ICSI-CCGRT – "GEETA SAAR" – A Brief of Premier on Company Law

Issue of shares at discount (Sec 53)

Section 53 of the Companies Act, 2013, effective from 01.04.2014 provides that

(1) Except as provided in section 54, a company shall not issue shares at a discount.

(2) Any share issued by a company at a *discounted price* shall be void.

The expression "discounted price" is proposed to be substituted with "discount" pursuant to the clause 12(i) of the Companies (Amendment) Bill, 2016

1. Meaning of the word 'discount':

As per the 9th edition of Black's Law Dictionary "Discount" means- 1. A reduction from the full amount or value of something, esp. a price. 2. An advance deduction of interest when a person lends money on a note, bill of exchange, or other commercial paper, resulting its present value. As per the 9th edition of Black's Law Dictionary "Discount share" means A share issued for less than par value.

It is pertinent to note that meaning of discount should be taken into account with relation to nominal value of the share only. Accordingly, no company can issue share below the nominal value except Sweat Equity Shares even if the market value of the share is below the nominal value of the share. Therefore, if the shares of the company are issued at a price lower than the market price but not below the nominal value of the shares, such an issue is not an issue at a discount. "At a discount" means at a price less than the nominal value. However, due to use of word "discounted price" there is an anomaly but the same is being proposed to be removed and the word discount is to be substituted for the word discounted price vide Companies (Amendment) Bill, 2016.

2. Types of securities covered under this Section

Provisions of this section is applicable only on the shares of the Company i.e. Equity Shares & Preference Shares. Debenture and other securities are not covered under the purview of this section. However, Debenture or other securities convertible into or exchanged with shares whether compulsory or optionally then the same may fall under the provisions of this Section. Accordingly, if the debenture or other securities convertible into or exchanged with shares of the Company then the same cannot be issued on discount. If a Company issued convertible debenture of other securities on discount which will be converted into or exchanged for shares of the same nominal amount immediately, that will be tantamount to issuing the shares at the rate of discount at which the debentures had been originally issued and, therefore, the issue of the shares in exchange or conversion will be illegal. [Mosely v. Koffyfontein Mines Ltd., (1904) 2 Ch 109 (CA) and See Famatina

Development Corpn, Ltd. v. Bury, (1910) AC 439 (HL); Trustees Corporation (India) Ltd. v. CIT AIR 1930 PC 151.]

Indian judiciary has gone a step ahead. While allowing the petition of the Company under section 79 for issue of non-cumulative convertible preference shares which was to be converted into equity shares at a discount of 16.67% after 18 months, the Company Law Board, in re: Jersey India Ltd.1997 88 CompCas 864 CLB, expanded the purview of Section stating as follows: "The Section has not contemplated a conversion at a discount as such nuances in corporate capital structuring perhaps were not in contemplation earlier. However, the objective behind the legal provision being what it is and since the power to allow more time is vested in the Company Law Board, the sanction relating to conversion at a discount is not beyond the scope of the Section."

3. Difference between Section 53 (1) and 53 (2)

Section 53 (1) is a restrictive provision that except as provided in Section 54 a Company shall not issue shares at discount. It means the Company can't discount the face value of shares. Whereas in case of sub-section (2) the term used is discounted price. It shall meet the two conditions one is there shall be a price fixed and the same is discounted.

4. Determining the price:

Pursuant to the provisions of Section 62 and Rules made thereunder every company proposes to issue shares or other securities under preferential allotment or private placement shall get its share valued by a registered valuer (i.e. a Merchant banker or Chartered Accountant in practice having 10 years of experience till the time Section 247 is brought into force). The price for proposed shares shall be fixed which shall not be less than the valuation of shares done by the registered valuer. If the shares are issued at price less than the price arrived at as per valuation, the provision of this sub-section shall be attracted. Such issue of shares shall be void. This is a new sub-section. The corresponding section 79 of Companies Act 1956 does not contain the word 'price'.

In case of issue of rights share there is no requirement under the provision of Section 62, hence the Board of Directors are at liberty to fix the price, however they shall exercise such power in the best interest of the Company. Hence, such shares can be issued at par. However, there is a view that due to use of word "discounted price" in section 53(2) of the Act hence, valuation is mandatory even for right issue so as to keep the issue price equal or more that the fair value of share. This anomaly is proposed to be removed and the word discount is to be substituted for the word discounted price vide Companies (Amendment) Bill, 2016.

5. Offence and Compoundability

Sec 53(3) provides that if the Company contravenes the provision of this section then penalty will be as followed:

For Company: The company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees. The offence is compoundable.

For Officer: Every officer who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees, or with both. The offenses under this section are compoundable under section 441 of the Act.
