term underwriting and state the circumstances in which underwriting commission can be paid as per provisions of sec 40 of Companies Act 2013.**

(A) (NEW SM, OLD SM, OLD PM, N14 - 8M)

**UNDERWRITING:**

- 1) It is a contract between the company and other person.
- 2) To ensure the minimum subscription of securities, companies usually prefer it.
- 3) Underwriters will subscribe the minimum portion of capital that is not subscribed by public.
- 4) For giving such service, underwriters take certain percentage as commission.

**UNDERWRITING COMMISSION:** The consideration payable to the underwriters is known as underwriting commission<sup>4</sup>.

**CONDITIONS FOR PAYMENT OF UNDERWRITING SUBSCRIPTION: [Sec.40 (6)]**

- 1) **Authorized by the Articles:** Articles of the company must authorize the payment of underwriting commission.
- 2) **Sources:** The commission may be paid out of –
  - a) issue proceeds(or)
  - b) profits of the Company (or)
  - c) Both.
- 3) **Rate of Commission:** The rate of commission paid or agreed to be paid shall not exceed:

In case of Shares	i) 5% of the issue price of shares or ii) a rate authorised by the articles, Whichever is less.
In case of Debentures	i) 2.5% of the issue price of debentures or ii) as specified in the Company's articles, Whichever is less

- 4) **No Commission to be paid on some securities:** Commission shall not be paid on those securities which are not offered to the public for subscription
- 5) **Disclosure in prospectus:** The prospectus of the Company shall disclose -
  - a) The name of the underwriter(s)
  - b) The rate and amount of the commission payable to the underwriter; and
  - c) The number of securities underwritten by the underwriters, whether absolutely or conditionally.
- 6) **Copy of payment of commission to be delivered to registrar:** A copy of underwriting agreement shall be delivered to the ROC at the time of registration of prospectus.

- 3) The Company shall be liable with fine: amount not less than 5 Lakhs rupees but extend to Rs.50 lakhs and every officer who is in default shall be punishable with Imprisonment: Term which may extend upto 1 year; or Fine: Amount shall not be less than Rs.50,000 which may extend to Rs.3 lakhs; or Both.
- 4) Such commission is paid at a specified rate on the issue price of the whole of the shares or debentures underwritten whether or not the underwriters are called upon to take up any shares or debentures. Thus, the underwriters are paid for the risk they bear in placing the shares before the public. Underwriting commission may be in addition to brokerage.

**SIMILAR QUESTIONS:**

1. Explain clearly the meaning of the term underwriting and underwriting commission. How does the Companies Act, 2013 regulate payment of such commission? Explain. (NEW SM)
- A. Refer above answer.
2. TDL Ltd., a public company, is planning to bring a public issue of equity shares in June, 2018. The company has appointed underwriters for getting its shares subscribed. As a Chartered Accountant of the company appraise the Board of TDL Ltd. about the provisions of payment of underwriter's commission as per Companies Act, 2013. (M18 (N) - 6M)
- A. Refer above answer
3. In what way does the Companies Act, 2013 regulate the payment of 'underwriting commission'? Explain the provisions of the Act, state the conditions to be complied with, before payment of such commission can be made to underwriters of the Company. (OLD PM, N15 - 4M)
- A. Hint: Authorization in Articles, Disclosures in Prospectus and Filing with ROC.  
For detailed answer refer the answer to above question

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 5)

**PRIVATE PLACEMENT**

**Q.No.5. What is private placement of securities and state the conditions for issue of private placement of securities? (Section 42) (A) (NEW SM, OLD SM)**

**"Private Placement"** means-

- 1) any offer of securities or invitation to subscribe or issue of securities to a select group of persons by a Company (other than by way of public offer)
- 2) through private placement offer cum application letter and
- 3) which satisfies the conditions specified in Sec 42.

**CONDITIONS FOR PRIVATE PLACEMENT:**

- 1) **Identified Persons:** A private placement shall be made only to a select group of persons who have been identified by the Board and are referred to as "identified persons".
- 2) **Maximum number of persons:**
  - a) During the entire financial year, the private placement shall not be made to more than 200.
  - b) Following persons shall be excluded while computing the number of persons-
    - i) Qualified Institutional Buyers (QIB)
    - ii) Employees of the Company to whom the securities have been offered under ESOP;
  - c) The restriction with respect to maximum number of persons would be considered individually for each kind of security i.e. equity shares, preference shares, and debentures.
  - d) Non applicability of provisions with respect to maximum number of persons
    - i) Non-Banking Financial Companies
    - ii) Housing Financial Companies
  - e) If a company offers invitation for subscription of securities to more than prescribed number of persons, it shall be deemed to be an offer made to public. (Deemed Public Offer)
- 3) **Procedure for Private Placement:** (Rule 14 of Companies (Prospectus and Allotment of Securities) Rules, 2014):
  - a) **Offer and Application:** A company making private placement shall issue private placement offer and application to identified persons.
  - b) **No Renunciation:** Provided that the private placement offer and application shall not carry any right of renunciation.

- c) **Notice and Explanatory Statement:** Explanatory statement annexed to the notice for shareholders' approval, the following disclosure shall be made:
- i) Particulars of the offer including date of passing of Board resolution.
  - ii) Kinds of securities offered and the price at which security is being offered.
  - iii) Basis or justification for the price (including premium, if any).
  - iv) Name and address of valuer who performed valuation.
  - v) Amount which the company intends to raise by way of such securities.
  - vi) Important terms and conditions of raising such securities such as:
    - Proposed time schedule,
    - Purposes or objects of offer,
    - Contribution being made by the promoters or directors either as part of the offer or separately in furtherance of objects;
    - Principle terms of assets charged as securities.
- d) **Pass a Special Resolution:** The proposal has to be approved by the shareholders of the company, by a special resolution for each of the offers or invitations at the General Meeting.
- Exception:** *However, in case of Private Placement by issue of Non-convertible debentures for an amount not exceeding limits u/s 180(1)(c) – only Board Resolution is adequate<sup>5</sup>.*
- e) **Mode of Payment to apply Private Placement:** The identified person shall apply for private placement and pay subscription money only by cheque or DD or any other banking channel but not by cash.
- f) **Separate Bank Account:** Monies received on application shall be kept in a separate bank account in a scheduled bank and shall be utilised only for the:
- i) adjustment against allotment of securities or
  - ii) repayment of monies where the company is unable to allot securities.
- g) **60 Days' Time limit for Allotment:**
- i) A company shall allot its securities within 60 days from the date of receipt of the application money.
  - ii) If the company is not able to allot the securities within that period, it shall repay the application money within 15 days from the expiry of 60 days and
  - iii) If the company fails to repay the application money within 15 days, it shall be liable to repay that money with interest at the rate of 12% per annum from the expiry of the 60 day.
- h) **Filing with ROC:**
- i) A Company can make private placement offer cum application only after filing a copy of Board Resolution or Special Resolution with ROC.
  - ii) A company making any allotment of securities under this section, shall file with the Registrar a return of allotment within 15 days from the date of the allotment.
  - iii) The return of allotment shall include a complete list of all allottees, with their full names, address, number of securities allotted and such other relevant information as may be prescribed.
  - iv) Only after filing return of allotment with ROC, the company can use the money for the purposes for which it is raised.
  - v) **Default:** If a company defaults in filing the return of allotment within 15 days, the company, its promoters and directors shall be liable to a penalty for each default of one thousand rupees for each day during which such default continues but not exceeding twenty-five lakh rupees.

5) (Sec. 180 – Deals with Restriction on Powers of BOD) (Limit – Existing Borrowings and Proposed NCD together shall not exceed PUC & Free Reserves of the company)

- 4) **Prohibition on further offer u/s. 42:** No fresh offer or invitation under Private Placement shall be made, unless in the previous offer or invitation –
- The allotments have been completed; or
  - Such offer or invitation has been withdrawn.
- 5) **Multiple Offers to Same Persons:** A company may make more than one issue of securities to such class of identified persons.
- 6) **Prohibition on Public Advertisement:** The Company shall not release any public advertisements or utilise any media, marketing or distribution channels or agents to inform the public at large about such an issue.
- 7) **Money not be utilized:** A company shall not utilize the monies raised through private placement unless–
- a) Allotment is made; and
  - b) The Return of Allotment is filed with ROC
- 8) **Consequences of Contravention (Sec 42):**

WHO IS LIABLE?	PENALTY
a) Company	i) Amount involved in the offer; or
b) Promoters	ii) Rs.2 Crores,
c) Directors	Whichever is lower

- 9) **Refund:** Company shall refund all monies to subscribers within a period of 30 days of the order imposing the penalty. Or else, it shall be liable to pay interest at the rate of 12% p.a. to the subscribers.

**Note:** Offer / invitation treated as public offer. Any offer or invitation not in compliance with the provisions of Sec 42 shall be treated as public offer and all the provisions of this Act, and the Securities Contracts (Regulation) Act, 1956 and the SEBI Act, 1992 shall be complied with.

**SIMILAR QUESTIONS:**

1. Describe the procedure for private placement of securities by a Company as per the provisions of the Companies Act, 2013.
  - A. Refer above answer.
2. State the conditions subject to which invitation for subscription of securities on private placement can be made by a Company as per companies Act, 2013?
  - A. Refer above answer.
3. Private companies as well as private placement by any Company, do not require the issue of a prospectus?
  - A. Yes, only public issue of shares require prospectus.

(IMMEDIATELY REFER PRACTICAL QUESTION CRD 6, 7)

**SECTION 2: QUESTIONS FOR ACADEMIC INTEREST – FOR STUDENTS SELF STUDY**

**(MAY GET SOME MCQs. SO, STUDENTS NEED TO READ THE SAME ON THEIR OWN)**

**Q.No.1. Explain the provisions of Companies Act, 2013 relating to “Return of Allotment”.**  
(C) (OLD PM) (M14 - 4M)

**RETURN OF ALLOTMENT [Sec.39 (4)]:** Whenever a Company makes any allotment of its securities, it shall file a Return of Allotment (*Form PAS-3*) within 30 days with the ROC.

**ATTACHMENTS AND INCLUSIONS IN FORM PAS - 3:**

- 1) **LIST OF ALLOTTEES:**
  - a) A list of allottees stating their name, address, occupation, and number of securities allotted to each of them.
  - b) It shall be duly certified by the signatory of Form PAS-3 as being complete and correct as per the records of the Company.

- 2) **COPIES OF CONTRACTS TO BE ATTACHED:** In case of securities (*other than bonus shares*), allotted as fully or partly paid up, for consideration other than cash, following shall be attached to Form PAS-3,
- A copy of the contract duly stamped, along with
  - A copy of any contract of sale, if relating to a property or an asset or a contract for services or other consideration.
- 3) **AUTHORIZATION BY ORDINARY RESOLUTION FOR BONUS SHARES:** In case of issue of bonus shares, a copy of the Ordinary Resolution passed in the GM, authorizing the issue of bonus shares, shall be attached to Form PAS -3.

*Reissue of forfeited securities is not allotment, since it is re-appropriation of already appropriated capital. Therefore, it is not required to file return of allotment in such case.*

**SIMILAR QUESTIONS:**

- What are the documents which have to be enclosed to PAS - 3?  
A. Hint: List of Allotees, Contract copy, Shareholders Resolution.
- Who has to sign on the List of Allotees?  
A. The same persons who signed on Form PAS-3.

**Q.No.2. What is meant by Deemed Public offer?**

**(C)**

**DEEMED PUBLIC OFFER:**

- 1) **Offer / invitation made to more than the prescribed number of persons:**

If a listed / unlisted Company,

- makes an offer to allot or invites subscription, or
- allots, or enters into an agreement to allot, securities
- to more than the prescribed number of persons,

Then the same shall be deemed to be an offer to the public and shall be governed by the provisions related to public offer irrespective of the fact as to whether -

- The Company is listed or unlisted; or
- It intends to get its shares listed on any stock exchange or not; or
- It has received the payment for the securities or not.

- 2) **Offer / invitation treated as public offer:** Any offer or invitation not in compliance with the provisions of Sec 42 shall be treated as public offer and all the provisions of this Act and the Securities Contracts (Regulation) Act, 1956 and the SEBI Act, 1992 shall be required to be complied with.

**Q.No.3. Distinguish between Public Offer and Private Placement**

**(B)**

Public offer	Private placement
It can be made by <u>public Company</u> .	It can be made by <u>private Company</u> or <u>public Company</u> .
Public offer is made to public <u>at large</u> to purchase securities of Company	Private placement is made to <u>limited number</u> of persons.
When public offer is made <u>prospectus required</u> to be prepared.	When securities are offered through private placement, <u>private placement offer letter</u> is prepared.

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### SECTION 3: PRACTICAL QUESTIONS FOR CLASSROOM DISCUSSION

**Q.No.1.** After receiving 80% of the minimum subscription as stated in the prospectus, a Company allotted 100 equity shares in favour of 'X'. The Company deposited the said amount in the bank but withdrew 50% of the amount, before finalisation of the allotment, for the purchase of certain assets. X refuses to accept the allotment of shares on the ground that the allotment is violative of the provisions of the Companies Act, 2013. Comment  
(NEW SM, OLD PM, MTP2 N18 (O), MTP1 M18 (O))

**PROVISION:** A Company cannot proceed with the allotment of securities to the public unless following conditions are satisfied:

- a) The minimum subscription as stated in the prospectus must be received within 30 days from the date of issue of prospectus (*as per SEBI, min. subscription is 90%*) and
- b) The amounts payable on application, on every security, shall not be less than -
  - i) 5% of nominal value (FV) of the security; or
  - ii) Such other percentage or amount as may be specified by SEBI
- c) If minimum subscription is not received within 30 days from the date of issue of the prospectus then the amount received shall be returned within 15 days from the date of closure of issue.

**ANALYSIS:** The Company has received 80% of the minimum subscription as stated in the prospectus. Hence, the allotment is in contravention of sec 39(1) of the Companies Act, 2013. It prohibits a Company from making any allotment of securities until it receives the amount of minimum subscription stated in the prospectus. U/s 39 (3), it is required to refund the money received (i.e. 80% of the minimum subscription) to the applicants. It has no other option available.

**CONCLUSION:** Therefore, in the present case X can refuse to accept the allotment of shares which has been illegally made by the Company.

**Q.No.2.** The BOD of a Company reissued securities which were forfeited for non-payment of calls. State whether Return of Allotment is required to be filed or not under the Companies Act, 2013?

**PROVISION:** As per to Sec 39(4) of the Companies Act, 2013, when a Company having share capital, makes any allotment of securities, it shall file with the ROC a return of allotment in prescribed manner.

Allotment is the act of appropriation by the BOD of the Company out of previously unappropriated capital of the Company to persons who have made application for securities. Therefore reissue of forfeited securities is not allotment, since it is the appropriation of the already appropriated capital.

**ANALYSIS:** By applying the above provisions in the given case, reissue of forfeited securities does not amount to allotment of securities because it is the appropriation of already appropriated capital.

**CONCLUSION:** Return of allotment is not required to be filled by the Company.

**Q.No.3.** The BOD of M/s Reckless Investments Ltd. have allotted shares to the investors of the Company without filing a prospectus with the ROC, Mumbai. Explain the remedies available to the investors in this regard.  
(NEW SM-TYK, OLD PM, MTP1 N18 (N))

**PROVISION:** As per Sec 23 of the Companies Act, 2013, a public Company can issue securities to the public only by issuing a prospectus. Sec 26 (1) lays down the matters required to be disclosed and included in a prospectus and requires the registration of the prospectus with the ROC before its issue.

**ANALYSIS:** In the given case, the Company has violated the above provisions of the Act and hence the allotment made is void (*i.e Irregular allotment*).

**CONCLUSION:** The Company will have to refund the entire moneys received and is also liable for punishment u/s 26 (9) of the Act.

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**Q.No.4.** A public limited Company which went in for Public issue of shares had applied for listing of shares in three Recognised Stock Exchanges and out of it only two had given permission for listing. Can the Company proceed for allotment of shares?  
(NEW SM, OLD PM)

**PROVISION:** Before making a Public Offer, every Company shall make an application to one or more recognised stock exchange or exchanges and obtain permission for the securities to be dealt with in such stock exchange or exchanges.

Sec 40 (2) further states that where a prospectus states that an application u/s 40(1) has been made, such prospectus shall also state the name or names of the stock exchange in which the securities shall be dealt with.

All monies received on application, from the public, for subscription to the securities, shall be kept in a separate bank A/c in a scheduled bank and utilized for the following purposes only -

- a) **Adjustment against allotment of securities:** If securities have been permitted to be dealt with in the stock exchange or stock exchanges specified in the prospectus; or
- b) **Repayment of monies:** If Company is unable to allot securities then repay all the application monies within the time specified by SEBI.

Penalty for default u/s 40(5)

- a) For Company – Fine: Amount not less than Rs.5 Lakhs but may extend up to Rs.50 lakhs.
- b) For every officer who is in default –
  - i) Imprisonment: Term which may extend upto 1 year; or
  - ii) Fine: Amount shall not be less than Rs.50,000 and it extend to Rs.3 lakhs; or
  - iii) Both.

**ANALYSIS:** From the above it is clear that the Company shall not only apply for listing of the securities at a recognized stock exchange but it shall also obtain permission thereof before making the public offer.

**CONCLUSION:** If the Company has offered the shares, before obtaining the approval from the recognised stock exchanges, it has violated the provisions of sec 40 and hence punishable u/s 40(5)

**Q.No.5.** Unique Builders Limited decides to pay 2.5% of the value of debentures as underwriting commission to the underwriters but the AOA of the Company authorize only 2% underwriting commission on debentures. The Company further decides to pay the underwriting commission in the form of flats. Examine the validity of the above arrangements under the provisions of the Companies Act, 2013.  
(NEW SM-TYK, OLD PM, N10 - 8M, N 19(O) -3, MTP M18 (N), RTP M18 (N&O))

**PROVISION:** Sec 40(6) of Companies Act, 2013 - Payment of commission for subscription

A Company may pay commission to any person in connection with the subscription to its securities subject to the following conditions prescribed under the Companies (Prospectus and Allotment of Securities) Rules, 2014:

- a) **Authorized by the Articles:** The payment of such commission shall be authorized in the Company's AOA;
- b) **Paid out of the proceeds of the issue/profit:** The commission may be paid out of proceeds of the issue or the profit of the Company or both;
- c) **Rate of Commission:** The rate of commission paid or agreed to be paid shall not exceed,
  - i) in case of shares, 5% of the issue price or a rate authorised by the AOA, whichever is less, and
  - ii) in case of debentures, shall not exceed 2.5% of the issue price, or as specified in the Company's articles, whichever is less;
- d) **No payment of commission:** No commission shall be paid to any underwriter on securities which are not offered to the public for subscription.

**ANALYSIS:** In the given problem the articles of the Company has prescribed 2% underwriting commission but directors decided to pay 2.5% underwriting commission. The directors cannot do so. Such commission cannot be more than that prescribed in the AOA. Therefore the directors are not empowered to do.

**CONCLUSION:**

- a) Hence the decision of Unique Builders Limited, to pay underwriting commission exceeding the percentage prescribed under AOA is not valid.
- b) The company may pay the underwriting commission in the form of flats as both the Companies Act and the Rules do not impose any restriction on the mode of payment though the source has been restricted to either the proceeds of the issue or profits of the company.

**Q.No.6.** PQR Bakers Limited wants to raise funds for its upcoming project. Accordingly, it has issued private placement offer letters for issuing equity shares to 55 persons, of which four are qualified institutional buyers and remaining are individuals. Before the completion of allotment of equity shares under this offer letter, company issued another private placement offer letter to another 155 persons in their individual names for issue of its debentures.

Being a public company is it possible for PQR Bakers Limited to issue securities under a private placement offer? By doing so, whether the company is in compliance with provisions relating to private placement or should these offers be treated as public offers? What if the offer for debentures is given after allotment of equity shares but within the same financial year?  
(NEW SM-TYK)

**PROVISION:** According to section 42 of the companies act, 2013 –

Any private or public company may make private placement through issued of a private placement offer letter. However, the offer shall be made to the persons not exceeding 200 in a financial year. For counting number of persons qualified institutional buyers and employees under Employees stock option scheme will not be considered. However, this limit should be counted separately for each type of security.

If a company makes an offer or invitation to more than the prescribed number of persons it shall be deemed to be an offer to the public and shall be governed by the provisions related to prospectus.

Also a company cannot make fresh offer under this section if allotments with respect to any offer made earlier have been completed or that offer has been withdrawn or abandoned by the company. This rule is applicable even if the issue is of different kind of security.

Any offer or invitation not in compliance with the provisions of this section shall be treated as a public offer and all provisions will apply accordingly.

**ANALYSIS AND CONCLUSION:** In the given case PQR limited is a public company and looking at above provisions we can say that even a public company can make private placement. Company has given offer to 55 persons out of which 4 are qualified institutional buyers hence the offer is given to effectively 51 persons which is well within the limit of 200 persons. From this angle company is in compliance with private placement rules.

But company has given another private placement offer which is non-compliance of provisions of section 42 hence the offers given by company will be treated as public offer and will be governed accordingly.

But if the company gives offer for debentures in the same financial year after allotment of equity shares is complete then both the offers can well be treated as private placement offers. Here we should not add 51 and 155 persons for checking the limit of 200 because this limit should be checked individually for each kind of securities.

**Q.No.7.** ABC Company is offering 1000 shares of Rs.10 each to a shareholder on private placement basis. Whether the offer made by the ABC is in order?

**PROVISIONS:** The value of private placement offer or invitation per person shall be with an investment size of not less than Rs. 20,000 of face value of securities, irrespective of the fact that the actual allotment amount (including share premium) may be much higher than the said limit. [Section 42 read with the Rule 14(2) of the Companies (Prospectus and Allotment of Securities) Rules, 2014]

**ANALYSIS AND CONCLUSION:** Here in the given case the face value of securities offered is less than Rs. 20,000. Here the offer made by ABC is not acceptable as a private placement under section 42.

**Note:** As per recent amendment in RTP May 2019, Section 42 and company rules relating to Private Placement were replaced with new provision. Such restriction of Rs. 20,000 for minimum application amount rule was not specified. So as per amendment there is no such restriction.

## SECTION 4: PRACTICAL QUESTIONS FOR STUDENTS SELF PRACTICE

**Q.No.1.** The BOD of a Company decides to pay 5% of issue price as underwriting commission to the underwriters. The Articles of Association of the Company permit only 3% commission. The BOD further decides to pay the commission out of the proceeds of the share capital. Are the decisions taken by the BOD valid under the Companies Act, 2013? (NEW SM, OLD PM, MTP2 M18 (O))

**PROVISION:** Refer PQ 5 in class room discussion

**ANALYSIS:** In the given problem the articles of the Company has prescribed 3% underwriting commission but directors decided to pay 5% underwriting commission. The directors cannot do so

Moreover, the directors can pay the commission out of capital since underwriting commission can be paid both out of capital as well as out of profits.

**CONCLUSION:** The BOD decision to pay 5% of commission is not valid but such payment out of capital is valid.

**Q.No.2.** The AOA of MSW Ltd. contained a provision that upto 4% of issue price of the shares may be paid as underwriting commission to the underwriters. The BOD decided to pay 5% underwriting commission. Can the BOD do so? State the provisions of law in this regard as stated under the Companies Act, 2013. (OLD PM, N15 - 4M)

**PROVISION & ANALYSIS:** Refer PQ 5 in class room discussion

In the given problem the articles of the Company has prescribed 4% underwriting commission but directors decided to pay 5% underwriting commission. The directors cannot do so

**CONCLUSION:** The BOD decision to pay 5% of commission is not valid.

**Q.No.3.** Teji Pvt. Ltd. received a cheque of Rs. 10 lakhs towards the share application money from Vinod on 31st March 2005. On the same day, the Board of directors allotted the shares, filed necessary returns and issued the share certificate. The cheque was subsequently deposited with the bank which bounced. Advise the Company.

**REF CASE LAW:** SBI vs. Kunwar Sarder Singh

**ANALYSIS AND CONCLUSION:** It was held that the allotment of the shares should have been made only after realization of application and allotment money. Directors of Company are liable to the Company for losses incurred by it. However, Company cannot dispute the amount mentioned on the certificate as already paid up.

**Q.No.4** A applied for the purchase of certain shares in a company on the condition that he would be appointed as cashier of the company. The company allotted the shares to A but he was not appointed the cashier of the company. Is A bound by the allotment? Give reasons.

**PROVISION:** The law on the point is that the allotment of shares must be in accordance with terms and conditions of application for allotment.

**ANALYSIS AND CONCLUSION:** In the present case, A's application to take share was conditional on his being appointed as cashier. In view of the above law, A is not bound by the allotment.

**Q.No.5.** Examine the validity of the following statement with reference to the provisions of the Companies Act, 2013.

"The Articles of Association of X Limited contain a provision that the underwriting commission may be paid up to 4% of the issue price of the shares. However, the Board of Directors have decided to pay the underwriting commission of 5% to Deal & Co., the underwriters."

**PROVISION:** Section 40 (6) of the Companies Act 2013, provides that a company may pay commission to any person in connection with the subscription to its securities, subject to the conditions prescribed under the *Companies (Prospectus and Allotment of Securities) Rules, 2014*.

Rule 13 states that the rate of commission paid or agreed to be paid shall not exceed, in case of shares, five percent (5%) of the price at which the shares are issued or a rate authorised by the articles, whichever is less.

**ANALYSIS:** In the given problem, the articles of X Ltd. have prescribed 4% underwriting commission but the directors decided to pay 5% underwriting commission.

**CONCLUSION:** Therefore, the decision of the Board of Directors to pay 5% underwriting commission to the underwriters (i.e. Deal & Co.) is invalid.

## SECTION 5: SECTION NUMBERS

CONCEPT	SECTION NO.
Allotment of securities	39
Listing of securities	40
Conditions for issue of private placement	42

## PENALTY

Section	Particulars	Penalty
Section 39 – Allotment of securities by company	If the Company, has not returned the application money received (when minimum subscription is not received) If a company having a share capital has not filed return of allotment with Registrar.	Company, Officer in Default (for each default) Rs 1,000 for each day during which such default continues or Rs 1 Lac, whichever Less.
Section 40- Securities to be dealt with in stock exchanges	If a company is making public offer and it fails to inform to one or more stock exchange and/or fails to follow other related provisions of Sec 40	Company, Officer in Default Company: Rs 5 Lac to 50 Lac Officer in Default Company: Fine: Rs 50,000 to 3 Lac Imprisonment: May Extend to 1 Year, Or Both
Section 42- Offer or invitation for subscription of securities on private placement	Default in repayment of application money within 15 days from the completion of 60 days from the receipt of application money. If a company makes an offer or accepts monies in contravention of Sec 42	Company - 12% interest p.a. from the expiry of 60 <sup>th</sup> day. Company, promoters and directors Penalty: May extend to amount raised through the private placement or 2 crore rupees, whichever is lower, and the company shall also refund all monies with interest as specified in Sec 42(6) to subscribers within a period of 30 days of the order imposing the penalty

## TIME - LIMITS

PARTICULARS	TIME – LIMIT
Time for allotment of securities under Private Placement (sec 42)	Within 60 days from the date of receipt of the application money for such securities.
Time limit for refund of application money in case of failure to allot the securities within 60 days (sec 42)	15 days from the date of completion of sixty days
Filing of Complete details of issue of private placement and information with ROC	Within a period of thirty days of circulation of relevant private placement offer letter.
Makes an offer or accepts monies in contravention of	Company shall refund all monies to subscribers

conditions for Private placement (sec.42 )	within a period of thirty days of the order imposing the penalty u/s 42
Time limit for refund of all moneys received by the Company in case of noncompliance of sec 39 (restriction on allotment of securities)	Within 15 days from the closure of the issue as per Rules.
Filing of return of allotment (PAS-3) to ROC u/s 39	Within 30 days from date of allotment of securities

## THE END

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