SECRETARIAL PRACTICE

STANDARD XII

The Constitution of India

Chapter IV A

Fundamental Duties

ARTICLE 51A

Fundamental Duties- It shall be the duty of every citizen of India–

(a) to abide by the Constitution and respect its ideals and institutions, the National Flag and the National Anthem;

(b) to cherish and follow the noble ideals which inspired our national struggle for freedom;

(c) to uphold and protect the sovereignty, unity and integrity of India;

(d) to defend the country and render national service when called upon to do so;

(e) to promote harmony and the spirit of common brotherhood amongst all the people of India transcending religious, linguistic and regional or sectional diversities, to renounce practices derogatory to the dignity of women;

(f) to value and preserve the rich heritage of our composite culture;

(g) to protect and improve the natural environment including forests, lakes, rivers and wild life and to have compassion for living creatures;

(h) to develop the scientific temper, humanism and the spirit of inquiry and reform;

(i) to safeguard public property and to abjure violence;

(j) to strive towards excellence in all spheres of individual and collective activity so that the nation constantly rises to higher levels of endeavour and achievement;

(k) who is a parent or guardian to provide opportunities for education to his child or, as the case may be, ward between the age of six and fourteen years.

The Coordination Committee formed by GR No. Abhyas - 2116/(Pra.Kra.43/16) SD - 4
Dated 25.4.2016 has given approval to prescribe this textbook in its meeting held on
30.01.2020 and it has been decided to implement it from the educational year 2020-21.

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The Constitution of India

Preamble

WE, THE PEOPLE OF INDIA, having solemnly resolved to constitute India into a SOVEREIGN SOCIALIST SECULAR DEMOCRATIC REPUBLIC and to secure to all its citizens:

JUSTICE, social, economic and political;

LIBERTY of thought, expression, belief, faith and worship;

EQUALITY of status and of opportunity; and to promote among them all

FRATERNITY assuring the dignity of the individual and the unity and integrity of the Nation;

IN OUR CONSTITUENT ASSEMBLY this twenty-sixth day of November, 1949, do HEREBY ADOPT, ENACT AND GIVE TO OURSELVES THIS CONSTITUTION.

NATIONAL ANTHEM

Jana-gana-mana-adhināyaka jaya hē
Bhārata-bhāgya-vidhātā,

Panjāba-Sindhu-Gujarāta-Marāthā
Drāvida-Utkala-Banga

Vindhya-Himāchala-Yamunā-Gangā
uchchala-jaladhi-taranga

Tava subha nāmē jāgē, tava subha āsisa māgē,
gāhē tava jaya-gāthā,

Jana-gana-mangala-dāyaka jaya hē
Bhārata-bhāgya-vidhātā,

Jaya hē, Jaya hē, Jaya hē,
Jaya jaya jaya, jaya hē.

PLEDGE

India is my country. All Indians are my brothers and sisters.

I love my country, and I am proud of its rich and varied heritage. I shall always strive to be worthy of it.

I shall give my parents, teachers and all elders respect, and treat everyone with courtesy.

To my country and my people, I pledge my devotion. In their well-being and prosperity alone lies my happiness.

Preface

Dear students,

We take pleasure in introducing the textbook for Standard XII based on the revised syllabus from the academic year 2020-2021.

Secretarial Practice is one of the subjects in the commerce stream which deals exclusively with the business world's largest and the most popular form of commercial enterprises viz. the Joint Stock Company. The Standard XI syllabus covers topics like features of a company, incorporation of a company, its management, role of company secretary, etc. The syllabus for Standard XII further deals with the working of Joint Stock Company by focusing on the methods used by a company to raise capital by issuing Shares, Debentures, Public Deposits, etc. in the financial market. Chapters on the important sources of capital, viz. Shares, Debentures and Public Deposits, covers only the provisions and procedures related to raising such capital. These chapters are followed by chapters on correspondence with contributors of capital.

The subject derives its contents from the Companies Act, 2013. Due care has been taken to present the matter in a simple language so that students can easily understand the legal and technical aspects of the Act. Charts and diagrams are given wherever necessary. Meaning of every new term or word has been explained in a box. Moreover, to make learning stimulating, additional information has been given in every chapter along with interesting activities for the students. Exercise given at the end of every chapter is exhaustive. Various types of questions have been asked to test conceptual clarity and encourage logical thinking and reasoning. Application-based questions have been included to enable students to apply theoretical knowledge to solve real life-like situations. Documents, Proformas, etc. have been given in the Q.R. Code on the title page.

The new Companies Act has been amended many times since its enactment in 2013. This book includes all the amendments made in the Act and the various Rules and Regulations of SEBI upto November 2019.

We are thankful to the subject committee members, study group members, translators, reviewers and all those who have contributed in designing this new version of the textbook.

We hope the textbook meets all the expectations of the academicians, teachers and students.

(Vivek Gosavi)
Director
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Pune
Date : 21 February 2020
Bharatiya Saur : 2 Phalguna 1941

Competency Statements

Unit No.	Topic	Competency Statements
1	Sources of Corporate Finance	• Understand the concept of Corporate Finance and its Importance. • Understand meaning of capital structure of a company • Understand various sources of owned and borrowed capital • Compare different sources of finance.
2	Capital raising	• Understand the provisions and procedures related to Issue of Shares, Debentures and Acceptance of Public Deposits.
3	Secretarial Correspondence	• Develop Communication skills related to Members, Debenture holders and Deposit holders.
4	Depository System	• Understand the concept of Depository system and its Importance. • Know the constituents of Depository System. • Learn the Functioning of Depository System.
5	Payment of Dividend and Interest	• Understand the concept of Dividend and Interest. • Compare between Interim and Final Dividend. • Learn about provisions on sources and for Declaration and Payment of Dividend.

6	Financial Markets	• Understand the Meaning of Financial Market. • Know the types of Financial Markets. • Learn about the Different Types of Financial Instruments. • Understand the Meaning and functions of Stock Exchange. • Know about BSE and NSE • Understand the different terms related to stock exchange. • Understand the role of SEBI in Capital Market.

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1 INTRODUCTION TO CORPORATE FINANCE

1.1 Meaning

1.2 Importance

1.3 Capital Requirements

(A) Fixed Capital and (B) Working Capital

1.4 Capital Structure

1.4.1 Definition

1.4.2 Components

1.5 Distinction

INTRODUCTION :

The term finance is related to money and money management. It is related to inflow and outflow of money. Success of any business organisation depends upon the efficiency with which it is able to generate and use funds.

Henry Ford rightly said, " Money is an arm or leg - use it or lose it." This statement clearly brings out the significance of finance for the success of a business.

1.1 CORPORATE FINANCE : MEANING

Corporate finance deals with the raising and using of finance by a corporation. It deals with financing the activities of the corporation, capital structuring and making investment decisions.

MEANING : DEFINITION

Henry Hoagland expresses the view that "corporate finance deals primarily with the acquisition and use of capital by business corporation."

The term corporate finance also includes financial planning, study of capital market, money market and share market. It also covers capital formation and foreign capital. Even financial organisations and banks play vital role in corporate financing.

The finance manager of any corporation has to ensure that -

a) the firm has adequate finance.

b) they are using the right source of funds that have minimum cost.

c) the firm utilises raised funds effectively.

d) they are generating maximum returns for it's owners.

The following two decisions are the basis of corporate finance.

1) **Financing Decision :** The business firm has access to capital market to fulfill it's financial needs. The firm has multiple choices of sources of financing. The firm can choose whether it wants to raise equity capital or debt capital. Firm can even opt for bank loan, public deposits, debentures etc. to raise funds. The finance manager ensures that the firm is well capitalised i.e. they have right amount of capital and that the firm has right combination of debt and equity.

Capital market is a market for long term debt instruments and equity shares. In this market, equity and debt instruments are issued and traded.

2) **Investment Decision :** Once the business firm has gained access to capital, the finance manager has to take decision regarding the use of the funds in systematic manner so that it will bring maximum return for its owners. For this, the firm has to take into consideration the cost of capital. Once they know the cost of capital, firm can deploy or use the funds in such a way that returns are more than cost of capital.

Cost of capital is minimum return expected by it's investors.

Finding investments and deploying them successfully in the business is known as investing decision. It is also called as 'capital budgeting'.

1.2 IMPORTANCE OF CORPORATE FINANCE :

In the functional management of business enterprise, importance is given to production, finance, marketing and personnel activities. Among all these activities, utmost importance is given to financial activities. The importance of corporate finance may be discussed as follows -

1. **Helps in decision making :** Most of the important decisions of business enterprise are determined on the basis of availability of funds. It is difficult to perform any function of business enterprise independently without finance.

   Every decision in the business is needed to be taken keeping in view of it's impact on profitability. There may be number of alternatives but the management is required to select the best one which will enhance profitability. Business organisation can give green signal to the project only when it is financially viable. Thus corporate finance plays significant role in decision making process.

2. **Helps in Raising Capital for a project :** Whenever a business firm wants to start a new venture, it needs to raise capital. Business firm can raise funds by issuing shares, debentures, bonds or even by taking loans from the banks.

3. **Helps in Research and Development :** Research and Development must be undertaken for the growth and expansion of business. Detailed technical work is essential for the execution of projects. Research and Development is lengthy process and therefore funds have to be made available through out the research work. This would require continuous financial support.

   Many a times, Company has to upgrade its old product or develop new product to attract the consumers. For this company has to conduct survey, market analysis, etc. which again requires financial support.

4. **Helps in smooth running of business firm :** A smooth flow of corporate finance is needed so that salaries of employees are paid on time, loans are cleared on time, raw material is purchased whenever required, sales promotion of existing products is carried out smoothly and new products can be launched effectively.

5. **Brings co-ordination between various activities :** Corporate finance plays significant role in control and co-ordination of all activities in an organisation. For e.g. Production will suffer, if finance department does not provide adequate finance for the purchase of raw materials and meeting other day-to-day financial requirements for smooth running of production unit. Due to this, sales will also suffer and consequently the income of concern as well as rate of profit will be affected. Thus efficiency of every department depends upon the effective financial management.

6. **Promotes expansion and diversification :** Modern machines and modern techniques are required for expansion and diversification. Corporate finance provides money to purchase modern machines and technologies. Therefore finance becomes mandatory for expansion and diversification of a company.

7. **Managing Risk :** Company has to manage several risks, such as sudden fall in sales, loss due to natural calamity, loss due to strikes, etc. Company needs financial aid to manage such risks.

8. **Replace old assets :** Assets such as plant and machinery become old and outdated over the years. They have to be replaced by new assets. Finance is required to purchase new assets.

9. **Payment of dividend and interest :** Finance is needed to pay dividend to shareholders, interest to creditors, banks, etc.

10. **Payment of taxes/fees :** Company has to pay taxes to Government such as Income Tax, Goods and Service Tax (GST) and fees to Registrar of Companies on various occasions. Finance is needed for paying these taxes and fees.

1.3 CAPITAL REQUIREMENTS :

When a business entrepreneur conceives an idea of setting up a business enterprise, the commercial viability of the idea is investigated. Once the entrepreneur is satisfied with the feasibility of the project, serious steps are taken to start the project. The first and foremost step is to take decision on the amount of capital requirement to start and run the business. This task has to be performed with utmost care. Therefore financial plan should be drafted keeping in mind present and future requirements of the business. Thus while deciding about the volume of capital requirement, an entrepreneur has to take into consideration - fixed capital requirement and working capital requirement. We shall now discuss these capital requirements in detail.

Financial plan refers to assessment of financial requirement and arranging sources of capital.

(A) Fixed Capital : Fixed capital is the capital which is used for buying fixed assets which are used for a longer period of time in the business. These assets are not meant for resale.

In simple words fixed capital refers to capital invested for acquiring fixed assets. It stays in the business for long period almost permanently. Examples of fixed capital are - capital used for purchasing land and building, furniture, plant and machinery etc. Such capital is required usually at the time of establishment of a new company. However, existing companies may also need such capital for their expansion and development, replacement of equipments, etc.

Initial planning of fixed capital requirement is made by company's promoters. For this, they first prepare a list of fixed assets needed by the company and cost of these assets is estimated. They collect information regarding price of land, cost of construction of building, cost of plant and machinery, etc. The cost of different fixed assets is calculated and the resulting figure would be the total of fixed capital requirement of a new firm.

In recent years, estimating fixed capital requirement has assumed great importance particularly because of modern industrial processes which require increased use of heavy and automated machineries.

An entrepreneur obtains funds for the purchase of fixed assets from capital market. Funding can come from issue of shares, debentures, bonds or obtaining even long term loans.

Factors affecting fixed capital requirement :

1. **Nature of business :** Manufacturing industries and public utilities have to invest huge amount of funds to acquire fixed assets. While Trading business may not need huge investments in fixed assets.
2. **Size of business :** Where a business firm is set up to carry on large scale operations, its fixed capital requirements are likely to be high. It is because most of their production processes are based on automatic machines and equipments.
3. **Scope of business :** There are business firms which are formed to carry on production or distribution on a large scale. Such businesses would require more amount of fixed capital.
4. **Extent of lease or rent :** If entrepreneur decides to acquire assets on lease or on rental basis, less amount of funds for fixed assets will be needed for the business.

> ***Lease :*** *A contract by which one person grants possession of some of his property especially land, building or machinery to another for a certain period of time.*

5. **Arrangement of sub-contract :** If the business wants to sub-contract some processes of production to others, limited assets are required to carry out the production. It would minimise fixed capital requirement of business.
6. **Acquisition of old assets :** If old equipments and plants are available at low prices, then it would reduce the need for investment in fixed assets.
7. **Acquisition of assets on concessional rate :** With the view to foster industrial growth at regional level, the government may provide land and building, materials at concessional rates. Plants and equipments may also be made available on instalment basis. Such facilities will reduce the requirement of fixed assets.
8. **International conditions :** This factor is very significant particularly in large organisations carrying business on international level. For example : companies expecting war, may decide to invest large funds to expand fixed assets before there is shortage of materials.

9. **Trend in economy :** If the future of the company is anticipated to be bright, it gives green signal to business entrepreneur to carry out all sorts of expansion of business firm. In that case, large amount of funds are invested in fixed assets so as to reap the benefits in future.

10. **Population trend :** When the population is increasing at high rate, certain manufactures find this as an opportunity to expand business. For example- automobile industry, electronic goods manufacturing industry, ready-made garments, etc. which necessitates huge amount of fixed capital.

11. **Consumer preference :** Industries providing goods and services which are in good demand, will require large amount of fixed capital. For example - Mobile phone manufactures as well as mobile network providers.

12. **Competitive factor :** This factor is prime element in decision making regarding fixed capital requirements. If one of the competitor's shifts to automation, the other companies in the same line of activity, will be compelled to follow that competitor.

(B) Working Capital

Working capital is the capital which is used to carry out the day to day business activities. After estimating fixed capital requirement of the business firm, it is necessary to estimate the amount of capital, that would be needed to ensure smooth functioning of the business firm. A business firm requires funds to store adequate raw material in stock. A firm would need capital to maintain sufficient stock of finished goods. In actual practice, goods are sold out in cash or on credit. Goods sold on credit do not fetch cash immediately. Firm will have to arrange for funds till the amount is collected from the debtors. Cash is also required to pay overheads. Since uncertainty is always a feature of business, some excess cash also should be maintained to meet unexpected expenses.

> ***Overheads :*** *Overhead means indirect cost or expenses required to run a business. Overhead expenses include accounting fees, advertising, insurance, interest, legal fees, rent, repairs, taxes, telephone bills, travel expenditure, etc.*

Thus, a business firm will have to arrange capital for the following :

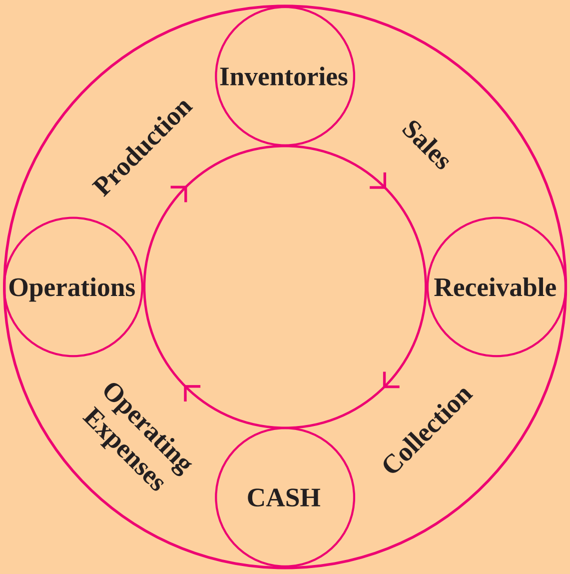
a) For building up inventories

b) For financing receivables and payables

c) For covering day-to-day operating expenses.

The capital invested in these assets is referred to as 'Working capital'. The concept of working capital is viewed differently by leading authorities. Some authorities consider working capital as equivalent to excess of current assets over current liabilities. Gerstenbergh, defines it as, "The excess of current assets over current liabilities." This approach refers to 'Net Working Capital'. Gerstenbergh does not call it as working capital. He prefer to call it as 'circulating capital'. Other authorities viewed working capital equivalent to current assets. According to J. S. Mill, "The sum of current assets is working capital." This approach has broader application. It takes into consideration all current assets, of the company. It refers to 'Gross Working Capital'.

Additional information :



Cycle flow of Working Capital

Cyclical flow of working capital :

A business firm needs fund to finance it's working capital needs. Prominent share of this fund is used to buy raw materials and remaining part is kept available to pay wages and expenditures. Thus the working capital which was in the form of cash is converted into inventories. Raw materials are converted into work-in-process and then to finished goods. With the sale of finished goods they turn into account receivables, presuming the goods are sold on credit basis. Normally account receivables have maturities of specific days after billing date. Collection of the receivable brings back the cycle to cash.

A part of cash may be used to pay creditors, pay income tax and declare dividend and rest of it is put into circulation again.

Factors affecting working capital requirement :

There is no precise standards to measure working capital adequacy. Management has to determine the size of working capital in the light of certain aspects of business firm and economic environment within which the firm operates.

1. Nature of business :

Firms engaged in manufacturing essential products of daily consumption would need relatively less working capital as there would be constant and sufficient cash inflow in the firm to take care of liabilities. Likewise public utility concerns have to maintain small working capital because of continuous flow of cash from their customers.

> ***Public utility concern :*** *These concerns provide services such as transport, gas, electricity, etc.*

On the contrary, if the business is dealing in luxurious products, it requires huge amount of working capital, as sale of luxurious items are not frequent.

Trading/merchandising firms which are concerned with distribution of goods have to carry big inventories of goods to meet customer's demand and have to extend credit facilities to attract customers. Hence they need large amount of working capital.

> *Merchandising firms are those which are concerned with buying and selling of goods, either as wholesaler or retailer, without altering the physical form of goods.*

2. Size of business :

The size of business also affects the requirement of working capital. A firm with large scale operations will require more working capital.

3. Volume of sales :

This is the most important factor affecting size of working capital. The volume of sales and size of working capital are directly related with each other. If volume of sales increases, there is an increase in the amount of working capital and vice a versa.

4. Production cycle :

The process of converting raw material into finished goods is called production cycle. If the period of production cycle is longer, then firm needs more amount of working capital. If manufacturing cycle is short, it requires less working capital.

5. Business cycle :

When there is a boom in the economy, sales will increase. This will lead to increase in investment in stocks. This requires additional working capital.

During recession, sales will decline and hence the need of working capital will also decline.

6. Terms of purchases and sales :

If the firm does not get credit facility for purchases but adopts liberal credit policy for its sales, then it requires more working capital.

On the other hand if credit terms of purchases are favourable and terms of credits sales are less liberal, then requirement of cash will be less. Thus working capital requirement will be reduced.

7. Credit control :

Credit control includes the factors such as volume of credit sales, the terms of credit sales, the collection policy, etc. If credit control policy is sound, it is possible for the company to improve it's cash flow. If credit policy is liberal, it creates a problem of collection of funds. It can increase possibility of bad debts. Therefore a firm requires more working capital.

The firm making cash sales requires less working capital.

8. Growth and Expansion :

The working capital requirement of a firm will increase with growth of a firm. A growing company needs funds continuously to support large scale operations.

9. Management ability :

The requirement of working capital is reduced if there is proper co-ordination between production and distribution of goods. A firm stocking on heavy inventory calls for higher level for working capital.

10. External factors :

If financial institutions and banks provide funds to the firm as and when required, the need for working capital is reduced.

1.4 CAPITAL STRUCTURE :

A company can raise it's capital from different sources. i.e. owned capital or borrowed capital or both. The owned capital consists of equity share capital, preference share capital, reserves and surplus. On the other hand, borrowed sources are debentures, loans, etc. A combination of different sources are used in capital structure. It is nothing but 'security mix.'

Capital structure means 'mix up of various sources of funds in desired proportion'. To decide capital structure means, to decide upon the ratio of different types of capital.

1.4.1 Definition

R. H. Wessel : " The long term sources of funds employed in a business enterprise".

John Hampton : "A firm's capital structure is the relation between the debt and equity securities that makes up the firm's financing of it's assets".

Thus capital structure is composed of owned funds and borrowed funds. Owned funds includes share capital, free reserves and surplus, whereas, borrowed funds represent debentures, Bank loans and long term loans provided by financial institutions.

Additional information :

Principles of Capital Structure : Two basic principles are observed while taking decision about capital structure.

(1) The ratio of 'debt to equity' should always be geared to the degree of stability of earning.

(2) The capital structure must be balanced with adequate 'equity cushion' to absorb the shocks of the business cycle and to afford flexibility.

1.4.2 Components of Capital Structure :

There are four basic components of capital structure. They are as follows :

(1) Equity share capital : It is the basic source of financing activities of business. Equity shares are shares which get dividend and repayment of capital after it is paid to preference shares. They own the company. They bear ultimate risk associated with ownership. They carry dividend at fluctuating rate depending upon the profits.

(2) Preference share capital : Preference shares carry preferential right as to payment of dividend and have priority over equity shares for return of capital when the company is liquidated. These shares carry dividend at fixed rate.

(3) Retained earnings : It is internal source of financing. It is nothing but ploughing back of profit.

(4) Borrowed capital : It comprises the following :

a) Debenture :

It is acknowledgement of loans raised by company. Company has to pay interest at an agreed rate.

b) Term loan :

Term loans are provided by bank and other financial institutions. They carry fixed rate of interest.

To understand the above concept, we shall consider following Balance sheet and calculate the values :

Balance sheet of ABC Company Ltd. as on 31st March, 2019

Liabilities	Amount ₹	Assets	Amount ₹
Share Capital		**Fixed Assets**	
10,000 equity shares of ₹10 each fully paid	1,00,000	Building	4,00,000
		Plant and Machinery	2,00,000
5,000 preference shares of ₹100 each fully paid.	5,00,000	**Current Assets**	
		Sundry Debtors	1,00,000
Reserves and Surplus	50,000	Inventories	50,000
Liabilities		Cash in hand	10,000
1000, 10% Debentures of ₹ 100 each fully paid	1,00,000	Cash at bank	40,000
Sundry creditors	30,000		
Bills payable	20,000		
	8,00,000		**8,00,000**

Capital Structure = Equity Share Capital + Pref. Share Capital + Reserves + Debentures

= 1,00,000 + 5,00,000 + 50,000 + 1,00,000

= 7,50,000

Activity : Visit website of any public limited company and find out details of its capital structure.

1.5 Distinction :

Points	Fixed capital	Working capital
1) Meaning	Fixed capital refers to any kind of physical asset i.e. fixed assets.	Working capital refers to the sum of current assets.
2) Nature	It stays in the business almost permanently.	Working capital is circulating capital. It keeps changing.
3) Purpose	It is invested in fixed assets such as land, building, equipments, etc.	Working capital is invested in short term assets such as cash, account receivable, inventory, etc.
4) Sources	Fixed capital funding can come from selling shares, debentures, bonds, long term loans, etc.	Working capital can be funded with short term loans, deposits, trade credit, etc.
5) Objectives of Investors	Investors invest money in fixed capital hoping to make future profit.	Investors invest money in working capital for getting immediate returns.
6) Risk	Investment in fixed capital implies more risk.	Investment in working capital is less risky.

SUMMARY

- Corporate finance deals with the acquisition and use of capital by business corporation.
- Fixed capital is that portion of capital which is invested in fixed assets such as land, building, equipments, etc.
- Working capital refers to a firm's investment in current assets such as cash, account receivable and inventories.
- Capital structure refers to the proportion of different sources of funds raised by a firm for long term finance.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. .... is related to money and money management.

   a) Production   b) Marketing   c) Finance

2. Finance is the management of .... affairs of the company.

   a) monetary   b) marketing   c) production

3. Corporate finance deals with the acquisition and use of .... by business corporation.

   a) goods   b) capital   c) land

4. Company has to pay .... to government.

   a) taxes   b) dividend   c) interest

5. .... refers to any kind of fixed assets.

   a) Authorised capital   b) Issued capital   c) Fixed capital

6. .... refers to the excess of current assets over current liabilities.

   a) Working capital   b) Paid-up capital   c) Subscribed capital

7. Manufacturing industries have to invest .... amount of funds to acquire fixed assets.

   a) huge   b) less   c) minimal

8. When the population is increasing at high rate, certain manufacturers find this as an opportunity to .... business.

   a) close   b) expand   c) contract

9. The sum of all .... is gross working capital.

   a) expenses   b) current assets   c) current liabilities

10. .... means mix up of various sources of funds in desired proportion.

    a) Capital budgeting   b) Capital structure   c) Capital goods

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Capital budgeting	1)	Sum of current assets
b)	Fixed capital	2)	Deals with acquisition and use of capital
c)	Working capital	3)	Fixed liabilities
d)	Capital structure	4)	Sum of current liabilities
e)	Corporate finance	5)	Fixed assets
		6)	Investment decision
		7)	Financing decision
		8)	Deals with acquisition and use of assets
		9)	Mix up of various sources of funds
		10)	Product mix

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. A key determinant of success of any business function.
2. The decision of finance manager which ensures that firm is well capitalised.
3. The decision of finance manager to deploy the funds in systematic manner.
4. Capital needed to acquire fixed assets which are used for longer period of time.
5. The sum of current assets.
6. The excess of current assets over current liabilities.
7. The process of converting raw material into finished goods.
8. The boom and recession cycle in the economy.
9. The ratio of different sources of funds in the total capital.
10. The internal source of financing.

D) State whether the following statements are true or false.

1. Finance is related to money and money management.
2. Business firm gives green signal to the project only when it is profitable.
3. Corporate finance brings co-ordination between various business activities.
4. Fixed capital is also referred as circulating capital.
5. Working capital stays in the business almost permanently.
6. The business will require huge funds, if assets are acquired on lease basis.
7. The business dealing in luxurious products will require huge amount of working capital.

8. A firm with large scale operations, will require more working capital.
9. Liberal credit policy creates a problem of bad debts.
10. Financial institutions and banks cater to the working capital requirement of business.

E) Find the odd one.

1. Land and Building, Plant and Machinery, Cash.
2. Debenture Capital, Equity Share Capital, Preference Share Capital.
3. Fixed Capital, Capital Structure, Working Capital.

F) Complete the sentences.

1. Planning of capital requirement is made by ....
2. When there is boom in economy, sales will ....
3. The process of converting raw material into finished goods is called ....
4. During recession period, sales will ....

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Financing decision	1)	....
b)	....	2)	Longer period of time.
c)	Investment decision	3)	....
d)	....	4)	Circulating capital
e)	Combination of various sources of funds	5)	....

(To have right amount of capital, Deploy funds in systematic manner, Fixed capital, Working capital, Capital structure)

H) Answer in one sentence.

1. Define corporate finance.
2. What is fixed capital ?
3. Define working capital.
4. What is production cycle ?
5. Define capital structure.

I) Correct the underlined word/s and rewrite the following sentences.

1. Finance is needed to pay <u>dividend</u> to debentureholders.
2. When there is <u>recession</u> in economy sales will increase.
3. <u>Share</u> is an acknowledgement of loan raised by company.
4. <u>Equity</u> shares carry dividend at fixed rate.

Q.2 Explain the following terms / concepts.

1. Financing decision
2. Investment decision
3. Fixed capital
4. Working capital

Q.3 Study the following case / situation and express your opinion.

(1) The management of 'Maharashtra State Road Transport Corporation', wants to determine the size of working capital.

a. Being a public utility service provider, will it need less working capital or more ?

b. Being a public utility service provider, will it need more Fixed Capital ?

c. Give one example of public utility service that you come across on day-to-day basis.

(2) A company is planning to enhance it's production capacity and is evaluating the possibility of purchasing new machinery whose cost is ₹ 2 crores or has alternative of machinery available on lease basis.

a. What type of asset is machinery ?

b. Capital used for purchase of machinery is fixed capital or working capital ?

c. Does the size of a business determine the fixed capital requirement ?

Q.4 Distinguish between the following.

1. Fixed Capital and Working Capital.

Q.5 Answer in brief.

1. Define capital structure and state it's components.
2. State any four factors affecting fixed capital requirement.
3. What is corporate finance and state two decisions which are basis of corporate finance.

Q.6 Justify the following statements.

1. The firm has multiple choices of sources of financing.
2. There are various factors affecting the requirement of fixed capital.
3. Fixed capital stays in the business almost permanently.
4. Capital structure is composed of owned funds and borrowed funds.
5. There are various factors affecting the requirement of working capital.

Q.7 Answer the following questions.

1. Discuss the importance of corporate finance.
2. Discuss the factors determining working capital requirement.

2 SOURCES OF CORPORATE FINANCE

2.1 Sources of Owned Capital

2.1.1 Shares

2.1.2 Retained earnings

2.2 Sources of Borrowed Capital

2.2.1 Debentures

2.2.2 Acceptance of deposits

2.2.3 Bonds

2.2.4 ADR / GDR

2.2.5 Commercial Banks

2.2.6 Financial Institutions

2.2.7 Trade Credit

2.3 Distinction

INTRODUCTION :

Finance holds the key to all business activities. No business activity can ever be pursued without financial support. Finance is necessary through out the activities of promotion, organisation and regular operations of business. All functions of business are ultimately dependent on finance.

The Finance needed by business organisation is termed as 'Capital'. Every business organisation needs certain capital for its activities. A joint stock company, which is a modern form of business organisation and being a large undertaking, requires huge capital for business. This huge capital collection or capital formation has special significance in the management of joint stock company.

Capital formation is a process of collection of capital from various sources according to financial plan of company.

A joint stock company collects huge funds through different sources. These various sources of finance available to business may be explained with the following chart :

Sources of Finance based on Types of Capital

- Owned Capital
  - Shares
    - Equity Shares
    - Preference Shares
  - Retained Earning
- Borrowed Capital
  - Debentures, Public Deposits, Bonds, ADR / GDR, Banks, Financial Institutions, Trade Credit

The above sources of finance may be external or internal.

External Source : When capital is raised from outsiders.

Internal Source : When capital is made available from within the organisation.

2.1 SOURCES OF OWNED CAPITAL

The capital raised by company with the help of owners (shareholders) is called owned capital or ownership capital. The shareholders purchase shares of the company and supply necessary capital. It is one form of owned capital.

Another form of owned capital is retained earnings. It is also known as ploughing back of profit. It is reinvestment of profit in the business by the company itself. Retained earning is an internal source of finance.

Owned capital is regarded as a permanent capital, as it is returned only at the time of winding up of the company.

Owned capital in the form of share capital, provides initial source of capital for a new company. It can be raised any time later to satisfy additional capital needs of a company. However, retained earnings cannot be an initial source of capital but it can be important source of capital when company runs it's business profitably during it's existence.

Promoters decide the share capital required by a company. This amount of share capital is known as authorised capital. It is stated in the Capital clause of Memorandum of Association of the company. Let us learn in detail the various sources of owned capital.

2.1.1 Shares

The term share is defined by Section 2 (84) of the Companies Act 2013, 'Share means a share in the share capital of a company and includes stock'.

Share is a unit by which the share capital is divided. The total capital of company is divided into small parts and each part is called share and the value of each part / unit is known as face value. Share is a small unit of capital of a company. It facilitates the public to subscribe to the capital in smaller amount.

A person can purchase any number of shares as he wishes. A person who purchases shares of a company is known as a shareholder or a member of that company.

- **Features of Shares :**

1. **Meaning :** Share is a smallest unit in the total share capital of a company.
2. **Ownership :** The owner of share is called as shareholder. It shows the ownership of a shareholder in the company.
3. **Distinctive Number :** Unless dematerialised, each share has distinct number for identification. It is mentioned in the Share Certificate.
4. **Evidence of title :** A share certificate is issued by a company under it's common seal. It is a document of title of ownership of shares. A share is not any visible thing. It is shown by share certificate or in the form of Demat share.
5. **Value of a Share :** Each share has a value expressed in terms of money. There may be:
   - **(a) Face value :** This value is written on the share certificate and mentioned in the Memorandum of Association.
   - **(b) Issue price :** It is the price at which company sells it's shares.

(c) **Market Value :** This value of share is determined by demand and supply forces in the share market.

6. **Rights :** A share confers certain rights on its holder such as right to receive dividend, right to inspect statutory books, right to attend shareholders' meetings and right to vote at such meetings, etc.

7. **Income :** A shareholder is entitled to get a share in the net profit of the company. It is called dividend.

8. **Transferability :** The shares of public limited company are freely transferable in the manner provided in the Articles of Association.

9. **Property of Shareholder :** Share is a movable property of a shareholder.

10. **Kinds of Shares :** A company can issue two kinds of shares :

    (a) Equity shares. (b) Preference shares.

- **Kinds of Shares** (As per Section 43 of the Companies Act 2013)

A company can issue different types of shares depending upon right to control, income and risk. The following chart shows different kinds of shares.

Shares

(A) Equity Shares

1) Equity Shares with voting right.
2) Equity Shares with differential voting right.

(B) Preference Shares

1) Cumulative Preference Shares.
2) Non-Cumulative Preference Shares.
3) Participating Preference Shares.
4) Non-participating Preference Shares.
5) Convertible Preference Shares.
6) Non-Convertible Preference Shares.
7) Redeemable Preference Shares.
8) Irredeemable Preference Shares.

A. **Equity Shares :** Equity shares are also known as ordinary shares.

Companies Act defines equity shares as 'those shares which are not preference shares'.

The above definition reveals that :

a) The equity shares do not enjoy preference for dividend.

b) The equity shares do not have priority for repayment of capital at the time of winding up of the company.

Equity shares are fundamental source of financing business activities. Equity share holders own the company and bear ultimate risk associated with the ownership.

After paying claims of all other investors the remaining funds belong to equity shareholders. Thus equity shareholders are 'residual claimants' of the income and assets.

Equity shareholders do not carry any fixed commitment of dividend. They are paid dividend at the rate recommended by Board of Directors. If there is no profit, no dividend will be payable. Similarly if there is less profit, lesser dividend will be paid. Thus the fortune of equity shareholders is tied up with the ups and downs of the company. If the company is successful, they enjoy great financial rewards and if the company fails, the risk falls mainly on them. It is exactly because of this position equity share capital is known as 'venture capital' or 'risk capital'. The owners of equity shares are real risk bearers.

However, equity shareholders participate in the management of their company. They are invited to attend general meetings. They are allowed to vote on all matters discussed at the general meeting. They elect their representatives to manage the company. Equity shareholders are thus real owners of the company.

■ Features of Equity Shares :

1. **Permanent Capital :** Equity shares are irredeemable shares. The amount received from equity shares is not refundable by the company during its life time. Equity shares become refundable only in the event of winding up of the company or company decides to buyback shares. Thus equity share capital is long term and permanent capital of the company.

2. **Fluctuating Dividend :** Equity shares do not have a fixed rate of dividend. The rate of dividend depends upon amount of profit earned by company. If company earns more profit, dividend is paid at higher rate. On the other hand if there is insufficient profit or loss, Board of Directors may postpone the payment of dividend. Equity shareholders cannot compel them to declare and pay dividend. The income of equity shares is uncertain and irregular. The equity shares get dividend at fluctuating rate.

3. **Rights :** Equity Shareholders enjoy certain rights :

   a) **Right to vote :** It is the basic right of equity shareholders through which they elect directors, alter Memorandum and Articles of Association, etc.

   b) **Right to share in profit :** It is an important right of equity shareholders. They have right to share in profit, when distributed as dividend. If the company is successful and makes handsome profit, they have advantage of getting large dividend.

   c) **Right to inspect books :** Equity shareholders have right to inspect statutory books of their company.

   d) **Right to transfer shares :** The equity shareholders enjoy the right to transfer shares as per the procedure laid down in the Articles of Association.

4. **No preferential right :** Equity shareholders do not enjoy preferential right in respect of payment of dividend. They are paid dividend only after dividend on preference shares has been paid.

Similarly, at the time of winding up of the company, the equity shareholders are paid last. Further, if no surplus amount is available, equity shareholders will not get anything.

5. **Controlling power :** The control of company is vested with the equity shareholders. They are often described as 'real masters' of the company. It is because they enjoy exclusive voting rights. The Act provides the right to cast vote in proportion to share holding. They can exercise their voting right by proxies, without even attending meeting in person.

   By exercising voting right they can participate in the management and affairs of the company. They elect their representatives called Directors for management of the company. They are allowed to vote on all matters discussed at the general meeting. Thus equity shareholders enjoy control over the company.

6. **Risk :** Equity shareholders bear maximum risk in the company. They are described as 'shock absorbers' when company has financial crisis.

   If the income of company falls, the rate of dividend also comes down. Due to this, market value of equity shares comes down resulting into capital loss. Thus equity shareholders are main risk takers.

7. **Residual claimant :** Equity shareholders as owners are residual claimants to all earnings after expenses, taxes, etc. are paid. A residual claim means the last claim on the earnings of company.

   Although equity shareholders come last, they have advantage of receiving entire earnings that is left over.

8. **No charge on assets :** The equity shares do not create any charge over assets of the company.

   Charge on assets : *Means an interest or lien created on assets of the company in favour of creditors. In case company fails to pay the debt, creditors can claim it from the company's assets.*

9. **Bonus Issue :** Bonus shares are issued as gift to equity shareholders. These shares are issued free of cost to existing equity shareholders. These are issued out of accumulated profits. Bonus shares are issued in proportion to the shares held. Thus capital investment of (ordinary) equity shareholder tends to grow on its own. This benefit is available only to the equity shareholder.

10. **Right Issue :** When a company needs more funds for expansion purpose and raises further capital by issue of shares, the existing equity shareholders may be given priority to get newly offered shares. This is called 'Right Issue'. The shares are offered to equity shareholder first, in proportion to their existing shareholding.

11. **Face Value :** The face value of equity shares is low. It can be generally ₹ 10 per share or even ₹ 1 per share.

12. **Market Value :** Market value of equity shares fluctuates according to the demand and supply of these shares. The demand and supply of equity shares depend on profits earned and dividend declared. When a company earns huge profit, market value of its shares increases. On the other hand when it incurs loss, the market value of it's shares decreases. There are frequent fluctuations in the market value of equity shares

in comparison to other securities. Therefore equity shares are more appealing to the speculator.

Speculator tries to make profit from a security's price change.

13. **Capital Appreciation :** Share Capital appreciation takes place when market value of shares increases in the share market. Profitability and prosperity of the company enhances reputation of company in the share market and it facilitates appreciation of market value of equity shares.

■ Types of Equity Shares :

The equity share can be of two types :

a) with voting rights.

b) with differential voting right.

a) Equity shares with normal voting right : Voting right of such equity holders is in proportion to his share holdings.

b) Equity shares with differential voting right : Such equity holders shall have varying rights regarding dividend, voting or otherwise in accordance with Rule 4 of Companies (Share Capital and Debentures) Rules 2014.

Thus company can issue shares with limited voting rights or no voting rights. They may be entitled to extra rate of dividend, if any.

B. Preference Shares :

As the name indicates, these shares have certain preferential rights distinct from those attached to equity shares.

The shares which carry following preferential rights are termed as preference shares:

a) A preferential right as to payment of dividend during the life time of company.

b) A preferential right as to the return of capital in the event of winding up of company.

The holder of preference share have a prior right to receive fixed rate of dividend before any dividend is paid to equity shares. The rate of dividend is prescribed at the time of issue.

Normally preference shares do not carry any voting power. They have voting right only on matters which affect their interest, such as selling of undertaking or changing rights of preference shares, etc. or they get voting rights if dividend remains unpaid.

The preference shareholders are co-owners of the company but not controllers. These shares are purchased by cautious investors who are interested in safety of investment and who want steady returns on investments.

■ Features of Preference Shares :

1. **Preference for dividend :** Preference shares have the first charge on the distributable amount of annual net profit. The dividend is payable to preference shareholders before it is paid to equity shareholders.

2. **Preference for repayment of capital :** Preference shareholders have a preference over equity shareholders in respect of return of capital when the company is liquidated. It saves preference shareholders from capital losses.

3. **Fixed Return :** These shares carry dividend at fixed rate. The rate of dividend is pre-determined at the time of issue. It may be in the form of fixed sum or may be calculated at fixed rate.

   The preference shareholders are entitled to dividend which can be paid only out of profits. If the directors, in financial crisis, decide not to pay dividend, the preference shareholders have no claim for dividend.

4. **Nature of Capital :** Preference shares do not provide permanent share capital. They are redeemed after certain period of time. A company can not issue irredeemable preference shares.

   Preference capital is generally raised at a later stage, when the company gets established. These shares are issued to satisfy the need for additional capital of the company.

   Preference share capital is safe capital as the rate of dividend and market value does not fluctuate.

5. **Market Value :** The market value of preference share does not change as the rate of dividend payable to them is fixed. The capital appreciation is considered to be low as compared with equity shares.

6. **Voting rights :** The preference shares do not have normal voting rights. They do not enjoy right of control on the affairs of the company. They have voting rights on any resolution of the company directly affecting their rights e.g. : Change in terms of repayment of capital, dividend payable to them are in arrears for last two consecutive years, etc.

7. **Risk :** The investors who are cautious, generally purchase preference shares. Safety of capital and steady return on investment are advantages attached with preference shares. These shares are boon for shareholders during depression period when interest rate is continuously falling.

8. **Face Value :** Face value of preference shares is relatively higher than equity shares. They are normally issued at a face value of Rs. 100/-.

9. **Rights or Bonus Issue :** Preference shareholders are not entitled for Rights or Bonus issues.

10. **Nature of Investor :** Preference shares attract moderate type of investors. Investors who are conservative, cautious, interested in safety of capital and who want steady return on investment generally purchase preference shares.

■ Types of Preference Shares.

Types of Preference Shares

Cumulative and Non-cumulative Preference Shares	Participating and Non-participating Preference Shares	Convertible and Non-convertible Preference Shares	Redeemable and Irredeemable Preference Shares

1. **Cumulative Preference Shares :** Cumulative Preference Shares are those shares on which dividend goes on accumulating until it is fully paid. This means, if the dividend is not paid in one or more years due to inadequate profits, then this unpaid dividend gets accumulated. This accumulated dividend is paid when company performs well. The arrears of dividend are paid before making payment to equity shareholders.

   The preference shares are always cumulative unless otherwise stated in the Articles of Association. It means that if dividend is not paid any year, the unpaid amount is carried forward to the next year and so on, until all arrears have been paid.

2. **Non-cumulative Preference Shares :** Dividend on these shares does not get accumulated. This means, the dividend on shares can be paid only out of profits of that year. The right to claim dividend will lapse, if company does not make profit in that particular year. If dividend is not paid in any year, it is lost forever.

3. **Participating Preference Shares :** The holders of these shares are entitled to participate in surplus profit besides preferential dividend. The surplus profit which remains after the dividend has been paid to equity shareholders, up to certain limit, is distributed to preference shareholders.

4. **Non-participating Preference Shares :** The preference shares are deemed to be non-participating, if there is no clear provision in the Articles of Association. These shareholders are entitled to fixed rate of divided, prescribed at the time of issue.

5. **Convertible Preference Shares :** The holders of these shares have a right to convert their preference shares into equity shares. The conversion takes place within a certain fixed period.

6. **Non-convertible Preference Shares :** These shares cannot be converted into equity shares.

7. **Redeemable Preference Shares :** Shares which can be redeemed after certain fixed period of time are called redeemable preference shares. A company limited by shares, if authorised by Articles of Association, issues redeemable preference shares. Such shares must be fully paid. These shares are redeemed out of divisible profit only or out of fresh issue of shares made for this purpose.

8. **Irredeemable Preference Shares :** Shares which are not redeemable i.e. payable only on winding up of the company are called irredeemable preference shares. As per Section 55(1) of the Companies Act 2013, a company cannot issue irredeemable preference shares.

2.1.2 Retained Earnings :

Business organisations are subject to variation in earnings. It would be a wise decision to keep aside a part of earning during a period of high profit. A prudent company does not distribute the entire profit earned among shareholders. A part of profit is retained by company in the form of reserve fund. These reserves are the retained earnings of the company. The sum total of retained earnings gets accumulated over the years. This accumulated profits are reinvested in the business rather than distributed as dividend.

"The process of accumulating corporate profits and their utilisation in business is called retained earnings."

In simple words, a part of net profit, which is not distributed to shareholders as dividend is retained by company in the form of 'Reserve Fund'. Company converts it's reserves into 'bonus share capital' and capitalises it's profit. This capitalisation of profit by issue of bonus shares is known as ploughing back of profit or self financing. Bonus shares are issued free of cost to the existing equity shareholders out of the retained earnings.

The Management can convert retained earnings into permanent share capital by issuing bonus shares. It is an important source of raising long term capital. It is simple and cheapest method of raising finance. It is used by established companies. It is an internal source of finance.

Determinants of retained earnings. :

1. **Total earnings of company :** If there is ample profit, company can save and retain some parts of profit. More the earnings, a company can save more. Attitude of top management also determines the amount of retained earnings.
2. **Taxation Policy :** The taxation policy of government is also an important determinant of corporate savings. If the taxes levied are at high rates, company cannot save much of the profits in the form of reserves.
3. **Dividend Policy :** It is a policy of Board of Directors in regards to distribution of profits. A conservative dividend policy is needed for having good accumulation of profit. But this policy affects shareholders as they get dividend at a lower rate.
4. **Government Control :** A government is regulatory body of economic system of the country. It's policies, rules and regulations ensures that the companies work as per its regulations. Company has to formulate it's dividend policy in accordance with the rules and regulations framed by the Government.

2.2 SOURCES OF BORROWED CAPITAL

Only owned capital is not sufficient to carry on all business activities of a joint stock company. A company needs borrowed capital to supplement it's owned capital.

Every trading company is entitled to borrow money. However, it is a normal practice to have an express provision in the Memorandum of Association, enabling a company to borrow money. Memorandum authorises company to exercise borrowing powers where as Articles of Association provides as to how and by whom these powers shall be exercised. The power to borrow money is normally exercised by Board of Directors of the company.

A private company may exercise it's borrowing powers immediately after incorporation. However public company cannot exercise it's borrowing power until it secures certificate of commencement of business.

The capital may be borrowed for short, medium or long term requirement. It is better to raise borrowed capital at a later stage of company's business, when company wants to expand or diversify it's business and it requires additional capital. This additional capital can be raised by : a) issue of debentures b) Accepting deposits c) bonds d) Loans from commercial banks and Financial institutions, etc. Interest is paid on borrowed capital. It is paid at fixed rate. Borrowed capital is repayable after a specific period of time.

2.2.1 Debentures

Debentures are one of the principal sources of raising borrowed capital to meet long and medium term financial needs. Over the years debentures have occupied a significant position in the financial structure of the companies.

The term debenture has come from the latin word 'debere' which means to 'owe'.

The term debenture has not been defined clearly under Companies Act.

Sec 2(30) of the Companies Act 2013, only states that, 'the word debenture includes debenture stock, bonds and any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not'.

Under the existing definition, debenture includes debenture stock. Debenture means a document which either creates or acknowledges debt. Ordinarily, debenture constitutes a charge on some property of company, but there may be a debenture without any such charge.

Palmer defines : "A debenture as an instrument under seal evidencing debt, the essence of it being admission of indebtedness."

Topham defines : "A debenture is a document given by a company as evidence of debt to the holder, usually arising out of loan, and most commonly secured by charge."

According to the above definitions, debenture is an evidence of indebtedness. It is an instrument issued in the form of debenture certificate, under the common seal of the company.

- **Features**

1. **Promise :** Debenture is a promise by company that it owes specified sum of money to holder of the debenture.
2. **Face Value :** The face value of debenture normally carries high denomination. It is ₹ 100 or in multiples of ₹ 100.
3. **Time of Repayment :** Debentures are issued with the due date stated in the debenture certificate. The principal amount of debenture is repaid on maturity date.
4. **Priority of Repayment :** Debentureholders have a priority in repayment of debenture capital over the other claimants of company.
5. **Assurance of Repayment :** Debenture constitutes a long term debt. They carry an assurance of repayment on due date.

6. **Interest :** A fixed rate of interest is agreed upon and is paid periodically in case of debentures. Payment of interest is a fixed liability of the company. It must be paid by company irrespective of the fact, whether the company makes profit or not.

7. **Parties to Debentures :**

   a) **Company :** This is the entity which borrows money.

   b) **Trustees :** A company has to appoint Debenture Trustee if it is offering Debentures to more than 500 people. This is a party through whom the company deals with debentureholders. The company makes an agreement with trustees, it is known as Trust Deed. It contains the obligations of company, rights of debentureholders, powers of Trustee, etc.

   c) **Debentureholders :** These are the parties who provide loan and receive, 'Debenture Certificate' as an evidence.

8. **Authority to issue debentures :** According to the Companies Act 2013, Section 179 (3), the Board of Directors has the power to issue debentures.

9. **Status of Debentureholder :** Debentureholder is a creditor of the company. Since debenture is a loan taken by company, interest is payable on it at fixed rate, at fixed interval until the debenture is redeemed.

10. **No Voting Right :** According to Section 71 (2) of the Companies Act 2013, no company shall issue any debentures carrying any voting right. Debentureholders have no right to vote at general meeting of the company.

11. **Security :** Debentures are generally secured by fixed or floating charge on assets of the company. If a company is not in a position to make payment of interest or repayment of capital, the debentureholder can sell off charged property of the company and recover their money.

12. **Issuers :** Debentures can be issued by both private company and public limited company.

13. **Listing :** Debentures must be listed with at least one recognised stock exchange.

14. **Transferability :** Debentures can be easily transferred, through the instrument of transfer.

• Types of Debentures

Debentures

On the basis of security	On the basis of transfer	On the basis of repayment	On the basis of conversion
1. Secured and	3. Registered and	5. Redeemable and	7. Convertible and
2. Unsecured Debentures.	4. Bearer Debentures.	6. Irredeemable Debenture.	8. Non convertible Debenture.

1. **Secured debentures :** The debentures can be secured. The property of company may be charged as security for loan. The security may be for some particular asset (fixed charge) or it may be the asset in general (floating charge). The debentures are secured through 'Trust Deed'.

2. **Unsecured debentures :** These are the debentures that have no security. The issue of unsecured debentures is permitted by the Companies Act, 2013.

3. **Registered Debentures :** Registered debentures are those debentures on which the name of holders are recorded. A company maintains 'Register of Debentureholders' in which the name, address and particulars of holdings of debentureholders are entered. The transfer of registered debentures requires the execution of regular transfer deed.
4. **Bearer Debentures :** Name of holders are not recorded on the bearer debentures. Their names do not appear on the 'Register of Debentureholders'. Such debentures are transferable by mere delivery. Payment of interest is made by means of coupons attached to debenture certificate.
5. **Redeemable Debentures :** Debentures are mostly redeemable i.e. Payable at the end of some fixed period, as mentioned on the debenture certificate. Repayment can be made at fixed date at the end of specific period or by instalment during the life time of the company. The provision of repayment is normally made in 'Trust Deed'.
6. **Irredeemable Debentures :** These kind of debentures are not repayable during life time of the company. They are repayable only after the liquidation of the company, or when there is breach of any condition or when some contingency arises.
7. **Convertible Debentures :** Convertible debentures give right to holder to convert them into equity shares after a specific period of time. Such right is mentioned in the debenture certificate. The issue of convertible debenture must be approved by special resolution in general meeting before they are issued to public. These debentures are advantageous for the holder. Because of this conversion right, convertible debentureholder is entitled to equity shares at a rate lower than market value.
8. **Non-convertible Debentures :** Non-convertible debentures are not convertible into equity shares on maturity. These debentures are redeemed on maturity date. These debentures suffer from the disadvantage that there is no appreciation in value.

2.2.2 Acceptance of Deposit

Public deposit is an important source of financing short term requirements of company. Companies receive fixed deposits from the public for the period ranging from 6 months to 36 months. Such deposits are called as Public Deposits.

Under this method, general public is invited to deposit their savings with the company for varied period. Interest is paid by companies on such deposits. The company issues 'Deposit Receipt' to depositor. The terms of deposit are mentioned in the 'Deposit Receipt'. Deposit Receipt is an acknowledgement of debt/loan by the company. Deposits are either secured or unsecured loans offered to the company.

Meaning :

As per section 2 (31) of Companies Act, 2013, 'deposit' includes any receipt of money by way of deposit or loan or in any other form by a company, but does not include such categories of amount as may be prescribed in consultation with the Reserve Bank of India.

The above expression has been further elaborated by Rule 2 (1)(c) of Companies (Acceptance of Deposits) Rules 2014. This Rule provides that 'deposit' means any receipt of money, in the form of deposit or loan by a company. However, 'deposit' does not include following :

1. Any amount received from Central Government or a State Government.
2. Any amount received as loan from any banking company.
3. Any amount received from foreign government or international banks.
4. Any amount received by a company from any other company.
5. Any amount raised by issuing commercial paper.
6. Any amount raised by issue of bonds.
7. Any amount received in trust.
8. Any amount received by way of subscription to any shares or debentures.

(Terms and conditions of acceptance of Deposits are discussed in detail in Chapter 5.)

2.2.3 Bond

Bond is a debt security. It is a formal contract to repay borrowed money with interest. Bond is a loan. The holder of bond is a lender to the institution. He is a creditor of the company. He gets fixed rate of interest.

All bonds have maturity date and is paid in cash at certain date in future.

According to Webster Dictionary, 'A bond is an interest bearing certificate issued by the government or business firm, promising to pay the holder a specific sum at a specified date.'

Thus a company borrows money and issues bonds as an evidence of debt. Interest is payable on bonds at fixed interval or on maturity of bonds.

Features

1. **Nature of Finance :** It is a debt Finance. It provides long term finance. The bonds can be issued for longer period i.e. 5 years, 10 years, 25 years, 50 years.
2. **Status of bondholder :** The bondholders are creditors. Since they are creditors and non-owners they are not entitled to participate in general meeting. They have no voting right and hence no participation in the management.
3. **Return on bonds :** The bondholder gets a fixed rate of interest. It is payable at regular interval or on the maturity of bond.
4. **Repayment :** Bonds have specific maturity date on when the principal amount is repaid.

2.2.4 American Depository Receipt (ADR) and Global Depository Receipt (GDR)

In India, the shares of public company are listed and traded on various stock exchanges like Bombay Stock Exchange (BSE) and National Stock Exchange (NSE).

With adoption of free economic policy and due to globalization some of the Indian company's shares are also listed and traded on foreign stock exchanges like New York Stock Exchange (NYSE) or National Association of Securities Dealer Automated Quotation (NASDAQ). To list shares on these stock exchanges, company has to comply with policies of those stock exchanges. The policies of these stock exchanges are different than the policies of Indian Stock Exchanges. Therefore, those Indian companies which can not list their shares directly on foreign stock exchanges, get listed indirectly using ADR and GDR.

ADR and GDR are Dollar/Euro denominated instrument traded in USA and Europe Stock Exchanges.

Indian Company issues shares to an intermediary called 'Depository'. Bank of New York, Citigroup etc. act as foreign Depository Bank. This Depository bank issues ADR and GDR to investors against these shares. The ADR / GDR represent fixed number of shares. These ADR / GDR are then sold to people in foreign country. The ADR / GDR are traded like regular shares. They are listed on stock exchanges. The prices fluctuate depending on demand and supply.

Both ADR and GDR are depository receipts, but only difference is the location where they are traded. If the Depository Receipt is traded in USA, it is called American Depository Receipts (ADR) and if it is traded in a country other than USA is called Global Depository Receipts (GDR).

Non-Resident Indians (NRI) and Foreign nationals can invest their money in India by purchasing ADR and GDR. They can buy ADR / GDR using their regular equity trading Account.

The company pays dividend in home currency to the depository bank and the depository bank converts it into the currency of investor and pays dividend.

The exchanges on which GDR is traded are as follows :

1) London stock exchange.
2) Luxembourg Stock exchange.
3) NASDAQ Dubai.
4) Singapore Stock exchange.
5) Hongkong Stock exchange.

Activity : Find out Indian Companies who have issued ADR as well as GDR.

2.2.5 Commercial Banks

There are number of sources of financing short and medium term business requirements. Among these, commercial bank constitute the most predominant source. Commercial banks play significant role in corporate financing in India. Commercial banks, by introducing variety of deposit schemes tailored to individual depositor's need, mop up savings of people and make use of these savings to meet varied requirements of corporate enterprises.

Commercial banks assist corporate enterprises -

1) By Granting term loans to companies.
2) By subscribing to shares and debentures of companies.
3) By underwriting the issue of securities of the Company.

Commercial banks also play an important role in providing short term finance. They have become primary source of financing working capital of the business. In India, primary source of financing working capital are bank credit and trade credit.

Banks have introduced many innovative schemes for disbursement of credit. They are as follows :

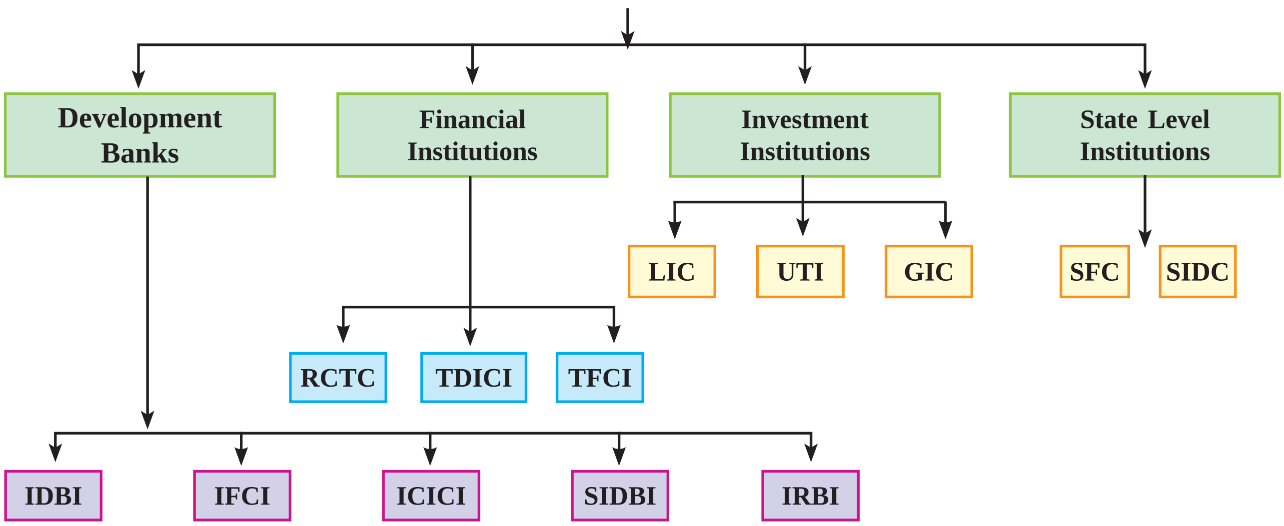
1. **Overdraft :** A company having current account with bank is allowed overdraft facility. The borrower can withdraw funds as and when needed. He is allowed to overdraw on his current account, up to the credit limit which is sanctioned by bank. Within this stipulated limit any number of drawings are permitted. Repayments can be made whenever required during the time period. The interest is determined on the basis of actual amount withdrawn.
2. **Cash Credit :** It is also an important and popular form of financial aid. This form of credit is operated in same manner as overdraft facility. The borrower can withdraw amount from his cash credit account up to a stipulated limit based on security margin. Cash credit is given against pledge or hypothecation of goods or by providing alternative securities. Interest is charged on outstanding amount borrowed and not on the credit limit sanctioned.
3. **Cash loans :** Under this, the total amount of loan is credited by bank to the borrowers account. Interest is payable on actual balance outstanding.
4. **Discounting bills of exchange :** The drawer of the bill i.e. (seller) can receive money from drawee (i.e. buyer) on due date or after the due date. Drawer can receive money before due date by discounting the bill with the bank. This is nothing but selling the bill to the bank. The bank gives money to drawer less than the face value of the bill. Thus bill of exchange are trade bills. They are accepted by bank and cash is advanced against them.

2.2.6 Financial Institutions

First industrial policy was declared in 1948 for rapid industrial development in the country. The Central Government and State Government have established special financial institutions for providing industrial finance. These institutions provide medium and long term finance. The assistance of these institutions has become important for new companies as well as going concerns.

Financial Institutions are classified into four categories as follows.

Financial Institutions in India



I. Development Banks

1. Industrial Development Bank of India (IDBI).
2. Industrial Finance Corporation of India Ltd. (IFCI)
3. Industrial Credit and Investment Corporation of India (ICICI)
4. Small Industries Development Bank of India (SIDBI)
5. Industrial Reconstruction Bank of India (IRBI)

II. Financial Institutions

1. Risk Capital and Technology Finance Corporation Ltd. (RCTC)
2. Technology Development and Information Company of India Ltd. (TDICI)
3. Tourism Finance Corporation of India Ltd. (TFCI)

III. Investment Institutions

1. Life Insurance Corporation of India (LIC)
2. Unit Trust of India (UTI)
3. General Insurance Corporation of India (GIC)

IV. State Level Institutions

1. State Finance Corporations (SFC)
2. State Industrial Development Corporation (SIDC)

Above mentioned institutions provide financial assistance in the following forms :

1. To provide term lending facilities.
2. To subscribe to shares and debentures.
3. To underwrite the issue of securities.
4. To lend money.
5. To guarantee term loans raised by company.

Activity :
Study the role of different financial institutions in raising funds for companies.

2.2.7 Trade Credit

No business can be run without 'credit'. Credit is the soul of business. Trade credit financing is major source of short term financing.

Manufacturers, wholesalers and suppliers of goods or materials are called 'trade creditors'. They sell tangible goods to other business concerns on the basis of deferred payment i.e. future payment credit is extended by these business concerns with an intention to increase their sales. The business firm extends credit, also because of custom that has been built up overtime.

Trade credit is not cash loan. It results from a credit sale of goods / services, which has to be paid at a future date after the sale takes place. In other words, when goods are delivered by supplier to a customer and the payment is made after some time, it is called as trade credit.

In distributive trade this kind of credit has great significance. The small retailers, to large extent rely on obtaining trade credit from supplier. It is an easy kind of credit which can be obtained without signing any debt instrument. It is readily available and is cheap method of financing.

Suppliers sell goods and willingly allow 30 days or more, for bill to be paid. They even offer discount, if bills are cleared within a short period such as 10 days or 15 days, etc. The terms of trade credit are not rigid.

2.3 DISTINCTION

1. Shares and Debentures

Points	Shares	Debentures
1. Meaning	A share is a part of share capital of a company. It is known as ownership securities.	A debenture is a certificate of loan taken by a company. They are also known as creditorship securities.
2. Status	A holder of shares is the owner of company. Therefore share capital is owned capital.	A holder of debenture is creditor of the company. Debenture capital is loan capital or borrowed capital.
3. Nature	It is permanent capital. It is not repaid during the life time of the company.	It is temporary capital. Generally it is repaid after a specific period.
4. Voting / Right	Shareholders being owners enjoy normal voting rights in general meeting. They participate in the management of the company.	Debentureholders being creditors, do not have any voting right. They can not participate in the management of the company.
5. Return on Investment	Return on shares is called dividend. Equity shareholders receive divided at fluctuating rate where as preference shareholders receive divided at fixed rate.	Return on debenture is called interest. It is fixed at the time of issue. Interest is paid even when company has no profit.
6. Security	Share capital is unsecured capital. No security is offered to the shareholder.	Debenture capital being loan capital is secured by creating a charge on Company's property.
7. Time of Issue	Shares are issued in the initial stages of the company formation.	Debentures are issued at a later stage, when the company has properties to offer as security.
8. Suitability	Shares are suitable for long term finance.	Debentures are suitable for medium term finance.

Points	Shares	Debentures
9. Types	Shares are classified into – a) Equity shares b) Preference	Debentures are classified as : a) Registered Debentures b) Bearer Debentures c) Secured Debentures d) Unsecured Debentures e) Redeemable Debentures f) Irredeemable Debentures g) Convertible Debentures h) Non - convertible Debentures
10. Position on liquidation	On liquidation of a company, share holders rank last in the list of claimants.	Debentureholders being creditors, rank prior to shareholders for repayment on liquidation of company.

2. Equity Shares and Preference Shares

Points	Equity Shares	Preference Shares
1. Meaning	Shares that are not preference shares are called equity shares i.e. these shares do not have preferential right for payment of dividend and repayment of capital.	Preferences shares are Shares that carry preferential right as to payment of : a) Dividend and b) Repayment of capital.
2. Rate of Dividend	Equity shares are given dividend at fluctuating rate depending upon the profits of the company.	Preference shareholders get dividend at fixed rate.
3. Voting Right	Equity shareholders enjoy normal voting right. They participate in the management of their company.	Preference shareholder do not enjoy normal voting right. They can vote only on matters affecting their interest.
4. Return of Capital	Equity capital can not be returned during the life time of the company. (except in case of buy back)	A company can issue redeemable preference shares, which can be repaid during the life time of the company.
5. Nature of capital	Equity capital is known as 'Risk Capital.'	Preference capital is 'Safe Capital' with stable return.
6. Nature of investor	The investors who are ready to take risk invest in equity shares.	The investors who are cautious about safety of their investment, invest in preference shares.

Points	Equity Shares	Preference Shares
7. Face value	The face value of equity shares is generally ₹ 1/- or ₹ 10/- it is relatively low.	The face value of preference shares is relatively higher i.e. ₹ 100/- and so on.
8. Right and bonus issue	Equity shareholder is entitled to get bonus and right issue.	Preference shareholders are not eligible for bonus and right issue.
9. Capital appreciation	Market value of equity shares increases with the prosperity of company. It leads to increase in the value of shares.	Market value of preference shares does not fluctuate, so there is no possibility of capital appreciation.
10. Risk	Equity shares are subject to higher risk. That is because of fluctuating rate of dividend and no guarantee of refund of capital.	Preference shares are subject to less risk. It is because of fixed rate of dividend and preferential right as regards to dividend and repayment of capital.
11. Types	Equity shares are classified into : a) equity shares with normal voting right. b) equity shares with differential voting right.	Preference shares are classified as : a) Cumulative Preference Shares b) Non-Cumulative Preference Shares c) Convertible Preference Shares d) Non-Convertible Preference Shares e) Redeemable Preference Shares f) Irredeemable Preference Shares g) Participating Preference Shares h) Non-Participating Preference Shares

3. Owned capital and Borrowed capital

Points	Owned Capital	Borrowed Capital
1. Meaning	It is that capital which is contributed by shareholders.	It is that capital which is borrowed from creditors. It is also known as debt capital.
2. Sources	This capital is collected by issue of equity shares and preference shares.	It is collected by way of issue of debentures, fixed deposits, loan from bank/financial institutions, etc.

Points	Owned Capital	Borrowed Capital
3. Return on Investment	The shareholders get dividend as income on their investment. Rate of dividend is fluctuating in case of equity shares but fixed in case of preference shares.	The debt capital holders get interest as income on their investment. Interest is paid at fixed rate.
4. Status	The shareholders are owners of the company.	The debt holders are creditors of the company.
5. Voting right	The equity shareholders enjoy normal voting right at the general meeting.	The creditors do not enjoy voting rights at the general meeting.
6. Repayment of Capital	The shareholders do not enjoy priority over creditors. They are eligible for repayment of Capital only after making payment to creditors at the time of winding up of the company.	The creditors get priority over the shareholders in case of return of principal amount at the time of winding up of the company.
7. Charge on assets	The shareholders do not have any charge on the assets of the company.	The secured debenture holders have a charge on assets of the company.

SUMMARY

- The various sources of finance can be divided as owned capital and borrowed capital.
- Share is a small unit of share capital of a company.
- Equity Shares do not enjoy preference for dividend and do not have priority for payment of capital at the time of winding up of company.
- Preference shares have prior right to receive fixed rate of dividend and return of capital in the event of winding up of the company.
- The debt acknowledged by a company by issuing debenture certificate is called debenture.
- Bond is an instrument issued by government or business firm as an evidence of debt.
- Retained earning is sum total of accumulated profit which are reinvested in the business.
- Public deposit is a loan accepted by company for short period of time ranging from 6 months to 36 months.
- Company can raise loan from banks in the form of overdraft,cash credit, cash loans, etc.
- Trade credit is a credit extended by manufactures and suppliers to customers.
- ADR and GDR are depository receipts through which Indian companies raise equity capital in international market.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statement.

1. .... is a smallest unit in the total share capital of the company.
   a) Debenture b) Bonds c) Share
2. The benefit of Depository Receipt is ability to raise capital in .... market.
   a) National b) Local c) International
3. .... are residual claimants against the income or assets of the company.
   a) Bondholders b) Equity Shareholders c) Debentureholders
4. .... participate in the management of their company.
   a) Preference shareholders b) Depositors c) Equity shareholders
5. .... shares are issued free of cost to existing equity shareholders.
   a) Bonus b) Right c) Equity
6. The holder of preference share has right to receive .... rate of divided.
   a) fixed b) fluctuating c) lower
7. Accumulated dividend is paid to .... preference shares.
   a) redeemable b) cumulative c) convertible
8. The holder of .... preference shares have right to convert their shares into equity shares.
   a) cumulative b) convertible c) redeemable
9. Debenture holders are .... of the company.
   a) creditors b) owners c) suppliers
10. .... is paid on borrowed capital.
    a) Interest b) Discount c) Dividend
11. Debentureholders get fixed rate of .... as return on their investment.
    a) interest b) dividend c) discount
12. Convertible debentures are converted into................ after a specific period.
    a) equity shares b) deposits c) bonds
13. Retained earnings are .... source of financing.
    a) internal b) external c) additional
14. The holder of bond is .... of the company.
    a) secretary b) owner c) creditor
15. Company can accept deposits from public, minimum for .... months.
    a) six b) nine c) twelve

16. Company can accept deposits from public, maximum for .... months.
    a) 12 b) 24 c) 36
17. A depository receipt traded in .... is called American Depository receipt.
    a) London b) Japan c) U.S.A.

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Equity Share Capital	1)	Agreement
b)	Debenture Trustees	2)	Capitalisation of Profit
c)	Preference Shareholders	3)	Bold Investor
d)	Debenture Certificate	4)	Venture Capital
e)	Bonus Shares	5)	Document of Ownership
		6)	Capitalisation of Loan
		7)	Safe Capital
		8)	Instrument of Debt
		9)	Trust Deed
		10)	Cautious Investor

C) Write a word or a term or a phrase which can substitute each of the following statement.

1. The 'real masters' of the company.
2. A document of title of ownership of shares.
3. The holders of these shares are entitled to participate in the surplus profit.
4. A party through whom the company deals with debentureholders.
5. Name the shareholders who participate in the management.
6. The value of share which is written on the share certificate.
7. The value of share which is determined by demand and supply forces in the share market.
8. The policy of using undistributed profit for the business.
9. It is an acknowledgement of loan issued by company to depositor.
10. A Dollar denominated instrument traded in USA.
11. The Depository Receipt traded in country other than USA.
12. Money raised by company from public for minimum 6 months to maximum 36 months.
13. Credit extended by the suppliers with an intention to increase their sales.
14. The credit facility provided to a company having current account with bank.

D) State whether the following statements are true or false.

1. Equity share capital is known as venture capital.
2. Equity shareholders enjoy fixed rate of dividend.
3. Equity shareholders are described as 'shock absorber' when company has financial crisis.

4. Debenture holders have right to vote at general meeting of the company.
5. Bond holders are owners of the company.
6. Depository bank stores the shares on behalf of GDR holder..
7. Financial institutions underwrite the issue of securities.
8. Cash credit is given against hypothecation of goods or any security.
9. Trade credit is major source of long term finance.

E) Find the odd one.

1. Debenture, Public deposit, Retained earnings.
2. Face value, Market value, Redemption value.
3. Share Certificate, Debenture Certificate, ADR.
4. Trade Credit, Overdraft, Cash Credit.

F) Complete the sentences.

1. The finance needed by business organisation is termed as ....
2. The convertible preference share holders have a right to convert their shares into........... .
3. Equity shareholders elect their representatives called ....
4. Bonus shares are issued as gift to ....
5. The bond holders are .... of the company.
6. Depository receipt traded in a country other than USA is called ....
7. First Industrial policy was declared in the year ....
8. When goods are delivered by supplier to customer on basis of deferred payment it is called as ....

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Equity shares	1)	....
b)	....	2)	Dividend at fixed rate
c)	Debentures	3)	....
d)	....	4)	Accumulated corporate profit
e)	Public Deposit	5)	....

(Fluctuating rate of dividend, Preference shares, Interest at fixed rate, Retained earnings, Short term loan.)

H) Answer in one sentence.

1. What is a share ?
2. What are Equity shares ?

3. What are preference shares ?
4. What are retained earnings ?
5. What is a debentures ?
6. What is a bond ?
7. In which country can ADR be issued ?
8. In which country can GDR be issued ?
9. What are convertible debentures ?
10. What are cumulative preference shares ?

I) Correct the underlined word/s and rewrite the following sentences.

1. Owned capital is <u>temporary</u> capital.
2. Equity shares get dividend at <u>fixed</u> rate.
3. Preference shares get dividend at <u>fluctuating</u> rate.
4. Retained earnings is an <u>external</u> sources of finance.
5. Debentureholder is <u>owner</u> of the company.
6. Bond is a source of <u>short</u> term finance.
7. Depository Receipt traded in USA is called as <u>Global Depository Receipt</u>.

Q.2 Explain the following terms / concepts.

1. Borrowed Capital
2. Owned capital
3. Ploughing back of profit
4. Overdraft
5. Trade credit

Q.3 Study the following case / situation and express your opinion.

(1) The Balance-sheet of a Donald Company for the year 2018-19 reveals equity share capital of Rs. 25,00,000 and retained earnings of Rs. 50,00,000.

a) Is the company financially sound ?

b) Can the retained earnings be converted into capital ?

c) What type of source retained earning is ?

(2) Mr. Satish is a speculator. He desires to take advantage of growing market for company's product and earn handsomely.

a) According to you which type of share Mr. Satish will choose to invest ?

b) What does he receive as return on investment ?

c) State any one right which he will enjoy as a shareholder.

(3) Mr. Rohit, an individual investor, invests his own funds in the securities. He depends on investment income and does not want to take any risk. He is interested in definite rate of income and safety of principal.

a) Name the type of security that Mr. Rohit will opt for.

b) What does he receive as return on his investment ?

c) The return on investment which he receives is fixed or fluctuating ?

Q.4 Distinguish between the following.

1. Equity shares and Preference shares.
2. Share and Debenture.
3. Owned capital and borrowed capital.

Q.5 Answer in brief.

1. What is public deposit ?
2. What is Global Depository Receipt ?
3. What is trade credit ?
4. What are the schemes for disbursement of credit by bank ?
5. State the features of Bonds.

Q.6 Justify the following statements.

1. Equity shareholders are real owners and controllers of company.
2. Preference shares do not carry normal voting right.
3. The debentures are secured by charge on assets of the company.
4. Retained earning is simple and cheapest method of raising finance.
5. Public deposit is good source of short term financing.
6. Bond holder is creditor of the company.
7. Trade credit is not cash loan.
8. Different investors have different preferences.
9. Equity share capital is risk capital.

Q.7 Answer the following questions.

1. What is share and state it's features ?
2. What is an equity share ? Explain it's features.
3. Define preference shares. What are the different types of preference shares.
4. What are preference shares? State it's features.
5. What is Debenture ? Discuss the different types of debentures.
6. Define Debenture and explain the features of debentures.

❑❑❑

3 ISSUE OF SHARES

3.1 Classification of Share Capital

3.2 Issue of Shares

3.3 Methods of Issue of Shares

(A) Public Issue or Public Offer of Shares
- Fixed Price Issue Method
- Book-Building Method
- Initial Public Offer
- Further Public Offer

(B) Offering Shares to Existing Equity Shareholders
- Rights Issue
- Bonus Issue/Bonus Share

(C) Offering Shares to existing employees
- Employee Stock Option Scheme (ESOS)
- Employee Stock Purchase Scheme (ESPS)
- Stock Appreciation Rights Scheme (SARS)
- Sweat Equity Shares

(D) Private Placement
- Preferential Allotment

3.4 Allotment of Shares

3.4.1 Provisions/Conditions for Allotment of Shares

3.4.2 Procedure for Allotment of Shares

3.5 Share Certificate

3.6 Calls on Shares

3.7 Forfeiture of Shares

3.8 Surrender of Shares

3.9 Transfer of Shares

3.10 Transmission of Shares

3.11 Distinction

INTRODUCTION :

In Chapter 2 we studied the different sources of finance that a company can use to raise funds. The capital structure of a company consists of its Owned Funds and Borrowed Funds. Owned Funds are made up of Equity shares, Preference shares and retained earnings. A company limited by shares, raises Share Capital by issuing shares.

In this chapter we will study in detail how a company issues different types of shares depending upon its needs. We will also learn about various concepts related to shares.

3.1 CLASSIFICATION OF SHARE CAPITAL :

Share capital refers to the capital made up of Equity Shares and Preference Shares. Usually, in share capital, the proportion of Equity shares is more than Preference shares.

Share Capital can be classified as –

Authorised or Nominal or Registered Capital
(1,00,000 Equity Shares × ₹ 10/- each = ₹ 10,00,000)

Issued Capital
(40000 Equity Shares × ₹ 10/- each = ₹ 4,00,000)

Un-Issued Capital
(60000 Equity Shares × ₹ 10/- each = ₹ 6,00,000)

Subscribed Capital
(30000 Equity Shares × ₹ 10/- each = ₹ 3,00,000)

Un-subscribed Capital
(10000 Equity Shares × ₹ 10/- each = ₹ 1,00,000)

Called-up Capital
(30000 Equity Shares × ₹ 5/- each = ₹ 1,50,000)

Un-Called Capital
(30000 Equity Shares × ₹ 4/- each = ₹ 1,20,000)

Reserve Capital
(30,000 Equity Shares × ₹ 1/-each = ₹ 30,000)

Paid-up Capital
(20000 Equity shares × ₹ 5/- each = ₹ 1,00,000)

Calls In Arrears
(10000 Equity shares × ₹ 5/- each = ₹ 50,000)

A. Authorised/Nominal or Registered Capital :

Authorised Capital is the maximum capital authorised by Memorandum of Association that a company can raise by issuing shares.

It is also called as Registered Capital as it is mentioned in the capital clause of Memorandum of Association and the company pays stamp duty on this amount at the time of incorporation. Authorised Capital is calculated considering the need of capital of a company at present and in future.

Authorised Capital is also called as Nominal Capital as usually a company never issues the entire Authorised Capital.

e.g. 'M' Ltd. Company has Authorised Capital of ₹ 10,00,000 which can be divided into 1,00,000 Equity shares having a face value of ₹ 10 each.

A company can increase its Authorised capital by altering its Memorandum of Association.

B. Issued and Unissued Capital :

Issued Capital is that part of Authorised Capital which is offered by the company to prospective investors for subscription. Thus, it is the shares that the company is offering to the public to buy.

The balance part of Authorised capital not offered to the public is called as 'Unissued Capital'. In future, the company can issue shares from the unissued capital.

The issued capital of a company may be equal to or less than the Authorised Capital. e.g. 'M' Ltd. Company can have Issued Capital of ₹ 4,00,000 divided into 40,000 Equity shares at face value of ₹10/- each and the unissued capital will be ₹ 6,00,000 divided into 60,000 Equity shares of ₹ 10/- each.

C. Subscribed and Unsubscribed Capital :

Subscribed capital is that part of Issued-capital which has been subscribed or taken up (bought) by investors (subscriber). The public may or may not subscribe for the entire Issued capital. Hence, that part of the Issued capital not subscribed by the investors is called as 'unsubscribed capital'. Thus, the subscribed capital may be equal to or less than the Issued capital.

e.g. If 'M' Ltd. Company has Issued capital of ₹ 4,00,000 i.e. has issued 40,000 Equity shares, then the company's subscribed capital can be ₹ 3,00,000 divided into 30,000 Equity shares of ₹ 10/- each. Hence, the unsubscribed capital will be ₹ 1,00,000 divided into 10,000 Equity shares of ₹ 10/- each.

D. Called-up Capital, Uncalled Capital and Reserve Capital :

At the time of Issue, full value of the shares is usually not demanded by the company. Company collects the full value of shares in instalments as per its requirement of funds.

Each Instalment is called as 'calls'. Called-up capital is that part of subscribed capital which a company has 'called' or demanded to be paid by the shareholders. The balance capital which is not demanded from the shareholders is called as uncalled capital.

Reserve Capital is a part of uncalled capital. A company can decide to keep aside a part of its uncalled capital to be called up only at the time of winding up of a company to meet its financial requirements.

e.g. 'M' Ltd. Company may have called up capital of ₹ 1,50,000 i.e. 30,000 Equity shares of face value of ₹ 10/- each out of which ₹ 5/- per share has been called up/demanded by the company.

If the company decides to keep Re. 1/- per share as capital to be collected at the time of the winding up, the Reserve Capital will be ₹ 30,000 i.e. 30,000 equity shares of ₹ 10/- each where Re. 1 per share is kept as Reserve Capital.

Uncalled capital will be ₹ 1,20,000 i.e. 30,000 Equity shares where ₹ 4 per share which will be called up in future.

E. Paidup Capital and Calls in Arrears :

Paid up capital is the total amount of money actually paid up by the shareholders when the company has called up or demanded them to pay.

The amount not paid up by the shareholders is called up as Calls in Arrears or unpaid calls.

Every shareholder has to pay calls as and when the company demands. Failure to pay the calls may lead to forfeiture of shares.

Forfeiture : *Taking away of shares by a company due to non-payment of calls.*

e.g. 'M' Ltd. company has made a call of ₹ 5 per share, so if all the shareholder have paid the calls, then the paid up capital will be ₹ 1,50,000 (30,000 Equity shares ₹ 5 per share). But if for e.g. 10,000 Equity shares calls are not paid then the paid up capital will be ₹ 1,00,000 (20,000 Equity shares × ₹ 5 per share) and Calls-in-Arrears will be ₹ 50,000 (10,000 Equity shares × ₹ 5 per share)

3.2 ISSUE OF SHARES :

A company may need capital to start a new project or to expand or diversify its existing business or to repay its old debts.

It can raise funds by taking loans or by issuing shares, debentures, bonds, etc.

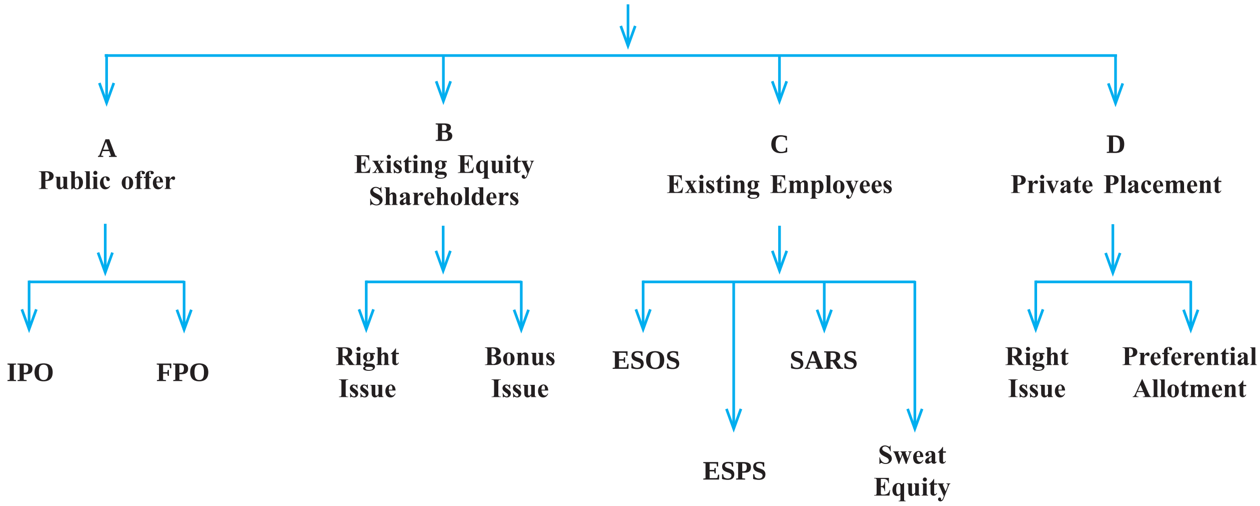
In case a company wants to raise capital by selling shares, it can issue :

a) Preference shares

b) Equity shares or ordinary shares

3.3 METHODS OF ISSUE OF SHARES :

METHODS OF ISSUE OF SHARES :



(A) Public Issue or Public offer of Shares : Public Issue or offer means offering the shares to the public. This is the most common method used by companies. The company invites the public to subscribe for its shares by issuing prospectus.

A company can use two pricing methods to offer shares to the public.

(a) Fixed Price Issue Method : Under this method, the company states in its prospectus, the quantity and the price at which the shares are offered to the public. The subscribers / investors are asked to pay a certain portion of face value of shares or entire issue price along with the application. The company comes to know the demand of its shares only after the subscription period ends. Company can issue shares at par or premium. Fixed Price method is used for all types of issues i.e. Public Issue, Right Issue, ESOS, etc.

Additional Information :

Issue of Shares At a Premium :

When a company issues shares at a price above the face value of a share, it is called as issue of share at premium. e.g. a share having a face value of ₹ 100 is issued at ₹ 150. ₹ 50 is the premium earned by the company and this has to be put in a separate account called as Securities Premium Account. The premium cannot be considered as profit and so cannot be used for distribution of dividend.

The Companies Act has not laid any restrictions on issue of shares at premium. However, it has imposed following conditions for utilisation of the Securities Premium Account :

(i) it can be used for issuing fully paid up Bonus Shares.

(ii) to write off preliminary expenses of the company.

(iii) to write off commission paid or discount allowed or expenses incurred on issue of shares or Debentures.

(iv) to pay premium on redemption of any Redeemable Preference shares or Debentures.

(b) Book Building Method : Under this method, the issuer company determines the number of shares and the issue price at which its shares will be sold by bidding process. The company issues a Red Herring Prospectus which contains price range or price band and asks the investors to bid on it. The lower end of the price band is called as 'floor price' while the highest end is called as 'cap price' or 'ceiling price'. The final price at which shares are offered to the investors is called as 'cut-off' price. Investors can bid any numbers of shares that they are willing to buy at any price within the price band. Bidding is kept open for 5 days. The bids along with the application money is to be submitted to the Lead Merchant Bankers called as 'Book Runners' who enters the bids in a book. After bidding is over, company fixes 'cut off price' based on the highest or best price at which all shares on offer can be sold. Company issues a Prospectus which contains the final price. Book Building Method is used for Public issues i.e. IPO and FPO.

Lead Merchant Bankers : *Institutions engaged in issue management either by making arrangement to buy or sell securities of an Issuing company or act as manager or provide advisory services.*

Issue of Shares at Discount :

Companies Act, prohibits a company to issue its shares at discount. However, it may be allowed in certain exceptional cases like when shares are issued to its creditors when the debts are converted into shares under a restoration or debt restructuring scheme as per RBI or Banking Regulation Act, 1949.

A company can make Public offer through two methods as follows :

Methods of Public Offer

IPO **FPO**

1) **Initial Public Offer (IPO) :** Initial Public Offer refers to the process of offering shares of a company to the public for the first time. A new company or an existing company which had raised its capital earlier from promoters or other investors may offer its shares to the public when it is in need of fresh funds. The first time, the company offers its shares to the public is called as Initial Public offer.

Before IPO, a company is not a listed company and its shares are privately held. But after IPO, a company becomes a listed company and its shares can be bought and sold by investors in the open market.

A company can make IPO through fixed price Issue method or Book-Building method.

2) **Further Public Offer or Follow on Public Offer (FPO) :** When a company issues shares to the public after an IPO, it is called as further (Follow on) public offer. Thus, every issue of shares by a listed company after its IPO is called as FPO. FPO leads to an increase in the subscribed capital of a company.

(B) Offering Shares to Existing Equity Shareholders : A company can raise funds by offering shares to its existing Equity shareholders as follows –

Issue of shares to existing Equity shareholders

Rights Issue **Bonus Shares**

1) **Rights Issue :** When a company wants to raise further capital, it can issue shares to its existing Equity shareholders in proportion to their existing shareholding. Such an issue of shares is called as 'Rights Issue' of shares.

Whenever a company makes further issue of shares, the existing Equity shareholders have 'pre-emptive rights' to subscribe to the new shares offered by the company.

Pre-emptive Rights : *Means first option to buy.*

A company can make a Rights Issue when it is making a private placement.

Private placement : *When securities are offered to a select group of people.*

Provisions : Company making Rights Issue has to fulfill the following provisions.

a) Rights shares are sold to the existing shareholders at a price which is lesser than its market price.

b) A company has to send 'Letter of offer' to the existing shareholders at the time of issuing Rights shares.

c) The letter of offer shall mention :

   i) the number of shares offered

   ii) the period of offer i.e. offer is valid for a period not less than fifteen days and not exceeding thirty days from the date of offer.

   iii) the right to renounce i.e. the shareholders have a right to give up their shares in favour of any other person.

d) The letter of offer can be sent by registered post, speed post, courier or through electronic mode.

e) If a shareholder does not respond to the Rights Issue offer within the stipulated time, it is implied that he is not interested in the offer and the company can offer the unsold shares to new investors.

> ***Stipulated time :*** *Means specified time.*
>
> ***Implied :*** *Means understood as truth.*

f) The company has to obtain minimum subscription i.e. 90% of the issue.

2) **Bonus Issue / Bonus Shares :** Bonus shares are fully paid shares issued free of cost to the existing equity shareholders in proportion to their shareholdings. Usually financially sound companies issue Bonus Shares out of its accumulated distributable profits or reserves. Hence as the profits or reserves are capitalised, it is also called as 'Capitalisation of Profits or Reserves'.

Provisions : Following are the provisions related to Bonus Issue –

a) A company can issue Bonus Shares only out of :

i) Free reserves or

ii) Securities Premium Account or

iii) Capital Redemption Reserve Account

> ***Securities Premium Account :*** *is an account in which the premium amount collected when shares are sold at premium is kept.*
>
> ***Capital Redemption Reserve Account :*** *is an account in which a company transfers part of its profits to be used for specific purposes. e.g. Issue Bonus Shares.*

b) A company cannot issue Bonus shares out of reserves created by Revaluation of Assets.

> ***Revaluation of Assets :*** *Value of assets recalculated to find out the current value of assets.*

c) It also cannot issue Bonus Shares instead of paying dividend.

d) Once the announcement for Bonus Shares is made by the Board of Directors, it cannot be then withdrawn.

e) Bonus shares are fully paid up shares.

f) Shareholders cannot renounce i.e. give away their Bonus shares to another person.

g) There is no minimum subscription to be collected.

(C) Offering Shares to Existing Employees : A company can raise funds by offering shares to its existing employees as follows –

1) ESOS	3) SARS
2) ESPS	4) Sweat Equity Shares

1) **Employees Stock Option Scheme (ESOS) :** Under this scheme, permanent employees, Directors or officers of the company or its Holding Company or Subsidiary company are offered the benefit or right to purchase the Equity Shares of the company at a future date at a pre-determined price.

ESOS encourages employees as they feel proud to be owners of the company for which they are working and company also benefits as it can retain good employees.

Provisions : Following are the provisions related to ESOS –

a) A company may offer the shares directly to the employees or through an Employee Welfare Trust.

b) The shares are offered at a price lesser than their market price.

c) There is a minimum vesting period of one year.

> ***Vesting Period :*** *Period during which the employee uses his option to apply for shares that has been granted to him.*

d) Usually company will specify the lock-in period i.e. period during which employee cannot sell his shares. Lock-in period is minimum 1 year.

e) Shares issued under this scheme do not enjoy any dividend or voting rights till the employee buys the shares.

f) Company has to get the approval of shareholders through special resolution to issue ESOS.

g) Employee cannot transfer his option to any other person nor can he pledge or mortgage the shares issued under ESOS.

h) Company has to set up a compensation committee to administer ESOS.Company has to fulfill the provisions of SEBI (Share Based Employee Benefits) Regulations, 2014.

> ***Pledge :*** *Give shares as a security for taking a loan.*
> ***Mortgage :*** *Convey title to shares as security to a lender for taking a loan.*

2) **Employee Stock Purchase Scheme (ESPS) :** Under this scheme the company offers Equity shares to its employees at a discounted price which they can buy at a future date. The company deducts a certain amount from the salary of the employee towards the payment for the shares.

Provisions : Company must fulfill the following provisions –

a) Different number of shares can be offered to different categories of employees.

b) Shares issued through ESPS should be immediately listed.

c) ESPS shares will have a minimum of one year lock-in period from date of allotment if ESPS is not a part of public issue.

d) Company has to fulfill the provisions of SEBI (Shares Based Employee Benefits) Regulations, 2014.

e) Company has to get the approval of the shareholders through a special Resolution to offer ESPS.

3) **Stock Appreciation Rights Scheme (SARS) :** Under this scheme the employees are given a right to receive appreciation in the value of specified number of shares of the company at a future date. The company allots a specified number of 'Stock Appreciation Right' units that are linked to the value of the company's shares on

the date of allotment. On the relevant date i.e. a future date, depending upon the appreciation in the value of shares which are linked to the SAR units, the employee is paid the appreciation value in cash or through Equity shares.

SARS is a form of bonus compensation given to the employees if the company performs well and its market price of shares goes up.

The employees does not have to pay for buying any shares. Company has to give employees a vesting period of minimum one year to exercise his option. There is no lock-in period for SARS. To issue SARS, company has to get approval of shareholders through a special resolution.

4) **Sweat Equity Shares :** These are shares issued by a company to its directors or employees at a discount or for consideration other than cash. It is issued in recognition of their valuable contribution to the company which has resulted in increased profits.

Sweat Equity shares rank pari passu with other Equity shares. These shares have a lock-in period of three years i.e. they cannot be transferred during this period. Company has to get the approval of shareholders through Special Resolution to issue Sweat Equity shares.

> ***Pari Passu :*** *means on 'equal footing' i.e. will be treated at par with other Equity Shares.*

(D) Private Placement : When a company offers its securities to a select group of persons not exceeding 200, it is called as Private Placement.

> ***Securities :*** *Means shares, bonds, debentures, etc.*

In other words, company offers its securities only to identified persons and not to the general public.

- The Board of Directors selects or identifies the persons to be included in the select group. They can be Mutual Funds, Institutional Investors, etc.
- Company has to issue private placement offer letter along with the application.
- The shares offered can be fully or partly paid up and the consideration should be paid by cheque, Demand Draft, etc. but not by cash.
- Right to renunciation is not given to applicants under Private Placement. Company has to get approval of shareholders through a Special Resolution.
- A company can make Private Placement in two ways :

Rights Issue **Preferential Allotment**

1) **Rights Issue :** (We discussed the same under the heading 'offering shares to Existing Equity shareholders.' on page 44)

2) **Preferential Allotment :** When a company issues specified securities i.e. Equity shares or securities that can be converted into Equity shares in future, to a select group of persons on preferential basis, it is called as 'Preferential Allotment'.

Usually the company offers preferential allotment to promoters, existing shareholders, employees, venture capitalists, etc.

The shares offered are fully paid up and the applicants have to pay the consideration in cash. Shares issued under preferential allotment have no voting rights. Approval of shareholders in the form of Special Resolution is needed to make Preferential allotment. Companies usually go for Preferential Allotment as it is not only less time consuming but also involves less paperwork and formalities.

> ***Venture Capitalists :*** *are institutions who provide capital to companies which has high growth potential in future. They usually buy the company's equity shares.*

Additional Information :

Private Placement	Preferential Allotment
1) Securities are offered to select group of persons not exceeding 200.	1) Selected securities i.e. Equity Shares or securities that can be converted into equity shares is offered to a select group of persons on preferential basis.
2) The shares offered through private placement can be fully paid up or partly paid up.	2) The shares offered are fully paid up.
3) Private placement offer letter is issued when shares are offered.	3) No such document is issued.

❑ **Buy Back of shares / securities :**

Buy Back means when a company purchases its own shares or other specified securities at a price higher than its market price.

Company can Buy Back from

- **existing shareholders on a proportionate basis of their shareholding**
- **Open market**
- **existing employees who were issued ESOS or Sweat Equity Shares**

Company can Buy Back its shares only when it has sufficient balance in (i) Free Reserves or (ii) Securities Premium Account or (iii) Proceeds of issue of any other shares.

Companies go for Buy Back of shares for various reasons such as to return surplus cash to its shareholders, safeguard company against unwelcome takeover bids, etc.

3.4 ALLOTMENT OF SHARES :

Meaning :

When a company gives shares to an applicant based on the application submitted, it is called as Allotment of Shares.

Supreme court has defined allotment as "the appropriation out of the previously unappropriated capital of the company of a certain number of shares to a person."

Appropriate : *distribute*

Un-appropriate : *undivided, whole.*

Thus as per this definition, Allotment of shares means allocating (giving) certain number of shares by Board of Directors out of the previously unallocated capital of the company to persons who have applied for the shares.

The company issues prospectus and application form. Applicant (subscribers) fills the form and submits it, with application money to the company's bankers. The Board of Directors approves the acceptance of such applications in the Board meeting by passing resolution. This is called as allotment of shares.

The Board of Directors has the power to allot shares.

Under the Companies Act, 2013, following companies have to issue shares (securities) in dematerialised form :

i) A company making a public offer in excess of Rs. 10 crores.

ii) Unlisted Public companies for its new issues with effect from 10th Sept. 2018.

iii) Such other class or classes of companies as may be prescribed.

Any other company can issue its shares in any form. Also the companies have the freedom to convert its shares into dematerialised form at any point of time. Companies issuing shares in dematerialised form has to comply with the provisions of the Depositories Act, 1996 and regulations issued there under.

3.4.1 Provisions or Conditions for Allotment of Shares :

Every company issuing shares has to comply with the provisions of the Companies Act, 2013 with regard to allotment of shares.

A public company has to also follow the Companies (Prospectus and Allotment of Securities) Rules, 2014 and SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018.

For Allotment of Shares, a company has to fulfil following :

A) Statutory Provisions

B) General Principles

(A) Statutory Provisions : These are provisions laid down by the Companies Act, 2013.

(1) Registration of Prospectus : A copy of the prospectus must be filed with the Registrar of Companies for registration on or before the date of its publication. This prospectus must be signed by every proposed Director (in case of newly formed company) or director or his duly authorised advocate.

(2) Application Money : The Companies Act states that along with the application form, the applicant has to pay a minimum of 5% of the nominal amount of the shares or such other amount as specified by SEBI. SEBI has specified (for public companies) the application money to be minimum 25% of the nominal amount of shares. The application money is to be paid in the Bank specified by the company.

(3) Minimum Subscription : Minimum subscription is the minimum amount of shares that must be taken or bought by the subscribers. This amount is mentioned in the prospectus. It must be collected within thirty (30) days from issue of prospectus.

SEBI has stated minimum subscription should be 90% of the issue.

(a) Usually when a company does not collect minimum subscription, it means its issue has been under subscribed i.e. the number of shares applied for is less than the shares offered by the company.

(b) If minimum subscription is not collected within the specified time, the entire amount received as application money should be returned to the subscribers within fifteen days of closure of issue. To avoid such a situation, company may enter into an underwriting agreement with the underwriters.

Underwriting agreement : *Company enters into an agreement with underwriters by paying them a commission. The underwriters assure the company to take up the unsold shares (Securities) so that the company is able to raise its minimum subscription.*

(4) Closing of subscription list : As per SEBI, the subscription list must be kept open for atleast three working days and not more than ten working days. Applicants can apply for shares only when the subscription list is open.

(5) Basis of allotment : Allotment of shares will be on the basis which will be decided for each category of subscribers. Allotment will be as per the minimum application size as fixed by the company.

(6) Over subscription : Over subscription means when applications received for shares are more than the number of shares offered by the company.

SEBI does not allow any allotment in excess of securities offered through offer document or prospectus. However, it may permit to allot not more than 10% of the net offer.

(7) Permission to deal on Stock Exchange : Every company, before making a public offer shall apply to one or more recognised Stock Exchanges to seek permission for listing its shares with them. The prospectus shall mention the name of the Stock Exchange and the fact that an application for permission to list in that stock exchange has been made by the company.

Listing : *getting the name of a company included in the official list of securities that can be traded on a Stock Exchange.*

(8) Appointment of Managers to the issue and various other agencies : Company has to appoint one or more Merchant Bankers to act as managers to the public issue. It also has to appoint Registrar to the issue, Collecting Bankers, Underwriters to the issue and Brokers to the issue, self certified syndicate banks, advertising agents etc.

Registrars to the issue - *Institution that keeps a record of shareholders, debentureholders on behalf of a company.*

Self certified syndicate banks - *Banks certified by SEBI which can offer ASBA facility to investors. (ASBA - refer pg 52 point 4)*

(B) General principles : These are rules that a company must follow in addition to the provisions of the Companies Act, 2013.

(1) Proper Authority : The Board of Directors or the allotment committee set up by the Board has the authority to allot shares.

(2) Allotment must be against application only : A company can allot shares only if it has received a written application for shares from the applicant.

(3) Reasonable time : As per the Act, allotment shall be done within 60 days of receipt of application money. Allotment can be made from the fifth day from date of issue of prospectus.

(4) Absolute and Unconditional allotment : Shares should be allotted on the same terms as stated in the prospectus and application form. No change in the terms of allotment or new conditions can be added at the time of allotment.

(5) Communication : Company has to inform the applicant that shares have been allotted to him by sending a letter of allotment or allotment advice. This letter gives details of number of shares allotted, amount of Allotment money to be paid, etc.

(6) Allotment should not be in contravention (violation) of any other laws : A Company cannot allot shares by violating or contradicting any other existing laws. e.g. Shares cannot be allotted to a minor.

If a company allots shares after fulfilling all the above mentioned requirements or provisions, such an allotment is called as 'Regular Allotment'. But if even one provision is not satisfied, then it is called 'Irregular Allotment' and such allotment is invalid.

3.4.2 Procedure for Allotment of Shares :

Allotment of shares means distributing shares to those applicants who have submitted a written application along with the application money.

Following is the procedure for allotment of shares :

(1) Appointment of Allotment Committee : When the subscription list is closed the Secretary informs the Board of Directors to make preparations for allotment of shares.

If the issue is par subscribed or under subscribed, the Board can do the allotment of shares. But if the issue is over subscribed, the Board has to appoint an Allotment Committee to undertake the work of allotment. The Allotment Committee will decide the basis of allotment and submit a report to the Board.

(2) Hold Board Meeting to Decide Basis of Allotment : Board Meeting is held to approve the allotment formula suggested by the Allotment Committee. A representative of SEBI is also present when the allotment committee prepares the allotment formula. If the shares are listed, the formula has to be also approved by the authorities of the concerned stock exchange.

Once the allotment formula is approved, the application and allotment list is made. This list contains the names of the allottees i.e. the applicants who will be allotted shares. The list has to be signed by the Chairman and Secretary.

(3) Pass Board Resolution for Allotment : At the board meeting, a resolution is passed to allot shares. The resolution also authorises the Secretary to issue letters of allotment and letters of regret.

Secretary has to send Letter of Allotment to allottees i.e. those applicants whose names appear in the application and allotment list. Secretary has to send Letter of Regret to those applicants to whom no shares have been issued. Along with the letter of regret, the application money is also refunded. Company which issues shares in electronic mode, does not issue Allotment Letter to individual applicants. Company informs the respective Depository i.e. NSDL or CDSL about the allotment of shares. It provides the Depository with the details of applicants who have been allotted shares, number of shares allotted, etc.

(4) Collection of Allotment Money : The letter of allotment states the money to be paid by the applicant on allotment of shares. The money has to be paid in the Bank specified by the company within the stipulated time.

For all public issues and Rights Issue (from Jan. 2016) ASBA is mandatory.

> ***ASBA :*** *Application Supported by Blocked Amount. It is an application made by an applicant to his bank to block the application money in the bank account. In case of allotment, the application money or the full issue value of the shares is transferred to the company's banker.*

(5) Arrangement Relating to Letters of Renunciation : An applicant who has been allotted shares can renounce the shares in favour of another person. The applicant has to fill up a form for renunciation and submit it with the original copy of the letter of allotment to the company. After approval from the Board, Secretary enters the name of the new allottees in the application and allotment list.

> ***Renounce :*** *give up, relinquish.*

(6) Arrangement Relating to Splitting of Allotment Letters : Sometimes, the applicant who has been allotted shares can request for splitting of allotment letters. Splitting means putting the shares in one or more name. After getting the approval of the Board for the splitting, Secretary enters the details of the split in the list of split allotments. Secretary has to also issue split letters.

(7) File Return of Allotment : Secretary has to file a 'Return of Allotment' with the Registrar of companies within 30 days of allotment of shares. The return of allotment contains details of allotment of shares including the names and addresses of allottees, value of shares allotted, amount paid or payable on each shares, etc.

(8) Prepare Register of Members and Issue Share Certificate : Secretary has to enter the names of all those applicants who have paid the allotment money in the Register of Members.

Secretary also has to prepare the Share Certificates and distribute it to all the members within two months of allotment of shares.

In case of shares held in electronic form (dematerialised), the entries of applicants are made by the Depository.

3.5 SHARE CERTIFICATE

It is a registered document issued by a company which is an evidence of ownership of specified number of shares of the company. Share certificate is a prima facie evidence of title to shares.

If any dispute about membership arises, the share certificate will be held as evidence and not the entries in the Register of Members.

Share certificate has to be issued under the common seal of the company, if any and signed by two Directors duly authorised by the Board of Directors and the Company Secretary or any other authorised person.

Company has to issue the share certificate to all allottees as well as transferees on transfer of shares. It is issued on partly or fully paid up shares.

Contents of Share Certificate :

Share certificate should be in Form SH-1 as prescribed under Companies (Share Capital and Debenture) Rules, 2014.

Following are the contents of a share certificate –

i) Name of the Company, CIN, Registered office address.

ii) Folio Number

iii) Share Certificate Number

iv) Name of Member

v) Nature of share, number of shares and distinctive number of the shares.

vi) Amount paid on shares

vii) Common Seal, if any and signature of two Directors and Company Secretary.

Time of issue of Share Certificate -

Time	To whom
i) Within two months from date of incorporation	to subscribers of the Memorandum of Association.
ii) Within two months from date of allotment	to allottees in case of allotment of shares.
iii) Within 1 month from date of receipt of instrument of transfer or intimation of transmission	to the transferee in case of transfer of shares and to the legal representative in case of transmission of shares.

For listed companies, share certificate should be issued within fifteen days from date of receipt of transfer request.

Duplicate Share Certificate : A company can issue duplicate share certificate if :

i) Original share certificate has been defaced, mutilated or torn and is surrendered to the company.

ii) It has been proved by the holder that the original share certificate is lost or destroyed.

In case of loss of share certificate, the company puts up a notice in the newspapers to announce the loss of the Share Certificate and asks the finder, if any, to return it to the company. If company does not get any response from the public, within the specified time, then the company can issue a duplicate Share Certificate.

Duplicate share certificate should be issued within three months from date of application. Company issues it only to registered shareholders. The duplicate Share Certificate should state in bold that it is a 'Duplicate Share Certificate'. Company has to pay heavy penalty if it has issued duplicate share certificate with the intent to defraud.

3.6 CALLS ON SHARES

At the time of issue of shares, a company may state that the issue price of the shares is to be paid in instalments as and when the company demands for it. So when a company demands the shareholder to pay a part or full amount of the balance amount unpaid on shares, it is called as 'Calls on Shares'.

Thus, besides the application money and allotment money, if a company demands the balance unpaid amount on shares, it is called as calls on shares. The unpaid amount on partly paid up shares is a liability of the share holder. If the shareholder fails to pay the calls, company can forfeit the shares.

Calls can be made only by the Board of Directors in the interest of the company. Company has to send a call letter/notice to the shareholders asking them to pay the call money and give them minimum 14 days notice to pay the call money to the Company's Banker. No call can be made for more than 25% of the nominal value of shares. The gap between two calls should not be less than one month from the date fixed for the payment of last preceding call. The rules and procedure to make calls are given in the company's Articles of Association.

3.7 FORFEITURE OF SHARES

If a shareholder fails to pay calls on shares within a certain period, the Board of Directors, if authorised by the Articles of Association, can forfeit i.e. take away the ownership of a member. This is called as forfeiture of shares. Only partly paid up shares can be forfeited

Board can forfeit shares only in the interest of the company. Company has to send a notice of forfeiture to the concerned member. The notice must give minimum 14 days period from the date of service of notice, to make the payment along with interest.

A company can reissue forfeited shares as these shares belong to the company. Reissue of forfeited shares is not the same as allotment of shares. On reissue, if company gets more money than the calls which was due, the excess amount is paid to the member. The Board can cancel forfeiture under certain circumstances provided the member requests the Board before it is reissued.

Effects of forfeiture

i) **Cessation of Membership :** On forfeiture, a member ceases to be member of a company and loses all membership rights. The member's name is removed from the Register of Members.

ii) **Liability of member :** A member is liable for unpaid calls even after forfeiture of shares. The liability ceases only when the company reissues the forfeited shares.

iii) **Liquidation of company :** If a company goes in for liquidation within one year of forfeiture of shares, the member whose shares have been forfeited is liable to pay the calls as a past member.

3.8 SURRENDER OF SHARES

This means voluntary return of shares by the member to the company for cancellation. Surrender of shares is allowed only if there is no other option but to forfeit the shares. Only partly paid up shares can be surrendered.

Surrendered shares can be reissued in the same way as forfeited shares. The Articles of Association of a company must provide for surrender of shares.

Surrendering of shares leads to reduction of capital, hence companies avoid surrender of shares.

3.9 TRANSFER OF SHARES

Transfer of shares means voluntary transfer of shares by a member of a company in favour of another person. A member may transfer the shares for consideration or give it away as gift. Every member has a right to transfer their shares.

In case of public companies, shares are freely transferable subject to the provisions of the Articles of Association. Whereas, in case of Private Company, there are restrictions on free transfer of shares.

A member has to apply to the company for transfer of shares by filling the 'Instrument of Transfer' and submit the share certificate along with the required transfer fees. Member who is transferring the shares is called as 'Transferor' and to whom the shares are to be transferred is called 'Transferee'.

A member can sell either a part or entire shares held by him.

Transfer is said to be completed only when transfer is registered in the Register of Members. Under Depository System, transfer of shares is automatically done on the basis of delivery against payment. Once the shares are transferred, the liability of the transferor ends.

Stamp duty has to be paid on transfer of shares in physical form but in demat form, no stamp duty is payable.

> ***Stamp duty :*** *As per the Indian Stamp Act 1899, a tax is payable to the Central Government when transfer deed is executed. Stamp duty is 0.25% on the market value of the shares as on date of execution of the transfer.*

Refusal to transfer shares :

Board of Directors has the authority to refuse registration of transfer of shares. A notice of refusal giving the reasons for refusing transfer by the Board is to be sent to the member within thirty days from the date on which the Instrument of transfer was delivered to the company.

The Board may refuse registering the transfer under following conditions :

i) When the provisions for transfer of shares as given in the Articles of Association is not fulfilled by the member.

ii) When the instrument of transfer is not as per the rules prescribed under the Companies Act.

iii) When the Instrument is not accompanied by the Share Certificate.

iv) When the company has a lien on the shares to be transferred.

A member may appeal to the NCLT against the refusal by the Board within a period of thirty days from date of receipt of refusal notice. If no notice is received, the member can appeal within 60 days in case of a Private Company and within 90 days in case of a Public Company.

Blank Transfer : When a member signs the Instrument of transfer without filling in the name of the transferee and hands it over to the transferee along with the share certificate, it is called 'Blank Transfer'.

Blank transfer enables easy purchase and sale of shares as the blank transfer form can be sold any number of times. The intermediate buyers need not pay Stamp Duty. A holder of Blank transfer form enjoys all rights a member is entitled to have.

Forged Transfer : Forged transfer is where the signature of the transferor is forged. Company should not register such transfer of shares.

3.10 TRANSMISSION OF SHARES

Transmission of shares takes place due to operation of law i.e. the shares of a member are automatically transferred to another person on the death, insolvency or insanity of a member. Thus transmission of shares is an involuntary action. There is only one party i.e. Legal Heir who initiates the process of transmission. The legal heir or official receiver need not pay any consideration for the shares. Original liability of the member continues incase of transmission. There is no need to submit Instrument of Transfer or pay stamp duty.

Operation of law - *Change or transfer as per existing laws and not due to any agreement.*

Following diagram shows to whom the shares will be transferred in case of transmission.

Event	To whom transferred
i) Death of member	to the legal heir of member
ii) Insanity	to the guardian of member.
iii) Insolvency	to official receiver appointed by court.

Activity :

Visit www.sebi.gov.in to view public issues related Draft offer Document filed by a company with SEBI.

3.11 DISTINCTION BETWEEN :

1. Initial Public Offer and Further Public Offer

Points	Initial Public Offer	Further Public Offer
1. Meaning	IPO refers to an offer of securities by an unlisted Public Company to the public for the first time.	FPO means an offer of securities by a listed Public Company to the public to raise subsequent capital.
2. Type of issuer company	It is issued by an unlisted Public Company.	It is issued by a listed Public Company.
3. When issued	It is usually issued by an existing company which wants to raise capital from the public for the first time.	It is usually issued by a listed Public company when it wants to raise further capital from the public.
4. Order of issue	IPO preceeds FPO. IPO is the first time sale of shares to the public.	FPO is always done after IPO. FPO is the second or subsequent sale of shares to the public.

Points	Initial Public Offer	Further Public Offer
5. Listing	Company has to get itself listed for the first time before issuing IPO.	Company making an FPO is already a listed company.
6. Risk	It is very risky for the investor as he cannot predict the company's performance.	It is less risky for the investor as he has an idea of the company's past performance and can judge its future performance.

2. Fixed Price Issue Method and Book Building Method.

Points	Fixed Price Issue Method	Book Building Method
1. Meaning	Under this method, the issue price of shares is mentioned in the prospectus and investors have to buy shares at that price only.	Under this method, the issue price is determined by a bidding process. The investors are given a price band and are asked to bid at a price within the band. This way company arrives at a price at which it will sell its shares.
2. Price of Shares	The exact price of shares is known in advance and it is mentioned in the prospectus.	The price of shares is not known in advance. Only the minimum price and maximum price at which the company is willing to sell the shares is known in advance.
3. Prospectus	Company has to issue a prospectus and it contains the details of price at which shares are offered and the total number of shares offered by the company.	Company issues a Red Herring Prospectus. It contains only the price band and the total size of issue.
4. Determination of Demand	Company comes to know the public demand for its shares only after closure of the issue	Company can know the public demand for its shares everyday. The bids are registered in the book everyday till the closure of the issue.
5. Payment of Application Money	Application money or entire money has to be paid by the investor at the time of submitting his application for shares.	Only application money has to be paid at the time of bidding. Money will be collected only after the issue price has been fixed.
6. When Used	It can be used for any issue i.e. Public Issue, Rights Issues, ESOS, etc.	It is usually used in Public issues i.e. IPO and FPO.

3. Rights Shares and Bonus Shares :

Points	Rights Shares	Bonus Shares
1. Meaning	In rights issue, shares are offered to the existing equity shareholders i.e. Company offers the shareholders the first option to buy the shares of the company.	Bonus shares are issued to the existing equity shareholders free of cost.
2. Payment	Subscribers have to pay for the Rights Shares. Company only gives them a right to buy these shares.	Bonus shares are issued free of cost to the shareholders.
3. Partly / fully paid up shares	Shareholders have to pay for these shares as Application Money, Allotment, Call Money etc. till the full money on shares is paid up.	Bonus shares are fully paid up shares. So no money has to be paid by the shareholders to the company.
4. Minimum Subscription	Company has to obtain minimum subscription. If the company fails to receive minimum subscription, it has to refund the entire application money received.	There is no minimum subscription to be collected as Bonus shares are issued free of cost by the company.
5. Right to Renounce	The shareholders can renounce his shares.	Shareholders cannot renounce his bonus shares.
6. Purpose of Issue	Rights issue is done by a company when it wants to raise fresh funds but wants to give a chance to their existing members to increase their shareholding.	When company has accumulated huge profits or reserves and company wants to reward its existing Equity shareholders, company issues Bonus shares.

4. Transfer of Shares and Transmission of Shares :

Points	Transfer of Shares	Transmission of Shares
1. Meaning	Transfer of shares means voluntarily or deliberately giving away one's shares to another person by entering into a contract with the buyer.	It means transfer of ownership of a member's shares to his legal representative due to operation of law. It takes place on death, insolvency or insanity of the members.
2. When done	It is done when the member wants to sell his shares or give his shares as gift.	It is done when the member dies or becomes insolvent or insane.

Points	Transfer of Shares	Transmission of Shares
3. Nature of Action	It is a voluntary action taken by the member.	It is an involuntary action. It is due to operation of law.
4. Parties involved	In transfer of shares there are two parties involved- the member who is called as transferor and the buyer who is called as transferee.	There is only one party e.g. the nominee of the member in case of death of the member or the legal representative.
5. Instrument of transfer	Transfer requires Instrument of transfer. It is a contract between the transferor and transferee.	No Instrument of transfer is needed.
6. Initiated by	Transferor initiates the transfer process.	Legal representative or official receiver initiates the process of transmission.
7. Consideration	Transfer of shares is done often by the member to receive some consideration (money) i.e. the buyer has to pay for the shares. (Except given as gift.)	No consideration is involved here. The legal heir or official receiver need not pay for the shares.
8. Liability	The liability of the transferor ends after the shares are transferred.	Original liability of the member continues in case of transmission of shares.
9. Stamp Duty	Stamp duty as per the market value of shares has to be paid.	No stamp duty is to be paid

SUMMARY

- Share capital refers to the capital made up of Equity Shares and Preference Shares.
- Share capital can be classified as :
  - i) Authorised / Nominal / Registered Capital - Means maximum capital authorised by Memorandum of Association that a company can collect.
  - ii) Issued and Unissued Capital : Issued capital refers to capital offered by a company to the investors. Unissued Capital is part of authorised capital not offered to the public.
  - iii) Subscribed and Unsubscribed Capital : Subscribed capital is the capital bought by the investors. Unsubscribed capital refers to the capital not subscribed by investors.
  - iv) Called up capital and Uncalled capital : Called up capital means the amount demanded by the company on shares issued by it. Uncalled capital means amount on shares not demanded by company.
  - v) Reserve Capital - Capital which is called up (demanded) only at the time of winding up of a company.
  - vi) Paid up capital and Calls in arrears : Paidup capital is the amount actually paid by the shareholders. Amount not paid by the shareholder is called as calls in arrears.

- Methods of issue of shares :
    - **Public Issue -** Means shares offered to public by a company through prospectus.
    - **Fixed price Issue Method -** the price of shares is stated in the prospectus.
    - **Book Building Method -** the price of shares is determined through a bidding process. Red Herring prospectus is issued.
    - **Initial Public Offer -** A new company or an existing company offering its shares to the public for the first time.
    - **Further Public Offer -** when a company issues shares to the public after an IPO.
    - **Rights Issue/Shares -** When a company wants to raise further capital and first offers the shares to its existing Equity shareholders.
    - **Bonus Issue/shares -** are fully paid up shares issued free of cost to the existing Equity shareholders.
    - **Employees Stock Option Scheme (ESOS) -** Scheme wherein permanent employees, directors, etc. are offered the right to purchase equity shares at a price lower than the market price but at a future date.
    - **Employee Stock Purchase Scheme (ESPS) -** Company offer shares at a discounted price but the price of shares is deducted on a regular basis from employee's salary.
    - **Stock Appreciation Rights Scheme (SARS) -** Scheme where the employees are given a right to receive appreciation in value of specified number of shares of the company at a future date.
    - **Sweat Equity Shares -** are shares issued to directors or employees at a discount or for consideration other than cash.
    - **Private Placement -** Company offers its securities to a select group of persons not exceeding 200.
    - **Preferential Allotment -** Company offers Equity shares or securities convertible into Equity shares to a select group of persons on preferential basis.
- **Allotment of Shares -** Means distributing shares to those applicants who have submitted the share application form along with the application money.
- **Share Certificate -** is a document issued by company to every shareholder. It is evidence of title to shares.
- **Calls on shares -** When a company demands the members to pay the balance unpaid money on shares besides the Application Money and Allotment Money.
- **Forfeiture of Shares -** means forcefully taking away of shares of a member for not paying Calls on Shares. It leads to cessation of membership.
- **Surrender of Shares -** When a member voluntarily gives away shares to the company as the member is not able to pay calls on Shares.
- **Transfer of Shares -** when a member voluntarily transfers shares to another person for monetary reasons or gives it as a gift to another person.
- **Transmission of shares -** When transfer of shares takes place due to death, insolvency or insanity of a member.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. .... refers to capital made up of Equity and preference shares

   a) Share capital b) Debt capital c) Reserve fund

2. .... capital refers to maximum capital a company can raise by issuing shares.

   a) Issued b) Authorised c) Paid up

3. .... means shares are offered to the public.

   a) Rights Issue b) Private Placement c) Public Issue

4. Under .... method, issue price of shares is based on bidding.

   a) Book Building b) Fixed Price c) Bonus Issue

5. In ...., shares of a company are offered to the public for the first time.

   a) Further Public Offer b) Initial Public Offer c) Public Offer

6. .... is offered to existing equity shareholders.

   a) IPO b) ESOS c) Rights Issue

7. Bonus shares are issued free of cost to ....

   a) existing Equity shareholders b) existing employees c) Directors

8. .... are offered to permanent employees, Directors and Officers of a company.

   a) Bonus Shares b) Rights Issue c) ESOS

9. Under ...., a company offers its securities to a select group of persons not exceeding 200.

   a) Private Placement b) IPO c) Public Offer

10. The .... have the power to allot shares.

    a) Director b) Board of Directors c) Company Secretary

11. Letter of .... is sent to applicants who have been given shares by the company.

    a) Regret b) Renunciation c) Allotment

12. .... is a proof of title to Shares.

    a) Share Certificate b) Register of Member c) Letter of Allotment

13. The gap between two calls should not be less than ....

    a) 14 days b) One month c) 21 days

14. Company can .... shares on non-payment of calls.

    a) forfeit b) surrender c) allot

15. Voluntarily giving away one's share to another person is called as .... of shares.

    a) Transfer b) Transmission c) Surrender

16. .... of shares takes place due to operation of law.

    a) Forfeiture b) Allotment c) Transmission

B) (I) Match the pairs.

Group 'A'		Group 'B'	
a)	Death of member	1)	Forfeiture of shares
b)	Voluntary return of shares to company by member	2)	Book Building Method
		3)	Offered to existing employees
c)	Price of shares mentioned in prospectus	4)	Surrender of shares
		5)	Transmission of shares
d)	ESPS	6)	Non-allotment of shares
e)	Regret Letter	7)	Offered to existing Equity shareholders
		8)	Transfer of shares
		9)	Fixed price issue method
		10)	Allotment of shares

B) (II) Match the pairs.

Group 'A'		Group 'B'	
a)	Issued capital	1)	Non-payment of calls
b)	FPO	2)	Any issue after IPO
c)	Bonus shares	3)	Offered to existing employees
d)	Issued within two months of allotment of shares	4)	Capital offered to public to subscribe
		5)	Share certificate
e)	Forfeiture of shares	6)	First time issue of shares
		7)	Free shares issued to existing equity shareholders
		8)	Maximum capital a company can raise
		9)	Allotment Letter
		10)	Operation of law

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. Capital collected by way of issue of Equity and Preference shares.
2. Part of issued capital subscribed by investors.
3. Capital that will be collected only at the time of winding up of a company.
4. Highest bid price in Book Building method.
5. Offering of shares by a company to the public for the first time.

6. Subsequent issue of shares after an IPO.
7. Pre-emptive right given to existing Equity shareholders to subscribe to new issue of shares by company.
8. It is also called as 'Capitalisation of Profits'.
9. Appropriation of shares to an applicant.
10. Committee set up to decide the formula for allotment of shares in case of over subscription.
11. Minimum amount to be collected from subscribers within thirty days of issue of prospectus.
12. Document which is a prima facie evidence of ownership of certain shares of a company.
13. Penal action taken by company on non-payment of calls.
14. Person to whom transferor is transferring the shares.
15. Transfer of shares due to operation of law.

D) State whether the following statements are true or false.

1. Only fully paidup shares can be forfeited.
2. The member transferring shares is called as transferor.
3. Share certificate is issued for partly or fully paid up shares.
4. Allotment of shares must be done within one month of receipt of application money.
5. Sweat Equity shares are offered to Directors or employees of a company.
6. Bonus Shares are issued at a discounted price to the Equity shareholders.
7. Floor price is the highest bid price under Book Building method.
8. Calls not paid by shareholder is called as calls in arrears.
9. Shares not offered to the public for subscription is called as subscribed capital.
10. Authorised capital is mentioned in capital clause of Memorandum of Association.

E) Find the odd one.

1. Authorised capital, Equity share capital, Issued capital, Paidup capital.
2. ESOS, ESPS, Rights Shares, Sweat Equity.
3. Floor Price, Cap price, Cut-off price, Face Value.
4. Bonus shares, Rights Shares, ESOS.
5. Allotment of shares, Forfeiture of shares, Surrender of shares.

F) Complete the sentences.

1. Share capital refers to capital made up of Equity shares and ....
2. Reserve capital is part of ....
3. Transfer of shares due to death, insolvency or insanity of member is called ....
4. The two parties involved in transfer of shares are transferor and ....
5. Voluntarily giving up of shares by a member due to inability to pay calls is called as ....

6. Company can forfeit only .... paid shares.
7. In case the original Share Certificate is torn or mutilated, company can issue ....
8. In case of transfer of shares, company has to issue to the transferee a new share certificate within ....
9. Letter sent to applicants for informing them shares are allotted is called as ....
10. When applications received are more than the number of shares offered, it is called as ....
11. In Book Building Method, the final price at which shares are offered to investors is called as ....
12. Shares issued free of cost to existing Equity shareholders is called as ....

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Public offer of shares	1)	....
b)	....	2)	Initial Public offer
c)	Rights Issue	3)	....
d)	....	4)	ESOS
e)	Operation of law	5)	....

(First time offer of shares, Shares offered to public, Shares offered to existing Equity shareholders, Shares offered to existing employees, Transmission of shares)

H) Answer in one sentence.

1. When does transmission of share take place ?
2. Name the parties involved in transfer of shares.
3. What is the time limit to issue share certificate on allotment of shares ?
4. What is the time limit for filing Return of Allotment with the Registrar on allotment of shares ?
5. When can a company forfeit shares ?
6. What is a share certificate ?
7. What is the minimum application money to be collected by company as per the Companies Act ?
8. With whom should the prospectus be filed before issuing it to the public ?
9. What is meant by private placement ?
10. To whom is Sweat Equity Shares offered by a company ?
11. To whom can a company issue Bonus Shares ?

12. What is the subsequent issue after IPO called as ?
13. Name the method under which the issue price of shares is fixed through a bidding process.
14. What is Public Issue ?
15. Name the capital which is mentioned in the capital clause of Memorandum of Association.

I) Correct the underlined word/s and rewrite the following sentences.

1. Issued capital is the maximum capital which a company can raise by issuing shares.
2. Under Fixed price issue method, the price of shares is fixed through bidding process.
3. FPO refers to offering of shares to the public for the first time.
4. Only fully paid up shares can be forfeited.
5. Bonus shares are offered to existing employees of a company.
6. Company enters into an underwriting agreement with the shareholders.
7. Letter of Allotment is sent to applicants when no shares are allotted to them.
8. Duplicate share certificate must be issued within one month from date of application.
9. Call money cannot exceed 5% of nominal value of shares.

J) Arrange in proper order.

1. a) Forfeiture of shares.
   b) Calls on shares.
   c) Allotment of shares.
2. a) Share certificate
   b) Allotment letter
   c) Application form
3. a) Return of allotment
   b) Application form
   c) Minimum subscription

Q.2 Explain the following terms/concepts.

1. Transmission of shares
2. Bonus shares
3. Allotment of shares
4. Employees Stock Option Scheme
5. Surrender of shares
6. Sweat Equity shares
7. Share certificate
8. Authorised capital
9. Forfeiture of shares
10. Paidup capital
11. Calls on shares
12. Subscribed capital
13. Minimum subscription
14. Transfer of shares
15. Initial Public Offer
16. Blank transfer
17. Further Public Offer
18. Forged transfer
19. Rights Issue
20. Private placement

Q.3 Study the following case/situation and express your opinion.

1. Eva Ltd. Company's capital structure is made up of 1,00,000 Equity shares having face value of ₹ 10 each. The company has offered to the public 40,000 Equity shares and out of this, the public has subscribed for 30,000 Equity shares. State the following in ₹.

   a) Authorised capital

   b) Subscribed capital

   c) Issued capital

2. TRI Ltd. Company is newly incorporated public company and wants to raise capital by selling Equity shares to the public. The Board of Directors are considering various options for this. Advise the Board on the following matters :

   a) What should the company offer - IPO or FPO ?

   b) Can the company offer Bonus Shares to raise its capital ?

   c) Can the company enter into Underwriting Agreement ?

3. Silver Ltd. Company has recently come out with its public offer through FPO. Their issue was over subscribed. The Board of Directors now wants to start the allotment process. Please advise the Board on :

   a) Should the company set up allotment committee ?

   b) How should the company inform the applicants to whom the company is alloting shares ?

   c) Within what period should the company issue share certificate ?

4. Red Tubes Ltd. has made a demand on its shareholders to pay the balance unpaid amount of ₹ 20/- per share (having a face value of ₹ 100) held by them. The company has sent letters asking the shareholders to pay the money to its Bankers within the specified time.

   a) Are the shareholders liable to pay ₹ 20 for the shares held by them ?

   b) Name the letter sent by the company to its shareholders asking them to pay ₹ 20/-

   c) What happens if a shareholder fails to pay the money within the specified time ?

5. X owns 100 shares while Y owns 500 shares of Red Tubes Ltd. The company has asked all its shareholders to pay the balance unpaid amount of ₹ 20. X pays the full money demanded by the company. Y, who is in a bad financial position is unable to pay any money.

   a) Can the company forfeit the shares of Y ?

   b) Can the company forfeit the shares of X ?

   c) Can X transfer his shares ?

Q.4 Distinguish between the following.

1. Initial Public Offer and Further Public Offer
2. Fixed Price Issue and Book Building

3. Rights Shares and Bonus Shares
4. Transfer of Shares and Transmission of Shares

Q.5 Answer in brief.

1. What is Book Building Method ?
2. State the provisions for Rights Issue.
3. State the provisions related to Bonus Shares.
4. State the general principles / rules for allotment of shares.
5. State the contents of Shares Certificate.
6. What are the effects of forfeiture of shares ?
7. When can the Board of Directors refuse transfer of shares ?
8. Explain Employee stock option scheme.
9. What is calls on shares ?
10. What is transfer of shares ?

Q.6 Justify the following statements.

1. Company has to fulfill certain provisions while making Right Issue.
2. To Issue Bonus Shares, a company has to fulfill certain provisions.
3. ESOS is offered by a company to its permanent employees, Directors and Officers.
4. Company has to fulfill general principles/rules for allotment of shares.
5. A company can issue duplicate share certificate.
6. Board of Directors have the authority to forfeit shares.
7. A member of a Public company can transfer shares.
8. The Board of Directors can refuse transfer of shares.

Q.7 Answer the following questions.

1. Explain the classification of share capital.
2. Explain the two methods a company can use to make its public offer of shares.
3. Explain briefly the different types of shares offered by a company to its existing Equity shareholders.
4. Explain the statutory provisions for allotment of shares.
5. Explain briefly the procedure for allotment of shares.

❑❑❑

4 ISSUE OF DEBENTURES

4.1 Regulations governing issue of debentures.

4.1.1 Provisions for issue of Debentures as per Companies Act, 2013

4.1.2 Provisions for issue of Debentures as per Companies (Share capital and Debentures) Rule 2014

4.1.3 Requirements as per SEBI

4.2 Procedure for issue of Debentures

4.3 Debentures Trustees

INTRODUCTION :

Companies prefer issuing debentures to raise funds as they can be repaid after a long period. A company can make public issue of debentures only if :

1) The company or its promoters or its Directors have not been prohibited from accessing the securities market by SEBI.
2) The company or its promoters or its Directors have not been declared as a willful defaulter or has not defaulted in repaying any principal or interest on any debt securities for a period of more than 6 months.

In this chapter, we will learn about the various regulations or provisions related to issue of debentures and the procedure for issuing debentures.

4.1 REGULATIONS GOVERNING ISSUE OF DEBENTURES

A company issuing debentures has to comply with the provisions of the Companies Act, 2013, Companies (Share Capital and Debentures) Rules, 2014, RBI Guidelines and SEBI's various regulations.

Depending upon the type of Debenture, Company has to fulfill the following provisions/ regulations :

Act/Regulations/Guidelines	Provisions
1) Companies Act, 2013, Section 71	→ Contains provisions for issue of Debentures.
2) Companies (Share Capital and Debentures) Rules 2014, Rule-18.	→ Contains provisions for issue of secured debentures.
3) SEBI (Issue and Listing of Debt Securities) Regulations, 2008.	→ Covers provisions for issue and listing of Debentures which are not convertible, either into wholly or partly into Equity shares. It is applicable if debentures are issued through public offer, private placement and for listed debentures. As per these provisions company has to follow disclosure requirements as applicable to public issue of equity shares.

Act/Regulations/Guidelines	Provisions
4) SEBI (Issue of Capital and Disclosure Requirement) Regulations, 2009	→ Provisions for issue of debentures and listing of debentures that are convertible, either partially, fully or optionally into listed or unlisted equity shares. As per these provisions, a company has to follow the same disclosure norms as applicable to equity shares.
5) SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.	→ Provisions which a listed company issuing non-convertible debentures, Perpetual debt instruments, etc. has to fulfill. The provisions relate to the various listing conditions which a company has to comply with.
6) RBI Guidelines	→ Meant for banks which raise capital by issuing non-equity instruments.

A company can issue secured as well as unsecured debentures. It can issue non-convertible debentures or debentures which can be converted fully or partly into equity shares. All debentures, are redeemable i.e. have to be repaid. Company can issue debentures to its members or make a public offer or offer it even through private placement.

Company can also list its debentures on Stock Exchanges.

The Board of Directors of a company has the authority to issue debentures. However, the Board can use their borrowing powers only up to the limit permitted by the Articles of Association. If in case, the Board wants to increase its borrowing powers, they have to get the approval of shareholders in a general meeting through a special Resolution.

Provisions For The Issue of Debentures as per

Companies Act, 2013	Companies (Share Capital and Debentures) Rules 2014	SEBI Regulation
1. No voting rights	1. Tenure of secured Debentures	1. Minimum Subscription
2. Types of Debentures	2. Create charge on Assets	2. Retention of over subscription
3. Payment of Interest and Redemption.	3. Appointment of Debenture Trustees.	3. Underwriting.
4. Debenture Certificate	4. Create Debenture Redemption Reserve.	4. Credit Rating.
5. Create Debenture Redemption Reserve		
6. Appoint Debenture Trustees		

Companies Act, 2013	Companies (Share Capital and Debentures) Rules 2014	SEBI Regulation
7. Debenture Trustees can approach NCLT (National Company Law Tribunal) 8. Impose Restrictions 9. Punishment for contravention of provisions of the Companies Act.		

4.1.1 Provisions for issue of debentures as per Companies Act, 2013.

Following are some of the provisions of the Act which a company has to comply while issuing debentures :

1. **No voting rights :** A company cannot issue debentures with voting rights. Debenture holders are creditors of the company and so they do not have any voting rights except in matters affecting them.
2. **Types of Debentures :** A company can issue secured or unsecured debentures and fully or partly convertible debentures or non-convertible debentures. To issue convertible debentures, a Special Resolution has to be passed in the General Meeting. All debentures are redeemable in nature.
3. **Payment of interest and redemption :** A company shall redeem the debentures and pay interest as per the terms and conditions of their issue.
4. **Debenture Certificate :** Company has to issue Debenture certificate to the debenture holders within 6 months of allotment of Debentures.
5. **Create Debenture Redemption Reserve :** Company has to create a Debenture Redemption Reserve account out of profits of the company available for payment of dividend. This money can be used only for redemption of debentures. As per Companies (Share Capital and Debentures) Amendment Rules 2019, MCA has removed Debenture Redemption Reserve requirement for Listed companies, NBFCs and Housing Finance Companies.
6. **Appointment of Debenture Trustees :** If the company issues prospectus or invites more than 500 people, (either to Public or its Member) company has to appoint one or more Debenture Trustees. Debenture trustees protect the interest of the debenture holders. Company has to appoint trustees by entering into a contract with them called as Debenture Trust Deed.

   > ***Debenture Trustees :*** *They are institutions that protect the interest of Debenture holders.*

7. **Debentures Trustees can approach NCLT :** Debenture Trustees have to redress the grievances of debenture holders. If the company defaults in repaying the principal amount, on maturity or defaults in paying interest there on, the Debenture Trustees can approach

the National Company Law Tribunal for redressal. NCLT can direct a defaulting company to repay the principal amount or interest.

Grievances : Complaints
Redressal : Remedy or compensation.

8. **Impose restrictions :** When the Debenture Trustee is of the opinion that the assets of the company are insufficient or likely to become insufficient to redeem the principal amount of debentures, it may approach the NCLT. NCLT can order a company to restrict incurring further liabilities so as to protect the interest of the debenture holders.

9. **Punishment for contravention of provisions of the Companies Act :** If the company fails to comply with any provisions of the Act, then the company and its officers shall be liable to pay fine or imprisonment or both as prescribed in the Act.

4.1.2 Provisions as per Companies (Share Capital and Debentures) Rules, 2014 (i.e. Rule 18)

If a company issues secured debentures, company must fulfill the following conditions :

1. **Tenure of secured debentures :**
   All secured debentures should be redeemed within 10 years from the date of its issue. Only certain companies like companies engaged in Infrastructure Projects, or companies permitted by the Ministry of Corporate Affairs, Central Govt. or RBI can issue debentures beyond a period of 10 years but not exceeding 30 years.

2. **Create charge on assets :** Company has to create a charge on the assets of the company or its subsidiary company or holding company. The value of charge should be adequate to cover the entire value of debentures issued and interest to be paid on it. If a Government company issues secured debentures which has Central or State Government's guarantee, then it need not create any charge on its assets.

3. **Appointment of Debenture Trustees :** Before issuing prospectus or offer letter, the company has to appoint a Debenture Trustee. Company also has to execute a Debenture Trust Deed. The Deed contains the terms and conditions agreed upon by the company and the Trustees and clearly states the role of the Debenture Trustee.

4. **Create Debenture Redemption Reserve :** Company has to create a Debenture Redemption Reserve account out of the profits available for payment of dividend. Company has to maintain at least 25% of the value of its outstanding debentures in the Debenture Redemption Reserve Account. Company has to invest or deposit on or before 30th April each year, a sum not less than 15% of the amount of its debentures maturing during the year ending on 31st March of the next year. Money from this account is used for redemption of debentures.

4.1.3 Requirements as per SEBI for issue of Debentures :

1. **Minimum subscription :** SEBI (Issue and Listing of Debt securities) Regulation, 2008 Regulation-12 state the minimum subscription to be collected by a company.

   As per SEBI, the minimum subscription for public issue of debentures is 75% of base issue size i.e. ₹ 100 crores. If the minimum subscription is not received, the entire money received should be refunded within 12 days from the date of closure of the issue.

2. **Retention of over subscription :** Company can retain over subscription money up to maximum 100 % of the base issue size or any lower limit as specified in the offer letter or letter of offer or prospectus.

3. **Underwriting :** Company may enter into an underwriting agreement with underwriters for its public issue of debentures. Appointment of underwriters must be mentioned in the offer letter or letter of offer or prospectus.

4. **Credit Rating :** SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 states that companies should get credit rating for issuing debentures.

   As per SEBI, Companies making a public issue or right issue of convertible debentures must obtain credit rating from one or more credit rating agencies. The rating should be mentioned in the offer letter or letter of offer or prospectus.

i) Credit Rating - Rating given to the debt securities by a credit Rating Agency which indicates the credit risk level.

ii) Credit Rating Agency - Agencies like CRISIL, CARE, etc. which rates the credit worthiness of a company issuing debentures, deposits and other debt securities.

Additional Information

CRISIL Rating scale for long Term Debt instruments including debentures.

Rating	Meaning	Rating	Meaning
CRISIL AAA	Highest Safety	CRISIL B	High Risk
CRISIL AA	High Safety	CIRISL C	Very High Risk
CRISIL A	Adequate Safety	CRISIL D	Default
CRISIL BBB	Moderate Safety		

4.2 PROCEDURE FOR ISSUE OF DEBENTURES

1. Pass Resolution in Board Meeting.
2. Hold Extra-ordinary General Meeting (E.G.M.)
3. Filing with Registrar of Companies.
4. Obtain Credit Rating.
5. Enter into Underwriting Agreement.
6. Issue Prospectus / Offer Letter / Letter of Offer
7. Open Separate Bank Account.
8. Receiving Application Money.
9. Hold Board Meeting.
10. Issue of debenture certificate.
11. Make Entries in the Register of Debenture.

Following is the procedure to be followed by a company issuing debentures –

1. **Pass resolution in Board Meeting :** In the Board Meeting following resolution will have to be passed :

   i) amount and type of debentures to be issued and the terms and conditions for issue.

   ii) approve prospectus or offer letter or letter of offer.

   iii) approve appointment of Debenture Trustees and get their written consent.

   iv) authorize Board to create charge on assets of the company.

   v) call Extra-ordinary General Meeting if the Board's borrowing powers need to be increased.

   vi) authorizes Board to open a separate bank account for receiving money from applicants.

2. **Hold Extra-ordinary General Meeting (EGM) :** If the borrowing powers of the Board is to be increased, EGM must be held to get the shareholders' approval through a Special Resolution.

3. **Obtain Credit Rating :** Company gets its debentures rated by one or more Credit Rating Agencies. The ratings must be mentioned in the prospectus/offer letter/Letter of offer.

4. **Filing with Registrar of Companies :** Secretary has to file the Special resolution and copy of Prospectus, offer letter / Letter of offer with Registrar of Companies within 30 days of Board Meeting.

5. **Enter into underwriting agreement :** Company enters into an underwriting agreement for underwriting its debenture issue.

6. **Issue prospectus / letter of offer / offer letter :** Company issues prospectus, if it is inviting the public to buy its debentures. Offer Letter is issued if a company makes private placement and Letter of offer for Rights Issue.

7. **Open Separate Bank Account :** Company opens a separate bank account in a scheduled Bank to receive the money from the applicants.

8. **Receiving application money :** Subscribers will submit their application along with the required amount to the specified bank within the time period mentioned in the prospectus or letter of offer / Offer Letter.

9. **Hold Board Meeting :** After the issue closes, a Board Meeting is held to decide and approve allotment of debentures. Board also approves creation of charges on the company's assets.

10. **Issue of Debenture certificate :** The allotment procedure has to be completed within 60 days from the receipt of application money. Company has to issue Debenture certificate within 6 months of allotment of debentures.

11. **Make entries in Register of Debenture holders :** Secretary has to make entries in the Register of Debenture holders within 7 days after the Board approval of allotment. However, if debentures are issued in demat form, company does not maintain the Register of Debenture holders.

4.3 DEBENTURE TRUSTEES :

A company which issues prospectus or invites more than 500 persons to buy its debentures has to appoint one or more Debenture Trustees. Companies issuing secured debentures also must appoint Debentures Trustees.

Debentures Trustees are institutions which protect the interest of the debenture holders. The company creates a charge on its movable or immovable assets or assets of its subsidiary company or holding company. Charge is created in favour of the Debenture Trustees. The Trustees become the custodian of the assets on which charge has been created.

Debenture Trustees are appointed before prospectus or letter of offer/offer letter is issued. The Trustees must give a written consent to act as Debenture Trustees. The prospectus or letter of offer/offer letter must mention the names of Debenture Trustees.

Debenture Trust Deed :

Company enters into a contract with one or more Debenture Trustees. The terms and conditions of the agreement is written in the Debenture Trust Deed. It is a legal instrument conveying the assets of a company to the Trustees.

The Deed also defines the rights of debenture holders and the duties and powers of Debenture Trustees. Company has to execute the Deed within 3 months of closure of the issue. Members as well as debenture holders can inspect the deed and also get a copy of it by paying a certain fee.

Activity :

(1) Find out about the Debenture Trustee Services offered by IDBI Trusteeship Service Ltd.

(2) Find out two institutions offering Debenture Trustee Services in India.

SUMMARY

- Companies prefer issuing debentures as they can be repaid after a long time.
- Companies can issue-secured or unsecured debentures, Non-convertible Debentures or convertible debentures either fully or partially convertible or redeemable debentures. Debentures can be listed on stock exchanges.
- Company can issue debentures to its members, public or make private placement.
- Companies have to comply with the provisions as per the companies Act, 2013, Companies/Share Capital and debentures, Rules, 2014 and regulations of SEBI.
- Company appoints one or more Debenture Trustees to protect the interest of Debenture holders. Debenture Trust Deed contains the terms and conditions agreed between the company and Debenture Trustee. Deed is signed within 3 months of closure of the issue.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. A company cannot issue .... with voting rights.

   a) Equity shares   b) Debentures   c) Securities

2. A company can issue .... convertible debentures.

   a) Only partly   b) Only fully   c) Partly or fully

3. Money from .... Account is used for redemption of debentures

   a) Capital   b) Debenture Redemption Reserve   c) Profit or loss

4. .... protects the interest of debenture holders

   a) Debenture Trustees   b) Debenture holders   c) Redemption Reserve

5. Secured debentures must be redeemed within .... from the date of its issue

   a) 10 days   b) 10 years   c) 15 years

6. A company issuing .... debenture must create a charge on the assets of the company.

   a) Secured   b) Unsecured   c) Redeemable

7. Debenture certificate must be issued within .... of allotment of debentures.

   a) 3 months   b) 6 months   c) 60 days

8. The details of allotment of Debentures must be entered in ....

   a) Register of debenture   b) Register of members   c) Register of creditors

9. A company which issues prospectus or invites more than 500 persons to buy its debenture has to appoint ....

   a) Register of companies   b) Debenture holders   c) Debenture trustees

10. The contract between company and Debenture trustees of companies is called as ....

    a) Debenture trust deed   b) Letter of offer   c) Prospectus

11. Procedure for allotment of Debenture should be completed within .... from the date of receipt of applications.

    a) 6 months   b) 3 months   c) 60 days

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Debenture Trustees	1)	Power to issue debentures
b)	Debenture holders	2)	Protects interest of shareholders
c)	Charge on assets	3)	Secured debentures
d)	Board of Directors	4)	NCLT
e)	Debenture certificate	5)	No voting rights
		6)	Unsecured debentures
		7)	Protects interest of debenture holders
		8)	Voting rights
		9)	Proof of ownership of shares
		10)	Issued within 6 months of allotment of debentures

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. Type of resolution needed to issue convertible debentures.
2. Account to be created for redemption of debentures.
3. Institution appointed by company to protect the interest of debenture holders.
4. Period within which secured debentures should be redeemed.
5. Type of debentures on which company has to create a charge on its assets.
6. The document which contains terms and conditions agreed upon by the company and the Debenture trustees.
7. Time period within which the procedure for allotment of debenture is to be completed from the date of receipt of applications.
8. Period within which debenture certificate must be issued by a company.
9. Institution which redresses grievances of debenture holders.
10. Authority which has power to issue debentures.

D) State whether the following statements are true or false.

1. Debenture holders have no voting rights.
2. Company cannot issue non-convertible debentures.
3. Special Resolution is needed to issue convertible debentures.
4. Debentures holders are paid interest.
5. Debenture Trustees can not approach NCLT to redress grievances of debenture holders..
6. All secured debentures should be redeemed within 20 years from date of its issue.
7. Company has to create a charge on its assets when it issues secured debentures.

8. Debenture trustees are appointed to protect the interest of shareholders.
9. Debenture certificate is issued within 6 six months of allotment of debentures.
10. After allotment of Debentures names of Debenture holders are entered in the Register of Members.

E) Find the odd one.

1. Debenture holders, Interest, Dividend.
2. Debenture Trustees, Court, NCLT.
3. Secured Debentures, Convertible debentures, Irredeemable debentures.
4. Debenture trustees, Trust Deed, Shareholders.

F) Complete the sentences.

1. A legal instrument conveying the assets of a company to the Debenture trustees is called ....
2. To protect the interest of Debenture holders, a company appoints ....
3. On receipt of application and money, the procedure for allotment of debentures should be completed within ....
4. Authority to create charge on company's assets is with the ....
5. Secured debentures should be redeemed within ....
6. To stop a company from incurring further liabilities, the Debenture trustee can approach ....
7. A company which issues prospectus or invites more than 500 persons to subscribe for its debentures, has to appoint ....
8. Return on investment on debenture is called ....
9. For public issue of debentures of ₹ 100 crores, minimum subscription should be ....
10. For public issue or rights issue of convertible debentures, as per SEBI, a company must obtain ....

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Debenture Trustees	1)	....
b)	....	2)	Charge on assets
c)	Register of Debenture	3)	....
d)	....	4)	Debenture certificate
e)	No voting rights	5)	....

(Issued within 6 months of allotment, Names of debentureholders, Secured debentures, Trust deed, Debenture holders.)

H) Answer in one sentence.

1. Who are debenture holders ?
2. What do debenture holders receive as return on investment ?
3. Whom does the company appoint to protect the interest of debentureholders ?
4. Within what period should secured debentures be redeemed ?
5. Name the document which is an agreement between the debenture trustee and company.
6. Who has the authority to create charge on assets of a company ?
7. Name the meeting in which approval for increasing the borrowing powers of Board of directors is passed.
8. Within what period should the debenture certificate be issued ?
9. What is the minimum subscription that a company must collect for an issue of debentures of ₹ 100 crores ?
10. When should a company appoint a credit rating agency ?

I) Correct the underlined word and rewrite the following sentences :

1. The details of debentureholders are entered in <u>Register of Members.</u>
2. Secured debentures must be redeemed within <u>15 years</u> from the date of its issue.
3. A company issuing <u>irredeemable</u> debentures must create a charge on assets of the company.
4. Return on investment on debentures is <u>dividend</u>.
5. Debenture Trustees redress the grievances of <u>shareholders.</u>
6. Debenture certificates are issued within <u>3 months</u> of allotment of debentures.
7. Procedure for allotment of debentures should be completed within <u>90 days</u> from date of receipt of applications.
8. To rate its debentures a company appoints <u>underwriters.</u>

J) Arrange in proper order.

1. a. Obtain Credit Rating.
   b. Entry in register of debenture
   c. Receive application with money
2. a. Issue debenture certificate
   b. Issue prospectus
   c. Open bank Account
3. a. Hold Board Meeting for allotment
   b. Issue debenture certificate
   c. Receive application with money

Q.2 Explain the following terms/concepts.

1. Debenture certificate
2. Debenture trustee
3. Charge on assets
4. Debenture trust deed

Q.3 Study the following case / situation and express your opinion.

1. Rose limited company proposes to issue debentures to the public to raise funds. After discussions, the Board of Directors have decided to issue secured, Redeemable non-convertible debentures with a tenure of Ten years. Please advise the board on following matters :

   a. Should the company appoint Debenture trustee ?

   b. Should the company create a charge on its assets ?

   c. Can the tenure of debentures be less than ten years ?

2. Violet Ltd. company plans to raise ₹ 10 crores by issuing debentures. The Board of Directors have some queries. Please advise them on the following –

   a. Can the company issue unsecured debentures?

   b. Can they issue irredeemable debentures?

   c. As the company is offering debentures to its members, can such debentures have normal voting rights ?

3. DDS financial plans to raise ₹ 10 crores by issuing secured, Non-convertible debentures. However, as per the Articles of Association, the Board of Directors has authority only to raise upto 5 crores. They are also considering whether to go for private placement or make public offer. Please advise them on the following –

   a. What can be the maximum tenure of the debentures to be issued ?

   b. Is the proposed issue within the borrowing powers of the Board ?

   c. Within what period should company issue Debenture certificate ?

Q.4 Answer in brief.

1. State any four provisions of Companies Act 2013 for issue of debentures.
2. What is debenture trust deed ?
3. Who are debenture trustees ?

Q.5 Justify the following statements.

1. A company has to create charge on its assets for issuing secured debentures.
2. Debenture trustees is appointed by a company issuing debentures.
3. A company can issue only certain types of debentures.

Q.6 Answer the following questions.

1. Briefly explain the provisions of Companies Act, 2013 for issue of debentures.
2. Explain briefly the procedure for issue of debentures.

❑❑❑

5 DEPOSITS

5.1 Acceptance of deposits

5.2 Terms and conditions for acceptance of deposits

5.3 Procedure for accepting deposits from public

5.4 Procedure for accepting deposit from Members

INTRODUCTION :

Accepting deposits from the public or from its own members is one of the sources of raising funds for a company. It is cheaper to raise funds through deposits. Moreover, there is no dilution of control as it is a type of short term loan taken by the company. However accepting deposits can be a risky option for a company in case it defaults in repaying the deposits. (Meaning and definition of Public Deposit was discussed in chapter 2.) In this chapter we will learn which companies can collect deposits, the terms and conditions to be fulfilled and the procedure to collect deposits from members and public.

5.1 ACCEPTANCE OF DEPOSIT.

All companies, accepting deposits, except :

i) A Banking Company

ii) A Non-Banking Finance Company (NBFC)

iii) A Housing Finance Company and,

iv) Such other company as the Central Government will specify have to comply with the provisions of (a) Section 73 to 76 of Companies Act, 2013 (b) Companies (Acceptance of Deposits) Rules 2014 and (c) Directives issued by Reserve Bank of India regarding acceptance of deposits.

Directives : Official instruction.

Following chart shows which companies can collect deposits from members and from public.

Acceptance of Deposits

- From Members
  - Private company
  - Public company (other than eligible company)
  - Eligible Public Company
- From Public
  - Eligible Public Company
  - Government Company

- **Private Company :** A private company can accept deposits from its members or Directors or relatives of Directors.
- **Public Company (Other than eligible company) :** These companies can accept deposits from its members or directors.
- **Eligible Public Company :** These companies can accept deposits from their members and also from the public. Eligible public company means a company having :

  a) A Net worth of not less than ₹ 100 crores or,

b) Turnover of not less than ₹ 500 crores and which has obtained prior approval of its shareholders through special resolution for accepting public deposits.

> *i) Net worth = Total of paid up capital + Free Reserves + Securities Premium Account after deducting accumulated losses deferred expenses and miscellaneous expenses not written off.*
>
> *ii) Turnover - Income from sales for a particular period.*

5.2 TERMS AND CONDITIONS FOR ACCEPTANCE OF DEPOSITS :

1. Amount of Deposit :

A) Private Company : A Private Company can accept deposits from its members or Directors or Relatives of Directors not more than 100 percent of its aggregate of paid up share capital and free reserves.

However, certain class of Private Companies as specified by the Companies Act, can accept deposits more than 100 percent of its aggregate of paid up share capital and free reserves.

B) Public Company (other than Eligible Company) : These Companies cannot accept fresh deposit from members if the amount of such deposits together with the previous deposits exceeds 35% of the aggregate of the paid up share capital and free reserves of the company.

C) Eligible Public Company :

Eligible Public Company :

From the Members	From Public
Cannot accept fresh deposits if the amount of such deposits together with the previous deposits exceeds 10% of aggregate of paid up share capital and free Reserves.	Cannot accept fresh deposits if the amount of such deposits together with the previous deposits exceeds 25% of aggregate of paid up share capital and free Reserves.

D) Government Company can accept deposits from public not exceeding 35% of the paid up share capital and free reserves of the company.

2. Period / Tenure of Deposit : No deposit can be accepted or renewed which is to be repaid within a period of six months or more than thirty six months.

In certain circumstances, a company may accept deposits repayable earlier than six months to meet its short term needs. Such deposits must have a tenure of minimum three months and the amount of such deposits cannot be more than 10% of aggregate of the paid up share capital and free reserves of the company. Under certain circumstances, on the request of the depositor, company makes premature repayment of deposits. Company may also renew its deposits with the same terms of issue and it will be considered as fresh deposits.

3. No demand deposit : Company cannot accept or renew deposits repayable on demand.

4. Secured or Unsecured Deposit : A company can accept secured or unsecured deposit which should be clearly mentioned in the circular or advertisement inviting deposits. If a company offers secured deposits, it has to create a charge on its tangible assets within 30 days of acceptance of deposits.

5. **Application Form :** A company has to provide application form. It should contain a declaration by the applicant that the deposit he is making is not made out of any money borrowed by him from another person.

6. **Joint names :** Company can accept deposits in joint names of depositors. But there should not be more than 3 names.

7. **Nomination :** Every depositor at any time, has the right to nominate any person as nominee in the event of death of the depositor.

8. **Circular or Advertisement :** If a company invites deposits from its members, it issues a circular. But if it invites deposits from the public, company has to issue an advertisement.

   a) Contents of circular or advertisement :

      i) Statement about the financial position of the company

      ii) The portion of secured and unsecured deposit of fresh issue

      iii) Credit rating obtained from a Credit Rating Agency (only for eligible public company)

      iv) Details of the scheme

      v) Name of Deposit Trustees

      vi) Amount due towards deposits of any previous deposits accepted by company

   b) Filing of circular or advertisement with Registrar of Companies :

      Company has to file a copy of circular or Advertisement signed by all directors with the Registrar of Companies.

   c) Issue of circular or Advertisement : Only after 30 days of filing a copy of circular or Advertisement with the Registrar of Companies, the company can issue the circular or advertisement.

      Company can send the circular to the members through registered post, speed post or as email.

      For inviting the public, company has to publish the advertisement in one English newspaper and one vernacular newspaper having wide circulation in the state where the company's registered office is located.

   d) Validity of circular or advertisement : The circular or advertisement is valid for 6 months from the end of the financial year in which it was issued or the date on which the Annual General Meeting was held, whichever is earlier.

9. **Appointment of Deposit Trustee :** When issuing secured deposits, eligible companies and public companies have to appoint one or more Deposit Trustees. The Trustees protect the interest of the depositor in case a company defaults in repaying the depositors. Company signs a contract with the Deposit Trustees called as Trust Deed. It contains the terms and conditions of the contract. The deed has to be signed at least 7 days before issuing the circular or advertisement.

   The Deposit Trustee on its own or on the request of one tenth of depositors, can call a meeting of all depositors when a company defaults in repaying deposits.

10. **Create charge on assets :** A Company accepting secured deposits from public, within thirty days of acceptance, has to create a charge on its tangible assets for an amount not less than the amount of deposits accepted. The minimum amount of security should be equal to the amount not covered by Deposit Insurance.

    The Security is created in favour of the Deposit trustees.

11. **Deposit Insurance :** A company needs to take Deposit Insurance at least 30 days before issue of circular or advertisement. If the amount of Deposit plus interest on it is up to ₹ 20,000, insurance is to be taken.

12. **Obtain credit rating :** Every company has to get credit rating of its deposits and include the ratings in the circular or advertisement. The Credit Rating Agency considers the net worth of the company, liquidity position, ability to repay deposits on time etc. and accordingly gives a rating. Rating shall be obtained every year during the tenure of the deposits.

13. **Open Deposit Repayment Reserve Account :** Every company accepting deposits, has to open in a scheduled Bank, a Deposit Repayment Reserve Account. Every year, on or before 30th April, company has to deposit an amount not less than 20% of the amount of deposits maturing during the current year and following financial year. This account can be used only for repaying deposit.

    Scheduled Banks : *Scheduled banks are included in the second schedule of RBI Act, 1934. These banks satisfy certain criteria laid by RBI and enjoy certain facilities of RBI. e.g. Scheduled banks are SBI, Bank of India, Dena Bank, etc.*

    Note : Point 8 (a) and (b), 10 and 13 is not applicable to private companies which accepts deposits from its members not exceeding 100% of aggregate of its paid up capital and Free Reserves.

14. **Deposit Receipt :** Company has to issue Deposit Receipt to the depositors within twenty one (21) days from date of receipt of money or realization of cheque. The receipt has to be signed by the officer duly authorized by the Board of Directors. The Receipt contains the name and address of the depositor, amount of deposit, rate of interest payable and date on which it is repayable etc.

15. **Register of Deposit :** A company has to maintain a separate Register for deposits accepted or renewed at its registered office. The details of the deposit along with the details of the depositors should be entered in the Register of Deposits within seven days from the date of issue of Deposit Receipt.

16. **Return of Deposit :** A company has to file, on or before 30th June every year, with the Registrar of Companies a Return of Deposit. The Return gives details of deposits with the company as on 31st March of that year.

17. **Interest :** The maximum rate of interest on deposits depends upon guidelines given by Reserve Bank of India from time to time. In case of premature repayment of deposits, company can deduct 1% interest from the rate of interest stated at the time of acceptance of deposit.

    For deposits matured and claimed but remains unpaid by company, the company has to pay a penal rate of interest at the rate 18% for the overdue period.

18. **Right to alter the Terms and Conditions :** A company cannot either directly or indirectly alter the terms and conditions of the deposit, Deposit Trust Deed and Deposit Insurance contract, once the circular or advertisement is issued and deposits are accepted by the company.

19. **Disclosure in financial statements :** A company has to disclose in its financial statement, by way of notes, the money received from Directors (or relatives of Directors, in case of a private company).

20. **Punishment :** As per the Companies Act, an officer of the company who is in default for contravention of the provisions of the Act is punishable for fraud.

    The Maharashtra Government has passed the Maharashtra protection of Interest of Depositors (in Financial establishments) Act, 1999 to protect the interest of depositors. Companies in Maharashtra will be punished for contravening the provisions of this Act also.

> ***Additional Information :***
>
> ***Difference between Loans and Public Deposits :*** *Loans - Means any sum borrowed by a company. It has to be repaid instantly or when demanded by the lender.*
>
> ***Deposits*** *- Sum borrowed by company but repaid only on fixed maturity date.*

5.3 PROCEDURE FOR ACCEPTING DEPOSITS FROM PUBLIC

Only eligible Public companies can accept deposits from public. Following is the procedure to be followed for accepting deposits from the public :

1. **Hold Board Meeting :** Board meeting is held to pass a resolution to accept deposits from public. The details of amount of deposit, terms and conditions of issue, etc. are decided in this meeting. Also the date and time to hold a general meeting of the shareholders to get their approval for collecting deposits is decided in this Board Meeting.

2. **Hold a General Meeting :** Company holds a General Meeting of the shareholders to seek their approval for accepting deposits. A Special resolution is passed and it has to be filed with the Registrar of Companies and if needed with RBI also.

3. **Hold Board Meeting :** Board meeting is held to approve the draft advertisement. All necessary information as needed under the Act should be included in the advertisement. The draft should be signed by majority of Directors of the company.

4. **Appoint Banker :** Company has to appoint a banker where the applicants will be submitting their application form along with deposit money.

5. **Obtain Credit Rating :** Company has to obtain a credit rating from a recognized Credit Rating Agency. This rating should be mentioned in the advertisement.

6. **Appoint Deposit Trustee :** Company has to appoint one or more Deposit Trustees. The Deposit Trust deed contains the terms and conditions agreed upon or between the company and the Trustee. The deed has to be signed at least 7 days before issuing the advertisement.

7. **Take Deposit Insurance :** Company enters into an agreement with the Insurance Company for taking Deposit Insurance. The agreement should be signed at least 30 days before issuing the advertisement.

8. **File a copy of advertisement with Registrar of companies :** A copy of the advertisement has to be filed with the Registrar of Companies. 30 days after filing it with the Registrar the company can publish the advertisement.
9. **Advertisement to the public :** Company has to issue the advertisement after 30 days of filling it with the Registrar of Companies. The advertisement has to be published in one English newspaper and one vernacular newspaper having wide circulation in the state where the company's registered office is located.
10. **Upload the advertisement on the company's website :** After releasing the advertisement to the public, it has to be uploaded on the company's website.
11. **Collect application form and money :** Company informs the banker to collect the application forms along with the deposit money.
12. **Issue Deposit Receipt :** Company has to issue Deposit Receipt within 21 days from the date of receipt of money or realization of cheque.
13. **Create charge on assets :** Company issuing secured deposits has to create a charge on its assets within 30 days of acceptance of deposit.
14. **Make entries in Register of Deposits :** Within seven days from the date of issue of Deposit Receipts, Secretary has to enter the details of deposits collected in the Register of Deposits. The entries have to be verified by authorized officer.
15. **File Return of Deposits with Registrar of Companies :** Company has to file a Return on Deposit before 30th June every year. The return has details of Deposits with company as on 31st March.

5.4 PROCEDURE FOR ACCEPTING DEPOSITS FROM MEMBERS :

The following is the procedure to accept deposits from members :

1. **Hold Board Meeting :** Secretary arranges for a Board Meeting. In the Board Meeting decision regarding amount of deposit, terms of issue of deposit, etc. and date to hold a general meeting to seek shareholders' approval is decided.
2. **Hold a General Meeting :** To seek the approval of share holders for accepting deposits, company holds a general meeting of share holders. The special resolution passed is to be filed with the Registrar of Companies.
3. **Hold Board Meeting :** After getting share holders' approval, a Board meeting is held to approve the draft of circular for inviting applications for deposits from members. The draft should be signed by majority of the Directors of the company.
4. **Appoint Banker :** Company appoints a Banker to collect the application forms and the deposit money.
5. **Obtain Credit Rating :** Company approaches a credit rating agency to rate it's deposit. The rating given by the Agency must be mentioned in the circular.
6. **Appoint Deposit Trustee :** Company appoints Deposit Trustees. The Trust deed is signed at least 7 days before issuing the circular.
7. **Take Deposit Insurance :** Company takes Deposit Insurance at least 30 days before issuing the circular.

8. **File a copy with Registrar of Companies :** A copy of the circular is filed with the Registrar of Companies. After 30 days of filing, the company can issue the circular.

9. **Issue circular to members :** Company has to send the circulars to members after 30 days of filing it with Registrar. It is sent by registered post, speed post or email. Company may even publish the circular in newspapers.

10. **Upload circular on company's website :** An eligible public company has to upload the circular on company's website. Whereas, it is optional for a private company and other public companies.

11. **Collect application form and money :** Company informs the bank to collect the application form along with the deposit money.

12. **Issue of Deposit Receipt :** Company has to issue Deposit Receipt within 21 days from the date of receipt of the money or realisation of cheque.

13. **Create charge on assets :** If a company accepts secured deposits, it has to create a charge on its assets within 30 days of acceptance of deposits

14. **Make entries in Register of Deposits :** Within 7 days from the date of issues of Deposit Receipt secretary has to enter the details of deposits collected in the Register of Depositors. It has to be signed by an authorised officer.

15. **File Return of Deposits :** Company has to file a Return of Deposit before 30th June every year. The Return has details of Deposits with the company as on 31st March.

Activity :

(1) Find out the various credit Rating Agencies in India.

(2) Find out any 5 Top performing companies fixed Deposit ratings given by credit Rating agency.

SUMMARY

- Raising funds through deposits is a cheap source for raising short terms loan for a company. Also there is no dilution of control.
- Private company, Public company (other than eligible company) and eligible public company can collect deposit from its members.
- Eligible public companies and Govt. companies can collect deposits from the public.
- Companies collecting deposits must comply with :
  a. Sections 73 to 76 of Companies Act, 2013.
  b. Companies (Acceptance of Deposits) Rules, 2014.
  c. Directives issued by RBI regarding acceptance of deposits.
- **All companies have to comply with following the terms and conditions for acceptance and renewal of Deposits.**

- **Amount of Deposit**

Type of Company	Collected From	% of paid-up share capital and free Reserve
i. Private Company	Members and Directors	Upto 100%
ii. Public Company (other than eligible company)	Members	Upto 35%
iii. Eligible Public Company	Members and Public	Upto 10% Upto 25%
iv. Government Company	Public	Upto 35%

- **Period / Tenure of Deposit :**
  - Minimum 6 months, maximum 36 months.
  - Premature repayment - after minimum 3 months.
  - Company can also renew Deposit with same terms and conditions of issue.
- Company cannot accept deposits repayable on demand made by depositor.
- Deposit can be secured or unsecured. For secured deposits, a charge on company's tangible assets is created.
- Application form has to be issued by company and must have a declaration by investor.
- Deposit can be in Joint names but not more than 3.
- Nomination can be done at any time by depositor.
- Circular - issued to invite members

  Advertisement - issued to invite public

  (i) Contents - must have all information

  (ii) Filing - with Registrar of companies

  (iii) Issue - after 30 days of filing with Registrar of companies.

  (iv) Validity upto 6 months from the end of financial year of issue or date of AGM, whichever is earlier.
- Deposit Trustee - One or more Deposit Trustees to be appointed by company if it is issuing secured deposits. Trust Deed has to be signed atleast 7 days before issuing circular or advertisement.
- Charge on assets to be created if secured deposit is issued by company within 30 days of acceptance of deposits from public.
- Deposit Insurance to be taken atleast 30 days before issue of circular or advertisement For Deposit + Interest upto ₹ 20,000 – full insurance

  For amounts above ₹ 20,000 – per depositor ₹ 20,000 – Insurance
- Obtain credit Rating from a Credit Rating Agency for its Deposit and mention the rating in circular/ advertisement.
- Open Deposit Repayment Reserve Account in a scheduled Bank - Every year on or before 30^{th} April, company has to deposit minimum 20% of the amount of deposits maturing during the year. This account is used to repay the deposits.

- Issue Deposit Receipt within 21 days from date of receipt of deposit money.
- Register of Deposit - details to be entered within 7 days from date of issue of Deposit Receipt.
- File Return of Deposit on or before 30th June every year with Registrar of companies with details of deposit as on 31st March of that year.
- Interest on (i) premature repayment - 1% less and (ii) deposits matured and claimed but remains unpaid - penal rate of interest of 18% p.a.
- Company cannot alter any terms and conditions of issue of deposits, Trust Deed and Deposit Insurance contract after the issue of Circular / advertisement.
- Disclose in financial statements, as notes, amount received from Directors or Relatives of Directors.
- Officer in default punishable for fraud.

• Company has to follow the prescribed procedure for accepting deposits from the public or from its members.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. Deposit is a type of ....

   a) Owned capital b) Short term loan c) Long term loan

2. Eligible public company and Government Company can collect deposits from ....

   a) It's employees b) Public c) RBI

3. Private company can accept deposits from its member or Directors upto not more than .... % of its aggregate of paid-up share Capital and free reserves.

   a) 100 b) 35 c) 25

4. A .... Company can accept deposits from public not exceeding 35% of its paid-up share Capital and free reserves.

   a) Government b) Private c) Eligible Public

5. Deposit can be accepted for a minimum of 6 months and maximum for .... months.

   a) 36 b) 3 c) 30

6. Company issues .... to invite its members to subscribe for its deposit scheme.

   a) Advertisement b) Circular c) Newspaper

7. Company can issue circular or advertisement for inviting deposits after .... days of filing it with Registrar of Companies.

   a) 30 b) 21 c) 7

8. Company has to appoint .... to protect the interest of depositors.

   a) Debenture Trustees b) Deposit Trustees c) Credit Rating Agency

9. Charge on assets is to be created when a company issues ....

a) Unsecured deposit b) Unsecured Debenture c) Secured deposit

10. Deposit Receipt is issued within .... days of receipt of deposit.

a) 7 b) 30 c) 21

11. For premature repayment of deposit, company deducts .... % of interest.

a)1 b) 18 c) 20

12. Return of deposit must be filed every year on or before ....

a) 30^{th} June b) 31^{st} March c) 30^{th} April

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Private Company	1)	10% of aggregate of paid-up share Capital + free reserves
b)	Deposit Trust Deed	2)	Signed at least 7 days before issuing advertisement
c)	Secured Deposit	3)	Maximum 30 months
d)	Tenure of deposit	4)	Charge on tangible assets
e)	Return of Deposit	5)	100% aggregate of paid-up share capital + free reserves
		6)	File on or before 31^{st} March every year
		7)	Signed 21 days after issuing advertisement
		8)	Maximum 36 months
		9)	Charge on intangible assets
		10)	File on or before 30^{th} June every year

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. A company which can accept deposits from its members, directors or their relatives not exceeding 100% of aggregate of paid up share capital and free reserves.
2. Company which can accept deposits from public up to 35% of its paid-up share capital and free reserves.
3. Minimum tenure of a deposit.
4. Maximum tenure of a deposit.
5. Period within which a company has to create a charge on its tangible assets.
6. Document issued by a company to invite its members to subscribe for its Deposits.
7. Agreement between company and Deposit Trustee.
8. Account that can be used only for repaying deposits.
9. Time within which company has to issue deposit Receipt.
10. Book which contains details of deposits accepted or renewed.

D) State whether the following statements are true or false.

1. Return of deposit must be filed every year on or before 31^{st} March.
2. Eligible public company can collect deposits from its members.

3. Government company can collect deposits from its members.
4. A private company can collect deposits from public.
5. Deposit can be accepted for a maximum of 36 months.
6. Eligible public company can collect deposits from public not exceeding 35% of its paid-up share capital and free reserves.
7. For secured deposits, company has to create a charge on its tangible assets.
8. Deposit Receipt is issued within 21 days of receipt of deposits.
9. Company appoints Credit Rating Agency to protect the interest of depositors.
10. Deposit Trust Deed is an agreement between company and Deposit Trustee.

E) Find the odd one.

1. Private company, Non-Eligible public company, Government company.
2. Deposit Trustee, Deposit Trust Deed, Special Resolution.
3. Appointment of Deposit Trustee, Appointment of Registrar of companies, Appointment of Credit Rating Agency.

F) Complete the sentences.

1. Deposit is a type of .... term loan.
2. Eligible Public company and Govt. Company can accept deposits from ....
3. To collect deposits from public, Eligible public company must have a net worth of not less than ₹ ....
4. A Government company can accept deposits from public not exceeding ....
5. Deposits can be accepted or renewed for a period not less than 6 months and not more than ....
6. Company cannot accept or renew deposits repayable on ....
7. Premature repayment of deposits can be done by a company but not before ....
8. To invite the public to subscribe for its deposits, a company issues ....
9. Agency which gives ratings of the deposits of a company is called ....
10. Account which is used only for repaying deposits is called ....

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Government Company	1)	....
b)	....	2)	Deposits from members
c)	36 months	3)	....
d)	....	4)	Charge on tangible assets
e)	Return of deposit	5)	....

(File on or before 30th June, Private Company, Secured deposits, Deposits from public, Maximum tenure of deposits.)

H) Answer in one sentence.

1. Which companies can accept deposits from public ?
2. What is the maximum deposit the Government company can collect ?
3. What is the tenure of a deposit ?
4. Who are Deposit Trustees ?
5. What is Deposit Trust Deed?
6. When does a company create charge on its tangible assets ?
7. Within what period should a company issue Deposit Receipt ?
8. When should a company file Return of Deposit ?
9. What is Deposit Repayment Reserve Account ?
10. What is Register of Deposit?

I) Correct the underlined word/s and rewrite the following sentences.

1. Government Company can accept deposit from <u>members.</u>
2. Company issues <u>advertisement</u> to invite its members for subscribing to its deposits.
3. Company appoints <u>Credit Rating Agency</u> to protect the interest of Depositors.
4. Deposit Receipt is issued within <u>seven days</u> from date of receipt of deposits.
5. <u>Register of deposits</u> is to be filed with the Registrar of companies on or before 30th June every year.
6. Charge on assets is created when company issues <u>unsecured</u> deposit.
7. Minimum tenure of deposit is <u>36</u> months.

J. Arrange in proper order.

1. a. Appoint Deposit Trustee.
   b. Hold General Meeting.
   c. Create charge on assets.
2. a. File Return of deposit
   b. Issue Deposit Receipt
   c. Issue advertisement.
3. a. Obtain Credit Rating.
   b. Entries in Register of Deposits.
   c. Issue Deposit Receipt.

Q.2 Explain the following terms / concepts.

1. Eligible Public Company
2. Tenure of Deposit
3. Secured Deposit
4. Deposit Trustee
5. Charge on tangible assets
6. Deposit Insurance
7. Deposit Repayment Reserve Account
8. Credit Rating
9. Deposit Receipt
10. Return of Deposit

Q.3 Study the following case/situation and express your opinion.

1. Apple Company Ltd. plans to raise funds through Public Deposits. It's net worth is ₹ 10 Crores.

   a. Can they accept deposits from the public ?

   b. Can they accept deposits which matures after 4 years.

   c. Within what period should the company issue deposit Receipt to it's depositors ?

2. ABC Company Ltd. is an eligible Public Company as per the Companies Act, 2013 with reference to accepting Public Deposits.

   a. Can the company accept deposits in joint names ?

   b. Can the company accept deposits from it's members ?

   c. Can the company issue secured deposits ?

3. Apple Company Ltd. is an eligible Public Company. It plans to raise secured deposits from the public. Please advise its Board on the following.

   a. Does the company need to get shareholders approval for accepting deposits ?

   b. Does the company have to appoint a Debenture Trustee ?

   c. Within what period should the company create a charge on it's assets ?

4. SUN Pvt. Ltd. company wants to raise funds through deposits.

   a. Can the company accept deposits from the public ?

   b. Which document should the company issue to invite deposits ?

   c. What is the maximum period for which they can accept deposits ?

Q.4 Answer in brief.

1. State the amount of deposits that different types of companies can collect by way of deposits.
2. State the contents of circular or Advertisement for Deposit.
3. State the provisions regarding appointment of Deposit Trustee.
4. State any four terms and conditions regarding acceptance of Deposit.

Q.5 Justify the following statements.

1. All companies cannot accept deposits from public.
2. There is a limit or restriction on the amount that a company can collect as Deposits.
3. Company has to fulfill certain provisions related to issue of circular or advertisement.
4. While issuing secured deposits, company has to appoint Deposit Trustee.
5. Companies have to create a charge on their tangible assets while issuing secured deposits.
6. Company issuing deposit must open Deposit Repayment Reserve Account.

Q.6 Answer the following questions.

1. Explain the type of companies that can raise deposits along with the maximum amount they can raise as deposits.
2. Explain the provisions related to circular or advertisement for inviting deposits.

6 CORRESPONDENCE WITH MEMBERS

6.1 Precautions to be taken by the Secretary while corresponding with Members

6.2 Circumstances under which a Secretary has to enter into correspondence with Members.

6.3 Specimen Letters

INTRODUCTION :

Shareholders are the owners who contribute capital for the company.

As a Chief Executive Officer of the company, the Secretary comes into contact with all the Members through correspondence. Secretary acts as a link between the Directors and the Members

The Secretary has to communicate the decisions of the Management and other information to the Members through correspondence.

The Secretary should be very cautious and careful while corresponding with Members of the company.

6.1 PRECAUTIONS TO BE TAKEN BY THE SECRETARY WHILE CORRESPONDING WITH MEMBERS :

The Company Secretary has to correspond with Members on various occasions. While writing various letters, the Secretary should give due respect to the Members, provide complete and correct information.

Thus, writing letters to the Members is a challenging task and it requires skill, knowledge and techniques.

1. **Correct Information :** The Secretary should always provide correct, up-to date and factual information to the Members. Due care should be taken while giving facts and figures.
2. **Lucid Language :** The Secretary must use simple words, simple sentences and adopt convincing style while writing letters to the Members. Technical words, long sentences should be avoided in the letter. It should be easy to understand.
3. **Prompt Response :** The Secretary must be prompt in sending replies to the letters received from the Members. Any questions or queries raised by the members must be promptly replied by the Secretary. Complaint letters should be promptly attended to without any delay.
4. **Secrecy :** The Secretary should not disclose any confidential information of the company to the Members. The Secretary should tactfully answer some letters without giving any secret information of the company.
5. **Politeness (Courtesy) :** A courteous letter shows sympathy, respect and mutual understanding. Politeness means use of courteous language. A complaint letter should be replied politely. Rude language should be strictly avoided while corresponding with Members.

6. **Legal matters :** The Secretary should compulsorily follow relevant provisions of the Companies Act, 2013 with latest amendments and other relevant laws while corresponding with Members. While drafting these letters, if necessary Secretary should consult with legal advisor on certain matters.
7. **Consideration :** The writer should give due importance and consideration to the reader and consider the problems of the member. While sending negative replies, he should draft these letters more carefully, so that Members should not be hurt. Secretary should make the member feel that the management honestly regrets refusal.
8. **Image of the Company :** The Secretary should try to project good image of the company in every situation. While drafting the letters, Secretary has to try his best to remove their doubts, queries and difficulties in a polite and courteous manner.

6.2 CIRCUMSTANCES UNDER WHICH A SECRETARY HAS TO ENTER INTO CORRESPONDENCE WITH MEMBERS

The following are the various occasions when the Secretary writes the letters to the members of the company -

- Allotment Letter
- Regret Letter
- Issue of Share Certificate
- Issue of Bonus Shares
- Execution of Right Issue
- Letter for Payment of Dividend
- Dividend Mandate
- Approval of Transfer of Shares
- Refusal of Transfer of Shares
- Notice and Agenda of General Meeting
- Notice of loss of Share Certificate
- Reply to certain queries raised by the members.
- Letters to legal representatives regarding Transmission of Shares

The following are the few circumstances under which the Secretary enters into correspondence with the members of the company.

1. Letter for issue of Share Certificate
2. Letter for Payment of Dividend through
   a) Dividend Warrant
   b) Electronic Payment of Dividend
3. Letter for issue of Bonus Shares
4. Reply letter to the query of the member on low rate of dividend.

6.3 SPECIMEN LETTERS :

1. **Letter for issue of Share Certificate :** A Share Certificate is a registered document of title to the shares issued by the company under the common seal duly stamped and signed by at least two Directors and countersigned by the Secretary of the company. Every company must issue or dispatch a Share Certificate to the allottee within two months after allotment of Shares.

As per the request of allottee, the company sends the letter for issue of Share Certificate. The letter contains the information about issue of Share Certificate such as Folio No., Share Certificate No., Distinctive No. of Shares, Total No. of Shares etc. According to SEBI's circular companies are required to send Share Certificates by 'Registered Post.'

COMFORT MOTORS LTD.

Registered Office : A/30, Aurora Towers, M. G. Road, Camp,
Pune 411 012.

CIN : U12111 MH 2000 PCL300477

Phone : 020-80032844
Fax : 020-50063015
Ref. No. C/MR-SC/30/19-20

Website : www.comfortmotorsltd.com
E-mail : comfort31@gmail.com
Date : 12th November, 2019

Mr. Jayant Modi
Abhiman Apartment
30, L. B. Road,
Pune - 411 001.

Sub. : Issue of Share Certificate

Dear Sir,

This is to inform you that as per your Request Application No. 50, I am hereby authorised to issue you a Share Certificate. The said Share Certificate will be delivered to you within 15 days from the date of this letter by registered post to your registered address as mentioned in the Register of Members.

Details of issue of Share Certificate are as follows :

1	2	3		4
Folio No.	Share Certificate Number	Distinctive Numbers		Total Number of Shares
		From	To	
1006	9630	301	400	100

It shall always be our endeavour to provide best of our services to you at all time.

Thanking you,

Yours faithfully,
For Comfort Motors Ltd.

Sign
Mr. Anand Swami
Company Secretary

2. **Payment of Dividend :** Dividend is the portion of the profits of the company which is distributed to the Shareholders of the company. Company can declare Final Dividend and Interim Dividend.

Dividend can be paid through Dividend Warrant or in an electronic mode (Electronically by ECS, NEFT etc.) to the registered Shareholder who is entitled to dividend.

Dividend is to be declared and approved by the shareholders at its Annual General Meeting on such a rate as may be recommended by the Board. Interim dividend is declared by the Board of Directors in the middle of the accounting year. Dividend is to be paid to the shareholders within 30 days from the date of declaration.

According to the instructions given by the Board, the Secretary sends a letter to the concerned shareholder for the payment of dividend. The letter contains detailed information about the payment of dividend such as - Number of Equity Shares held, Dividend Warrant Number, Gross Dividend, TDS (if any), Net amount of dividend, Distinctive No. (if any) etc.

Under the Income Tax Act 1961, any company making a payment has to deduct tax at source, if payment is above a certain threshold limit. TDS i.e. Tax Deducted at source has to be deducted at the rates prescribed by the Income Tax Department.

The company pays Dividend through :

a) Dividend Warrant

b) Electronically (ECS - Electronic Clearing Service, NEFT - National Electronic Fund Transfer)

A. Payment of Dividend through Dividend Warrant :

ANMOL STEEL INDUSTRIES LIMITED

Registered Office : 30, Anmol Niwas, J. M. Road, Nariman Point,
Mumbai - 400 020.
CIN : L30408 MH 2003 PLC110845

Phone : 022-97675877	Website : www.anmolindustrieslimited.com
Fax : 022-30010331	E-mail : anmol5@gmail.com
Ref. No. A/MR-D/7/19-20	Date : 7th May, 2019

Mrs. Jyoti Surti
12, Laxmi Niwas,
Amrapali Marg, Bandra,
Mumbai - 400 050.

Sub. : Payment of Dividend on Equity Shares
(Equity Shares of ₹ 10 each at par)

Dear Madam,

I am instructed by the Board of Directors to convey to you that in the 16th Annual General Meeting held on 20th April, 2019, Final Dividend @ ₹ 2.5 per equity share of ₹ 10/- each has been approved by the members for the year ending 31st March, 2019.

Your company has complied with all the statutory provisions (Sec. 123 of the Companies Act. 2013) relating to declaration of dividend.

Details of dividend payable to you are as follows :

1	2	3		4	5	6	7
Register Folio No.	No. of Shares held	Distinctive Nos.		Dividend Warrant No.	Gross Dividend	Income Tax Deducted (TDS)	Net Dividend
		From	To				
A-30	100	301	400	B-9931	₹ 250/-	NIL	₹ 250/-

The 'Dividend Warrant' is attached herewith. Please detach the 'Dividend Warrant' along the perforated line.

Thanking you,

Yours faithfully,
For Anmol Steel Industries Limited.

Sign
Secretary

Encl. : Dividend Warrant

B. Electronic Payment of Interim Dividend : Payment through ECS or NEFT.
(Interim Dividend paid by Electronic mode.)

GURUSAI AUTO LIMITED

Registered Office : 31, Tulsi Complex, Lodhi Road, Camp,
Pune - 411 001.
CIN : L40103 MH 1999 PLC300477

Phone : 020-24032844 | Website : www.gurusailimited.com
Fax : 020-24356101 | E-mail : sai31@gmail.com
Ref. No. S/MR-D/12/19-20 | Date : 3rd June, 2019

Mr. Jayant Modi
15, Sagar Apartment,
Van Vihar Road,
Pune - 411 030.

Sub. : Payment of Interim Dividend through Electronic Clearing Service (ECS), Direct Credit / NEFT

Dear Sir,

We are pleased to inform you that the Board of Directors of Gurusai Auto Limited in its meeting held on Thursday, 28th May 2019 has declared Interim Dividend @ Re. 1/- (i.e. 10%) per equity share of face value of Rs. 10/- each.

As per the instructions given by you (either in person or through Depository Participant), we have remitted the amount of aforesaid Interim Dividend to your Banker for crediting your Bank Account, i.e. Dividend will be payable by electronic transfer. Your company has complied with all the provisions relating to declaration and payment of dividend.

Details of Dividend payable to you are given below –

1	2	3	4	5	6
No. of Equity Shares held on Record Date (May 31st, 2019)	Dividend Per Share (₹)	Dividend Amount (₹)	DPID and Client ID No.	Date of Remittance	Bank A/c. (BOB)
500	1	500	12033200 07479005	3rd June, 2019	5656000 22105 Bank of Baroda

Please verify the credit of amount in your Pass Book / Statement of accounts.

As per the provisions of the Income Tax Act, 1961 no tax is required to be deducted at source in respect of Dividend payment, but dividend Distribution Tax has been paid by the Company.

Thanking you,

Yours faithfully,
For Gurusai Auto Limited

Sign
(Mr. Jitesh M. Gandhi)
Company Secretary

3. **Letter for issue of Bonus Shares :** Bonus Shares are fully paid up shares given by a company as a gift, out of its accumulated profits or reserves to existing equity shareholders in proportion of shares held by them. It is given free of cost.

   When Bonus Shares are issued, equity shareholders are informed by sending the letter. This letter contains - Total number of Shares held on record date, Total number of Bonus Shares issued, DPID No., Client ID No., Date of credit, etc.

   Total number of Bonus Shares issued are credited to Shareholders Demat Account or share certificate is issued if shares are in physical form.

Record Date : *It is the date fixed by the company to decide the Shareholders who are eligible for receiving Bonus Shares. The Company considers the names of those Shareholders, whose names appear in its records as shareholder as on the Record Date.*

It is the cut-off date for determining the number of registered members who are eligible for corporate benefits like Dividends and Bonus Shares.

YASH INDUSTRIES LIMITED

Registered Office : 102, New MIDC, Usha Tower, Shahu Chowk,
Mumbai - 400 031.

CIN : L40407 MH 2005 PLC710007

Phone : 022-23252323 | Website : www.yashindustrieslimited.com
Fax : 022-23600445 | E-mail : yash30@gmail.com
Ref. No. Y/MR-B/5/19-20 | Date : 16th October, 2019

Ms. Yukta Shroff
715, Narayan Peth,
Laxmi Road,
Pune - 411 038.

Sub. : Issue of Bonus Shares

Dear Madam,

I am directed by the Board of Directors to inform you that in accordance with the resolution passed in the Extra-ordinary General Meeting of the company held on 14th October, 2019 Shareholders have unanimously approved the recommendation of Board of Directors to issue Bonus Shares. Bonus Shares are issued in the ratio of 1:1, i.e. one additional equity share for every equity share held as on record date 13th October, 2019.

The Details of issue of Bonus Shares are as follows :

<table>
<tr><th>1</th><th>2</th><th>3</th><th>4</th><th>5</th></tr>
<tr><td rowspan="2">No. of Shares held on record date</td><td rowspan="2">No. of Bonus Shares Issued / Allotted</td><td>D.P. ID No.</td><td>Client ID No.</td><td rowspan="2">Date of Credit to Demat A/c</td></tr>
<tr><td colspan="2">Credited to Demat Account No.</td></tr>
<tr><td>25</td><td>25</td><td>IN 300100</td><td>10116061</td><td>16-10-2019</td></tr>
</table>

The Company has complied with the provisions for the issue of Bonus Shares.

The Bonus Shares issued will rank pari passu with the existing equity shares.

Thanking you,

Yours faithfully,
For Yash Industries Limited

Sign
(Mr. S. R. Naik)
Company Secretary

4. **Reply Letter :** Reply Letter to the query of the member on low rate of dividend given by the company. This letter is send to the member who is not satisfied with the payment of dividend made by the company.

   After receiving complaint letter from the concerned member about low rate of dividend, the company Secretary sends the reply letter to the member.

   The reply letter contains or specifies the reasons for low rate of dividend.

SHREE CEMENT INDUSTRIES LIMITED

Registered Office : 31, Tulsi Tower, Bandra (East),

Mumbai - 400 050

CIN : L50307 MH 2000 PLC160699

Phone : 022-24245025
Fax : 022-45456035
Ref. No. S/MR-D/25/19-20

Website : www.shreecementindustriesltd.com
E-mail : shree3@gmail.com
Date : 20th April, 2019

Ms. Kishor Malpani
15/21, Lotus Apt.,
Borivali (W),
Mumbai - 400 103.

Sub. : Resolving Query on Low Rate of Dividend declared by the Company

Dear Sir,

This is to inform you that as per your letter dated 15th April, 2019 I am hereby authorised to resolve your query regarding the low rate of dividend paid by the company to it's faithful members. The reasons for low rate of dividend are mentioned below :

1. That during the last year, due to the floods, company's factory situated at Mahim (E) was not in a condition to operate in a full fledge manner.
2. That due to such unavoidable circumstances of natural disaster company faced huge financial losses.
3. That due to such circumstances Board of Directors has decided to transfer Rupees 12.5 crores to General Reserves which is 50% more than the amount transferred to Reserves last year.

Hope you will be satisfied by the above information as provided by the company. We assure you that company will easily recover from such unavoidable circumstances and will deliver much better dividend in the coming years.

Thanking you,

Yours faithfully,
For Shree Cement Industries Limited

Sign
(Mr. Suhas Bajaj)
Company Secretary

SUMMARY

- Joint stock company requires huge capital to run its business. The capital is contributed by the shareholders by purchasing shares of the company. Members are the owners of the company.
- Routine administration of the company is managed by the Board of Directors. Important decisions need approval of the shareholders at the general meeting.
- Various points like providing correct information, use of lucid language, prompt response, maintain secrecy, etc. to be considered by the Secretary in correspondence with members.
- The secretary has to correspond with members on various important occasions.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statement.

1. Directors are the ....

   a) paid employee of the company

   b) representatives of the share holders

   c) creditors of the company

2. Dividend is to be paid to the shareholders within .... days from the date of declaration.

   a) 30 b) 40 c) 20

3. Registered shareholders receive dividend through .... warrant.

   a) share b) debenture c) dividend

4. Shares issued free of cost to the shareholders are known as .... shares.

   a) preference b) equity c) bonus

5. Share Certificate should be ready for delivery by the company within .... months after the allotment of shares.

   a) 3 b) 5 c) 2

6. Secretarial correspondence with members should be ....

   a) lengthy b) shortcut c) prompt and precise

7. Dividend is recommended by ....

   a) Board of Directors b) shareholders c) Depositors

8. Dividend is paid out of .... of the company.

   a) Capital b) Building Fund c) Profit

9. .... is issued by the company to its registered shareholders after the declaration of dividend at the Annual General Meeting of the company.

   a) Dividend Warrant b) Interest Warrant c) Share Warrant

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Dividend Warrant	1)	Instrument for payment of Interest
b)	Return on Shares	2)	Capitalisation of Building Fund
c)	Bonus Shares	3)	Electronic Clearing Service
d)	ECS	4)	Capitalisation of Reserve Fund
e)	NEFT	5)	National Electronic Fund Transfer
		6)	Dividend
		7)	Electronics Co-operative Society
		8)	National Electronic Fixed Transfer
		9)	Instrument for Payment of Dividend
		10)	Interest

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. Shares given free of cost to the existing equity shareholders.
2. Instrument for payment of dividend.
3. The shareholders to whom the bonus shares are issued..
4. The authority which recommends the rate of dividend.
5. An officer who comes into contact with all the members of the company through correspondence.
6. A special kind of cheque issued by a company on its banker to pay certain sum of money as dividend to its members.

D) State whether the following statements are true or false.

1. Bonus shares are issued to existing equity shareholders.
2. Building fund is used for issue of bonus shares..
3. Bonus shares means capitalisation of reserve fund.
4. Registered shareholder gets dividend through dividend coupons.
5. Dividend is the portion of the profits of the company which is allotted to the holders of the debentures of the company..
6. Every company must issue or despatch a share certificate to the allottee within three months after allotment of shares .
7. A complaint letter should not be replied promptly.

E) Find the odd one.

1. Secrecy, Dividend, Interest.
2. Bonus Letter, Dividend Letter, Board of Directors
3. Dividend Warrant, Interest Warrant, Demat
4. Secretary, Board of Directors, Lucid Language

F) Complete the sentences.

1. Dividend is recommended by ....
2. A company capitalises its Reserve Fund for issue of .... shares.
3. Payment of dividend must be made within .... days of its declaration.
4. Dividend is approved by the .... in the Annual General Meeting.
5. The .... has to communicate the decisions of the management to the members by conducting correspondence.

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Return on shares	1)	....
b)	Capitalisation of Reserve Fund	2)	....
c)	Correspondence	3)	....
d)	....	4)	Payment of Dividend Electronically.

(Written communication, Bonus shares, Dividend, ECS)

H) Answer in one sentence.

1. What is dividend warrant ?
2. What is capitalisation of reserve ?
3. What is Dividend ?
4. Who recommends the rate of dividend ?
5. Which type of shareholders enjoy the benefit of Bonus Shares ?
6. What is meant by payment of dividend electronically ?

I) Correct the underlined word/s and rewrite the following sentences.

1. Dividend is recommended by <u>shareholders.</u>
2. The person who purchases shares of the company is called <u>Depositor.</u>
3. Bonus shares are issued as a free gift to the <u>preference</u> shareholders.
4. Payment of dividend must be made within <u>21</u> days of its declaration.
5. A company must issue the Share Certificate within <u>three</u> months of allotment of shares.

J) Arrange in proper order.

1. a) Allotment of shares
   b) Application for shares
   c) Share certificate

2. a) Member
   b) Applicant
   c) Bonus shares

Q.2 Explain the following terms/concepts.

1. Capitalisation of Reserves 2. Bonus Shares 3. Dividend Warrant

Q.3 Answer in brief.

(1) Which precautions are to be taken by the Secretary while corresponding with members ?

(2) What are the circumstances under which Secretary undertakes correspondence with members ?

Q.4 Justify the following statements.

1. The Company Secretary should take certain precautions while corresponding with members.
2. There are certain circumstances when a Secretary has to correspond with members.

Q.5 Attempt the following.

1. Write a letter to the shareholder regarding issue of Bonus Shares.
2. Write a letter to the member for the issue of Share Certificate.
3. Write a letter to the member for the payment of dividend through Dividend Warrant.
4. Write a letter to the member for the payment of Interim dividend electronically.
5. Draft a reply letter resolving the query of the member on low rate of dividend.

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7 CORRESPONDENCE WITH DEBENTUREHOLDERS

7.1 Precautions to be taken by the Secretary while Corresponding with Debentureholders

7.2 Circumstances under which a Secretary has to enter into correspondence with Debentureholders

7.3 Specimen Letters

INTRODUCTION :

The capital of a company is raised by issuing shares or debentures to the public. The share capital is the owned capital while Debenture Capital is the borrowed capital of a company.

Debenture is an acknowledgement of a debt. Debenture capital is a borrowed capital of a company. Debentureholder is a creditor of the company. Compared to equity shares Debenture is considered as safe and secured capital. Debentures are issued for a specific period and it carries fixed rate of interest as a return on investment in debentures.

The Secretary has to communicate the decisions of the management and other information to the Debentureholders by conducting correspondence. He should be very cautious and careful while corresponding with debentureholders of the company.

Certificate of Debenture should be issued within a period of 6 months from the date of allotment of debentures.

A Company cannot issue debentures to more than 500 people without appointing a Debenture Trustee.

7.1 PRECAUTIONS TO BE TAKEN BY THE SECRETARY WHILE CORRESPONDING WITH DEBENTUREHOLDERS :

The following precautions are to be kept in mind by the Secretary while corresponding with the debentureholders -

1. **Politeness (Courtesy) :** Being the creditors, due respect should be given to the debentureholder in secretarial correspondence. The tone of language in the letter should be courteous. Rude and harsh language should be strictly avoided.

2. **Prompt Response :** The Secretary should promptly reply and respond to the queries and complaints of the debentureholders without any delay.

3. **Legal provisions :** The Secretary should follow the statutory provisions of the Companies Act, 2013 and other relevant laws while corresponding with debentureholders. Secretary should be cautious and careful while corresponding with debentureholders on legal matters.

4. **Transparency :** To maintain greater transparency with debentureholders, it is necessary to disclose all correct and accurate information of the company, credit rating of the company, true and real facts of companies affairs, etc. in correspondence.

5. **Conciseness :** The letter to the debentureholders should be concise i.e. brief, short and to the point. Un-necessary and irrelevant information must be avoided.
6. **Precise Information :** The Secretary should provide precise and up to date information to the debentureholders. The information must be factual and true.
7. **Secrecy :** As a confidential officer of the company, secretary should not disclose any important and secret information related to the company while corresponding with debentureholders.
8. **Image and Goodwill of the company :** While corresponding with debentureholders, the Secretary should always try to maintain goodwill and create a good image of the company in the mind of debentureholders.

7.2 CIRCUMSTANCES UNDER WHICH A SECRETARY HAS TO ENTER INTO CORRESPONDENCE WITH DEBENTUREHOLDERS :

The following are the few circumstances under which the Secretary enters into correspondence with the debentureholders :

1. Informing the applicant about allotment of debentures.
2. Informing about Payment of Interest though :
   a) Interest Warrant
   b) Electronic Payment of Interest
3. Letter for conversion of debentures into equity shares.
4. Letter for redemption of debentures.

7.3 SPECIMEN LETTERS

1. **Letter of Allotment of Debentures :** When a company allots debentures to the applicant, Letter of allotment of debentures is sent to the debentureholders. This letter of allotment is to be preserved by the debentureholder as he gets Debenture Certificate in exchange of this letter.

   This letter contains the details of issue of debentures i.e : Number of debentures applied for, Number of debentures allotted, Distinctive numbers of debentures, Amount received, Types of debentures, Rate of Interest, Maturity date, etc.

DISHA INDUSTRIES LIMITED

Registered Office : 45/A, Maharaja complex, Panchvati Karanja Road,
Nashik - 422 003.

CIN : L56002 MH 2000 PLC403633

Phone : 422-09645262
Fax : 422-69876500
Ref. No. D/DH/18/19-20

Website : www.dishalimited.com
E-mail : disha5@gmail.com
Date : 20th May, 2019.

Mr. Vijay Mittal
230, Dwarka Karanja Road,
Nashik - 422 036.

Sub. : Allotment of Debentures

Dear Sir,

In response to your application No. DI8013 dated 30th April, 2019, I am directed by the Board of Directors to inform you that, you have been allotted 100, **10% Non-convertible secured** debentures of ₹100/- each. The tenure of debentures is **5 years**.

These debentures are allotted to you as per the Board Resolution passed at the Board Meeting held on 16th May, 2019 and as per terms and conditions of Articles of Association of the company and Debenture Trust Deed.

The Details of Allotment of Debentures are as follows :

1	2	3	4		5
Folio No.	No. of Debentures Applied	No. of Debentures Allotted	Distinctive Numbers		Amount Received (₹)
			From	To	
D - 90	100	100	301	400	₹ 10,000

The Debenture Certificate is enclosed herewith.

Thanking you,

Yours faithfully,
For Disha Industries Limited.

Sign.
Mr. Avinash Natu
Company Secretary

Encl :- Debenture Certificate

2. **Payment of Interest :** Debenture Capital is a Loan or borrowed capital of a company. Denentureholders are the creditors and get fixed rate of interest as a return on their investment in debentures. Interest is a debt. It does not depend upon profits.

Company pays interest through Interest Warrant sent along with this letter. This letter contains details such as No. of debentures, Distinctive numbers, Gross amount of interest payable, TDS deducted, Net amount of interest payable etc.

Board Resolution is required for the payment of interest on debentures.

The company pays interest through - a) Interest Warrant b) Electronically

A. Interest Warrant : Payment of Interest through Interest Warrant.

ROLTA INDIA LIMITED

Registered Office : Rolta Tower, 'B' wing, Rolta Technology park,
MIDC, Andheri (W), Mumbai - 400 053.

CIN : L74999 MH 1989 PLC052384

Phone : 022-26205555
Fax : 022-10206431
Ref. R/DH/07/19-20

Website : www.roltalimited.com
E-mail : rolta31@gmail.com
Date : 10^{th} June, 2019

Mrs. Diya Saluja
Aditi Appartment, M.G. Road,
Mira Road (E), Mumbai - 401 107.

Sub. : Payment of interest on debentures.

Dear Madam,

I am directed to inform you that, the Board of Directors has passed a resolution in the Board meeting held on 05^{th} June, 2019 regarding payment of interest on your 100, 10% Non-convertible debentures of ₹ 100/- each.

The details of payment of interest payable to you are as follows :

1	2	3		4	5	6	7
Folio No.	No. of Debentures	Distinctive Numbers		Gross Amt. of Interest	T. D. S. (10% On Interest)	Net Amt. of Interest (₹)	Interest Warrant No.
		From	To				
C - 240	100	601	700	₹ 1,000	NIL	₹ 1,000	IW 9646

The Interest warrant is enclosed herewith. Please detach the Interest Warrant along the perforated line.

Thanking you,

Yours faithfully,
For Rolta India Limited.

Sign.
(Mrs. Simran Unecha)
Company Secretary

Encl :- Interest Warrant

B. Electronic Payment of Interest : Payment through Electronic mode (ECS, NEFT etc.)

BALAJI STEEL LTD.

Registered Office : Sr. No. 78, Plot No. 48, Balaji Tower,
Mall Road, Pune - 411 038.
CIN : L54430 MH 1999 PLC300477

Phone : 020-20106552 Website : www.balajisteelltd.com
Fax : 020-30205441 E-mail : balaji30@gmail.com
Ref. B/DH/30/19-20 Date : 12^{th} March, 2019

Mrs. Amruta Dixit
30/20, Left Bhusari Colony,
Kothrud Depot,
Pune - 411 038.

Sub. : Payment of Interest on Debentures
Electronically through ECS or NEFT.

Dear Madam,

I am instructed by the Board of Directors to convey to you that, the Board has passed a resolution in the Board meeting held on 10^{th} March, 2019 finalizing to pay interest @ 10% on Redeemable Debentures of ₹ 100/- each for the year ending 31st March, 2019.

Your company has complied with all the provisions relating to payment of interest on debentures.

Details of Interest payable to you are as follows :

1	2	3		4	5	6
Register No.`	No. of Debentures	Distinctive Numbers		Gross Amt. of Interest (₹)	T. D. S. (10%)	Net Amt. of Interest (₹)
		From	To			
C - 440	100	601	700	₹ 1,000	NIL	₹ 1,000

Interest will be paid by electronic transfer i.e. by crediting the said interest to your bank account, as per details provided by you to the company.

Thanking you,

Yours faithfully,
For Balaji Steel Ltd.

Sign.
(Mr. Nikhil Dixit)
Company Secretary

3. **Conversion of Debentures :** Convertible Debentures are the debentures which are converted into equity shares on the expiry of specified period and at a specified rate mentioned in the terms of issue. After receiving Letter of Option, the secretary sends letter informing the debentureholders that the debentures are converted into equity shares. It also states that the share certificate will be issued to them in due course or it may be sent along with this letter.

   Company has to get approval of shareholders by passing special resolution at the Extra Ordinary General Meeting for conversion of debentures into equity shares. After receiving the approval, the company sends letter of conversion of debentures to debentureholder.

KRISHNA ELECTRONICS LIMITED

Registered Office : 10, Krishna sadan, Shivaji Chowk,

Solapur - 413 001.

CIN : L53888 MH 1987 PLC042262

Phone : 024-97463402
Fax : 024-96429201

Website : www.krishnaelectronicsLtd.com
E-mail : krishna30@gmail.com

Ref. K/DH/31/19-20

Date : 5th June, 2019

Mr. Mahesh Malpani
20, Balaji Complex,
Laxmi Road,
Solapur - 413 018.

Sub. : Conversion of Debentures into Equity Shares

Dear Sir,

I am directed to inform you that in accordance with the terms decided at the time of issue of 1,00,000, 10% fully convertible debentures, the debentures are due for conversion.

In accordance with the above, a Special Resolution was passed by the shareholders in the Extra - Ordinary General Meeting held on 25th May, 2019 for approval of conversion of debentures into equity shares in the ratio of 2 : 1. As per your Letter of Option you have been allotted 50 Equity shares in lieu of 100 Debentures.

Details of your holding after conversion are as follows :

1	2	3	4		5
Folio No.	No. of Debentures held	No. of Equity Shares Issued	Distinctive Numbers		Share Certificate No.
			From	To	
465	100	50	501	550	2219

Duly signed and executed share certificate is enclosed herewith.

Debenture Certificate will be null and void w.e.f. 25th May, 2019.

Thanking you,

Yours faithfully,
For Krishna Electronics Ltd.

Sign.
(Mr. Nitin Saraf)
Company Secretary

Encl :- Share Certificate

4. **Redemption of Debentures :** Letter of Redemption of debentures is issued to the debentureholders whose debentures are to be redeemed after the specified period.

A Debenture Redemption Reserve Fund (DRRF) is created by the company for the purpose of redemption of debentures.

Debenture Redemption form is sent along with this letter. This form and necessary documents have to be submitted by the debentureholders to the company, for further procedure of redemption.

This letter informs the debentureholders that their debentures have become due for redemption.

SWASTIK MARBLE LIMITED

Registered Office : 30/C, Aachal Towers, Swastik Bhavan, Camp,
Pune - 411 001.
CIN : L34508 MH 2011 PLC311299

Phone : 020-23467011
Fax : 020-23466022
Ref. S/DH/13/19-20

Website : www.swastikmarbleltd.com
E-mail : swastik30@gmail.com
Date : 10^{th} October, 2019

Mrs. Asmita Malpani
25, Narayan Peth,
Amruta Apartment,
Pune - 411 030.

Sub. : Redemption of Debentures.

Dear Madam,

This is to inform you that 100000, 10% Non-convertible Debentures issued in May, 2014 are due for redemption on 12^{th} November, 2019. According to the Board Resolution No. 3462, passed at the Board Meeting held on 8^{th} October, 2019, Debentures shall be redeemed out of 'Debenture Redemption Reserve Fund' of the company.

Please arrange to submit enclosed 'Debenture Redemption Form' along with the original Debenture Certificate to the company, on or before 3^{rd} November, 2019.

On completion of the above formalities, the redemption amount will be credited to your bank account.

You are requested to provide us your Bank Account details.

Thanking you,

Yours faithfully,
For Swastik Marble Limited,

Sign.
(Mrs. Usha Surti)
Company Secretary

Encl :- Debenture Redemption Form

SUMMARY

- Debenture is a borrowed capital of the company. Debentureholder is creditor of the company. They receive interest as return on investment. They have less risk as they get back their capital prior to shareholders in case of winding up of the company. Debentures may be secured by creating a charge over the assets of the company.
- The Secretary has to correspond with debentureholders under special circumstances, such as - Allotment of debentres, payment of interest through Interest Warrant or electronically, conversion of debentures into equity shares, redemption of debentures etc.
- Various points like politeness, prompt response, compliance with the legal provisions, transparency, conciseness etc. to be considered by the Secretary while corresponding with the debentureholders.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. Debenture capital is a .... capital of a company.
   a) borrowed b) owned c) permanent
2. Debentureholders are .... of the company.
   a) Owners b) Creditors c) Debtors
3. Borrowed Capital is provided to the company by ....
   a) Equity shareholder b) Debentureholder c) Preference shareholder
4. Interest on Registered Debentures is given through ....
   a) Interest coupons b) Interest warrant c) Refund order
5. .... are the creditors of the company.
   a) Shareholders b) Debentureholders c) Directors
6. Bearer Debentureholders get interest through ....
   a) Interest Warrants b) Refund orders c) Interest coupons
7. Return of income on debentures is .... at fixed rate.
   a) Dividend b) Loan c) Interest
8. .... is an acknowledgement of debt issued by the company under common seal.
   a) Debentures b) Shares c) Reserve
9. Debentures repayable after a certain period are .... debentures.
   a) Convertible b) Registered c) Redeemable
10. The rate of interest payable on debentures is ....
    a) uncertain b) floating c) fixed

11. Debentureholders receive .... certificate from the company.

a) Share   b) Bond   c) Debenture

12. Interest warrants are sent to .... of the company.

a) Shareholders   b) Debentureholders   c) Owners

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Debentureholder	1)	Borrowed Capital
b)	Interest on Registered Debentures	2)	Interest coupons
c)	Convertible Debentures	3)	Evidence of Loan
d)	Debenture Certificate	4)	Safe and secured investment
e)	Investment in Debentures	5)	Interest warrant
f)	Redeemable Debentures	6)	Conversion into Debentures
g)	Debentures	7)	Risky investment
		8)	Evidence of shares
		9)	Creditor
		10)	Conversion into equity shares
		11)	Redeemed after fixed period
		12)	Redeemed at winding up of company
		13)	Owner
		14)	Owned Capital

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. Return on investment in debentures.
2. Documentary evidence of holding the debentures.
3. Status of debentureholders.
4. Debentures which can be converted into equity shares.
5. The person who purchases debentures of the company.
6. An acknowledgement of debt issued by the company under its common seal.
7. Debentures whose details are mentioned in the Register of debentureholders.

D) State whether the following statements are true or false.

1. Debentureholders get regular dividend.
2. Debenture is a loan capital of the company.
3. Convertible Debentures can be converted into equity shares.
4. Interest on debentures is paid notwithstanding the volume of profit.
5. Debentureholders enjoy full membership rights of the company.
6. Dividend warrants are used to pay interest to the debentureholders.
7. All types of debentures are eligible for conversion into equity shares.
8. Debentures are never redeemed by the company.
9. Debentureholders are the owners of the company.
10. Debentures are always fully paid-up.

E) Find the odd one.

1. Depository, Interest, Dividend
2. Interest warrant, Dividend Warrant, Demat
3. Debentureholder, Shareholder, Dematerialisation
4. Debentureholder, Shareholder, SEBI

F) Complete the sentences.

1. Debentureholder is a .... of the company.
2. Company issues .... certificate to the debentureholder after allotment of debentures.
3. Debentureholder gets .... at fixed rate as a return or income.
4. In case of Registered Debentures, Interest .... are used to pay interest.
5. The .... has to correspond with debentureholders on important occasions.
6. The person who purchases the debentures of a company is called ....
7. Interest does not depend upon .... of the company.
8. Company cannot issue debentures with .... rights.
9. Debenture certificate should be issued within a period of .... months, from the date of allotment of debentures.
10. A company cannot issue debentures to more than 500 people without appointing a ....
11. The power to issue debentures has been vested with the ....

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Return on Debentures	1)	....
b)	Debenture certificate	2)	....
c)	....	3)	Debentureholders
d)	....	4)	Debenture
e)	....	5)	Power to issue debentures

(Debt capital, Board of Directors, Creditors, Issued within 6 months, Interest)

H) Answer in one sentence.

1. Who is debentureholder ?
2. What is the income of debentureholder ?
3. What is debenture ?
4. What is convertible debentures ?
5. Who takes decision to allot the debentures ?
6. Which form is enclosed alongwith the letter of redemption of debentures ?
7. Which certificate will be issued after allotment of debentures ?

I) Correct the underlined word/s and rewrite the following sentences.

1. The person who purchases debentures of the company is called <u>shareholder</u>.
2. Debentureholders get regular <u>dividend</u> at fixed rate.
3. A <u>Share Certificate</u> must be issued after allotment of debentures.
4. A Debenture Redemption Reserve Fund is created by the company for the redemption of <u>Shares.</u>
5. A <u>Demat Request Form</u> is sent alongwith the letter of Redemption of Debentures.
6. A company must issue Debenture Certificate within <u>8</u> months of allotment of debentures.

J) Arrange in proper order.

1. a) Board Resolution
   b) Allotment of Debentures
   c) Board meeting

2. a) Interest warrant
   b) Allotment of Debentures
   c) Board meeting

Q.2 Explain the following terms/concepts.

1. Debentures
2. Debentureholder
3. Interest on Debentures
4. Redemption of debentures
5. Conversion of Debentures
6. Interest warrant
7. Conciseness
8. Precise information
9. Courtesy
10. Debenture certificate

Q.3 Answer in brief.

1. Which are the precautions to be taken by the Secretary while corresponding with debentureholders ?
2. What are the circumstances under which correspondence can be made with debentureholders ?

Q.4 Justify the following statements.

1. The company secretary should take certain precautions while corresponding with debentureholders.
2. There are certain circumstances when a secretary has to correspond with debentureholders.

Q.5 Attempt the following.

1. Draft a letter of allotment to debentureholder.
2. Write a letter to the debentureholder regarding payment of interest through Interest Warrant.
3. Draft a letter to debentureholder informing him about redemption of debentures.
4. Write a letter to debentureholder informing him about conversion of debentures into equity shares.
5. Write a letter to the debentureholder regarding payment of interest electronically.

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8 CORRESPONDENCE WITH DEPOSITORS

8.1 Precautions to be taken by the Secretary while Corresponding with Depositors.

8.2 Circumstances under which a Secretary has to enter into correspondence with Depositors

8.3 Specimen Letters

INTRODUCTION :

Deposit is a short term source of finance of the company and it is used in order to satisfy short term working capital needs of the company. Company cannot accept deposits for a period less than 6 months or more than 36 months. The company is liable to pay regular interest on the deposits at a fixed rate along with the principal amount on maturity.

Company Secretary has to conduct correspondence with depositors regarding – Acceptance of deposits, payment of interest on deposits, renewal of deposits, repayment of deposits and so on. Secretary conducts such correspondence on behalf of the company and also as per the instructions of the Board of Directors. The Secretary should be very cautious and careful while corresponding with depositors of the company.

8.1 PRECAUTIONS TO BE TAKEN BY THE SECRETARY WHILE CORRESPONDING WITH DEPOSITORS

The following precautions or points to be kept in mind by the Secretary while corresponding with depositors :

1. **Legal Provisions :** The Secretary should ensure that provisions relating to invitation, acceptance, renewal and repayment of deposits are duly complied with by the company, while corresponding with depositors. Secretary should observe the legal provisions.
2. **Courtesy :** Polite replies are essential while writing letters to the depositors. Rude words should be strictly avoided.
3. **Prompt Response :** The Secretary should give prompt replies to the queries and complaints of the depositors without any delay.
4. **Accuracy :** Letter written to the depositors should be accurate and precise. Factual and correct information should be provided to them.
5. **Image and Goodwill :** While writing letters, the Secretary has to maintain the goodwill of the company.
6. **You Attitude :** Letter should be written from depositors point of view, after taking into consideration the requirements of the depositors.

7. **Conciseness :** The letters must be concise i.e. short, brief and to the point. Un-necesssary and irrelevant information should be avoided.

8. **Maximum Secrecy :** It is necessary to maintain maximum secrecy as regards secretarial correspondence with depositors.

8.2 CIRCUMSTANCES UNDER WHICH A SECRETARY HAS TO ENTER INTO CORRESPONDENCE WITH DEPOSITORS :

The Secretary has to communicate various decisions of the Board of Directors to the depositors.

The following are the few circumstances when the Secretary enters into correspondence with the Depositors :

1. Thanking depositors for depositing amount and showing faith in the company.
2. Intimation about payment of interest through -

   a) Interest Warrant b) Electronic payment of Interest
3. Letter informing about renewal of deposits.
4. Informing depositors about repayment of deposit on maturity.

8.3 SPECIMEN LETTERS

1. Thanking depositors for depositing amount with the company.

The letter of thanks is sent to the depositors by a company immediately after receiving the deposits. This letter gives detailed information regarding the deposits i.e. Amount of deposit, Date of deposit, Period of deposit, etc.

The Deposit Receipt which is a proof of receipt of deposit is sent to the depositor along with this letter within 21 days from the date of acceptance of deposits.

GURU INDUSTRIES LTD.

Registered Office : 45, Guru Towers, J. M. Road,
Pune 411 021.
CIN : L30121 MH 2007 PLC070504

Phone : 020-12110072
Fax : 020-30040077
Ref. No. G/DEP/09/19-20

Website : www.gurulimited.com
E-mail : guru30@gmail.com
Date : 10th April, 2019

Mr. Sharangdhar Naik
78/68, Guru Appartment, Shaniwar Peth,
Pune - 411 011.

Sub. : Thanking Depositor for Fixed Deposit

Dear Sir,

We are in receipt of your application dated 5th April 2019 for investment of ₹ 1,00,000 in the fixed deposit as per the terms and conditions stated in advertisement for a period of 2 years. We are thankful to you for the initiative and the trust you have shown in depositing a substantial amount in our company.

The details of deposits accepted are given in the following schedule :

1	2	3	4	5	
Fixed Deposit Receipt No.	Amount of Deposit (₹)	Period of Deposit (years)	Rate of Interest (%)	Bank Details	
				Name of the Bank	Bank Account No.
678	₹ 1,00,000	2 years	12.5%	City Bank	222040

The Board of Directors of our company expresses its gratitude for depositing money in our company.

We assure you of our best services and thank you for the confidence shown in our company.

Thanking you,

Yours faithfully,
For Guru Industries Ltd.

Sign
Mr. Nitin Modi
General Manager and
Company Secretary

Encl : Fixed Deposit Receipt No. 678

2. Payment of Interest.

Deposit is a borrowed capital. Depositors get interest as a return on their investment of money in deposits. This letter is sent by the company to the depositor when interest on deposit becomes due. In this letter the Company Secretary gives detailed information about payment of interest such as - Amount of deposit, Rate of interest, Gross amount of interest, TDS, Net amount of interest, Interest Warrant No., etc. The company pays interest through : a) Interest Warrant b) Electronically

A) Payment of Interest through Interest Warrant.

KISHOR TEXTILE LTD.

Registered Office : 104/B, Bombay House, S. V. Road, Borivali (W),
Mumbai 400 103.
CIN : L05065 MH 2000 PLC430644

Phone : 022-60304636
Fax : 022-40202323
Ref. No. K/DEP/34/19-20

Website : www.kishortesxtilelimited.com
E-mail : kishortext30@gmail.com
Date : 28th July, 2019

Mrs. Lata Dixit
C-702, Madhuban Apt., Shivaji Nagar,
Camp,
Pune - 411 001.

Sub. : Payment of Interest on Fixed Deposits

Dear Madam,

I am instructed by the Board of Directors to inform you that the interest @10% on your Fixed Deposit approved by the Board has become due. We are enclosing herewith 'Interest Warrant' No. 3345, dated 25th July, 2019 drawn on Axis Bank, Borivali Branch for ₹ 2,500/-.

Your company has complied with all the provisions relating to payment of interest on deposits

The details of your Fixed Deposit and interest payable on deposit are given in the following schedule :

1	2	3	4	5	6	7
Interest Warrant No.	Fixed Deposit Receipt. No.	Deposit Amount (Rs.)	Rate of Interest (%)	Gross Amount of Interest	TDS @ (10%)	Net Amount of Interest Payable (₹)
3345	2032	₹ 25,000	10%	₹ 2,500	NIL	₹ 2,500/-

Interest Warrant is enclosed herewith.

Please detach the Interest Warrant along the perforated line.

Thanking you,

Yours faithfully,
For Kishor Textile Ltd.

Sign
Mr. Nikhil Dixit
Company Secretary

Encl : Interest Warrant

B) Electronic Payment of Interest : Payment through Electronic Mode - (ECS, NEFT.)

NOVEL SEWING MACHINES LTD.

Registered Office : Survey No. 78, Plot No. 48, Novel Sadan, D.P. Road, Bavdhan,
Pune : 411 038
CIN : L302090 MH 2000 PLC070504

Phone : 022-60603021
Fax : 020-96864636
Ref. No. N/DEP/10/19-20

Website : www.novelsewingltd.com
E-mail : novelsewing07@gmail.com
Date : 14th March, 2019

Miss. Kshitija Bihani
125, Laxmi Road
Narayan Peth,
Pune : 411 030

Sub. : Payment of Interest on Fixed Deposit
Electronically through ECS or NEFT.

Dear Madam,

I am instructed by the Board of Directors to convey to you that the Board has passed a resolution in the Board meeting held on 12th March,, 2019 to pay interest @ 10% on deposits for the year ending 31st March, 2019.

Your company has complied with all the provisions relating to payment of interest on deposits.

Details of Interest payable to you are as follows :

1	2	3	4	5	6
Fixed Deposit Receipt. No.	Deposit Amount (₹)	Rate of Interest (%)	Gross Amount of Interest (₹)	TDS @ (10%)	Net Amount of Interest payable (₹)
2032	Rs. 25,000	10%	₹ 2,500	NIL	₹ 2,500

Interest will be payable by electronic transfer (ECS/NEFT), i.e. by crediting said interest to your bank account as per details provided by you to the company.

Thanking you,

Yours faithfully,
For Novel Sewing Machine Ltd.

Sign
Miss. Sarita Singh
Company Secretary

3. Renewal of Deposit

A process whereby the deposit holder continues with the deposit for an additional time period after the completion of the initial time period of investment (deposit) is called as 'Renewal of Deposit'.

The additional period can be similar or different from the original time period.

The printed application forms for Renewal of Deposits are to be sent to all depositors at least one month before the maturity date.

The company sends this Letter of Renewal if the depositor renews his deposits. The details about renewal of deposit are informed and a Renewal Deposit Receipt is enclosed.

DIAMOND INTERNATIONAL LTD.

Registered Office : 24, Dimond House, Nariman Point,
Mumbai 400 021

CIN : L15522 MH 2000 PLC301244

Phone : 022-50202113	Website : www.dimondlimited.com
Fax : 022-20304112	E-mail : dimond5@gmail.com
Ref. No. D/DEP/61/19-20	Date : 22^{nd} March, 2019

Miss. Ashi Singh
26, Gulmohar Apartment,
Andheri (W)
Mumbai - 400 058.

Sub. : Renewal of Fixed Deposit

Dear Madam,

We hereby acknowledge the receipt of your application for renewal of deposit of ₹ 1,00,000 for a further period of two years. Alongwith the application we have also received original Fixed Deposit Receipt (FDR) No. 4625, and the same has been placed before the Board for consideration and approval.

The Board of Directors by passing a resolution at the Board meeting held on 17^{th} March, 2019 has decided to renew the deposits for a further period of 2 years on the same terms and conditions.

A Deposit Receipt No. 5925 is enclosed along with this letter.

Thanking you,

Yours faithfully,
For Diamond International Ltd.

Sign
Miss Kavya Ambani
Company Secretary

Encl : Fixed Deposit Receipt No. 5925

4. Repayment of Deposit

On maturity of tenure of deposits, it is binding on the company to repay the deposit. Default in repayment of deposit results in levy of penalty. The letter for repayment of deposit is to be sent to the depositor, when the deposit is to be redeemed. The letter informs the depositor that the fixed deposit receipt is received by the company. This letter includes information about Repayment of Deposit such as - Tenure of Deposit, Fixed Deposit Receipt No., deposit amount, rate of interest, maturity amount, TDS, Net amount, due date of payment of deposits, etc.

DHARA OIL LTD.

: Registered Office :

64, Dhara Bhavan, Pimpri Road, Pune - 411 018.
CIN : L55331 MH 1996 PLC302177

Phone : 022-65254023
Fax : 020-49396423
Ref. No. D/DEP/16/19-20

Website : dharaoillimited.com
E-mail : dhara16@gmail.com
Date : 13th November, 2019

Mr. Ravindra Khanna
C-15, Swami Apartment,
Narayan Peth, Pune - 411 030

Sub. : Repayment of Fixed Deposit

Dear Sir,

This is to inform you that your Fixed Deposit Receipt No. 5925 dated 1st December, 2017 for ₹ 1,00,000/- will be due for repayment on 30th November, 2019.

We have received from you the original Deposit Receipt No. 5925 duly discharged along with your instruction for repayment. The Board of Directors in the meeting held on 12th Novemeber, 2019 has passed a resolution for redemption of the deposits.

The details of repayment of deposit are as under :

1	2	3	4	5	6	7	8
Tenure of Deposit	Fixed Deposit Receipt. no.	Deposit Amt. (₹)	Rate of Int. (10%)	Maturity Amt. (₹)	TDS (10%)	Net Amt.	Due Date of Deposit
2 years	5925	₹ 1,00,000	₹ 20,000	₹ 1,20,000	₹ 2,000	₹ 1,18,000	30th Nov, 2019

Please find enclosed herewith a crossed cheque of ₹ 1,18000, bearing No. 426025 dated 30th November, 2019 drawn on Bank of Maharashtra, Shivaji Nagar, Pune - 411 005.

Thanking you,

Yours faithfully,
For Dhara Oil Ltd.

Sign
Mr. Ashok Bhattad
Company Secretary

Encl : Crossed Cheque No. 426025

SUMMARY

- Depositors are creditors of the company. They are the short term financers. Depositors get interest as a return on investment of money in company deposits.
- The Deposit holders do not enjoy any management rights and they are not entitled to vote in the company meetings as they are the creditors of the company. They provide short term finance.
- The Secretary has to correspond with the Depositors under special circumstances such as - Thanking Depositor for keeping fixed deposit, payment of interest, renewal of deposits and repayment of deposit on maturity. Various points like - legal provisions, courtesy, prompt response, goodwill, accuracy, conciseness, maximum secrecy etc. to be considered by the Secretary while corresponding with depositors.
- The depositor may renew the deposits on completion of term of deposit. Company can repay the amount of deposit as per the terms and conditions of repayment of deposits.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. Depositors are .... of a company.

   a) Members b) Creditors c) Debtors

2. Depositors provide .... Capital to the company.

   a) Short Term b) Long Term c) Medium term

3. A Company cannot accept deposit for more than .... months.

   a) 24 b) 36 c) 45

4. A company cannot accept deposit for less than .... months.

   a) 6 b) 3 c) 5

5. Deposits are .... loans of the company.

   a) fixed b) short term c) long term

6. Public Deposits are accepted to meet the requirement of .... Capital.

   a) fixed b) working c) owned

7. .... has the power to invite deposits from Public.

   a) Shareholders b) Auditors c) Board of Directors

8. Rate of interest on deposits is ....

   a) fixed b) fluctuating c) moderate

9. The return or income for the investment of money in deposits is called ....

   a) Dividend b) Interest c) Discount

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Depositors	1)	Fixed
b)	Rate of Interest on Deposits	2)	Evidence of ownership
c)	Deposit Receipt	3)	Debtors
		4)	Creditors
		5)	Evidence of deposit
		6)	Fluctuating

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. Return on investment on deposit.
2. Instrument for payment of interest on deposit.
3. An acknowledgement of the fixed deposit accepted by a company.
4. Return of deposits on maturity date.
5. Maximum period of deposits.

D) State whether the following statements are true or false.

1. Fixed deposit is a short term source of finance for the company.
2. Fixed Deposit holder is creditor of the company.
3. Deposits are invited by the company without issuing statutory advertisement.
4. Fixed Deposit holders are entitled to receive dividend.
5. A Private Company cannot accept the deposits from the general public.
6. Depositors are given voting rights.

E) Find the odd one.

1. Dividend, Depositor, Deposit Receipt
2. Depositor, Depository, Deposit Receipt

F) Complete the sentences.

1. Depositors are the .... of the company.
2. The .... must be cautious and careful while writing letters to the depositors.
3. Deposit is a .... term source of finance of the company.
4. A company can accept deposits for the minimum period of .... months.
5. Depositors are entitled to receive .... at fixed rate.

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Depositor	1)	....
b)	Return on Deposits	2)	....
c)	....	3)	Maximum Period of Deposits
d)	Minimum Period of Deposits	4)	....

(Interest, Creditor of the company, 36 months, 6 months)

H) Answer in one sentence.

1. Who is depositor ?
2. What is the return on deposit ?
3. What is Interest Warrant ?
4. What is renewal of deposit ?
5. Which document is enclosed along with the Renewal Letter ?
6. When will the company return the deposit ?
7. What is minimum and maximum period of deposit ?

I) Correct the underlined words and rewrite the following sentences.

1. Depositors are <u>owners</u> of the company.
2. Deposits are the <u>internal</u> source of financing.
3. Deposit is a <u>long</u> term source of capital.
4. Depositors are entitled to receive <u>dividend</u>.

J. Arrange in proper order.

1. a. Renewal of Deposit
   b. Acceptance of Deposits
   c. Deposit Receipt

2. a. Payment of Interest
   b. Deposit Receipt
   c. Acceptance of Deposits

Q.2 Explain the following terms/concepts.

1. Depositor
2. Deposit
3. Interest on Deposit
4. Deposit Receipt
5. Renewal of Deposit
6. Repayment of Deposit

Q.3 Answer in brief.

1. What precautions are to be borne in mind by the Secretary, while corresponding with Depositors.
2. What are the circumstances under which the Secretary makes correspondence with depositors.

Q.4 Justify the following statements.

1. The Company Secretary should take certain precautions while corresponding with depositors.
2. There are certain circumstances when a secretary has to correspond with Depositors.

Q.5 Attempt the following.

1. Draft a letter of thanks to the depositor of a company.
2. Draft a letter to depositor informing him about payment of interest through Interest Warrant.
3. Write a letter to depositor regarding renewal of his deposit.
4. Draft a letter to depositor regarding repayment of his deposit.
5. Draft a letter to depositor informing him about payment of interest electronically.

❑❑❑

9 DEPOSITORY SYSTEM

9.1 Depository System - Meaning

9.2 Importance of Depository System

9.3 Benefits of Depository System

9.4 Constituents of Depository System

9.5 Concepts/Terms related to Depository System

9.6 Functioning of Depository System

9.6.1 Demat process

9.6.2 In case of IPO

9.6.3 In case of transfer A) Off market B) Market

9.7 Depositories in India (A) NSDL (B) CDSL

9.8 Distinction

INTRODUCTION

Securities can be held in two modes -

A) Physical B) Electronic / Dematerialized

Securities means shares, debentures, bonds, units of mutual funds, securities issued by the Government etc.

(A) Physical mode of holding securities : It means securities are held in the form of paper certificates. It has following disadvantages :

1) **Risk** : Certificates of papers can be lost, damaged, torn, stolen, misplaced during transit, etc.

2) **Efforts in Duplicating :** Obtaining duplicate certificates (if original certificate is lost) involves time, efforts and money.

3) **Delay in allotment of securities :** Allotment of new securities takes longer time.

4) **Delay in Transfer and Transmission of securities :** More time is involved in transfer and transmission of securities as it involves actual handling of physical certificates.

5) **Risk of Bad Delivery :** Delivering certificates which are torn, forged, etc. creates problems in buying and selling of securities.

(B) Electronic / Dematerialized mode of holding securities : It means securities are held in electronic or dematerialized form.

9.1 MEANING OF DEPOSITORY SYSTEM

Under Depository System, securities are held in electronic form. The transfer and settlement of securities are done electronically. The Depository System maintains accounts of the shareholder, enables transfer, collects dividends, bonus shares, etc. on behalf of the shareholder. This system is also called as scripless trading system.

In India the Depository System was introduced by passing the Depository Act in 1996. Under this Act, a competitive multi-depository system consisting of two depositories, viz. NSDL and CDSL was set up. It will be of interest to note that the world's first Depository was set up in 1947 in Germany.

- The Depository System resembles the Banking system in many aspects.

Depository System	Banking System
1. It keeps the securities safe. 2. Securities are held in accounts having unique IDs. 3. There is no physical handling of securities during allotments, transfers, etc. 4. The transfer of securities between accounts is done.	1. It keep the money safe. 2. Funds are held in accounts having unique numbers. 3. There is no physical handling of money. 4. The transfer of funds between accounts is done.

In the Depository System, the Depository is the custodian of the securities in electronic form and the Depository Participant acts as a link between the Depository and the Investor.

9.2 IMPORTANCE OF DEPOSITORY SYSTEM

Depository System has a very important role to play in the successful functioning of the capital market.

1) It aims at eliminating huge volume of paperwork involved in paper or scrip based system.
2) It offers scope for paperless trading by using the state-of-art technology.
3) It leads to elimination of storage and handling of certificates.
4) It reduces the cost and efforts involved in storage and handling of physical certificates.

9.3 BENEFITS / ADVANTAGES OF DEPOSITORY SYSTEM

A) To Investors :

1) **Elimination of Risk :** All risks associated with physical certificates like delays, lost, theft, mutilation, bad deliveries, etc. are totally eliminated.
2) **Safety :** It is the most safe and secure way of holding securities. The entire system functions under the Depository Act and is monitored by SEBI. e.g. The Investor can keep his account in a 'Freeze / Lock' mode to avoid / prevent unexpected debit or credit or both by giving instructions to the DP.
3) **Easy Transfer of shares :**
   (a) Efforts in filling transfer forms and lodging the documents is eliminated.
   (b) Also the stamp duty levied on transfer of physical shares is not applicable.
   (c) Processing time in transfer of securities is reduced and neither the securities nor the cash is tied / held up for unnecessarily long time.
4) **Updates and Intimation :** The investor is provided with the status of the holdings and transactions by DP and occasionally by the Depository too.

5) **Security against Loan :** Dematerialised securities are preferred by banks and financial institutions as security against loan.

6) **No concept of 'Lots' :** The system of odd and even lot stands abolished. The market lot is one share for dematerialised securities.

7) **Nomination Facility :** Individual Investors can avail of nomination facility. This simplifies the process in the event of the death of the investor.

8) **Automatic Credit :** The account of investor is automatically credited/debited in case of a change initiated by the company which impacts the securities. This is called 'Corporate Action'. Few examples which can be termed as Corporate Action are : Payment of Dividend, Issue of Bonus Shares, Offering of Rights Shares, Early Redemption of Debentures, Mergers and Acquisitions, etc.

B) To Companies :

1) **Up-to-date Information :** The up-to-date information about investors is provided by the depository.

2) **Reduction in costs and efforts :** Costs, efforts and time involved in printing and distribution of certificates in cases of new issues, bonus, transfers, etc. is saved.

3) **Better Investor - Company Relationships :** The complaints arising out of loss of certificates, signature differences, long lapses of time in executing requests, etc. is substantially reduced. It leads to better communication with investors and increased goodwill for the company.

4) **International Investment :** Under Depository System, better and quicker services can be provided and this attracts investments from abroad.

9.4 CONSTITUENTS OF DEPOSITORY SYSTEM

All operations under the Depository System is performed by Depository with the help of its constituents as explained below :

Constituents of Depository System

- The Depository
- The Depository Participant (DP)
- The Beneficial Owner (BO)
- The Issuer Company

(1) The Depository :

1) It is an organization like the Central Bank where securities are held in electronic form at the investor's request.
2) It also provides different services related to different transactions in such securities.
3) It is responsible for safe-keeping of the investor's securities.
4) There is no direct access to investor with the Depository.
5) It works as a link between the company and investors.

Additional Information

Depository in India :

1. There are two depositories viz NSDL and CDSL which are registered with SEBI.
2. Depositories must be registered as a company under the Companies Act.
3. Depositories must be registered as a Depository under the SEBI Act, 1992 and obtain a Certificate of Commencement of business from SEBI.
4. It should have bye-laws framed with previous approval of SEBI.
5. It should have a tie-up with one or more depository participants to render depository services on its behalf.
6. It is equipped with adequate system to safeguard and prevent manipulations of records and transactions as per the directions of SEBI.
7. Depository should have been established by one or more of the following :
   a) Public financial Institution.
   b) Bank.
   c) Foreign Bank .
   d) Recognized Stock Exchange.
   e) A Body corporate engaged in providing financial services
   f) A Body corporate constituted or recognized in foreign country for providing custodial, clearing or settlement services in securities market with an approval from the Central Government.
   g) Institution engaged in providing financial services established abroad and approved by Central Government.
8. Depository is deemed to be registered owner of securities on behalf of Investor (Beneficial owner) to effect transfer of securities on Investor's behalf.
9. Legal framework of a Depository
   a) SEBI Act, 1992
   b) SEBI (Depositories and Participants) (Amendment) Regulations 2012
   c) Bye-laws of Depository
   d) The Companies Act.

(2) Depository Participant (DP) :

1. It is the agent of Depository
2. DP is registered under the SEBI Act. It enjoys rights and obligations as specified under SEBI (Depository and Participants) Regulations of 1996.
3. It is an intermediary appointed by Depository.
4. DP acts as a link between Depository and the investor.
5. It directly deals with customers. It sends statement of accounts periodically.
6. It functions like a securities bank.
7. It facilitates Demateralisation.

8. It credits securities in the event of Rights Issue, Bonus Issue, etc.
9. It handles instant transfers of pay-outs like dividend, interest, etc.
10. It settles trade electronically.
11. Following can work as DPs :
    a) Financial Institutions
    b) Banks
    c) Approved Foreign Banks
    d) Custodians : Responsible for overseeing operations of assets/fund.
    e) Stock Brokers
    f) Clearing Corporation
    g) NBFC (Non Banking Financial Company)
    h) Registrar to an Issue or Share Transfer Agents
12. The DP maintains account of securities of each investor.
13. The DP has a unique number for identification.

(3) The Beneficial Owner (BO) :

1. The BO is the investor of securities who has availed the services of Depository Participant.
2. BO is entitled to all rights, benefits and is subject to all liabilities with respect to securities held by Depository.
3. The BO can also be called as client of Depository and DP.
4. BO/Client is required to open a Demat account with the DP for electronic holding of securities. BO has to pay charges to the DP for availing the services of DP.
5. BO is given a unique account number in which securities are held.

(4) The Issuer Company :

1. It means the company which has issued the securities which are dematerialized.
2. It must register with the Depository.

9.5 CONCEPTS/TERMS RELATED TO DEPOSITORY SYSTEM

1) **Dematerialization :** (Demat) is a process whereby a client can get physical certificates converted into electronic mode. The client has to surrender the certificates along with the Demat Request Form (DRF). The DP forwards these to the Depository who in turn forwards it to the Issuer. After confirmation from Issuer, the Depository will credit the securities in the Demat A/c with DP.
2) **Rematerialization :** (Remat) is the process whereby a client can get his electronic holdings of securities converted into physical certificates. The client has to give written request in the form of RRF (Remat Request Form) to the DP. The DP forwards the RRF to Issuer and the Depository. The Issuer prints the certificates and sends them to the client and simultaneously confirms the acceptance of Remat request to the Depository. The Depository via the DP debits account of the client with those securities.
3) **Fungibility :** In financial terms, fungibility means the state of being interchangeable. Some financial assets are fungible while some are not fungible. e.g.

a) land is not fungible as every unit of land has its unique quality which adds to or reduces its value.

b) Currency note is fungible as there is no difference between two currency notes of the same value.

Similarly, securities issued by the same company of the same class have same value no matter who owns them. The securities held in Demat/Electronic form are fungible. They are interchangeable, substitutable and cannot be distinguished from each other. Securities bear no notable features like distinctive number, certificate number or folio number.

4) International Securities Identification Number (ISIN)

1) It is a code that uniquely identifies a specific securities issue.
2) ISINs in any country are allotted by that country's NNA (National Numbering Agency)
3) ISIN is a standard numbering system which is accepted globally.
4) The International Organisation of Standardization (ISO) currently defines ISIN's structure.
5) In India, issuing ISIN to securities is assigned by SEBI to NSDL (for demated shares) SEBI works as NNA in India.
6) For Government securities, allotment of ISIN is done by the RBI.
7) ISIN consists of a 12 (Twelve) digit alpha-numeric code which is divided in 3 (Three) parts.
8) The company has to apply for ISIN for its securities with documents like prospectus.

Additional Information

ISIN :

1. It is a 12 (Twelve) character long alpha numeric code or ID Number.
2. It has 3 components (a) a prefix (b) a basic No. (c) a check digit.

   (a) The prefix is a two digit country code as given by ISO 6166 which is IN for India.

   (b) The basic No. is made of nine alphanumeric digits and/or alphabets.

   (c) The check digit at the end of ISIN is completed to check the validity of the ISIN

To Explain further :

1) The first two characters is the country code e.g. IN for India.
2) The third character is Issuer type as follows :

   i) Central Govt. : A
   ii) State Govt. : B
   iii) Municipal Corporation : C
   iv) Union Territory : D
   v) Company, Statutory Company, Corporation : E
   vi) Mutual Fund : F
3) The 4th to 7th characters (next four characters) represent company identity; of which first 3 characters are numeric and fourth is an alpha.
4) The 8th to 9th characters represent security type of a given Issue and are numeric. Some codes are given below : Security Type :

Equity shares : 01, Post Savings scheme : 02, Preference Shares : 03, Debentures : 12, Government Security : 14.

5) The 10th and 11th characters are serially issued for each security of the issuer entering the system -

6) The last digit is a double-add-double check digit.

e.g. this is how ISIN decoding is done :

INE002A01018 = $\boxed{\text{IN}}$ $\boxed{\text{E}}$ $\boxed{\text{002A}}$ $\boxed{\text{01}}$ $\boxed{\text{01}}$ $\boxed{\text{8}}$

IN = is the country code i.e. India

E = indicates that issuer is a company

002A = Identity of company

01 = Equity shares

01 = serially issued digits to the security

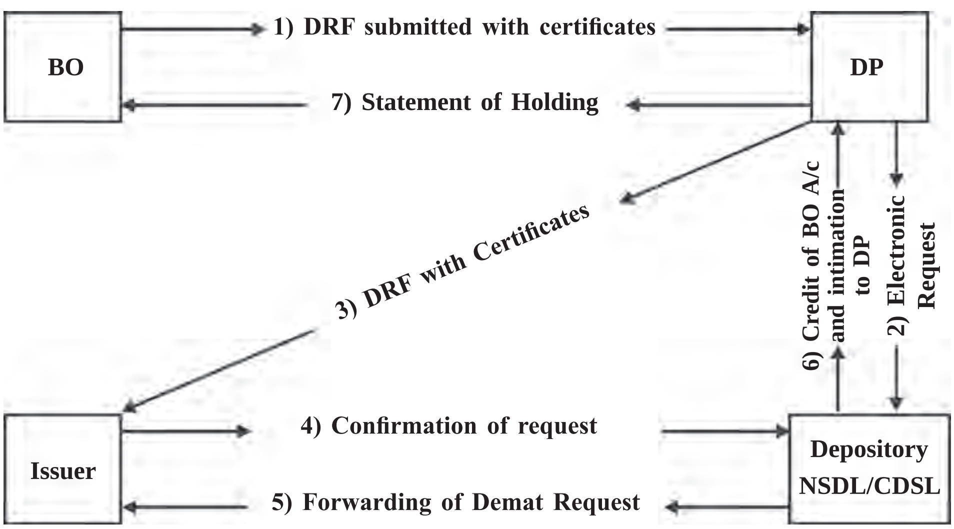
8 = is the check digit

9.6 FUNCTIONING OF DEPOSITORY SYSTEM

9.6.1 In case of conversion of physical certificates into electronic/ Dematerialisation Process :

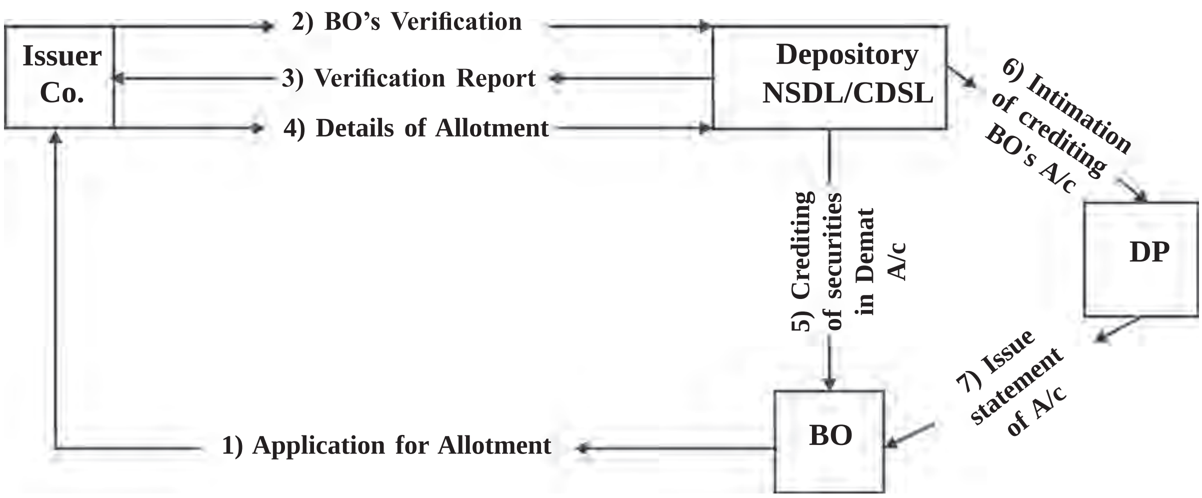
1) Investor submits DRF in triplicate and certificates to DP
2) DP enters the Demat request in its system and sends it to Depository.
3) DP dispatches the physical certificates and copy of DRF to the Issuer.
4) The Issuer verifies and confirms to Depository about demating of the securities.
5) Depository records the request in the system and forwards it to the Issuer.
6) Depository credits the demated securities to beneficiary account (Demat A/c) of Investor. Depository intimates the DP.
7) DP issues a statement of account to the Investor.

Illustrative Representation



9.6.2 In case of IPO (Initial Public Offer)

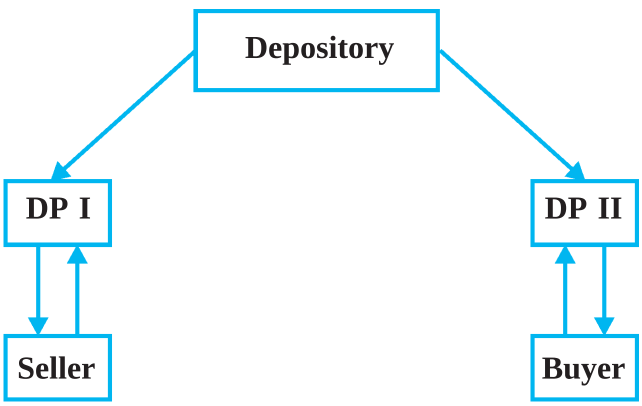
1) The investor (BO) submits his application for securities to the Issuer Company.
2) The Issuer Company verifies details of BO with the Depository.
3) After verification of BO's details, the Depository gives its report to the Issuer Company.
4) Issuer Company gives details of allotment of securities to Depository.
5) Depository credits the account of the BO.
6) Depository intimates the DP about crediting BO's account.
7) DP issues statement of account to BO.



9.6.3 Transfer of securities under the Depository system :

1. **In case of Sale of Shares :** The Transferor i.e. investor has to inform his DP by issuing DIS (Delivery Instruction Slip) which is filled and signed with the details of the security sold. At the end of the transaction the securities are debited in his Demat Account. Transfer can be done as off market trade or as market trade.

   a) **Off Market Trade :** Any trade settled directly between two parties on mutually agreed terms without the involvement of clearing corporation, share broker or stock exchange is called as Off Market Trade.
   Examples include legacy transfers, gifts, shifting of securities between a client and a sub broker, etc.

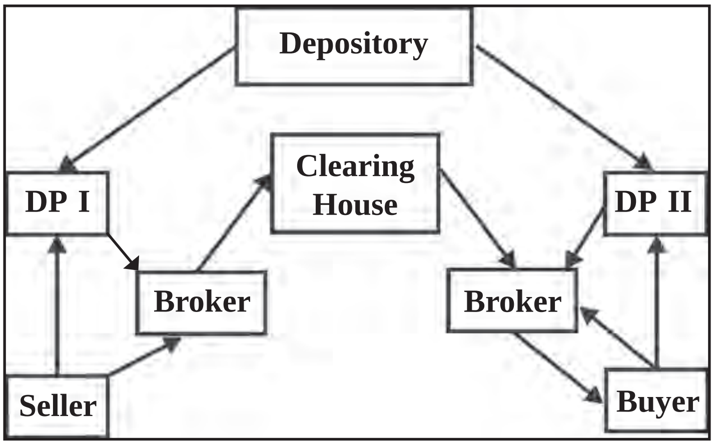


Procedure :

1) Transferor i.e. the seller gives delivery instructions to his DP to move securities from transferor's account to the buyer's account.
2) Transferee i.e. the buyer will receive the credit of the securities through his DP into the buyer's account after confirmation from Depository to the DP.
3) The funds / money will be paid by the buyer to the seller directly.

b) Market Trade :

Any trade which is settled through a clearing corporation is called "Market Trade'. These trades are done through stock brokers on a stock exchange.



Procedure :

1) Transferor gives delivery instruction to his DP. So securities move from Transferor's account to the Transferor's Broker account.
2) Securities then are transferred from brokers account to clearing house of the stock exchange as per the delivery instruction.
3) On the Pay-out-day, securities move from clearing house to the account of broker of the buyer.
4) After instructions and confirmation from Depository, securities move to the buyer's account.

2. In case of Purchase of Shares : The client i.e. the transferee sends the intimation to the DP giving details of security bought. The Depository after the due process informs the DP to transfer/credit the securities in the name of transferee. DP makes book entries in the accounts of investors to record all sales/ purchases of securities.

9.7 DEPOSITORIES IN INDIA :

The Depository Act of 1996 paved the way for the establishment of depositories in India. There are two Depositories which exist in India viz : 1) NSDL 2) CDSL.

A) **NSDL : National Securities Depository Limited :**

1) It is the first and the largest depository in India established in November, 1996.
2) It is promoted by IDBI (Industrial Development Bank of India), Unit Trust of India (UTI) and National Stock Exchange (NSE).
3) NSDL has its headquarters in Mumbai.

4) NSDL is a public limited company registered under the Companies Act.
5) NSDL provides various services to investors and other players in the capital market like Stock Exchanges, Banks, Issuers, Clearing Members, etc.
6) It renders services like account maintenance, dematerialization and rematerialization, settlement of trades through market transfers and off market transfer, nomination, transmission, distribution of non-cash corporate actions, dividend distributions, facility of freezing or locking of investors' accounts, Investor grievances, etc.

B) CDSL : The Central Depository Services Limited :

1) CDSL began its operations in February 1999.
2) It was promoted by Bombay Stock Exchange jointly with several banks.
   i) It has its headquarters in Mumbai.
   ii) CDSL has a wide DP network and offers the Demat services similar to NSDL across the country

Both these institutions have played a tremendous role in success of Depository System in India.

9.8 DISTINCTION : Dematerialization and Rematerialization.

Points	Dematerialization	Rematerialization
1. Meaning	Process of converting Physical certificates of securities into electronic form.	It is the process of conversion of electronic form of securities into physical form.
2. Conversion	Here, the paper form of securities is converted in to digitally/ electronically held securities.	Here, the electronic records are converted into physical/paper form securities.
3. Use of Form	It uses 'DRF' : Viz. 'Dematerialization Request Form' from Investor to the DP.	It uses 'RRF' : viz Rematerialization Request Form' from Investor to the DP.
4. Sequence	This is an initial process. It is a primary and Principal function of the depository.	This is a reverse process. It is a secondary and supporting function of depository. Already demated securities are remated.
5. Identification of Securities	Demated securities have no distinctive numbers. They are fungible.	Remated securities will have certificate and distinctive numbers as issued by company.
6. Securities Maintenance Authority	Depository is the custodian of securities and records.	The issuing company is the record keeping authority. Securities are maintained by the investor.
7. Difficulty of Process	Demat is an easy process. Also its not a time consuming process.	Remat is not only a time consuming but also a complex process.

N.B. : These two processes are diametric opposites of each other. Remat reverses the results of Demat.

SUMMARY

- Securities can be held either in (a) Physical Mode or (b) Electronic / Digital / Dematerialized modes.
- The physical mode has limitations like Risk of handling, Delays, Increased efforts, Time and cost.
- The paperless holding of securities is achieved by Depository System which was introduced in India by passing The Depository Act 1996.
- Depository System provides various benefits to Investors and the Issuing Company.
- Constituents of Depository System are Depository, DP, Beneficial Owner and the Issuer Company.
- Dematerialization means conversion of Physical securities into electronic form and Rematerialzation means conversion of electronically held securities into physical certificates.
- India has a Multi-Depository system. It has two Depositories (a) NSDL (1996), (b) CDSL (1999).

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. In physical mode, securities are held in .... form.
   a) Paper b) Dematerialization c) Electronic
2. Risk of losing certificates exists in .... mode.
   a) Physical b) Dematerialised c) Digital
3. In Depository System, securities are held in .... form.
   a) Scrip based b) electronic c) Physical
4. .... is the institute which facilitates electronic holding of securities.
   a) Depository Participant b) Issuer c) Depository
5. There is no payment of .... when securities are demated.
   a) Octroi b) Wealth Tax c) Stamp Duty
6. Depository Act was passed in ....
   a) 1919 b) 1996 c) 1999
7. India has a .... depository system.
   a) sole b) multi c) single
8. .... is a constituent of depository system.
   a) Government b) Issuer c) Trust
9. .... is the oldest depository in India.
   a) Dow Jones b) NSDL c) CDSL

10. Demat account is opened by ....

a) Beneficial Owner b) CDSL c) SEBI

11. Demated shares are...................... .

a) Non-transferable b) Fungible c) Bearer

12. .... is a unique code given to a security.

a) IBM b) BBM C) ISIN

13. In India ISIN for corporate securities is allotted by ....

a) NSDL b) Central Govt. c) State Govt.

14. .... has to apply for ISIN.

a) Company b) Depository Participant c) Depositors

15. .... has to pay charges to maintain Demat Account.

a) Investor b) Issuer c) Depository

16. NSDL is promoted by ....

a) NSE b) BSE c) FTSE

17. CDSL is promoted by ....

a) NSE (b) BSE c) FTSE

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Bad Delivery	1)	1956
b)	Depository Act	2)	A 12 digit number/code.
c)	ISIN	3)	Connects Government and Bank.
d)	Depository Participant	4)	Second Depository in India.
e)	CDSL	5)	The Issuer Company.
f)	Depository	6)	Problem faced in physical mode.
g)	Beneficial owner	7)	A 10 digit number/code.
		8)	Connects Depository and Investor.
		9)	First Depository in the world.
		10)	Coustodian of securities in electronic form.
		11)	Problem faced in electronic mode.
		12)	1996
		13)	Government Organisation.
		14)	The Investor.

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. This mode of holding securities may result in loss and theft of certificates.
2. The organization which holds the securities in electronic mode.
3. This system eliminates storing of certificates.
4. This system allows faster and easier transfer of securities.
5. The oldest Depository of India.
6. The country where depository system started for the first time.
7. The registered owner of securities.
8. The Agent of the Depository.
9. This process converts securities into electronic form from physical form.
10. This process converts securities into physical form from electronic form.
11. This means securities are without distinctive identity number.
12. This is the unique code for security given in depository system.

D) State whether the following statements are true or false.

1. Physical mode of holding securities is risky.
2. Allotment of securities take longer time when in physical mode.
3. Transfer of securities is easier in electronic mode.
4. Bad delivery is likely in Depository System.
5. Depository system began in the USA for the first time in the world.
6. India has a multi Depository System.
7. Depository system is very similar to banking system.
8. DP is a constituent of Depository System.
9. DP is an agent of Depository.
10. A Bank can work as a DP.
11. DRF is required for conversion from physical to electronic.
12. ISIN is a unique code given to the specific securities.

E) Find the odd one.

1. Elimination of storage of Certificates, Theft of Certificates, Torn Certificates.
2. NSDL, CDSL, NBFC
3. Depository, DP, RBI.
4. DP, BO, State Government.
5. Issuer, BO, Central Government.
6. DRF, RRF, PPF

F) Complete the sentences.

1. Central location for keeping securities in demated form is ....
2. Freezing of debit/credit of securities is possible in ....
3. First Depository of the world started in the year ....
4. The Indian Depository Act was passed in the year .,............ .
5. Link between Depository and Investor is ....
6. Account of securities of the Investors is maintained by ....
7. The process which converts physical securities in electronic form is ....
8. The process which converts digital securities in physical form is ....
9. The Issuer company must register with ....
10. The unique code identifying a security is ....
11. The first depository of India is ....

G) Select the correct option from the bracket.

(I)

Group 'A'		Group 'B'	
a)	Dematerialization	1)	....
b)	....	2)	DP
c)	First depository of world	3)	....
d)	CDSL	4)	....

(1999, Agent of Depository, Germany, Physical to electronic)

(II)

Group 'A'		Group 'B'	
a)	First depository in India	1)	....
b)	....	2)	Rematerialisation
c)	Fungibility	3)	....
d)	....	4)	ISIN

(12 digit code, NSDL, Electronic to physical, No distinctive number)

H) Answer in one sentence.

1. What is Depository System ?
2. Give examples of action termed as corporate action.
3. When was Depository Act passed in India ?
4. What is a DP ?
5. What is Dematerialisation ?
6. What is Rematerialisation ?

7. What is ISIN ?
8. Name the depositories in India.

I) Correct the underlined word/s and rewrite the following sentences.

1. <u>Electronic</u> mode of holding securities is risky.
2. Allotment and Transfer of securities is time consuming in <u>electronic mode</u>.
3. <u>Banking</u> system leads to a scrip less capital market.
4. Storage of Certificates is not required in <u>Physical</u> mode of holding
5. India has a <u>single</u> Depository system.
6. Depository Participant in India has to register under the <u>Partnership Act</u>.
7. Demat accounts are opened and maintained by the <u>Depository</u>.
8. Securities are fungible in <u>Physical</u> mode.
9. ISIN is a code given to <u>a company.</u>
10. ISIN of Indian Government securities is issued by <u>NSDL</u>.

J. Arrange in proper order.

1. a) Gets Statement of Accounts
   b) Open Demat Account
   c) Submit DRF
2. a) Investor (BO) submits application for securities to issuer company.
   b) Depository intimates the DP about crediting BO's Account.
   c) Issuer company gives details of allotment to Depository.

Q.2 Explain the following terms/concepts.

1. Depository system
2. Dematerialization
3. Rematerialization
4. Fungibility
5. ISIN

Q.3 Study the following case/situation and express your opinion.

1. Mr. Z holds 100 shares of Peculiar Co. Ltd. in Physical mode and wishes to convert the same in electronic mode :
   a) Mr. Z holds a Saving Bank Account with CFDH Bank Ltd. Can he deposit his shares in this account for demat ?
   b) What type of account is needed for the same ?
   c) Is it the RBI which will be the custodian of shares of Mr. Z after demating ?
2. Mr. R holds 100 shares of Peculiar Co. Ltd. in Demat mode :
   a) He wants to transfer one share each to his wife, daughter and son. Can he do so ?
   b) Does he need to submit DRF or DIS if he wants to transfer his shares ?
   c) Can he nominate his wife in his demat account ?

3. Mrs. Z wishes to open a Demat account in her name :
   a) Can she open the account going to Mumbai office of NSDL ?
   b) Is she required to pay for opening of account and its maintenance ?
   c) Does she have to send the shares to respective company for demating ?
4. Mr. L wants to demat his 25 shares of Peculiar Co. Ltd. bearing certificate No. 100 and distinctive No. 76-100.
   a) Which form is he required to fill as a written request to the DP ?
   b) Does he have to fill instrument of transfer if he wishes to transfer the same after demat ?
   c) Does he have to quote certificate no. and distinctive no. if he wishes to transfer his shares after it is in demat form ?
5. Mr. S holds 50 shares of Peculiar Co. Ltd. in demat form. The company has declared a dividend of ₹ 5/- per share and Bonus of 1:1 to its shareholders.
   a) How will Mr. S get his dividend ?
   b) Will he get Bonus share in Physical or demat ?
   c) Who is entitled to dividend and Bonus : Mr. S or the depository ? (NSDL in this case)

Q.4 Distinguish between the following.

1. Dematerlization and Rematerlization

Q.5 Answer the brief.

1. Explain disadvantages of physical mode of holding securities.
2. Explain any four advantages of Depository system to Investor.
3. Explain four advantages of Depository system to the Company.
4. Explain Depository as constituent of Depository System.
5. Explain DP as the constituent of Depository system.

Q.6 Justify the following statements.

1. Electronic holding of securities is safer than physical holding.
2. Depository provides easy and quicker transfer of shares.
3. Depository system results in reduced time, cost and efforts.
4. Depository system is very similar to the Banking system.
5. DP is an important constituent of Depository system.
6. Depository system allows both : Physical to electronic and electronic to physical conversion.
7. ISIN is necessary component of Demat.

Q.7 Answer the following questions.

1. What is Depository System and explain its advantages.
2. Explain the constituents of Depository system.

❑❑❑

10 DIVIDEND AND INTEREST

10.1 Dividend - Meaning

10.2 Features of Dividend

10.3 Legal provisions on dividend

10.3.1 Legal Provisions on sources of dividend

10.3.2 Legal Provisions for declaration of dividend

10.3.3 Legal provisions for payment of dividend

10.4 Unpaid and unclaimed dividend

10.5 Modes of payment of dividend

10.6 Interim dividend

10.7 Interest

10.7.1 Meaning

10.7.2 Features

10.8 Distinction

INTRODUCTION :

Profit making and its maximization is the prime aim of all business organisations including a Joint Stock Company. The shareholders invest with an aim of earning returns out of the profits of the company.

Profit is the difference between revenues and the expenses for a given period.

10.1 DIVIDEND - MEANING

The term dividend is derived from Latin word 'Dividendum' which means 'that which is to be divided'.

It is that part of the profits of the company which is distributed amongst its shareholders. Dividend is 'a share in distributable profits of the company to which the shareholder is entitled when it is formally declared by the company.'

Definition :

1. The Institute of Chartered Accountants of India has defined Dividend as, "a distribution to shareholders out of profits or reserves available for this purpose."
2. The Supreme Court has defined it as, "In case of going-concern, it means portion of profits of a company, which is allotted to the holders of shares in a company."

a) *Going concern means a business that is operating and making profits.*

b) *'Profits available for Distribution and profits available for Dividend' are different terms.*

The former means maximum profits which law allows a company to distribute to the shareholders by way of Dividend.

The latter means profits which the Directors consider should be distributed after making provision for transfer to reserve, past losses etc.

10.2 FEATURES OF DIVIDEND

1. It is the portion of profits of the company paid to its shareholders.
2. It is payable out of the profits of the company.
3. Dividend is an unconditional payment made by the company.
4. Company can pay dividend only to the shareholders viz. (1) Equity (2) Preference.
5. If the company has issued equity shares with differential rights as to dividend, the terms of issue of such shares will govern rights of shareholders about receiving the dividend.
6. Dividend cannot be declared out of capital.
7. Dividend can be declared only on recommendation of the Board of Directors.
8. Dividend as recommended by Board of Directors is approved and declared by a resolution passed at the Annual General Meeting by the shareholders.
9. Dividend for any previous year cannot be declared once that year's Annual Account has been approved in the AGM.
10. Dividend once approved and declared by shareholders creates a debt. It cannot be revoked.
11. Dividend includes Interim Dividend.
12. Dividend must be paid in cash and not in kind.
13. Dividend is to be paid on paid-up value of shares.
14. Dividend cannot be paid on calls paid in advance.

Note : Usually the term Dividend refers to Annual/final Dividend unless it is specifically mentioned as Interim Dividend.

10.3 LEGAL PROVISIONS ON DIVIDEND

10.3.1 Legal provisions on sources of Dividend

a) Company may declare and pay dividend for any financial year out of the following:

1) Current Profits i.e. profits of the company of that year arrived at, after providing for depreciation and transfer to Reserves.
2) Out of profits of the company of any previous financial year, after providing for depreciation.
3) Money provided by the Central or State Government to pay dividend.

b) Dividend can be paid out of Capital Profits :

On fulfiling these condition :

(i) Capital profits are realised in cash

(ii) Articles of Association of the company permits such a distribution

(iii) It remains as profits after revaluation of all Assets and Liabilities.

Capital Profits arise when a company sells part of its fixed assets at price higher than original cost of such assets or premium earned on the issue of shares.

c) Dividend cannot be paid out of Capital.

d) Dividend can be paid out of free reserves of company.

Free Reserves are the reserves available for distribution of profits as per latest audited Balance Sheet of the Company.

10.3.2 Legal Provisions for declaration of Dividend :

1) **Board Meeting :** Dividend can be declared only on recommendation of Board of Directors. Board Meeting should be called to pass resolution about :

   a) Rate of Dividend and amount of Dividend to be paid

   b) Book closure date for dividend

   c) Date of Annual General Meeting.

   d) Bank with which a separate account should be opened to remit the dividend amount.

2) **Shareholders' Approval :**

   a) Dividend is approved by shareholders by passing an Ordinary Resolution at the Annual General Meeting.

   b) Shareholders can declare a lower rate of dividend than what is recommended by the Board but not higher than that.

   c) Once the dividend is declared at the General meeting it cannot be revoked. Company is not permitted to declare it second time in that year.

3) **Separate Bank Account :** The company must deposit the dividend amount in a separate bank account opened in a scheduled bank called as Dividend Account within 5 (Five) days of its declaration.

   - **Listed company :** Where a company's shares are listed on the Stock Exchanges, additional requirements with respect to Listings agreements must be followed like.

     a) Notify stock exchange where company's securities are listed at least 2(two) days in advance of the date of meeting of the Board at which recommendation of final dividend is to be considered.

     b) Intimate Stock Exchange immediately about declaration of dividend after the Board Meeting.

     c) Give notice of Book closure to the stock exchange at least 7(seven) working days before the closure.

     d) Close the Register of Members and the Transfer Register.

     e) It must use electronic mode of payment such as Electronic Clearing Services (ECS) or National Electronic Fund Transfer (NEFT); as approved by the Reserve Bank of India (RBI)

> *1)* ***Book closure :*** *It means the time period when company does not handle any adjustments to the Register or requests to transfer Shares.*
>
> *2)* ***Record Date :*** *It is the cut-off date for determining the number of registered members who are eligible for corporate benefits like Dividends and Bonus shares.*

     f) Listed company has to express the dividend on per share basis only.

4) Prohibition to Pay Dividend :

a) A company which has failed to repay deposit or any interest on deposit cannot declare any dividend **on its equity shares.**

b) No dividend can be declared if company has defaulted on :

1) Redemption of Debentures or payment of interest, Redemption of Preference shares, payment of interest to financial institution, etc.

10.3.3 Legal Provisions for payment of Dividend :

1) Dividend must be paid in cash and not in kind.

2) Dividend may be paid by cheque or warrant or by any electronic mode to the shareholder.

3) Joint holding of shares : Dividend warrant should be sent to the registered address of the first named joint shareholder as per the Register of Members or to such a person at his address as the shareholder or joint shareholders have given to the company in writing.

4) Time limit within which Dividend is to be paid. Company must pay dividend within 30 (Thirty) days from the date of its declaration.

5) Dividend is payable only to the registered shareholders of the company.

Preference shareholders are entitled to the dividend before it is paid to the equity shareholders as per the terms of issue of the preference shares. Equity shareholders will get dividend from residual profits. i.e. after paying to preference shareholders and arrears of dividend on cumulative preference shares.

6) If shares are held in electronic form, dividend will be paid to the beneficial owner as per the statements furnished by the Depository. If shares are held in Physical form, dividend is paid to the shareholders whose names appear in Company's Register of Members.

7) Default : Default in paying dividend in the given time results in -

(a) Punishment to every Director of the company.

(b) Company will be liable to pay simple interest at the rate of 12% p.a. during the period when the default continues.

- If company fails to comply with any of the requirement of this section, the company and directors shall be liable to pay fine.

10.4 UNPAID AND UNCLAIMED DIVIDEND

The dividend declared by company but has not been paid by it or claimed by a shareholder within 30 days of its declaration is termed as Unpaid and Unclaimed Dividend.

Following rules govern the Unpaid/Unclaimed Dividend :

- **Unpaid Dividend Account (Unpaid / Unclaimed Dividend)**

a) Total amount of dividend which remains unpaid/unclaimed should be transferred to 'Unpaid Dividend Account' opened in a scheduled Bank by the company.

b) This transfer should be within 7 (seven) days of the end of 30 days within which payment was to be made. In other words this transfer should happen within 37 (Thirty seven) days from the declaration of dividend.

c) Within 90 (Ninety) days of transfer of amount in the 'Unpaid Dividend Account', the company is required to put on its website or any other website as approved by the Central Government, a statement which shows names, last known addresses and unpaid amount payable to each shareholder.

d) Any claimant to the Unpaid Dividend Account may apply to the company for the payment of money claimed.

e) Any amount in the unpaid Dividend Account of a company which remains unpaid/ unclaimed for a period of 7 (seven) years from the date of such a transfer shall be, transferred by the company to 'Investors Education and Protection Fund' (IEPF).

f) The claimant of money will have to follow the procedures and submit necessary documents to get claim from IEPF along with a statement in the prescribed form which gives details of such transfers.

IEPF has been set up by the Central Government, since 2001. Examples of some amounts to be transferred to IEPF are - matured deposits with companies, matured debentures with companies, etc.

10.5 MODES OF PAYMENT OF DIVIDEND

Dividend payable in cash may be paid by cheque or warrant or by electronic mode to the entitled shareholder.

Let's discuss the different ways in which dividend can be paid by company :

1) **Dividend Warrant :** It is a cheque sent by a company to a shareholder for payment of dividend to the registered address of the shareholder.

2) **Dividend Mandate :** A shareholder may wish to get dividend credited directly in the bank account. Shareholder is required to send a request to the company in the prescribed form called. 'Dividend Mandate'. Dividend mandate authorizes the company to pay dividend directly to shareholder's bankers.

Additional Information :

Benefit of 'Dividend Mandate' :

1) Saves efforts, time and cost : It saves time of the company in preparing and sending the cheques to the shareholders and simultaneously efforts and time of the shareholders to deposit the same and await its credit into the account.

2) Reduces the chances of loss of physical cheque in transit.

3) **Electronic Mode :** Company can use electronic mode to pay dividends to its shareholders.

(a) A listed company has to mandatorily use RBI approved electronic mode of payment such as ECS. (Electronic Clearing Services), NEFT (National Electronic Fund Transfer).

(b) Make arrangements with bank and in collaboration with other banks, if required, to pay the Dividend Warrants at par.

ECS and NEFT both are electronic transfer of fund modes. ECS is mainly used for debits and credits for low-value transaction which are frequent and repetitive; while NEFT is used for high-value transactions.

Dividend warrants at par means cheque of dividend where payee gets exact amount stated in the cheque without any charge payable even if it is issued out of the state.

10.6 INTERIM DIVIDEND - MEANING :

Dividend declared by the Board of Directors between two Annual General Meetings is called Interim Dividend. Interim dividend is paid in the middle of the accounting year i.e. before the finalisation of annual accounts for the year. Opinion of the company's Auditors should be taken before declaring Interim Dividend.

Features of Interim Dividend :

1. The Board of Directors has the power to declare Interim Dividend.
2. Interim Dividend is only a payment on account of the whole dividend for the year.
3. Company should provide depreciation for the entire year and not proportionately for a part of the year before declaring Interim Dividend.
4. Interim dividend cannot be paid out of any reserves.
5. Articles of Association of the company must authorize the Board of Directors to declare Interim Dividend.
6. The Board Meeting has to pass a resolution for declaring the Interim Dividend.
7. The amount to be given as Interim Dividend must be credited in a separate Bank account in a scheduled bank within 5 (five) days of its declaration.
8. Interim Dividend should be paid within 30 days of its declaration.
9. Unpaid / Unclaimed Interim Dividend should be transferred to 'Unpaid Dividend Account within 7 days of the expiry of 30 days of declaration i.e. 37 days of its declaration.
10. Any amount remaining unpaid/unclaimed in the 'Unpaid Dividend A/c' for 7 (seven) years should be transferred to IEPF.

10.7 INTEREST

10.7.1 Meaning

In financial terms, it is a payment made for using money of another. i.e. Borrower takes money from the lender.

So interest is the cost of renting money, for the borrower and it is the income from lending money for the lender.

10.7.2 Features

1) Interest is the price paid for the productive services rendered by capital.
2) It is directly related to risk. Higher the risk, higher is the interest.
3) Rate of Interest is expressed as annual percentage of Principal.
4) Rate of interest is determined by various factors like money supply, fiscal policy, volume of borrowings, rate of inflation etc.

5) Interest is a charge against the profit of the company. Even if company makes no profit, interest should be paid.
6) It is payable at a fixed and generally pre-determined rate.

Company has to pay interest if it has borrowed money from creditors like Debentures holders, Depositors, Bond holders, etc.

10.8 DISTINCTIONS

(1) Interim Dividend and Final Dividend

Points	Interim Dividend	Final Dividend
1. Meaning	It is declared and paid between two AGMs.	It is declared and paid after the close of the financial year.
2. Who Declares	It is decided and declared by the Board of Directors in the Board Meeting.	It is decided and recommended by the Board of Directors. It is declared by the shareholders in the AGM.
3. Authorization	It can be declared only if Articles of Association permits its declaration.	It's declaration does not need authorization by Articles of Association.
4. When Declared	It is declared between two Annual General Meetings of the company.	It is declared at the Annual General Meeting of the company
5. Rate of Dividend	Rate of Interim dividend is lower than final dividend.	Rate of final dividend is always higher than Interim Dividend.
6. Source	It is declared out of profits of the current accounting year.	It is declared from different sources like; current year's profits, free reserves, capital profits, Money provided by Govt. for dividend, etc.
7. Accounting Aspect	It is declared before preparation of the final accounts of the company	It is declared only after the accounts of the year are prepared and finalized.

(2) Dividend and Interest

Points	Dividend	Interest
1. Meaning	Dividend is the return payable to the shareholders of the company for their investment in the share capital.	It is the return payable to the creditors of the company viz. Debenture holder / Deposit holders for the loan given by them to the company.
2. Given to whom	It is paid to the member i.e. the owners of the company.	It is paid to the creditor of the company.

Points	Dividend	Interest
3. Obligation	It is to be paid only when company has made profits. Therefore no obligation / compulsion to pay dividend.	It is not linked to the profits of the company. Payment of interest is an obligation and is to be paid by the company compulsorily.
4. When Payable	It is payable when a company earns sufficient profit in a year after fulfilling all obligations.	It is payable every year irrespective of the profits of the company.
5. Rate	It is paid at a fluctuating rate to the equity shareholders since it is linked to the profits of company.	Rate of interest is fixed and pre-determined at the time of issue of the security.
6. Resolution	Payment of Final Dividend requires a Board resolution and an ordinary resolution at the AGM while Interim Dividend can be paid by passing only a Board Resolution.	Payment of interest does not require passing of a resolution at any meeting.
7. Accounting Treatment / Aspect	Dividend is an appropriation of profit.	Interest is a charge on profit.

SUMMARY

- The owners of company viz. the shareholders expect return on their investment in the form of profits of the company.
- Dividend is the share of profit paid to (a) Preference (b) Equity shareholders by the company.
- Dividend can be (a) Interim and (b) Final.
- Company has to follow legal provisions with respect to (a) Sources of Dividend (b) Declaration of Dividend (c) Payment of Dividend.
- Interim Dividend is a part of Final Dividend and it is paid before the end of the financial year from the profits earned during the year.
- Final Dividend is paid on actual profits arrived at after closure of books of accounts at the end of the financial year.
- The Board of Directors decide the quantum of dividend.
- Unpaid / unclaimed Dividend arises due to either company is unable to pay it or shareholder is unable to claim it within 30 days of declaration.
- Interest is an obligation paid by company when it raises borrowings in the form of (a) Debentures (b) Deposits (c) Loans.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. Dividend is paid to ....

   a) Shareholder b) Debentureholder c) Depositor

2. .... is profit shared by company with a shareholder.

   a) Interest b) Rent c) Dividend

3. Dividend is recommended by ....

   a) Managing Director b) Secretary c) Board of Directors

4. Interim Dividend is declared by ....

   a) Board of Directors b) Debentureholders c) Depositors

5. Final Dividend is declared by ....

   a) Board of Directors b) Shareholders c) Depositors

6. Dividend cannot be declared out of ....

   a) Capital b) Profit c) Reserves

7. Dividend amount should be transferred in a separate Bank Account within .... days of its declaration.

   a) 5 b) 15 c) 50

8. Dividend should be paid within .... days of its declaration.

   a) 3 b) 13 c) 30

9. .... holders get dividend from residual profits.

   a) Equity share b) Preference share c) Debenture

10. Dividend is paid first to .... shareholders.

    a) Equity b) Preference c) Deferred

11. .... warrant is a cheque containing dividend amount sent by company to the shareholders.

    a) Dividend b) Share c) Interest

12. IEPF is created by .... where unpaid dividend is transferred by company.

    a) Central Govt. b) Company c) Shareholders

13. Payment of .... Dividend must be authorised by the Articles of Association.

    a) Interim b) Final c) Bonus

14. .... is a return paid to creditors by the company.

    a) Dividend b) Interest c) Rent

15. .... is not linked to profits of the company.

    a) Dividend b) Interest c) Bonus

B) Match the pairs.

(I)

	Group 'A'		Group 'B'
a)	Dividend	1)	Equity Shareholders
b)	Interest	2)	Appropriation of profit.
c)	Interim Dividend	3)	Recommendation of Secretary.
d)	Final Dividend	4)	Registrar of company.
e)	Fluctuating Rate of Dividend	5)	Obligatory to pay.
		6)	Decided and Declared by the Board of Directors.
		7)	Decided by Board; declared by Members.
		8)	Decided by President of India.
		9)	Company not allowed to pay.
		10)	Declared by Govt. of India

(II)

	Group 'A'		Group 'B'
a)	Dividend	1)	Must inform stock exchange about Dividend declaration
b)	Interest	2)	Creditors
c)	IEPF	3)	Registered Shareholders.
d)	Unpaid Dividend Account	4)	Balance of unpaid Dividend Transferred here.
e)	Listed Company	5)	Unregistered company.
		6)	Non-listed company.
		7)	Unpaid/Unclaimed Dividend.
		8)	Balance of unpaid Bonus transferred here.
		9)	Must inform Government about Dividend declaration.
		10)	General Public.

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. The return on investment paid to the shareholders of the company.
2. The meeting where final dividend is declared.
3. The company which has to intimate stock exchange about declaration of dividend.
4. The shareholders who get dividend at a fixed rate.
5. The shareholders who get dividend at a fluctuating rate.

6. Request by shareholder in prescribed form for payment of dividend into shareholders bank amount.
7. Number of days within which payment of dividend be completed by company, after its declaration.
8. Dividend declared between two AGMs.
9. Dividend decided and declared by the Board.
10. The return paid to the creditors by the company.

D) State whether the following statements are true or false.

1. Dividend is paid to registered shareholders of the company.
2. Dividend is decided by the Board.
3. Dividend is decided by the shareholders.
4. Dividend once declared cannot be revoked.
5. Dividend cannot be paid out of capital.
6. Shareholders decide about the rate and amount of profit to be given as dividend.
7. All categories of shareholders get a fixed rate dividend.
8. IEPF is the fund created by company.
9. Interest is a liability for company.
10. Interest is paid to shareholders of company.

E) Find the odd one.

1. Final Dividend, Interim Dividend, Interest.
2. Out of Capital, Out of free reserve, Out of money given by government.
3. Dividend Account, Dividend Mandate, Unpaid/Unclaimed Dividend Account.
4. Dividend warrant, Dividend Mandate, Cheque.

F) Complete the sentences.

1. Word dividend is derived from Latin term ....
2. Dividend is paid to.......................... .
3. Dividend can be declared only on recommendation of ....
4. Dividend must be paid in.......................... .
5. The meeting at which final dividend is approved is ....
6. Dividend cannot be paid out of ....
7. Interim dividend is decided and declared by ....
8. Predecided and a fixed rate of dividend is paid to ....
9. Payment of dividend must be completed within ....
10. Payment of Interim Dividend needs to be authorized by ....
11. The obligatory payment made by company to its creditors is called as ....

G) Select the correct option from the bracket.

(I)

Group 'A'		Group 'B'	
a)	Dividendum	1)	....
b)	Interest	2)	....
c)	....	3)	Final Dividend
d)	....	4)	Interim Dividend
e)	Govt. Fund	5)	....

(Creditors, IEPF, Latin term, At Board Meeting, At AGM)

(II)

Group 'A'		Group 'B'	
a)	Preference Shares	1)	....
b)	Equity Shares	2)	....
c)	Deposit holders	3)	....
d)	....	4)	Payment of Dividend
e)	....	5)	Dividend Declared but not paid/claimed

(Unclaimed/Unpaid Dividend, Fixed rate Dividend, Dividend at a Fluctuating Rate, Interest, Within 30 days)

H) Answer in one sentence.

1. What is Dividend ?
2. Who has right to recommend Dividend ?
3. What is final Dividend ?
4. What is Interim Dividend ?
5. Who declares Interim Dividend ?
6. Which shares get dividend at a fixed rate ?
7. Which shares get dividend at a fluctuating rate ?
8. At which Meeting Interim Dividend is decided and declared ?
9. What is Interest ?
10. State the time within which Unpaid Dividend be transferred to unpaid dividend Account ?

I) Correct the underlined word/s and rewrite the following sentences.

1. Dividend is paid to <u>creditors.</u>
2. Interest is paid to <u>shareholders</u>.
3. <u>Final</u> Dividend is paid between two AGMs.
4. <u>Special Resolution</u> must be passed to declare Final Dividend.

5. Dividend must be paid within <u>60 days</u> of its declaration.
6. The Dividend to be paid should be transferred to Dividend A/c within <u>30 days</u> of its declaration.
7. <u>Dividend</u> is an obligation to be paid by a company every year.
8. <u>Preference</u> shareholders are given the last priority in payment of dividend.
9. <u>Preference</u> shareholders get dividend from residual profits.
10. <u>Dividend</u> is payable every year irrespective of profits made by company.

J) Arrange in Proper Order :

1. a) Recommendation of Dividend.
   b) Checking sufficiency of profits
   c) Board Meeting

2. a) Transfer to Dividend Account
   b) Transfer to IEPF
   c) Transfer to Unpaid Dividend Account

3. a) Closure of Register of Members.
   b) Intimate Stock Exchange of Board Meeting.
   c) Intimate Stock Exchange of declaration of dividend.

4. a) Decision on Rate of Dividend
   b) Transfer to IEPF
   c) Payment of Dividend.

5. a) Payment of Interim Dividend
   b) Board meeting deciding and declaring Interim Dividend.
   c) Authorization of Articles of Association.

Q.2 Explain the following terms/concepts.

1. Profit
2. Dividend
3. Interest
4. Final Dividend
5. Interim Dividend
6. Unpaid Dividend
7. Unpaid Dividend Account
8. Dividend Mandate
9. IEPF
10. Rate of Dividend.

Q.3 Study the following case/situation and express your opinion :

1. LMN Co Limited decides to declare dividend for the financial year 2018-19 in which it has earned profits less than their expectations.
   a) Is Board right in recommending a dividend of Rs. 5/- per share out of free reserves?
   b) Can Board declare the dividend though it is not approved by AGM ?
   c) Can the Board give dividend in the form of gifts ?

2. ABC Co. Ltd. decides to pay Interim Dividend

   a) Can it be paid out of free reserves ?

   b) Is the Board right in declaring the same at the Board Meeting ?

   c) Can the company distribute the same within 30 days of its declaration ?

3. RAJ Company limited decides to pay Interim Dividend

   a) Is the Board justified to decide Interim Dividend of ₹ 5/per share even though profits till date are insufficient ?

   b) Can the Board declare it out of Free Reserves ?

   c) Can the Board declare it out of Capital ?

4. DIAMOND Co. Ltd. is considering to declare Interim Dividend.

   a) In how many days of declaration it should transfer the funds to Dividend Account ?

   b) In how many days it must pay it to shareholders?

   c) In how many days of declaration it must transfer the funds to the Unpaid Dividend A/c?

5. The Board of Directors of STAR Co. Ltd. which is a listed company recommends a dividend of ₹ 15/- per share to be paid in cash.

   a) Is it justified to pay the dividend firstly to its Preference Shareholders and then after to Equity Shareholders?

   b) Is the AGM required to approve the same?

   c) Can the company pay dividend in cash?

6. GOLD Co. Ltd. declares a dividend of ₹ 10/- per share for F.Y. 2018-19.

   a) Is company under default, if dividend was not paid within 30 days of its declaration ?

   b) Is company right in transferring the unpaid dividend to its Debenture Reserve Account ?

   c) Does the company have to transfer the amount of unpaid dividend to IEPF after 30 days ?

Q.4 Distinguish between the Following.

1. Final Dividend and Interim Dividend
2. Dividend and Interest

Q.5 Answer in brief.

1. State any four points to be kept in mind by a Listed Company with respect to Dividend.
2. Discuss any four features of dividend.
3. Explain the features of Interest.

Q.6 Justify the following statements.

1. Dividend is paid out of profits of the company.
2. Interim dividend cannot be paid out of free reserves.
3. AGM is crucial for Final Dividend.
4. Listed Company has to follow additional guide lines on dividend matters.
5. Equity shares get last priority in dividend.
6. Unpaid dividend cannot be used by the company.
7. Interest is a liability/obligation of the company.
8. Approval of members is not needed for Interim Dividend.

Q.7 Answer the following questions.

1. Define Dividend and explain its features..
2. What is Interest? Explain its features.
3. Discuss legal provisions for declaration of dividend.
4. Explain Interim Dividend.

11 FINANCIAL MARKET

11.1 Financial Market - Meaning

11.2 Functions of Financial Market

11.3 Types of Financial Market

11.3.1 Money Market
- Meaning
- Features
- Important participants
- Instruments

11.3.2 Capital Market
- Meaning
- Features
- Instruments
- Types

11.4 Distinction

1. Money Market and Capital Market
2. Primary Market and Secondary Market

INTRODUCTION :

In an economy individuals, corporates, Government, etc. may have excess funds and may want to invest it. They are called investors. On the other hand there may be businessmen, corporates, Governments etc. which may need funds who are called as Borrowers. The investors lend money to the Borrowers through a market called as Financial Market.

11.1 FINANCIAL MARKET - MEANING

A Financial Market is a market where Financial assets i.e. Financial instruments are exchanged or bought and sold. Financial market helps in mobilisation of savings and convert it into investments. Thus financial market acts as an intermediary between investors and borrowers.

Financial instruments are documents in the form of legal agreement between two parties having a monetary value. It represents a financial asset to one party and a financial liability to another party e.g. securities like shares, bonds, debentures, derivatives, commercial papers etc. are financial instruments.

Derivatives *- Is a financial instrument which derives its value from an underlying asset. The underlying assets can be shares/stock, bonds, currencies, commodities etc.*

Financial Market attracts funds from investors and channelises them to corporations. The term Financial Market represents the market which raises finance for long term via the Capital Market and short term via - the Money Market.

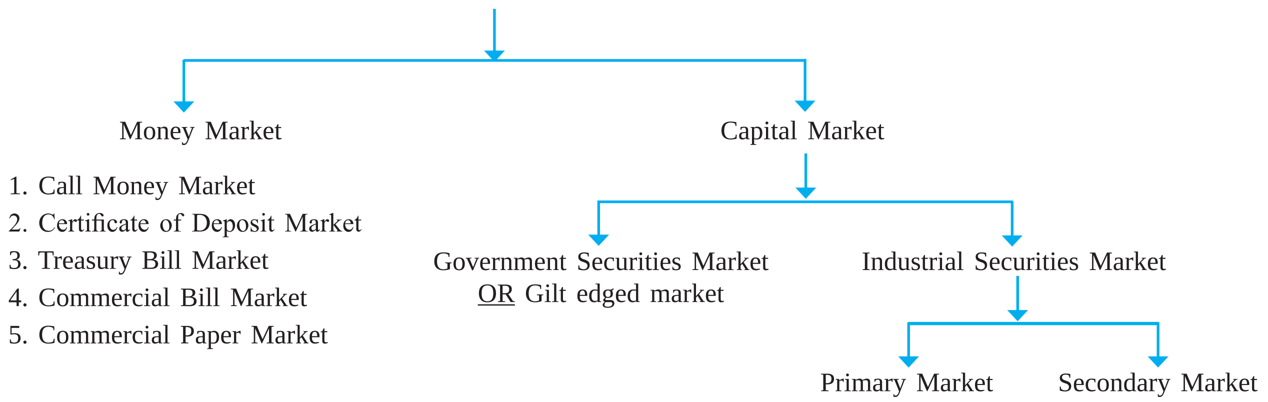
11.2 FUNCTIONS OF FINANCIAL MARKET

1. **Transfer of Resources :** Financial Market facilitates the transfer of real economic resources from lenders to ultimate users.
2. **Productive usage :** Financial Market allows productive use of the funds. In the hands of the investors their excess funds would have remained idle. Borrowers use these Funds for productive purposes.
3. **Enhancing Income :** Financial Market allows lenders to earn interest or dividend on their surplus funds, thus leading to the enhancement of the individual and the national income.
4. **Capital Formation :** Financial Market provides a channel through which savings flow to industrial and commercial organisations in the form of capital. This leads to capital formation.
5. **Price determination :** The financial instruments traded in a financial market get their prices from the mechanism of demand and supply. The investors are the suppliers of the funds and the corporates are the users. The interaction between the two and other market factors will help to determine the prices.
6. **Sale Mechanism :** Financial Market provides a mechanism for selling of a financial asset by an investor so as to offer the benefit of marketability and liquidity of such assets.
7. **Mobilizing Funds :** Idle funds in the hands of the investors can be productively used by corporates. Investors who have savings must be linked with corporates that require investment. So financial market enables the investors to invest their saving according to their choices and risk assessment. This will utilize idle funds and the economy will boom.
8. **Liquidity :** Financial market provides a mechanism for liquidating the financial instruments. This means at any given time, the investors can sell their financial instruments and convert them into cash. This is an important factor for investors who do not want to invest for a long period.
9. **Easy access :** Both investors and industries need each other. The financial market provides a platform where both the buyers and sellers can find each other easily.
10. **Industrial development :** Financial market helps in transforming savings into capital. Corporates use the funds of investors to undertake productive or commercial activities thereby leading to economic development.

11.3 TYPES OF FINANCIAL MARKET

Financial market is mainly classified as money market and capital market.

CLASSIFICATION OF FINANCIAL MARKET



11.3.1 Money Market :

- **Meaning :** Money market is a market for lending and borrowing of funds for short term. It is a market wherein lending and borrowing of funds take place for a short period of time which varies from one day to a year. Also the financial instruments traded in this market can be converted into cash easily without any loss of time and value. It is an important part of the financial system that helps in fulfilling the short term and very short term requirements of companies, banks, financial institutions, government agencies etc. It is a market for financial assets which are close substitutes for money. The instruments like commercial paper, treasury bills etc. are traded in the money market.

- **Features of Money Market :**

  1) The funds borrowed and lent in money market are for short term. The maximum period for which the funds are traded in the market is one year.
  2) It is a wholesale market for short term debt as the transaction volume is large.
  3) Trading may take place over the telephone, after which written confirmation is done by way of e-mails.
  4) Participants of money market include RBI, commercial banks, mutual funds, financial institutions, primary dealers and corporates.
  5) There is an impersonal relationship between the participants of the money market.
  6) Money market has no geographical area i.e. there is no fixed place for carrying out transactions.
  7) The instruments of money market can be converted easily into cash or have very short maturity periods. Moreover, the returns on investment is also low.
  8) Major segments of money market are :

     a) Call money market

     b) Certificate of Deposits market

     c) Treasury Bill market

     d) Commercial Bill market

     e) Commercial papers market

- **Some Important Participants in Money Market :**

  1) Reserve Bank of India : It is the most important participant in the money market. Through the money market, RBI regulates money supply and implements its monetory policy. It issues government securities on behalf of the government and also underwrites them. It acts as an intermediary and regulator of the market.

  2) Central and State Government : Central Government is a borrower in the Money Market, through the issue of Treasury Bills (T-Bills). The T-Bills are issued through the Reserve Bank of India (RBI). The T-Bills represent zero risk instruments. Due to its risk free nature banks, corporates, etc. buy the T-Bills and lend to the government as a part of its short-term borrowing programme. The state governments issue bonds called as State Development Loans.

  3) Public Sector Undertakings (PSU) : Many listed government companies can issue commercial paper in order to obtain its working capital.

4) **Scheduled Commercial Banks :** Scheduled commercial banks are very big borrowers and lenders in the money market. They borrow and lend in call money market, short notice market, Repo and Reverse Repo market.

5) **Insurance Companies :** Both the general and life insurance companies are usual lenders in the money market. They invest more in capital market instruments. Their role in the money market is limited.

6) **Mutual Funds :** Mutual Funds offer varieties of schemes for the different investment objectives of the public. Mutual funds schemes are liquid schemes. These schemes have the investment objective of investing in money market instruments.

> ***Additional Information :*** *A mutual fund is a type of financial vehicle made up of a pool of money collected from many investors to invest in a securities such as stocks, bonds, money market instruments and other assets.*

7) **Non Banking Finance Companies (NBFCs) :** NBFCs use their surplus Funds to invest in government securities, bonds etc. (Example of NBFC - Unit Trust of India)

8) **Corporates :** Corporates borrow by issuing commercial papers which are nothing but short-term promissory Notes. They are the lender to the banks when they buy the certificate of deposit issued by the banks.

9) **Primary Dealers :** Their main role is to promote transactions in government securities. They buy as well as underwrite the government securities.

- **Instruments of Money Market :** In the money market, only those financial instruments are traded which are immediate substitute for money. Some of these instruments are explained as follows :

1) **Call money and Notice money :** Call money and Notice money market is an important segment of the money market in India. Under Call money, funds are lent or borrowed for very short periods i.e. one day. Under Notice money, funds are lent or borrowed for periods between 2 days to 14 days. Funds have to be repaid within a specified time on the receipt of notice given by the lender. When one bank faces temporary shortage of cash, then another bank with surplus cash lends money to it. Hence Call/ Notice money market is also called as interbank Call money market.

2) **Treasury Bills (T-Bills) :** Treasury Bills are short term securities issued by Reserve Bank of India on behalf of the Central Government of India to meet the government's short term funds requirement. Treasury Bills have three maturity periods - 91 days, 182 days and 364 days. These bills are sold to banks and individuals, firms, institutions, etc. These bills are negotiable instruments and are freely transferable. The minimum value of T-bills is ₹ 25,000 or in multiples of ₹ 25000. These are issued at a discount and repaid at par and hence they are also called Zero Coupon Bonds.

3) **Trade Bills/ Commercial Bills :** Bill of Exchange also called as Trade bills are negotiable instruments or bills drawn by a seller on the buyer for value of goods sold under credit sales. These have short-term maturity period generally of 90 days and can be easily transferred. If the seller wants immediate cash, he can discount the trade bills with Commercial banks i.e. sell it to banks for cash. When the trade bills are accepted by Commercial banks it is known as Commercial Bills. Banks can rediscount the bills any number of times till the maturity of the bill.

4) **Commercial Papers (CPs) :** Commercial Paper is an unsecured promissory note issued by highly rated companies, All India Financial Institutions, like SIDBI, Exim Bank etc. and Primary Dealers with a fixed maturity period which varies from 7 days to maximum 1 year. The minimum value of CP is ₹ 5 lakhs or in multiples of ₹ 5 lakhs. It is issued at a discount to the face value and are highly liquid as it gives better returns than normal bank deposits. Individuals, Banks, Mutual funds, Companies, etc. invest in Commercial Papers.

5) **Certificate of Deposits (CDs) :** These are unsecured negotiable promissory notes usually issued by Commercial Banks and Financial Institutions. It is a receipt of funds deposited in a bank for a fixed period at a specified rate of interest. It can be issued for a minimum value of ₹ 1 lakh or in multiples of ₹ 1 lakh. They can be issued at a discount to the face value. They have a maturity period of minimum 7 days and maximum 1 year. (Maximum maturity may be 3 years, if the CDs are issued by Financial Institutions.) CDs can be bought by individuals, companies, etc.

6) **Government Securities :** The marketable debts issued by the government or by semi-government bodies which represent claims on the government is known as government securities. These securities are issued by agencies such as Central Government, State Government, local self-government e.g. Municipalities etc. These securities are safe investment as payment of interest and repayment of principal amount are guaranteed by the government.

7) **Repo or Repurchase Agreement :** Repo is an agreement where the seller of a security, (i.e. one who needs money) agrees to buy it back from the lender at a higher price on a future date. Usually this agreement is made between RBI and commercial banks. Repo rate is the rate at which banks borrow from RBI and Reverse repo rate is the rate at which RBI borrows from banks. RBI uses the repurchase agreement to control the money supply in the economy. These agreements are the most liquid of all money market investments having maturity ranging from 24 hours to several months.

8) **Money Market Mutual Funds (MMMFs) :** A Mutual Fund which invests in Money market instruments like Call Money, Repos, T-bills, CDs, etc. is called as MMMFs. This type of Mutual Fund invest in debt instruments which mature in less than 1 year and have low risk. Individuals and corporates are allowed to invest in MMMFs.

Activity : Collect additional information about Treasury Bills and Commercial Bills.

11.3.2 Capital Market :

- **Meaning :** It is the market for borrowing and lending long term capital required by business enterprises. The financial assets dealt with in the capital market have long or indefinite maturity period. The capital market is a core of a country's financial system as it helps in mobilisation of resources.

As per SEBI, capital market is a market for long term debt and equity shares. In this market, the capital funds comprising of both equity and debt are issued and traded. This also includes private placement of debt and equity as well as organized markets like stock exchanges.

One of the important functions of the capital market is to provide ease of transactions for both the investors and companies.

- **Features of Capital Market :**

Following are the main features of the capital market :

1) **Link between investors and borrowers :** The capital market links investors with the borrowers of funds. It routes money from savers to entrepreneurial borrowers.

2) **Deals in medium and Long-term investment :** Capital market is a market where medium and long term financial instruments are traded. Through this market, corporates, industrial organizations, financial institutions access long-term funds from both domestic and foreign markets.

3) **Presence of Intermediaries :** Capital market operates with the help of intermediaries like brokers, underwriters, merchant bankers, collection bankers etc. These intermediaries are important elements of a capital market.

4) **Promotes capital formation :** Capital market provides a platform for investors and borrowers of long term funds to trade. This leads to capital formation in an economy as it mobilizes funds.

Capital formation is the net addition to the existing stock of an economy's capital.

5) **Regulated by government rules, regulations and policies :** Capital market operates freely. However, it is regulated by government rules, regulations and policies. e.g. SEBI is the regulator of Capital markets.

6) **Deals in marketable and non-marketable securities :** Capital market trades in both marketable and non-marketable securities. Marketable securities are securities that can be transferred. e.g. Shares, Debentures etc. and non-marketable securities are those which cannot be transferred. e.g. Term Deposits, Loans and Advances.

7) **Variety of Investors :** Capital market has a wide variety of investors. It comprises both individuals like general public and institutional investors like Mutual Funds, Insurance companies, Financial Institutions, etc.

8) **Risk :** Risk is very high here as the instruments have long maturity periods. However, the return on investments is very high.

- **Instruments in capital market :**

1) Equity shares.
2) Preference shares.
3) Debentures.
4) Bonds.
5) Government securities
6) Public Deposits

- **Types of Capital Market :**

Capital market is mainly classified as –

1) **Government Securities Market or Gilt edged markets -** In this market, Government and semi-government securities are traded.

2) **Industrial Securities Market -** In this market, industrial securities, i.e. shares and debentures of new or existing corporates are traded. This market is further divided into :

A) Primary or New Issues Market- here companies sell fresh shares, debentures, etc. for the first time to the public.

B) Secondary Market - here already existing shares, debentures, etc. are traded through the Stock Exchanges.

A. Primary Market :

In Primary market, companies sell their shares, Debentures, etc. for the first time to raise fresh capital. It exclusively deals with the issue of new securities, i.e. securities that are issued to investors for the very first time. Hence this market is also known as New Issues Market.

The main function of the primary market is to facilitate capital formation. It is a place where investors can invest their surplus funds profitably and companies can raise capital easily. On the basis of type of funds raised, Primary market can be classified as Equity market and Debt market. In Equity market, securities like Equity shares, Preference Shares, Rights Issue, etc. are issued. In Debt market, debentures, bonds, fixed deposits, etc. are issued.

Methods of Raising funds in the Primary market :

1) **IPO (Initial Public Offer) :** Initial Public Offer refers to the process of offering shares of a company to the public for the first time. Investors can directly buy the securities from the issuing company.
2) **FPO (Further/follow-on public offer) :** When a company issues shares to the public after an initial public offer (IPO) it is called further/ follow-on public offer.
3) **Rights Issue :** When a company is in need of additional funds, they can first collect it from their current investors by giving them an opportunity to buy the shares of the company. Such an issue of shares is called as Rights Issue as the existing shareholders are given the "right" to buy new shares before it is offered to the public.
4) **Private placement :** Private placement means when a company offers its securities to a select group of persons identified by Board excluding qualified institutional buyers and employees (i.e. financial institutions, Banks, Insurance companies, etc.) not exceeding 200. This helps the company raise the funds efficiently, quickly and economically.

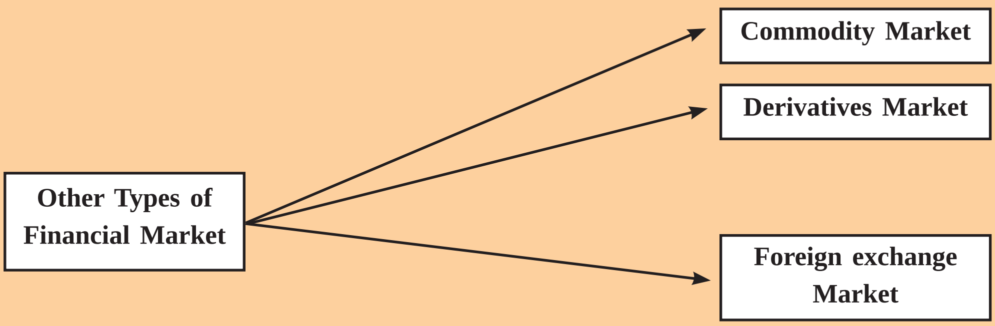
B. Secondary Market :

Secondary market is more commonly known as the stock market or the stock exchange. Here the previously issued securities are bought and sold by the investors. After IPO, when the shares are listed at the Stock Exchange, they can be traded in the secondary market. In this market the securities are traded between investors.

The main difference between the primary and the secondary market is that, in the primary market only new securities are issued, whereas in the secondary market the already existing securities are traded. There is no fresh issue in the secondary market.

Additional Information :

Other Types of Financial Market



a) **Commodity Market :** Market in which commodities are bought and sold between producers, traders, exporters and consumers.

b) **Derivatives Market :** In this market derivatives are traded. Derivatives can be classified as Future Contracts, Forward contracts, Options, Swaps, etc.

c) **Foreign exchange Market :** In this market foreign currencies are traded i.e. foreign currencies are bought with domestic currencies and foreign currencies are sold for domestic currencies.

11.4 DISTINCTION

1) Money Market and Capital Market

Points	Money Market	Capital Market
1) Meaning	It is a component of the financial market where short-term borrowing takes place.	It is a component of financial market where long-term borrowings takes place.
2) Time period	In money market, the instruments traded have maturity period of one year or less than one year.	In capital market, the instruments traded have maturity period of more than one year.
3) Instruments	Certificate of deposits, Repurchase agreements, Commercial paper, Treasury bills, etc. are the instruments traded in the money market.	Stocks, Shares, Debentures, Bonds, Securities of the government are the instrument of capital market.
4) Purpose of borrowing	Funds are borrowed to meet working capital requirements or for small investments.	Long term funds are required to establish new business, expand or diversify business or purchase of fixed assets.
5) Institutions	Participants in the market are Central banks, Commercial banks, Acceptance houses, Non-bank financial institution, Bill brokers, etc.	Stock exchanges, Commercial banks and Non-bank institutions, financial intermediaries, etc. are the participants in the market.
6) Risk	In the money market, risk factor is very less because maturity period of the instruments is less than one year.	In capital market, the risk is more as compared to in the money market. The reason behind this is the instruments have long maturity period.
7) Return on Investment	Return on investment in money market is less as they are highly liquid and safe.	Return on investment in capital market is comparatively high as they are more risky.
8) Role in Economy	This market increases liquidity of funds in the economy.	This market helps in mobilization of savings in the economy.

2) Primary Market and Secondary Market

Points	Primary Market	Secondary Market
1) Meaning	The issue of new shares by the company is done in the primary market.	The securities issued earlier are traded in the secondary market.
2) Mode of Investment	Direct investment in the securities. Securities are acquired directly from the company.	Indirect investment as the securities are acquired from other stakeholders.
3) Parties in action	The parties dealing in this market are company and investors.	The parties dealing in this market are only investors.
4) Intermediary	The underwriters are the intermediaries.	The security brokers are the intermediaries.
5) Value of security	The price of security in the primary market is fixed as it is decided by the company.	The price of security is fluctuating, depending on the demand and supply conditions in the market.

SUMMARY

- **Financial Market**

A Financial Market is a market in which people trade financial securities and derivatives at low transaction costs.

- **Functions of Financial Market**

1) Transfer of Resources
2) Productive usage
3) Enhancing Income
4) Capital Formation
5) Price determination
6) Sale Mechanism
7) Mobilizing Funds
8) Liquidity
9) Easy access
10) Industrial development

- **Money Market :**

Money market can be understood as the market for short term funds. It is a market wherein lending and borrowing of funds take place for a short term which varies from one day to a year.

- **Capital Market :**

It is the market for borrowing and lending long term capital required by business enterprises. The financial assets dealt with in the capital market have long or indefinite maturity period.

- **Primary Market :**

The most important type of capital market is the primary market. It is also known as new issue market.

- **Secondary Market :**

Secondary market is more commonly known as the stock market or the stock exchange. Here the previously issued securities are bought and sold by the investors.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. A financial market is a market in which people trade .... and derivatives at low transaction costs.

   a) Gold   b) Financial securities   c) Commodities

2. When the trade bills are accepted by commercial banks it is known as ....

   a) Treasury bills   b) Commercial bills   c) Commercial papers

3. Money market is a market for lending and borrowing of funds for .... term.

   a) short   b) medium   c) long

4. Central Government is a borrower in the money market through the issue of ....

   a) Commercial Papers   b) Trade Bills   c) Treasury Bills

5. .... is the market for borrowing and lending long term capital required by business enterprises.

   a) Money Market   b) Capital Market   c) Gold Market

B) Match the pairs.

Group 'A'		Group 'B'	
a)	Financial market	1)	Long term fund
b)	Money market	2)	New issue market
c)	Primary market	3)	Trading of commodities
d)	Commercial paper	4)	Short term fund
		5)	Trading of financial securities
		6)	Share market
		7)	Unsecured promissory note
		8)	Secured promissory note

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. A market where people trade financial securities and derivatives at low transaction cost.
2. A market which provides long term funds.
3. A market which provides short term funds.
4. A money market instrument used by bank when one bank faces temporary shortage of cash.
5. A bill which is issued by Reserve Bank of India on behalf of the Government of India.
6. A market which exclusively deals with the new issue of securities.

D) State whether the following statements are true or false.

1. A Financial Market is a market in which people trade financial securities and derivatives at high transaction costs.
2. Money market is the market for the long term funds.

3. Capital market is the market for the long term funds.
4. Primary market is also known as new issue market.
5. Secondary market is commonly known as stock market.
6. Commercial paper is a secured promissory note.
7. Treasury bills are issued by commercial banks.

E) Find the odd one.

1. Treasury Bills, Shares, Certificate of Deposit.
2. FPO, Private Placement, Commercial paper.
3. New Issues Market, Call Money Market, Secondary Market.

F) Complete the sentences.

1. Funds borrowed and lent in money market are for ___________ term.
2. When trade bills are accepted by commercial banks, it is known as _________
3. Unsecured negotiable promissory notes issued by a commercial bank is called as _______
4. New shares, debentures, etc. are traded in ____________ market.
5. In capital market the instruments traded have maturity period of more than ______ year.

G) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Money market	1)	_____________________
b)	Zero risk instrument	2)	_____________________
c)	_______________	3)	Capital market
d)	_______________	4)	Secondary market

(Buying and selling of existing securities, Treasury Bills, Funds for long term, Fund for short term)

H) Answer in one sentence.

1. What is financial market ?
2. What is call money market ?
3. What is Certificate of Deposits ?
4. What is Trade Bill ?
5. What is new issue market ?

I) Correct the underlined word/s and rewrite the following sentences.

1. In <u>Primary</u> market, already existing securities are traded.
2. Companies sell fresh shares for the first time to the public in <u>secondary market</u>.
3. In <u>Money</u> market, the instruments traded have maturity period of more than one year.
4. Financial market can be classified as capital market and <u>call money</u> market.

Q.2 Explain the following terms/concepts.

1. Financial market
2. Capital market
3. Money market
4. Call money market

5. Treasury bills
6. Commercial bills
7. Repurchase agreement
8. Primary market
9. Secondary market

Q.3 Study the following case / situation and express your opinion.

(1) Joy ltd. Company is a newly incorporated company. It wants to raise capital for the first time by issuing equity shares.

a. Should it go to primary market or secondary market to issue its shares ?

b. Should it offer its shares through public offer or rights issue ?

c. What will be the issue of Equity shares by Joy Ltd.Co. called as, IPO or FPO ?

(2) Mr. X is the CFO (Chief Financial Officer) of PQR Co. Ltd. which is a reputed company in the field of construction business. Often Mr. X has to decide on investing surplus funds of the company for short durations. And at times, he also has to decide the sources from where he can raise funds for short durations.

a. Assume on behalf of the company Mr. X has Rs. 5 lakhs and wants to invest for a short period. Should he buy Equity shares or Certificate of Deposit ?

b. The company has surplus funds and wants to invest it. However, he needs the money back in 4 months, so should he invest in Treasury Bills or Government Securities ?

c. Can the company issue Certificate of Deposit ?

Q.4 Distinguish between the following.

1. Primary market and Secondary market.
2. Money market and Capital market.

Q.5 Answer in brief.

1. State any four functions of financial market.
2. State any four features of money market.
3. State any four features of capital market.
4. Explain any 4 types of money market instruments.

Q.6 Justify the following statements.

1. Financial markets acts as link between investor and borrower.
2. Money market makes available short term finance through different instruments.
3. Capital market is useful for corporate sector.
4. There are many participants in money market.

Q.7 Answer the following questions.

1. Explain the functions of financial market.
2. State the instruments in money market.
3. State the features of capital market.

❑❑❑

12 STOCK EXCHANGE

12.1 Stock Exchange : Meaning

12.2 Functions of Stock Exchange

12.3 Major Stock Exchanges in India

12.4 Important terms related with Stock Exchange.

12.5 SEBI

12.5.1 Functions of SEBI

12.6 Distinction

INTRODUCTION :

A Stock Market is an important constituent of Capital market. It is a part of the financial market where corporate securities are bought and sold. It is an organised Capital market where second hand securities are bought and sold for investment and speculation purposes. Only listed Securities can be traded on a stock exchange.

Listed Securities : *Securities those are included in the trading list of the stock exchange. To get its securities listed, a company has to apply to the stock exchange and comply with its rules and regulations.*

A Stock Exchange is also called as a Secondary Market or Stock Market or Share Market or Share Bazar.

12.1 STOCK EXCHANGE : MEANING

Stock exchange is a specific place where various types of securities are purchased and sold. The term securities include equity shares, preference shares, debentures, government securities and bonds, etc. including units of Mutual Funds. Stock markets act as intermediary between investors and borrowers. To provide safety and stability to the investors, Stock exchanges in India are regulated by SEBI.

London Stock Exchange which was founded in 1571 is the oldest Stock Exchange in the world while Bombay Stock Exchange which was founded in 1875 is the oldest stock exchange in India.

Definitions of Stock Exchange :

According to the Securities Contracts (Regulation) Act 1956, the term stock exchange is defined as, “An association, organization or body of individuals, whether incorporated or not, established for the purpose of assisting, regulating and controlling of business in buying, selling and dealing in securities.”

Husband and Dockerary have defined stock exchange as :

“Stock exchanges are privately organized market which are used to facilitate trading in securities.”

The important features of a stock exchange are as follows -

1. **Market for Securities :** Stock exchange is a place where all types of corporate securities as well as securities of government and semi-government bodies are traded.

2. **Second Hand Securities :** Securities traded in Stock exchange are those securities which are already issued by the companies. In other words, second hand securities are bought and sold among investors in a stock exchange.
3. **Listed Securities :** Only securities that are listed with the stock exchange can be traded on a stock exchange. Listing of securities helps in protecting the interest of investors as companies have to strictly comply with the rules laid down by the stock exchange.
4. **Organised and Regulated Market :** All Listed Companies have to comply with the guidelines of SEBI. Companies will also have to function as per the rules and regulations laid down by the Stock exchange.
5. **Specific Location :** Stock exchange is a specific physical place where securities are traded. It is a market place where brokers and intermediaries meet to conduct dealings in securities. Today, all trading is done electronically on a stock exchange.
6. **Trading only through Members :** Securities in a Stock exchange can be traded only by the members of the exchange on their own behalf or through authorised brokers.

• Management of Stock Exchange :

Executive committee of stock exchange looks after the overall activities and management of stock exchange. The composition, powers and the name of the executive committee differs from exchange to exchange. There are other supporting committees to assist the executive committee like advisory committee, listing committee, etc.

• Organization Structure of Stock Exchanges in India :

In India, the stock exchange may be organized in one of the following three forms.

i) Voluntary non-profit making organization.

ii) Companies with liability limited by shares

iii) Companies with liability limited by guarantee.

The Securities Contract (Regulations) Act 1956, provides rules for their functioning, licensing, recognition and for controlling speculations.

• Membership of Stock Exchange :

The eligibility criteria for membership may differ from stock exchange to stock exchange (For additional information refer website of respective stock exchange.)

12.2 FUNCTIONS OF STOCK EXCHANGE

1. **Mobilisation of Savings :** Stock markets are organised and regulated market which protects the interests of the investors. This encourages small and big investors to invest in securities through the stock exchange. It thus provides a ready market for buying and selling securities.
2. **Capital formation :** Investors in securities are attracted due to good returns on investments and capital appreciation. This attracts more investors to invest through the stock exchange. Corporates too can easily raise funds by offering various types of securities to meet the needs of different types of investors. Thus Stock exchange serves as a tool for capital formation.

3. **Pricing of Securities :** The stock market helps to value the securities on the basis of demand and supply factors. The securities of profitable and growth oriented companies are valued higher as there is more demand for such securities. The valuation of securities is useful for investors, government and creditors. The investors can know the market value of their investment. The creditors can estimate the credit worthiness of a company.
4. **Economic Barometer :** A stock exchange is a reliable barometer to measure the economic condition of a country. Every major change in country and economy is reflected in the prices of shares. The rise or fall in the share prices indicates the boom or recession cycle of the economy. Stock exchange is also known as a pulse of economy or economic mirror as it reflects the economic conditions of a country.
5. **Protecting Interest of Investors :** Stock exchange protects the interest of investors. In stock market only the listed securities are traded. Stock exchange allows listing only after verifying the soundness of company. The companies which are listed have to operate within the strict rules and regulations laid down by the stock exchange. This ensures safety of dealing through stock exchange.
6. **Liquidity :** The main function of stock market is to provide ready market for sale and purchase of securities. The presence of stock market gives assurance to investors that their investment can be converted into cash whenever they want. The investors can invest in long term investment projects without any hesitation, as because of stock exchange they can convert long term investment into short term and medium term or even liquidate their investments whenever they want.
7. **Better Allocation of Capital :** The shares of profit making companies are quoted at higher prices and are actively traded so such companies can easily raise fresh capital from stock market. The prices of securities traded in the exchange indicates the opportunities for investments. So stock exchange facilitates allocation of investors fund to productive and profitable channels.
8. **Contributes to Economic Growth :** In stock exchange, securities of various companies are bought and sold. Investors invest in companies which give good return on investments. Hence companies, too, try to invest in most productive investment projects. This leads to capital formation as well as economic growth.
9. **Providing Scope for Speculation :** To ensure liquidity and demand or supply of securities the stock exchange permits healthy speculation of securities.
10. **Promotes the Habit of Savings and Investment :** The stock market offers attractive opportunities of investment in various securities. These attractive opportunities encourage people to save more and invest in securities of corporate sector rather than investing in unproductive assets such as gold, silver, etc.

12.3 MAJOR STOCK EXCHANGES IN INDIA

Following are the two most important Stock Exchanges in India.

1. **Bombay Stock Exchange (BSE) :** BSE - Bombay Stock Exchange, was set up in 1875. At that time it was called as The Native Share and Stock Brokers' Association. It is located in Dalal Street in Mumbai.

It is Asia's first Stock exchange. It is the first listed stock exchange in India. It is the 11th largest stock exchange in the world in terms of market capitalisation. It has the largest number of companies listed with it. (Approximately over 5000 companies are listed in the BSE.) It is now a demutualised and corporatized entity registered under the Companies Act, 1956.

The BSE switched to an electronic trading system in 1995. This automated, screen-based trading platform is called BSE On-Line Trading (BOLT). The BSE has also introduced a centralized exchange based internet trading system, **bsewebx.co.in** to enable investors anywhere in the world to trade on the BSE Platform.

2. **National Stock Exchange (NSE) :** NSE was set up by a group of leading Indian Financial Institutions in 1992 as a company and was recognized as a Stock Exchange in 1993 under the Securities Contracts (Regulation) Act, 1956. It started trading activities in 1994. It is the largest and most modern stock exchange in India.

   The NSE is located in Mumbai. It was the first demutualized electronic exchange in India. NSE was the first exchange in the country to provide a modern, fully automated screen-based electronic trading system which offered easy trading facility to the investors. The main index of NSE is the NIFTY which was launched in 1996.

12.4 IMPORTANT TERMS RELATED TO STOCK EXCHANGE

1. **Broker :** He is a member of a stock exchange who is licensed by stock exchange to buy or sell shares on his client's behalf. He is an agent between the investors and Jobber. His income is in the form of commission or brokerage.
2. **Jobber :** A Jobber is a dealer in stock exchange who carries on trading of securities in his own name. He buys securities as an owner and sells them at a higher price. The profit he makes is his income.

   He is a professional speculator in the stock exchange. He is not permitted to deal with investors directly.
3. **Bull (Tejiwala) :** A Bull is a speculator who expects the price of a share to rise in the future and buys with the hope of selling them at the higher prices to earn profit. His views are optimistic. Bulls actions leads to higher prices for securities as there is excess of purchase over sales.
4. **Bear (Mandiwala) :** A bear is a speculator who expects fall in the price of a security. Hence he sells his securities at the prevailing prices to avoid loss as he expects further fall in prices. Bears action leads to lowering the prices of securities as there is excess of sales over purchase.
5. **Stag :** A stag is a member who buys new issues of securities from Primary market and sells them later at higher prices, when the securities are listed, on the stock exchange.
6. **Lame Duck :** A lame duck is a bear broker whose expectations have gone wrong and makes a loss in his dealings. In other words, he had expected the prices of securities to fall (so he sold his securities) but instead, the prices have gone up.
7. **Wolves :** A Wolf is a broker who is a smart speculator. He is quick to judge the trends in the market and trades quickly thereby making profit.

8. **Settlement :** It refers to the scrip wise, i.e. security wise netting of trades by a broker after the trading period is over. (e.g. for equity spot markets it is T + 2 days T.i.e. Trading day.)
9. **Contract Note :** It is a note given by a broker to his client. It will be in a specific form. It validates the transaction. Both the broker and the client will have one copy each immediately after the transaction within 24 hours.
10. **Trading Ring :** The trading or auction of shares takes place on the floor of the stock exchange which is also known as Trading Ring. These days there is no trading room as all transactions are done electronically.
11. **Insider Trading :** Insider trading is the trading of a public listed company's securities by individual with access to non-public information about the company. Trading based on insider information is illegal. This is because it is seen as unfair to other investors who do not have access to the information.
12. **Day Trading :** The practice of buying and selling of securities within the same trading day before the close of the markets on that day is called 'Day Trading'.
13. **Sensex :** It is the Index of the BSE which represents the increase or decrease in prices of stocks of selected group of companies. Sensitive Index called as Sensex is made up of 30 largest and actively traded stocks of listed companies. It was created in 1986.

Index is a measurement of changes in the security prices. It is the benchmark index of the stock market.

14. **Nifty :** It is the index of the NSE. It is made up of 50 listed companies. It includes all the 30 Sensex stocks. It was created in 1996.
15. **Rally :** If the Sensex or Nifty moves in upward direction over a period of 14 to 20 trading sessions, it is called as a Rally. Bulls are active during the market rally.
16. **Crash :** If the Sensex or Nifty moves in downward direction, it is called as a crash. Bears are active during this period.
17. **Market capitalisation :** It is the total value of a company's outstanding (issued) shares multiplied by its current market price. It indicates the worth of the company.
18. **Stop-loss :** It is an instruction or order given by an investor to the broker to buy or sell a security when it reaches a certain price. This instruction is given by the investor when he wants to avoid losses when the prices fall below the stop price.

12.5 Securities and Exchange Board of India (SEBI)

The Securities and Exchange Board of India (SEBI) is the regulator of the capital markets in India. The SEBI was established in 1992 under the Securities and Exchange Board of India Act, 1992. It has its headquarters in Mumbai and has many regional and local offices all over India.

12.5.1 Functions of SEBI :

SEBI was set up with the objective of promoting the securities market, protecting the interest of the investors in securities market and to regulate the securities market. SEBI issues rules and regulations to be followed by the issuers of securities, the market intermediaries and the investors. It is a regulator of all the Stock exchanges in India.

The various functions of SEBI are -

1. To protect the interest of investors in securities market.
2. To promote the development of securities markets.
3. To regulate the business in stock exchanges and any other securities market.
4. To register and regulate the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustee of trust deeds, registrars to an issue, merchants bankers, underwriters, and such other intermediaries who may be associated with securities market.
5. To register and regulate the working of the Depositories, Depository Participants, Custodians of securities, foreign institutional investors, credit rating agencies.
6. To register and regulate the working of venture capital funds and collective investment schemes including mutual funds.
7. To promote and regulate self-regulatory organizations.
8. To prohibit fraudulent and unfair trade practice relating to securities markets.
9. To promote investors' education and training of intermediaries of securities market.
10. To prohibit insider trading in securities.

Activity : Find the meaning of Beta, Blue chip Stocks, Penny Stock and Mid Caps Stock.

12.6 DISTINCTION

Jobber and Broker

Points	Jobber	Broker
(1) Meaning	Jobber is one who buys and sells securities in his own name.	Broker is an agent who deals in buying and selling of securities on behalf of his client.
(2) Nature of Trading	A jobber carries out trading activities only with the broker.	A broker carries out trading activities with the jobber on behalf of his investors.
(3) Restrictions on Dealings	A jobber is prohibited to directly buy or sell securities in the stock exchange. Also he cannot directly deal with the investors.	A broker acts as a link between the jobber and the investors. He trades i.e. buys and sells securities on behalf of its investors.
(4) Agent	A jobber is a special mercantile agent.	A broker is a general mercantile agent.
(5) Form of Consideration	A jobber gets consideration in the form of profit.	A broker gets consideration in the form of commission or brokerage.

Activity :

1. Visit to Broker's Office.
2. Visit to Stock Exchange.

SUMMARY

- **Stock Exchange :**

Stock exchange is a specific place where trading of the securities is arranged in an organized manner.

According to the Securities Contracts (Regulation) Act 1956, the term stock exchange is defined as, "An association, organization or body of individuals, whether incorporated or not, established for the purpose of assisting, regulating and controlling of business in buying, selling and dealing in securities."

- **Functions of Stock Exchange :**

1. Mobilisation of Savings
2. Capital Formation
3. Economic Barometer
4. Pricing of Securities
5. Protecting Interest of Investors
6. Liquidity
7. Better Allocation of Capital
8. Contributes to Economic Growth
9. Providing scope for Speculation
10. Promotes the Habits of Savings and Investment

- BSE and NSE are the major stock Exchanges in India
- SEBI (Securities and Exchange Board of India)

The Securities and Exchange Board of India (SEBI) is the regulator for the securities market in India. The SEBI was established in accordance with the provisions of the Securities and Exchange Board of India Act, 1992.

EXERCISE

Q.1 A) Select the correct answer from the options given below and rewrite the statements.

1. A stock exchange is where stock brokers and traders can buy and sell ....

   a) gold b) securities c) goods

2. The .... is the first stock exchange to be recognized by the Indian Government under the Securities Contracts (Regulation) Act.

   a) BSE b) NSE c) OTCEI

3. .... is a dealer in stock exchange who carries on trading of securities in his own name.

   a) Jobber b) Broker c) Bull

4. A .... who expects fall in price of a securities.

   a) bull b) bear c) jobber

5. The practice of buying and selling within the same trading day before the close of the market on that day is called ....

   a) insider trading b) day trading c) auction

B) Match the pairs.

Group 'A'		Group 'B'	
a)	SEBI	1)	Expects the price of shares rise in future.
b)	Day Trading	2)	Expects the price of shares fall in future.
c)	Bull	3)	Buying and selling of securities within the same trading day.
d)	Bear	4)	To protect the interest of investors in securities market.
e)	BSE	5)	Buying and selling of securities to particular investors.
		6)	One of the oldest stock exchange in India.
		7)	To protect the interest of companies in securities market.
		8)	Buying and selling of securities within a week.
		9)	Newest Stock Exchange in India.
		10)	One who invests in new issues of securities.

C) Write a word or a term or a phrase which can substitute each of the following statements.

1. A specific place where trading of securities is arranged in an organized method.
2. The first stock exchange to be recognized by the Indian Government under the Securities Contracts Regulation Act.
3. A dealer in stock exchange who carries on trading of securities in his own name.
4. A speculator who expects the price of shares rise in the future.

D) State whether the following statements are true or false.

1. A stock exchange is a reliable barometer to measure the economic condition of a country.
2. Bombay Stock Exchange is the oldest stock exchange in India.
3. A broker is a dealer in stock exchange who carries on trading of securities in his own name.
4. Bear is a speculator who expects the prices of shares to rise in the future.

E) Complete the sentences.

1. The oldest Stock Exchange in India is the ____________
2. The largest and most modern stock exchange in India is the ____________
3. A person who buys or sells shares on behalf of his clients is called as __________
4. A speculator who expects fall in prices of shares is called as ________

F) Select the correct option from the bracket.

Group 'A'		Group 'B'	
a)	Regulator of capital market	1)	______________________
b)	________________	2)	Nifty
c)	Jobber	3)	______________________
d)	________________	4)	Oldest Stock Exchange in the world.

(London Stock Exchange, Index of NSE, SEBI, Trades in securities in his own name)

G) Answer in one sentence.

1. What is Stock Exchange ?
2. Who is Broker ?
3. Who is Jobber ?
4. Who is Bull ?

5. Who is Bear ?
6. Who is Lame Duck ?
7. What is Trading Ring ?
8. What is Sensex ?
9. What is Rally ?
10. What is Crash ?

H) Correct the underlined word/s and rewrite the following sentences.

1. One of the functions of SEBI is to protect the interest of <u>issuers of securities</u> in the securities market.
2. A <u>Broker</u> cannot directly deal with investors.
3. A <u>Bear</u> expects the prices of shares to rise in future.
4. A <u>Bull</u> buys new issues of securities from primary market.
5. A stock market is an important constituents of <u>money</u> market.

Q.2 Explain the following terms/concepts.

1. Stock exchange
2. Broker
3. Jobber
4. Bull
5. Bear
6. Contract Note

Q.3 Study the following case/situation and express your opinion.

1) Mr. Y is a practising Company Secretary offering advisory services to companies, institutions, etc. on corporate laws including Companies Act. He has received few queries from his clients, please assist Mr. Y in answering them.
   a) BDl bank wants to offer DP services. Whom should they approach for registering as DP ?
   b) KM Financial wants to offer Debenture Trustee services. Where should they apply for getting registered ?
   c) TT Ltd. Co. wants to issue an IPO. Should it get itself registered with SEBI ?

2) Mr. P has a recently got his B.Sc. degree. He has enrolled for a course in securities market. As a new student of this subject, he has few queries as follows :
   a) Does a Company need to be listed on a stock exchange to sell its securities through the stock exchange ?
   b) What is the term used for referring to a stock exchange's ability to reflect the economic conditions of a country ?
   c) What is the term which refers to the functions of stock exchange as a provider of ready market for sale and purchase of security ?

Q.4 Distinguish between the following.

1. Jobber and Broker.

Q.5 Answer in brief.

1. State the functions of SEBI.
2. State any four features of Stock Exchange.

Q.6 Justify the following statements.

1. The Securities and Exchange Board of India (SEBI) is the regulator for the securities market in India.
2. Stock exchanges work for the growth of the Indian economy.

Q.7 Answer the following questions.

1. Explain the functions of Stock Exchange.

❑❑❑

ANSWER KEY

CHAPTER 1 : INTRODUCTION TO CORPORATE FINANCE

Q.1 A) 1) Finance, 2) monetary, 3) capital, 4) taxes, 5) Fixed capital, 6) Working capital, 7) huge, 8) expand, 9) current assets, 10) Capital structure.

B) a. 6) Investment decision, b. 5) Fixed assets, c. 1) Sum of current assets, d. 9) Mix up of various sources of funds, e. 2) Deals with acquisition and use of capital

C) 1) Finance, 2) Financing decision, 3) Investment decision, 4) Fixed capital, 5) Working capital, 6) Working capital, 7) Production cycle, 8) Business cycle, 9) Capital structure, 10) Retained earnings.

D) 1) True, 2) True, 3) True, 4) False, 5) False, 6) False, 7) True, 8) True, 9) True, 10) True

E) 1) Cash, 2) Debenture Capital 3) Capital Structure.

F) 1) Finance manager, 2) Increase, 3) Production cycle, 4) Decrease,

G)

a) Financing decision	1) To have right amount of capital
b) Fixed capital	2) Longer period of time.
c) Investment decision	3) Deploy funds in systematic manner.
d) Working capital	4) Circulating capital
e) Combination of various sourses of funds	5) Capital structure

I) 1) Interest, 2) boom, 3) Debenture, 4) Preference shares

CHAPTER 2 : SOURCES OF CORPORATE FINANCE

Q.1 A) 1) Share, 2) International, 3) Equity shareholders, 4) Equity shareholders, 5) Bonus, 6) fixed, 7) cumulative, 8) convertible, 9) creditors, 10) Interest, 11) Interest, 12) equity shares, 13) internal, 14) creditor, 15) six, 16) 36, 17) U.S.A.

B) a. 4) Venture Capital, b. 9) Trust Deed, c. 10) Cautious Investor, d. 8) Instrument of debt., e. 2) Capitalisation of Profit

C) 1) Equity shareholders, 2) Share Certificate, 3) Participating Preference shares, 4) Debenture Trustees, 5) Equity shareholders, 6) Face value, 7) Market value, 8) Retained earning, 9) Deposit Receipt, 10) American Depository Receipt (A.D.R.), 11) Global Depository Receipt (G.D.R.), 12) Public Deposits, 13) Trade Credit, 14) Overdraft.

D) 1) True, 2) False, 3) True, 4) False, 5) False, 6) True, 7) True, 8) True, 9) False

E) 1) Retained earnings, 2) Redemption value, 3) ADR, 4) Trade Credit

F) 1) Capital, 2) Equity shares, 3) Directors, 4) Equity shareholders, 5) Creditors, 6) Global Depository Receipt, 7) 1948, 8) Trade Credit

G)

a) Equity shares	1) Fluctuating rate of Dividend
b) Preference shares	2) Dividend at fixed rate
c) Debentures	3) Interest at fixed rate
d) Retained earnings	4) Accumulated corporate profit
e) Public Deposit	5) Short term loan.

I) 1) Permanent 2) Fluctuating 3) Fixed 4) Internal 5) Creditor 6) Long 7) ADR/American Depository Receipt.

CHAPTER 3 : ISSUE OF SHARES

Q.1 A) 1) Share capital, 2) Authorised, 3) Public Issue, 4) Book Building, 5) Initial Public Offer, 6) Rights Issue, 7) Existing Equity Shareholders., 8) ESOS, 9) Private placement, 10) Board of Directors, 11) Allotment, 12) Share Certificate, 13) One month, 14) Forfeit, 15) Transfer, 16) Transmission.

B) (I) a. 5) Transmission of shares, b 4) Surrender of shares, c. 9) Fixed price issue method, d. 3) offered to existing employees, e. 6) Non - allotment of shares.

(II) a. 4) Capital offered to public to subscribe, b. 2) Any issue after IPO, c. 7) Free shares issued to existing equity shareholders, d. 5) Share certificate, e. 1) Non-payment of calls.

C) 1) Share capital, 2) Subscribed capital, 3) Reserve capital, 4) Cap price/ceiling price, 5) Initial public offer/IPO, 6) Further Public Offer/Follow on Public Offer FPO, 7) Rights Issue/shares, 8) Bonus shares, 9) Allotment of shares, 10) Allotment committee, 11) Minimum subscription, 12) Share certificate, 13) Forfeiture of shares, 14) Transferee, 15) Transmission of shares.

D) 1) False, 2) True, 3) True, 4) False, 5) True, 6) False, 7) False, 8) True, 9) False, 10) True

E) 1) Equity share capital, 2) Rights shares, 3) Face value, 4) ESOS, 5) Allotment of shares

F) 1) Preference shares, 2) Uncalled capital, 3) Transmission of shares, 4) Transferee, 5) Surrender of shares, 6) Partly paid up shares, 7) Duplicate share certificate, 8) 1 month of date of receipt of instrument of transfer, 9) Letter of allotment, 10) Over subscription, 11) Cut-off price, 12) Bonus shares,

G)

a) Public offer of shares	1) Shares offered to public
b) First time offer of shares	2) Initial Public Offer
c) Rights Issue	3) Shares offered to existing Equity shareholders
d) share offered to existing employees	4) ESOS
e) Operation of law	5) Transmission of shares.

I) 1) Authorised capital 2) Book builing method 3) IPO 4) partly paid 5) equity shareholders 6) underwriters 7) Letter of Regret 8) three 9) 25 %

J) 1. c) Allotment of shares b) Calls on shares a) Forfeiture of shares
2. c) Application form b) Allotment letter a) Share certificate
3. b) Application form c) Minimum subscription a) Return of allotment

CHAPTER 4 : ISSUE OF DEBENTURES

Q.1 A) 1) Debentures, 2) Partly or fully, 3) Debenture redemption reserve, 4) Debenture trustees, 5) 10 years, 6) secured, 7) 6 months, 8) Register of debenture, 9) Debenture trustees, 10) Debenture trust deed, 11) 60 days

B) a. 7) protects interest of debenture holders, b. 5) No voting rights,
c. 3) Secured debentures, d. 1) power to issue debentures,
e. 10) issued within 6 months of allotment of debentures

C) 1) Special resolution, 2) Debenture redemption reserve, 3) Debenture Trustees, 4) 10 years, 5) Secured debentures, 6) Debenture trust deed, 7) 60 days, 8) 6 months from allotment of debentures, 9) Debenture trustees, 10) Board of directors

D) 1) True, 2) False, 3) True, 4) True, 5) False, 6) False, 7) True, 8) False, 9) True, 10) False.

E) 1) Dividend, 2) Court, 3) Irredeemable debentures, 4) Shareholders

F) 1) Debenture trust deed, 2) Debenture trustee, 3) 60 days, 4) Board of directors, 5) 10 years from date of its issue, 6) NCLT, 7) Debenture Trustee, 8) Interest, 9) 75 % of the issue, 10) Credit rating.

G)

a. Debenture trustees	1) Trust deed,
b. Secured Debentures	2) charge on assets,
c. Register of debentures	3) names of debenture holders,
d. Issued within 6 months of allotment	4) debenture certificate,
e. No voting rights	5) debenture holders

I) 1) Register of Debenture holders 2) 10 years 3) secured 4) Interest
5) debenture holders 6) 6 months 7) 60 days 8) credit rating agency.

J) 1) a. Obtain Credit Rating
c. Receive application with money,
b. Entry in register of Debenture

2) b. Issue prospectus, c. Open Bank Account, a. Issue Debenture Certificate

3) c. Receive application with money, a. Hold Board Meeting for allotment
b. Issue debenture certificate.

CHAPTER 5 : DEPOSITS

Q.1 A) 1) Short term loan, 2) Public, 3) 100, 4) Government, 5) 36, 6) Circular, 7) 30, 8) Deposit Trustee, 9) Secured Deposit, 10) 21, 11) 1, 12) 30^{th} June

B) a. 5) 100% of aggregate of paid-up share capital and free Reserve,
b. 2) Signed at least 7 days before issuing Advertisement,
c. 4) Charge on tangible assets,
d. 8) Maximum 36 months, e. 10. File on or before 30^{th} June every year.

C) 1) Private Company, 2) Government Company, 3) 6 months, 4) 36 months, 5) Within 30 days of acceptance of deposits, 6) Circular, 7) Deposit Trust Deed, 8) Deposit Repayment Reserve Account, 9) Within 21 days from date of receipt of deposit, 10) Register of Deposit.

D) 1) False, 2) True, 3) False, 4) False, 5) True, 6) False, 7) True, 8) True, 9) False, 10) True

E) 1) Government Company, 2) Special Resolution, 3) Appointment of Registrar of Companies

F) 1) Short term loan, 2) Public, 3) ₹ 100 crores, 4) 35% of its paid-up share capital and free reserve, 5) 36 months, 6) Demand, 7) 3 months, 8) Advertisement, 9) Credit Rating Agency, 10) Deposit Repayment Reserve Account

G)

a. Government Company	1) deposits from public,
b. Private Company	2) deposits from member,
c. 36 months	3) Maximum tenure of deposits,
d. Secured deposit	4) charge on tangible assets,
e. Return of deposits	5) file on or before 30^{th} June.

I) 1) public 2) circular 3) Deposit Trustees 4) 21 days 5) Return of deposit 6) secured 7) 6

J) 1) b. Hold General Meeting, a. Appoint Deposit Trustee, c. Create charge on Assets
2) c. Issue Advertisement, b. Issue Deposit Receipt a. File Return of deposit
3) a. Obtain Credit Rating, c. Issue Deposit Receipt, b. Entries in Register of Deposits.

CHAPTER 6 : CORRESPONDENCE WITH MEMBERS

Q.1 A) 1) representatives of the shareholders, 2) 30, 3) dividend, 4) bonus, 5) 2, 6) prompt and precise, 7) Board of Directors, 8) Profit, 9) Dividend warrant.

B) a. 9) Instrument for Payment of Dividend,
b. 6) Dividend,
c. 4) Capitalisation of Reserve Fund,
d. 3) Electronic Clearing Service,
e. 5) National Electronic Fund Transfer.

C) 1) Bonus Shares, 2) Dividend Warrant, 3) Equity Shareholders, 4) Board of Directors, 5) Company Secretary, 6) Dividend Warrant.

D) 1) True, 2) False, 3) True, 4) False, 5) False, 6) False, 7) False

E) 1) Secrecy 2) Board of Directors, 3) Demat, 4) Lucid language

F) 1) Board of Directors, 2) Bonus, 3) 30, 4) Shareholders, 5) Secretary.

G)

a. Return on Shares	1) Dividend,
b. Capitalisation of Reserve Fund	2) Bonus Shares,
c. Correspondence	3) Written Communication,
d. ECS	4) Payment of Dividend Electronically

I) 1) Board of Directors, 2) Shareholder, 3) Existing Equity, 4) 30, 5) Two

J) 1. b) Application for shares, a) Allotment of shares, c) Share certificate
2. b) Applicant, a) Member, c) Bonus shares

CHAPTER 7 : CORRESPONDENCE WITH DEBENTUREHOLDERS

Q.1 A) 1) borrowed, 2) Creditors, 3) Debentureholder, 4) Interest Warrant, 5) Debentureholder, 6) Interest coupons, 7) Interest, 8) Debentures, 9) Redeemable, 10) Fixed, 11) Debenture, 12) Debentureholders.

B) a. 9) Creditor, b. 5) Interest warrant, c. 10) Conversion into equity shares, d. 3) Evidence of Loan, e. 4) Safe and Secured investment, f. 11) Redeemed after fixed period, g. 1) Borrowed Capital.

C) 1) Interest, 2) Debenture Certificate, 3) Creditors, 4) Convertible Debentures, 5) Debentureholder, 6) Debenture, 7) Registered Debentures.

D) 1) False, 2) True, 3) True, 4) True, 5) False, 6) False, 7) False, 8) False, 9) False, 10) True

E) 1. Depository, 2. Demat, 3. Dematerialisation, 4. SEBI

F) 1. Creditor, 2. Debenture, 3. Interest, 4. warrant, 5. Secretary, 6. Debentureholder, 7. Profit, 8. Voting, 9. 6, 10. Debenture Trustees, 11. Board of Directors.

G)

a. Return on Debentures	1) Interest
b. Debenture certificate	2) Issued within 6 months
c. Creditors	3) Debentureholder
d. Debt capital	4) Debentures
e. Board of Directors	5) Power to issue Debentures.

I) 1. Debentureholder, 2. Interest, 3. Debenture certificate, 4. Debentures, 5. Debenture Redemption Form, 6. 6

J) 1. c) Board meeting, a) Board Resolution, b) Allotment of Debentures.
2. c) Board meeting, b) Allotment of Debentures, a) Interest warrant

CHAPTER 8 : CORRESPONDENCE WITH DEPOSITORS

Q.1 A) 1. Creditors, 2. Short term, 3. 36, 4. 6, 5. Short term, 6. Working, 7. Board of Directors, 8. Fixed, 9. Interest

B) a. 4. Creditors, b. 1. fixed, c. 5. Evidence of deposits

C) 1. Interest, 2. Interest Warrant, 3. Fixed Deposit Receipt, 4. Repayment of Deposit, 5. 36 months,

D) 1. True, 2. True, 3. False, 4. False, 5. True, 6. False

E) 1. Dividend, 2. Depository

F) 1. Creditors, 2. Secretary, 3. Short, 4. 6 (six), 5. Interest

G)

a. Depositor	1) Creditor of the company
b. Return on Deposits	2) Interest
c. 36 months	3) maximum period of deposits
d. Minimum Period of Deposits	4) 6 months

I) 1. Creditors, 2. external, 3. Short, 4. Interest

J) 1. b. Acceptance of Deposits, c. Deposit Receipt, a. Renewal of Deposit
2. c. Acceptance of Deposits, b. Deposit Receipt, a. Payment of Interest.

CHAPTER 9 : DEPOSITORY SYSTEM

Q.1 A) 1. Paper, 2. Physical, 3. Electronic, 4. Depository, 5. Stamp Duty, 6. 1996, 7. multi, 8. Issuer, 9. NSDL, 10. Beneficial Owner, 11. Fungible, 12. ISIN, 13. NSDL, 14. Company, 15. Investor, 16. NSE, 17. BSE

B) a - 6) Problem faced in physical mode, b - 12) 1996, c - 2) A 12 Digit code, d - 8) connects Depository and Investors, e - 4) Second Depository in India, f - 10) Custodian of securities in electronic form, g - 14) The investors.

C) 1. Physical mode, 2. Depository, 3. Depository, 4. Depository, 5. NSDL, 6. Germany, 7. BO, 8. DP, 9. Demat, 10. Remat, 11. Fungibility, 12. ISIN.

D) 1. True, 2. True, 3. True, 4. False, 5. False, 6. True, 7. True, 8. True, 9. True, 10. True, 11. True, 12. True,

E) 1. Elimination of storage of certificate, 2. NBFC, 3. RBI, 4. State Govt., 5. Central Govt., 6. PPF

F) 1. Depository, 2. Depository/Depository system, 3. 1947, 4. 1996, 5. DP, 6. DP, 7. Demat, 8. Remat, 9. Depository, 10. ISIN, 11. NSDL.

G) (i)

a. Dematerialisation	1) physical to electronic
b. Agent of Depository	2) DP
c. First Depository of World	3) Germany
d. CDSL	4) 1999

(ii)

a. First Depository in India	1) NSDL
b. Electronic to physical	2) Rematerialisation
c. Fungibility	3) No distinctive number
d. 12 digit code	4) ISIN

I) 1) Physical, 2) Physical, 3) Depository, 4) Electronic/ Depository, 5) Multi, 6) SEBI Act, 7) DP, 8) Electronic, 9) Securities, 10) RBI

J) 1. b) Open Demat Account, c) Submit DRF, a) Gets Statement of Accounts

2. a) Investor (BO) submits application for securities to issuer company, c) Issuer company gives details of allotment to Depository, b) Depository intimates the DP about crediting BO's Account.

CHAPTER 10 : DIVIDEND AND INTEREST

Q.1 A) 1. Shareholder, 2. Dividend, 3. BOD, 4. BOD, 5. Shareholder, 6. Capital, 7. 05, 8. 30, 9. Equity share, 10. Preference, 11. Dividend 12. Central Govt., 13. Interim, 14. Interest, 15. Interest,

B) (I) a - 2) Appropriation of profit, b - 5) Obligatory to pay, c - 6) Decided and declared by the Board of Directors , d - 7) Decided by Board; declared by members. e - 1) Equity shareholders.

(II) a - 3) Registered shareholders, b - 2) Creditors, c - 4) Balance of unpaid Dividend Transferred here, d - 7) Unpaid/Unclaimed Dividend, e - 1) Must inform stock exchange about Dividend declaration

C) 1. Dividend, 2. AGM, 3. Listed Company, 4. Preferences shareholder, 5. Equity shareholders, 6. Dividend Mandate, 7. 30 days, 8. Interim Dividend, 9. Interim Dividend, 10. Interest,

D) 1. True, 2. True, 3. False, 4. True, 5. True, 6. False, 7. False, 8. False, 9. True, 10. False

E) 1. Interest, 2. Out of Capital, 3. Dividend mandate, 4. Dividend Mandate

F) 1. Dividendum, 2. Registered shareholders, 3. BOD, 4. Cash, 5. AGM, 6. Capital, 7. BOD, 8. Preference shareholders, 9. 30 days, 10. Articles of Association, 11. Interest

G) (I)

a. Dividendum		1) Latin term
b. Interest		2) Creditors
c. At AGM		3) Final Dividend
d. At Board Meeting		4) Interim Dividend
e. Govt. Fund		5) IEPF

(II)

a. Preference Shares	1) Fixed rated Dividend
b. Equity shares	2) Fluctuating rated Dividend
c. Deposit holders	3) Interest
d. Within 30 days	4) payment of Dividend
e. Unpaid / Unclaimed Dividend	5) Dividend Declared but not paid / claimed

I) 1. Registered shareholder, 2. Creditors, 3. Interim, 4. Ordinary Resolution, 5. 30 days, 6. 05 days, 7. Interest, 8. Equity, 9. Equity, 10. Interest

J) 1. b) Checking sufficiency of profits,
c) Board Meeting,
a) Recommendation of Dividend

2. a) Transfer to Dividend Account,
c) Transfer to Unpaid Dividend Account,
b) Transfer to IEPF.

3. b) Intimate Stock Exchange of Board Meeting,
c) Intimate Stock Exchange of declaration of dividend,
a) Closure of Register of Members.

4. a) Decision on Rate of Dividend,
c) Payment of Dividend,
b) Transfer to IEPF.

5. c) Authorization of Articles of Association,
b) Board meeting deciding and declaring Interim Dividend,
a) Payment of Interim Dividend.

CHAPTER 11 : FINANCIAL MARKET

Q.1 A) 1) Financial securities, 2) Commercial bills, 3) Short, 4) Treasury Bills, 5) Capital market

B) a) - 5) Trading of Financial securities, b) - 4) short term fund.
c) - 2) New Issue Market d) - 7) Unsecured promissory note.

C) 1) Financial Market, 2) Capital Market, 3) Money market,
4) Call money/Notice money, 5) Treasury Bill, 6) Primary market/New issue market

D) 1. False, 2. False, 3. True, 4. True, 5. True, 6. False, 7. False

E) 1. Shares, 2. Commercial paper, 3. Call Money Market.

F) 1. Short, 2. Commercial Bills, 3. Certificate of Deposit, 4. Primary/New Issues, 5. One.

G)

a. Money market	1) Funds for short term
b. Zero risk instrument	2) Treasury Bill
c. Funds for long term	3) Capital market
d. Buying and selling of existing securities	4) Secondary market

I) 1. Secondary 2. Primary, 3. Capital, 4. Money.

CHAPTER 12 : STOCK EXCHANGE

Q.1 A) 1) Securities, 2) BSE, 3) Jobber, 4) bear, 5) day trading

B) a) - 4) To protect interest of investors in securities market.

b) - 3) Buying and selling within the same trading day.

c) - 1) Expects the price of shares rise in future.

d) - 2) Expects the price of shares fall in future.

e) - 6) One of the oldest stock exchange in india.

C) 1) Share Market/stock exchange/stock market 2) Bombay stock exchange, 3) Jobber, 4) Bull

D) 1. True, 2. True, 3. False, 4. False

E) 1. Bombay Stock Exchange, 2. National Stock Exchange, 3. Broker 4. Bear

F)

a. Regulation of Capital Market	1) SEBI
b. Index of NSE	2) Nifty
c. Jobber	3) Trades in securities in his own name
d. London Stock Exchange	4) Oldest Stock Exchange in the world.

H)

1. Investors	2. Jobber	3. Bull
4. stag	5. Capital	

❑❑❑

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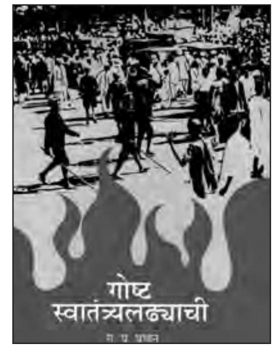

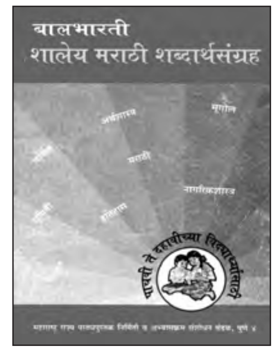

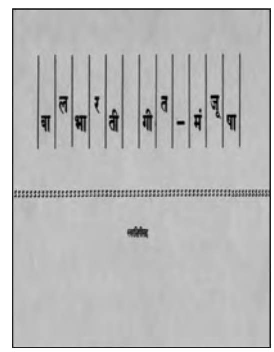

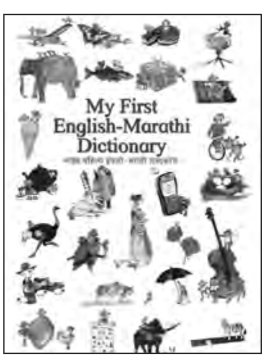

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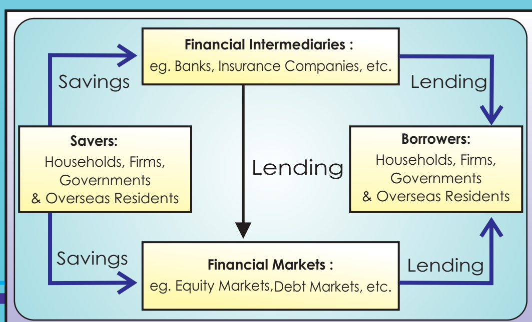

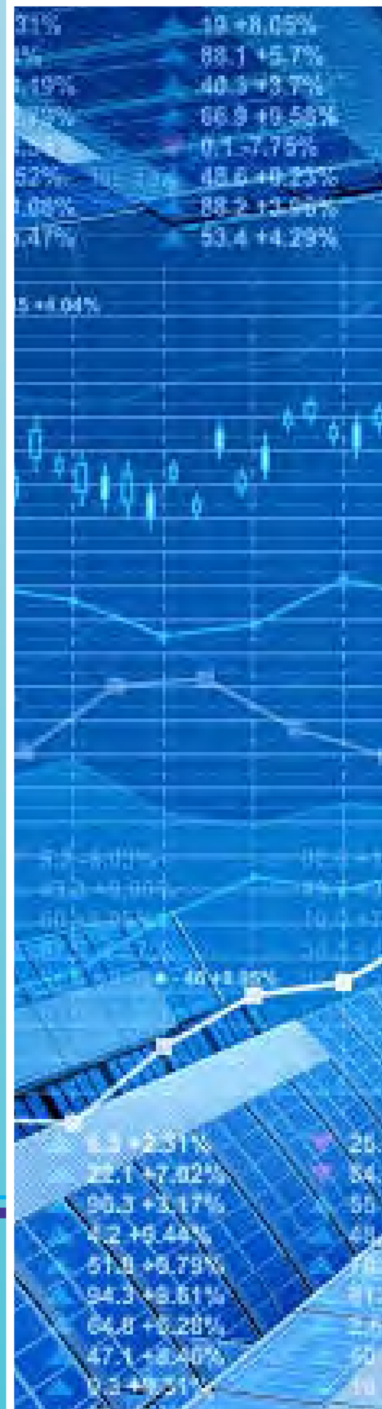

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