news flash

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MINISTRY OF CORPORATE AFFAIRS AMENDS THE UNLISTED PUBLIC COMPANIES (PREFERENTIAL ALLOTMENT) RULES

The Ministry of Finance had issued Unlisted Public Companies (Preferential Allotment) Rules, 2003 ("**Rules**") for preferential issue of equity shares, fully convertible debentures, partly convertible debentures or any other financial instruments, which would be convertible into or exchanged with equity shares at a later date by unlisted public companies.

The Ministry of Corporate Affairs **("MCA")** has now amended the Rules by a notification dated 14th December, 2011 ("**Notification**") as follows:

(1) The definition of preferential allotment has been substituted for the sake of additional clarity and now includes the term *hybrid instruments convertible into shares*. The Notification further provides that:

(a) the name, father's name, address and occupation of persons to whom the preferential allotment is proposed to be made should be mentioned in the shareholders resolution; and

(b) the proposed offer should not be made to more than 49 persons. This proviso confirms the provision set out in Section 67(3) of the Companies Act, 1956 ("**Act**").

(2) The Rules required a special resolution at a shareholder's meeting in case of preferential allotments. The Notification now clarifies that this requirement is also applicable to *hybrid instruments convertible into shares*. The existing requirement of acting upon such a resolution within 12 months of passing it, still remains.

(3) A new provision has been inserted, as follows:-

(a) No fresh offer or invitation shall be made unless the allotment with respect to any offer or invitation made earlier has been completed in accordance with the provisions of Section 60B (9) of the Act. This provision when read with Section 60B (9) of the Act now categorically requires an unlisted public company to file a final prospectus (in respect of its preferential issue) with the Registrar of Companies upon closing of the offer of securities. It is not clear whether the prospectus had to be filed hitherto.

(b) Any offer or invitation not in compliance with Section 81(1A) read with of section 67(3) of the Act shall be treated as a public offer and the provisions of the Securities Contracts (Regulation) Act, 1956 and the Securities and Exchange Board of India Act, 1992 ("**SEBI**") shall be complied with. Section 81(1A) of the Act provides for passing of a special resolution for the preferential allotment. Section 67(3) of the Act states *inter alia* that an offer or invitation of shares/ debentures shall not be treated as

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a public offer if such offer or invitation is made to less than 50 persons and is not intended to be made available, whether directly or indirectly, for subscription or purchase to persons, other than the select persons receiving the offer or invitation.

(c) All allotments should be completed within 60 days from the receipt of the application money. However if the allotment is not made as aforesaid, the company shall repay the application money within 15 days thereafter, failing which it will be required to be re-paid with interest at 12% p.a.

(d) All money payable on subscription shall be paid through cheque or demand draft or other approved banking channels. All such money received on such application shall be kept in a separate bank account and shall only be used for:
    (i) adjustment against allotment of securities; or
    (ii) repayment of monies where the company is unable to allot securities.

(e) A company offering securities shall not release any public advertisements or utilize any media, marketing or distribution channels or agents to inform the public at large about such an offer.

Implications

The procedure for preferential allotment has become more stringent. The compliance with SEBI regulations has been specifically stated. Further, the Notification increases the disclosure and compliance requirements. The MCA intends to control and check flow of black money and money laundering by barring cash payments. Lastly, these changes will lead to greater transparency and improved level of corporate governance.

Disclaimer

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