

Comparative analysis – Issue of shares & securities on private placement basis, preferential offer & rights basis under Companies Act



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The concept of 'offer and issue of shares or securities' by a company is important from the perspective of raising funds, capital re-organisation, change in control of the company, strategic investments in the company, etc. Depending upon the type of issue (public offer, rights offer, preferential offer, etc.), the nature of compliances, timelines, disclosures, valuation requirement, reporting to the Ministry of Corporate Affairs changes. In certain cases, the disclosure or compliances or reporting requirements also depends upon the type of company (i.e. private company or public company).

Taking into account the section 23 of the Companies Act, 2013 ('the Act'), a public company may issue securities to public through prospectus i.e. public offer or through private placement or through rights issue or bonus issue. A private company may issue securities by way of rights issue or bonus issue or through private placement. Chapter III of the Companies Act, 2013 ('the Act') relates to 'Prospectus and Allotment of Securities'. The Part I of the said Chapter relates to 'Public Offer' and Part II relates to 'Private Placement'.

In this article, the author discusses some practical and important points of comparison w.r.t. issue of shares on private placement basis (under section 42 of the Companies Act) and rights issue (under section 62 of the Companies Act) and the Rules made there under:

Sr. No.	Points of Comparison	Issue of shares on rights basis under the Companies Act	Issue of securities on private placement under the Companies Act	Comment, if any
1.	Type of security for the said issue.	Section 62 of the Act provides for issue of 'shares'.	Section 42 of the Act provides for issue of 'securities'. 'Securities' has been defined in section 2 of the Companies Act, which refers to the definition under the Securities Contracts (Regulation) Act, 1956.	The title of section 42 of the Companies Act mentions 'shares', but the entire section provides for issue of 'securities' and not 'shares'.
2.	Approval required	Board approval is required for offer and issue of shares under section 62 of the Companies Act	Primarily, board approval and then shareholders' approval by special resolution is required for offer and issue of securities under section 42 of the Companies Act.	-

3.	To whom the shares/ securities offered?	Shares are offered to existing equity shareholders on proportionate basis (as nearly as circumstances admit) to the paid-up share capital of the company.	Offer is made only to a select group of persons who have been identified by board of directors ('identified persons').	Identified person has been referred to and defined to in section 42(2) of the Act. Proportionate shareholding or existing shareholder – is irrelevant for section 42 of the Act.
4.	Limit on number of persons to whom offer can be made	Section 62 of the Act does not provide any explicit restriction on the limit on number of persons to whom offer can be made.	Section 42 of the Act provides that 'identified persons' shall not exceed 50 or such higher number as may be prescribed, in a financial year. Rules made under section 42 of the Act provide that an offer or invitation to subscribe securities under private placement shall not be made to persons more than 200 in the aggregate in a financial year.	This point is important/relevant when unlisted public company with more than 200 shareholders offers equity shares on rights basis. W.r.t. private placement, there are some exceptions (discussed in subsequent points).
5.	Exceptions w.r.t. the limit of number of persons	Section 62 of the Act does not provide for such exceptions.	According to section 42, Qualified Institutional Buyers (QIBs) and employees of the company being offered securities under ESOP scheme ¹ are excluded.	-
6.	Validity of resolution passed	Section 62 of the Act does not provide for time period for validity of resolution.	According to section 42 of the Act, in case of offer or invitation of any securities to QIBs, it shall be sufficient if company passes a previous special resolution only once in a year for all the allotments to such buyers during the year.	-
7.	Contents of explanatory statement, if any	Explanatory statement is not applicable for rights issue, as shareholders approval is not applicable. However, the board of directors can discuss and take	Rule 14(1) of Companies (Prospectus and Allotment of Securities) Rules, 2014 provides for the detailed disclosures to the shareholders.	Rule 13 of the Companies (Share Capital and Debentures) Rules, 2014 provides for disclosures w.r.t. issue of shares on preferential basis. Rule 14 of the Companies (Prospectus and Allotment of Securities) Rules, 2014, provides for disclosures w.r.t.

		note of the reason for raising funds and issue of shares on rights basis.		private placement of securities.
8.	Offer Letter requirement	There is a reference of letter of offer in section 62 of the Companies Act, but there is no specific format of offer letter. (as compared to section 42 of the Act).	According to section 42 of the Act, company making private placement shall issue private placement offer and application in prescribed form (i.e. PAS – 4) to identified persons, whose names and addresses are recorded by the company.	There is no specific format of offer letter for offer of shares under section 62 of the Companies Act. However, important / key points of offer letter under section 42 of the Act/Rules may be included / referred to for preparing offer letter under section 62 of the Act.
9.	Offer period	According to section 62, offer shall be made by notice specifying number of shares offered and limiting a time not being less than 15 days and not exceeding 30 days from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined. For rights issue, the time period within which the offer shall be made for acceptance shall be not less than 7 days from the date of offer. (Rule 12A of the Companies (Share Capital and Debentures) Rules, 2014).	Interesting to note that there is no specific provision in section 42 or related Rules w.r.t. the offer period for offer of securities under private placement.	Under section 62 of the Act: (a) Offer of shares on rights basis can be made for lesser number of days as may be prescribed (i.e. 15 days); (b) For private Cos. – in case 90% of members of private company have given their consent (in writing or in electronic mode), the lesser period shall apply ² .
10.	Mode of sending offer letter	The Offer Letter for rights issue shall be dispatched through registered post or speed post or through electronic mode or courier or any other mode having proof of	Private placement offer cum application letter shall be sent to identified persons either in writing or in electronic mode.	-

		delivery to all the existing shareholders at least 3 days before the opening of the issue		
11.	Right of renunciation	Unless the Articles of Association of the company provides otherwise, the rights offer shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him or any of them in favour of any other person. The Offer Letter shall contain a statement w.r.t. right of renunciation.	Private placement offer under section 42 of the Act shall not carry any right of renunciation.	For rights offer, the 'right of renunciation' is subject to the provisions in articles of association. In case of private placement offer, renunciation of offer is out of question. It is an offer only to identified persons.
12.	Maintenance of records of offers made	Section 62 of the Act does not provide for maintenance of records of offers made.	The company shall maintain a complete record of private placement offers in Form PAS – 5.	-
13.	Mode of payment of consideration	Section 62 of the Act does not provide for a prescribed mode of payment of consideration i.e. share application money.	According to section 42(4), the private placement offer can be subscribed by identified person by making payment by cheque or demand draft or other banking channel and not by cash.	-
14.	Consequences, in case of inadequate subscription	Section 62 of the Act provides that after expiry of offer period for rights issue (or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered), the board of directors may	There is no consequence provided in section 42 of the Act, in case of inadequate subscription. The offer would lapse.	The powers of the board of directors under section 62(1) (a)(iii) of the Companies Act are discretionary powers. The board 'may' dispose the unsubscribed shares of the rights offer.

		dispose of them in such manner which is not disadvantageous to the shareholders and the company.		
15.	Payment of share application money, in case of joint applicant	Section 62 of the Act does not provide for payment of share application money, in case of joint applicant.	Monies payable on subscription to securities to be held by joint holders shall be paid from the bank account of the person whose name appears first in the application.	-
16.	Time limit to issue of offer letter or offer letter cum application letter	The time period within which the offer shall be made for acceptance shall be not less than 7 days from the date of offer.	A private placement offer cum application letter shall be sent to identified person (either in writing or in electronic mode) within 30 days of recording the name of such person.	-
17.	Utilization of money raised before allotment of shares	There is no specific provision that prohibits utilization of money raised before allotment of shares.	The company shall not utilise monies raised through private placement unless allotment is made and the return of allotment is filed with the Registrar of Companies.	-
18.	Simultaneous fresh offer of shares	There is no specific provision or restriction for simultaneous fresh offer of shares.	Fresh offer or invitation u/s 42 of the Act shall not be made unless the allotments w.r.t. any offer or invitation made earlier have been completed or that offer or invitation has been withdrawn or abandoned by the company. However, subject to maximum number of identified persons, a company may, at any time, make more than one issue of securities to such class of identified persons as may be prescribed.	-
19.	Time period for allotment of shares / securities.	U/s 62 of the Act, there is no specific provision for time period for allotment of shares. However, the board may specify the	A company making an offer or invitation u/s 42 shall allot its securities within 60 days from the date of receipt of the application money for such securities.	For the offer u/s 62 of the Companies Act, the letter of offer may provide for the time period for allotment of shares. Also, according to the provisions of Rule 2(1)(c)(vii)

		<p>same in the resolution. The same may also be part of the Articles of Association. The provisions of Rule 2(1)(c)(vii) of the Companies (Acceptance of Deposits) Rules, 2014 is also relevant.</p>		<p>of the Companies (Acceptance of Deposits) Rules, 2014 – without prejudice to any other liability or action, if the securities for which application money or advance for such securities was received cannot be allotted within 60 days from the date of receipt of the application money or advance for such securities and such application money or advance is not refunded to the subscribers within 15 days from the date of completion of 60 days, such amount shall be treated as a 'deposit' under the said Rules.</p>
20.	Requirement of having separate bank account	U/s 62 of the Act, there is no requirement of having separate bank account.	Monies received on application u/s 42 of the Act shall be kept in a separate bank account in scheduled bank and shall not be utilised for any purpose other than: (i) For adjustment against allotment of securities; or (ii) For the repayment of monies where the company is unable to allot securities.	-
21.	Restrictions on the release any public advertisements	There is no such restriction under section 62 of the Act (probably taking into consideration rights issue of unlisted public company or listed public company, subject to compliance of SEBI Regulations).	The company offering securities u/s 42 of the Act shall not release any public advertisements or utilise any media, marketing or distribution channels or agents to inform the public at large about such an offer.	-
22.	Requirement of filing return of allotment	For allotment under section 62 of the Act, the company shall, within 30 days from the date of allotment file	A return of allotment of securities u/s 42 of the Act shall be filed with the Registrar within 15 days of allotment in e-Form PAS-3, along with complete list of all	

		with the Registrar of Companies, a return of allotment in e-Form PAS – 3.	the allottees containing prescribed details.	
23.	Filing of resolution with Registrar of Companies under the Cos. Act	<p>There is no such provision for issue of shares on rights basis under section 62 of the Act.</p> <p>The board of directors of a company shall exercise the power to issue securities (including debentures, whether in or outside India) on behalf of the company by means of resolutions passed at board meeting only (section 179(3) of the Cos. Act). The said provision is applicable to private company and public company, both.</p> <p>The resolution for issue of shares shall be filed with the Registrar of Companies in e-Form MGT – 14. (section 179(3) and section 117 of the Companies Act). The said compliance is applicable to only public company.</p>	The company shall issue private placement offer cum application letter only after relevant special resolution or board resolution has been filed with the Registrar of Companies.	-
24.	Requirement of Valuation	There is no specific requirement of valuation for offer of shares under section 62(1)(a) of the Act.	According to section 62(1)(c) of the Act, the price of shares is determined by the valuation report of a registered valuer, subject to the compliance with the applicable provisions of Chapter III and any other	-

			conditions as may be prescribed.	
25.	In case default to refund share application money	There is no specific provision given in section 62 of the Act. The provisions of the Companies (Acceptance of Deposits) Rules, 2014 are also applicable (as discussed above).	If a company defaults in filing the return of allotment within the period prescribed, then the company, its promoters and directors shall be liable to a penalty for each default of Rs. 1,000/- for each day during which such default continues but not exceeding Rs. 25 lacs.	-
26.	Penal consequences in case of non-compliance with relevant provisions	There is no specific provision given in section 62 of the Act for the penal consequence in case of non-compliance.	If a company makes an offer or accepts monies in contravention of sec. 42 of the Act, the company, its promoters and directors shall be liable for a penalty which may extend to the amount raised through the private placement or Rs. 2 crore, whichever is lower, and the company shall also refund all monies with interest to subscribers within a period of 30 days of the order imposing the penalty. Notwithstanding sec. 42 (9) and (10), any private placement issue not made in compliance of the provisions of section 42 shall be deemed to be a public offer and all the provisions of Cos. Act and the SCRA, 1956 and SEBI Act, 1992 shall be applicable.	-

Meaning of the expression – 'select group of persons': In *Canning Industries Cochin Ltd. v. SEBI* [2020] 115 taxmann.com 379 (SAT – Mumbai), the issue before SAT was – Whether offer of an unlisted public company (with 1,929 shareholders) of Unsecured Fully Convertible Debentures on rights basis (and without right of renunciation) amounts to 'public issue' of securities under Companies Act and SEBI Act. In this, there was reference and discussion on private placement of securities under section 42 of the Companies Act. SAT observed that "*The offer of shares to the Company's shareholders cannot be termed as an offer to a 'select group of persons'. The expression 'select group of persons' is not a technical expression but has to be understood in its ordinary popular sense, namely, an offer made privately such as to friends and relatives or a selected set of customers distinguished from approaching the general public or to a section of the public by advertisement, circular or prospectus addressed to the public.*"

Valuation of shares of listed company in case of issue of shares under Sec. 62(1)(c) of Cos. Act read with Cos. Rules & SEBI ICDR Regulations: In *PNB Housing Finance Ltd. v. SEBI* [2021] 129 taxmann.com 136 (SAT – Mumbai), the question before SAT was – For the preferential offer by Appellant Company (i.e. listed entity) is it required to get its shares valued from Registered Valuer as required under the Articles of Association or whether the Appellant Company is required to get the pricing calculated in accordance with the pricing mechanism provided under Regulation 164 of SEBI (ICDR) Regulations? In this, there was reference and discussion on private placement of securities under section 42 of the Companies Act. SAT³ observed that "*Section 62(1)(c) further provides that the determination of the price of the shares by the valuation report of the registered valuer would also be subject to any other conditions as may be prescribed. In this regard, the Rules which has been framed are called the Companies (Share Capital and Debentures) Rules, 2014. Rule 3 provides that the Rules of 2014 will apply to all unlisted public companies, all unlisted companies and listed companies so far as they do not contradict or conflict with any other Regulations framed in this regard by SEBI, that is to say, that if the Rules of 2014 are contradictory or is in conflict with any provisions of the Regulations framed by SEBI in that case the Rules of 2014 will not apply to such listed companies with regard to the issuance of the shares or securities. Rule 3(c) of the Rules of 2014 makes it very clear that the Regulations framed by SEBI will be given primacy if any provision of the Rules of 2014 are in conflict with the Regulations framed by SEBI.... Thus, a combined reading of section 62(1)(c) read with rule 13 of the Rules of 2014 makes it clear and explicit, namely, that such shares shall be offered by a Company where the price of such shares is determined by the valuation report of a registered valuer. However, in the case of a listed Company whose shares or other securities are listed on a recognised Stock Exchange, the Company is not required to determine the shares through a registered valuer in view of the second proviso to rule 13(1) read with rule 13(2) and that the price is required to be determined in accordance with the Regulations framed by SEBI which in the instant case is Regulation 164 of the ICDR.*"

Private Placement v. Preferential Offer: Both – private placement and preferential offer have been defined in the Companies Act or Rules made thereunder. "Private placement" means any offer or invitation to subscribe or issue of securities to a select group of persons by a company (other than by way of public offer) through private placement offer-cum-application, which satisfies the conditions specified in section 42 of the Act⁴. 'Preferential Offer' means an issue of shares or other securities, by a company to any select person or group of persons on a preferential basis and does not include shares or other securities offered through a public issue, rights issue, employee stock option scheme, employee stock purchase scheme or an issue of sweat equity shares or bonus shares or depository receipts issued in a country outside India or foreign securities⁵.

Rule 13 of the Companies (Share Capital and Debentures) Rules, 2014 defines the expression 'shares or securities' as it means equity shares, fully convertible debentures, partly convertible debentures or any other securities, which would be convertible into or exchanged with equity shares at a later date. Section 42 of the Act / Rule 14 of the Companies (Prospectus and Allotment of Securities) Rules, 2014 refers to 'securities' and there is no further reference to the same. Therefore, in this case, 'securities' means as defined under SCRA, 1956.

Rule 14 of the Companies (Prospectus and Allotment of Securities) Rules, 2014 is more detailed and covers almost all aspects w.r.t. private placement of securities, whereas Rule 13 of the Companies (Share Capital and Debentures) Rules, 2014 does not cover all aspect for the issue of shares on preferential basis. Interestingly, Rule 13 of the Companies (Share Capital and Debentures) Rules, 2014 creates few exceptions for compliance of Rule 14 of the Companies (Prospectus and Allotment of Securities) Rules, 2014 if preferential offer made by a company to one or more existing members only.

In my view, academically, there could be differences between private placement and preferential offer. However, for the purposes of issue of securities by the company and applicable provisions and compliances,

both the expressions have the same meaning. In fact, the Rules needs to be amended to give the desired meaning to the relevant provisions.

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1. ESOP scheme under the provisions of clause (b) of sub-section (1) of section 62.
 2. Notification No. GSR 464(E), dated 5-6-2015.
 3. Observations of Justice Tarun Agarwala, Presiding Officer. Split decision.
 4. Explanation I to Section 42(3) of the Companies Act.
 5. Explanation to Rule 13 of the Companies (Share Capital and Debentures) Rules, 2014 (for the purpose of said Rules).