

# *An Analysis on the "Issue Of Shares On Preferential Basis"*

**navneet k. arora & co.**  
COMPANY SECRETARIES

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JE-9/104, Khirki Extn. Commercial Complex,  
(Opposite M Block Tikona Park),  
Malviya Nagar, New Delhi-110017  
+91 11 29545877

info@navneetaroracs.com  
aroranavneet@rediffmail.com  
www.navneetaroracs.com

# Proprietor 's Profile at a Glance

## Navneet K. Arora & Co., Company Secretaries

### BASIC DETAILS

- ✂ Name of the Proprietor – **CS Navneet Arora**
- ✂ Year of Passing of ICSI Final Examination – **June 1990**
- ✂ Date of becoming Associate Member of ICSI (ACS - 8421) – **3<sup>rd</sup> March 1992**
- ✂ Date of becoming Fellow Member of ICSI (FCS - 3214) – **21<sup>st</sup> July 1997**
- ✂ Date of holding Certificate of Practice (CP - 3005) – **20<sup>th</sup> November 1998**
- ✂ Experience (No. of Years) – **25 Years (15 Years in Practice)**



### EDUCATIONAL QUALIFICATION:

- ✂ Master of Commerce.
- ✂ Fellow Member of The Institute of Company Secretaries of India
- ✂ Post Graduate Diploma in Financial Management

### PROFESSIONAL ASSOCIATION / RECOGNITION / MEMBERSHIP OF CONFEDERATION BODIES:

- ✂ Member - **All India Management Association New Delhi (AIMA).**
- ✂ Professional Member - **PHD Chamber of Commerce and Industries, New Delhi.**
- ✂ Appointed as **Peer Reviewer** by ICSI to conduct peer review of Practicing Member of ICSI.
- ✂ ICSI Certified participant of **National Workshop on Diligence Report for Banks.**
- ✂ **Convener South Delhi Study Group of NIRC of the ICSI** -2011, 2012, 2013 & 2014. Also Past Governing Body Member of Kanpur Chapter of NIRC of the ICSI & Past Member of various Professional Development Committee of NIRC of the ICSI.
- ✂ Regular Participant, Speaker of Seminars / Workshop on the Professional Development Program of various Professional Management Institutes including Institute of Company Secretaries of India (ICSI), Asia Pacific Institute of Management (AIM), National Foundation for Corporate Governance (NFCG) etc.

# *Issue Of Shares On Preferential Basis*

- ❑ Preferential Allotment is the process by which allotment of securities/shares is done on a preferential basis to a selected group of investors.
- ❑ This method is distinctive from others in the sense that the entire allotment is made to pre-identified people, who may or may not be existing shareholders of the company, at a pre-determined price.
- ❑ For raising funds, it is not always preferable or feasible for a company to issue securities to the public at large as it is time consuming as well as an expensive option. In such situations, the securities can be offered to a comparatively smaller group of individuals, such as the directors or the existing shareholders. This entire process is known as preferential allotment.
- ❑ Generally, preferential allotments are made to people who wish to take a strategic stake in the company. For instance, venture capitalists, existing shareholders like promoters who wish to enhance their stake in the company, financial institutions, buyers of the company's products or its suppliers.
- ❑ The rationale is to provide a route by which the company can secure the equity participation of those who it feels can be of value as shareholders, but for whom it may be inordinately costly and/or impractical to buy shares from the market.

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❖ **Extract of the relevant provisions prescribed in Section 62 of the Companies Act, 2013 as under:-**

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

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

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

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

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

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

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(c) to any persons, if it is authorized 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.

- (2)** The notice referred to in sub-clause (i) of clause (a) of sub-section (1) shall be dispatched 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.
- (3)** Nothing in this section 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: Provided 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.
- (4)** Notwithstanding anything contained in sub-section (3), 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: Provided that 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.

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- (5) In determining the terms and conditions of conversion under sub-section (4), 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.
- (6) Where the Government has, by an order made under sub-section (4), 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 under sub-section (4) or where such appeal has been dismissed, the memorandum of such company shall, where such order has the effect of increasing the authorized share capital of the company, stand altered and the authorized 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.

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## ❖ **Relevant Rules / Procedure in the Companies (Share Capital and Debentures) Rules, 2014 as under:-**

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

Provided that 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.

[Explanation.- For the purposes of this rule, (i) the expression 'Preferential Offer' means an issue of shares or other securities, by a company to any select person or group of persons on a preferential basis and does not include shares or other securities offered through a public issue, rights issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities; (ii) the expression, "shares or other securities" means equity shares, fully convertible debentures, partly convertible debentures or any other securities, which would be convertible into or exchanged with equity shares at a later date.]



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- (2) 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 Securities and Exchange Board, 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, namely:-
  - (a) the issue is authorized by its articles of association;
  - (b) the issue has been authorized by a special resolution of the members;
  - (c) the securities allotted by way of preferential offer shall be made fully paid up at the time of their allotment.
  - (d) 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:
    - (i) the objects of the issue;
    - (ii) the total number of shares or other securities to be issued;
    - (iii) the price or price band at/within which the allotment is proposed;
    - (iv) basis on which the price has been arrived at along with report of the registered valuer;
    - (v) relevant date with reference to which the price has been arrived at;
    - (vi) the class or classes of persons to whom the allotment is proposed to be made;
    - (vii) intention of promoters, directors or key managerial personnel to subscribe to the offer;
    - (viii) the proposed time within which the allotment shall be completed;



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

(x) the change in control, if any, in the company that would occur consequent to the preferential offer;

(xi) 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;

(xii) the justification for the allotment proposed to be made for consideration other than cash together with valuation report of the registered valuer.

(xiii) The pre issue and post issue shareholding pattern of the company in the format given by MCA.

(e) the allotment of securities on a preferential basis made pursuant to the special resolution passed pursuant to sub-rule (2)(b) shall be completed within a period of twelve months from the date of passing of the special resolution.

(f) if 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.

(g) 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;

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(h) where convertible securities are offered on a preferential basis with an option to apply for and get equity shares allotted, the price of the resultant shares 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;

(i) 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;

(j) where the preferential offer of shares is 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.

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*Thanking you*

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**navneet k. arora & co.**  
COMPANY SECRETARIES

E8/1, Near Geeta Bhawan Mandir, Shivalik Road, Malviya Nagar, New Delhi-110017

☎ 011- 65233450, 011-29545877, 9810328141, 011-26686432

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