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Analysing developments impacting business

AMENDMENTS TO COMPANIES ACT PRIVATE PLACEMENT NORMS NOW IN EFFECT: SIMPLIFIED OR MORE COMPLEX?

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On 7 August 2018, the Central Government has issued a notification bringing into force the provisions of Section 10 of the Companies (Amendment) Act, 2017 amending Section 42 of the Companies Act, 2013 (Act) relating to private placement norms for issue of securities. Further, consequential amendments required to the Companies (Prospectus and Allotment of Securities) Rules, 2014, as amended (PAS Rules) pursuant to Companies (Prospectus and Allotment of Securities) Second Amendment Rules, 2018 have also been notified.

The Report of the Company Law Committee (CLC) issued in February 2016 recommended changes to private placement norms to simplify the processes, avoid duplication of disclosures, lessen regulatory interference and ensure greater self-regulation. This led to amendment of Section 42 of the Act. Although the procedural requirements have been simplified, disclosure requirements have been enhanced significantly, but penalty for violation of norms of private placement has been significantly reduced.

Amendments at a Glance

➤ Changes in Procedural Requirements

- Stringent condition on utilisation of funds: The most significant change in the amendment is that an issuer is not permitted to utilise any monies raised through private placement till the allotment is complete and the return of allotment (PAS 3) is filed with the Registrar of Companies (ROC) within 15 days of allotment. The timelines for filing the return on allotment has been reduced to 15 days unlike the erstwhile provision of 30 days. The requirement of keeping money in a separate bank account continues.
- Relaxation in filing of PAS-4 and PAS-5 with ROC: Offer Letter in Form PAS-4 and record of persons to whom the Offer Letter is issued in Form PAS-5 are required to be maintained by the Company and are no longer required to be filed with the ROC. The requirement of filing of the Offer Letter with the Securities and Exchange Board of India by listed issuers has also been dispensed with.
- Exemption of Shareholders resolution under Section 42 for Non-Convertible Debentures (NCDs): Prior to the amendment, NCDs could be issued on a private placement basis provided a shareholders' resolution was passed once a year for all NCD issuances in that year. This requirement was in addition to the already existing borrowing limits approved by the shareholders of the company under Section 180(1)(c) of the Act. Now, the PAS Rules permit issue of NCDs pursuant to a board resolution so long as it is within limits for raising debt as approved by the company under Section 180(1)(c) of the Act (exceeding paid-up share capital and free reserves). The requirement of shareholders' resolution under Section 42 of the Act is only applicable in case the issuance exceeds the limits approved

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under Section 180(1)(c) of the Act. Accordingly, the requirement of one omnibus shareholders' resolution in addition to the borrowing limits resolution under Section 180 for NCD issuances in a calendar year has been dropped so long as Section 180 has been complied with.

- Resolutions to be filed prior to issue of Offer Letter: Prior to issuing the Offer Letter, the special resolution approving the issuance of securities and/or board resolution for issue of securities has to be filed with the ROC. In this regard, it has also been clarified that private companies (which were earlier exempted from filing of board resolutions) will have to file board resolutions passed for issue of securities.
- Simultaneous issue of different securities permitted: As a general rule, no fresh issue of securities can be undertaken unless the previous offer of securities has been withdrawn or securities have been allotted pursuant to the said offer. It has been clarified that there can be simultaneous issue of more than one security if they are different securities – e.g., issue of debentures and issue of equity shares can take place simultaneously. The 200 person limit is to be reckoned for each kind of security, individually.
- No right of renunciation: The Offer Letter shall be issued to specific persons and they shall not have the right to renounce their right to subscribe in favour of other person.
- No minimum allotment size: The PAS Rules earlier specified that the minimum investment size shall be INR 20,000 in face value of securities. This stipulation has been dropped.
- Relevant Date for valuation: The price of the securities should be arrived at as of a date which is at least 30 days prior to the scheduled date of the general meeting approving the issuance.

➤ Changes in Disclosure Requirements

- Private placement offer cum application letter (Offer Letter): The erstwhile private placement offer letter has been replaced with the Offer Letter. A company is required to issue the Offer Letter in Form PAS-4. The intent of the CLC was to reduce the duplication of disclosures and hence they had suggested to do away with private placement offer letter. However, the Offer Letter remains and the new form prescribed for the Offer Letter sets out extensive disclosure requirements - in addition to the items covered in the erstwhile private placement offer letter, disclosures covered in the explanatory statement to the general meeting and financial position of the company have to be made in the Offer Letter. Further, while the PAS Rules may have introduced certain additional disclosures for equity linked instruments, to the extent such disclosures are not relevant to NCDs, the scope of its applicability has been clarified. While the disclosures have been increased, the Offer Letter is no longer required to be filed with the ROC or SEBI.
- Incremental Disclosures in the Offer Letter: In addition to the disclosure requirements under the erstwhile PAS Rules, a company undertaking an unlisted or listed private placement of NCDs or qualified institutions placements of securities, shall have to disclose certain additional information. Some of the key additional disclosures include information pertaining to (i) default in filing of annual filings under the Act and rules made thereunder; (ii) class and names of the proposed allottees and the percentage of post private placement capital that may be held by them; (iii) change in control pursuant to the private placement; (iv) the number of persons to whom allotment on preferential basis/private placement/rights issue basis have already been made during the year (both in terms of number of securities and price); (v) details of significant and material orders passed by any regulator, court or tribunal impacting the going concern of the issuer and its future operations; (vi) allotments made in last one year for consideration other than cash; (vii) report in respect of valuation of security; (ix) justification for allotment proposed to be made for consideration other than cash along with a valuation report; (x) terms of raising securities – duration, if applicable, rate of dividend or rate of

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interest, mode of payment and repayment; (xi) proposed schedule for which the Offer Letter is valid; (xii) principal terms of assets charged as security, if any; and (xiii) pre and post issue shareholding pattern.

- Explanatory statement for Shareholders Resolution: The explanatory statement to the notice for shareholders' resolution in relation to private placement should include the following: (i) particulars of the offer including date of passing of board resolution; (ii) kind of securities offered and the offer price; (iii) basis or justification for the offer price; (iv) name and address of the valuer who has done the valuation; and (v) amount being raised through the private placement; (vi) material terms of raising securities, proposed time schedule, purposes or objects of the offer, contribution being made by the promoters or directors either as part of the offer or separately in furtherance of objects; and principal terms of assets charged as securities. However, in terms of the proviso to the Rule 13(1) of the Companies (Share Capital and Debentures) Rules, 2014, the price of shares to be issued on a preferential basis by a listed company is not required to be determined by the valuation report of a registered valuer.

➤ Changes in Penal Provisions

- Penalties: If return of allotment in Form PAS-3 is not filed within 15 days from the date of allotment of securities, the Company, its promoters and directors shall be liable to a penalty of INR 1,000 (Rupees One thousand) for each day of default and is capped at INR 2,500,000 (Rupees Two million five hundred thousand). Further, for a non-compliance of the private placement provisions, now the penalty is capped at the amount raised through the private placement process or INR 20,000,000 (Rupees Twenty million), whichever is lower. Earlier, the penalty imposed was capped at higher of the two amounts.

Comments

The changes to the private placement norms while they provide some respite, have largely made compliances more cumbersome for issuance of equity linked securities. For instance, dropping of minimum investment size, separate shareholders' resolution, removal of unnecessary filing requirements are a welcome changes; however, the additional conditions on use of funds and increase in level of disclosures in the Offer Letter and a cut-off date for valuation increase compliance burden on the companies.

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