

# Chapter 4:

## Declaration and Payment of Dividend;

Read with Companies (Declaration and Payment of Dividend) Rules, 2014.

### Types of Dividend & basis concepts

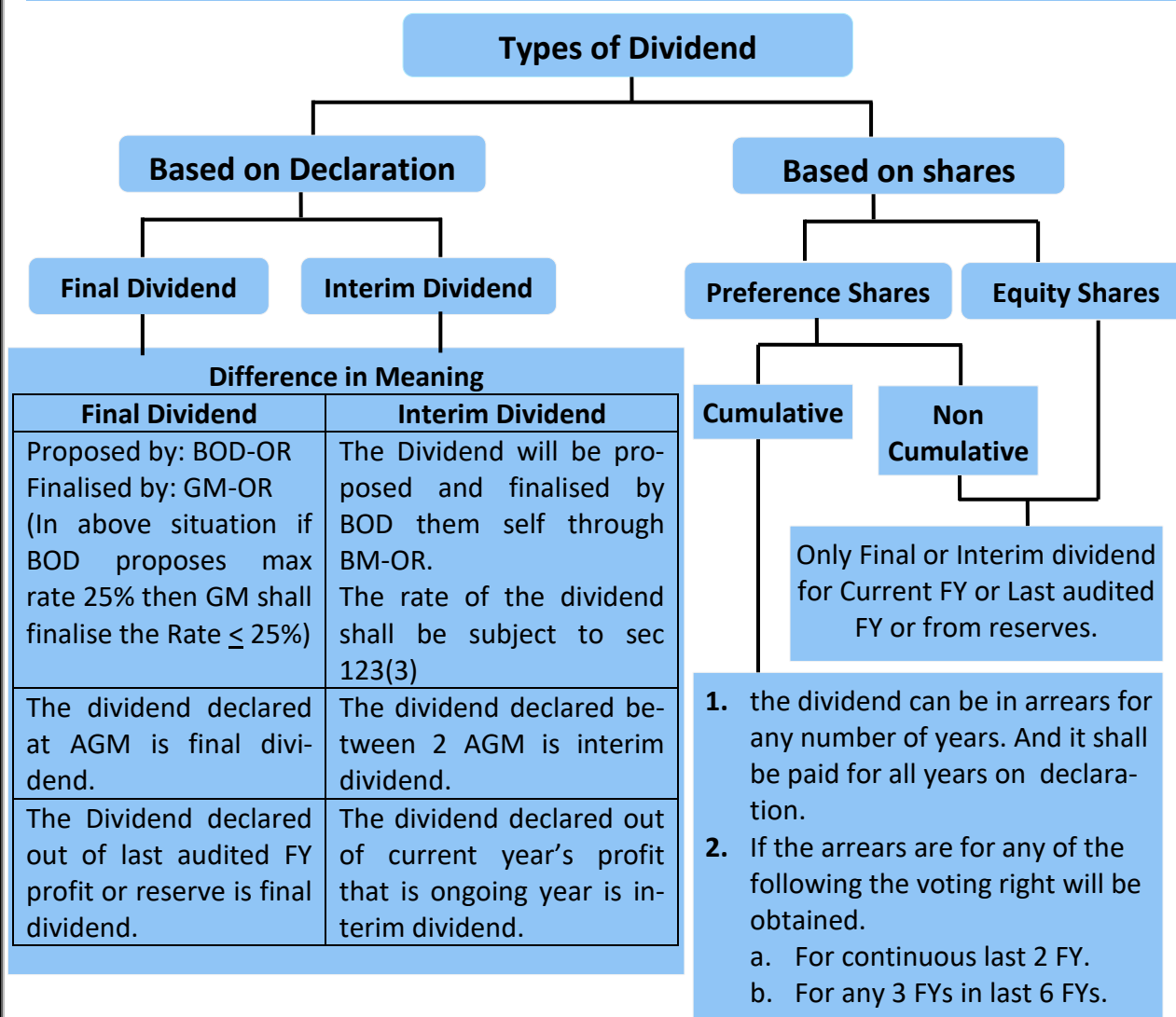
#### Why Provision is Made?

It is a generalised concept which author thinks that every student shall be aware of and it is just blended with the provision of this section 123 for better understanding.

#### Applicability

To all companies.

#### Concept



**Past Exam Questions (PE) / Practice Manual Questions (PM)****Declaration of dividend at the rate higher than notified by BOD**

**PM:** The shareholders at an annual general meeting passed a resolution for payment of dividend at a rate higher than that recommended by the directors. Discuss the validity of the resolution under the Companies Act, 2013.

**Ans:**

**Provision:** [Relevant section 102, 123 of the Companies Act, 2013 as follows]

Under section 102 (2) of the Companies Act, 2013 one of the businesses transacted thereat is the declaration of dividend. The initiation of the dividend is the power of the BOD of the company by OR. The BOD may initiate any percentage of the dividend. But the same is subject to finalisation by the GM by way of OR. But the rule is GM cannot declare the dividend at the rate higher than notified by BOD. For example Dividend Proposed by: BOD-OR is 25 % then dividend finalised by : GM-OR shall be  $\leq 25\%$ .

**Explanation:**

In the given case the BOD initiated the rate of the dividend and the GM want to declare the dividend at the rate higher than rate initiated by BOD. The GM will not be successful in this case as the GM do not have power to declare dividend at the higher rate than notified by BOD.

**Answer:**

Thus GM cannot declare dividend at the rate higher than initiated by BOD.

**Declaration of dividend at AGM for rate more than recommended by BOD**

**N08:** Examine the validity of the resolution passed at the Annual General Meeting of a public company for payment of dividend at a rate higher than that recommended by the board of directors. Is it possible for the board of directors of the company to revoke the dividend declared at the Annual General Meeting?

**Ans:**

**Provision:** [Relevant section 102, 123 & 127 of the Companies Act, 2013 as follows]

Under section 102 (2) of the Companies Act, 2013 one of the businesses transacted thereat is the declaration of dividend. The initiation of the dividend is the power of the BOD of the company by OR. The BOD may initiate any percentage of the dividend. But the same is subject to finalisation by the GM by way of OR. But the rule is GM cannot declare the dividend at the rate higher than notified by BOD. For example Dividend Proposed by: BOD-OR is 25 % then dividend finalised by : GM-OR shall be  $\leq 25\%$ .

Dividend declared by GM above the rate specified by BOD shall be void in law i.e. ultra-virus and need not be paid.

**Explanation:**

- (a) In the given case the BOD initiated the rate of the dividend and the GM want to declare the dividend at the rate higher than rate initiated by BOD. The GM will not be successful in this case as the GM do not have power to declare dividend at the higher rate than notified by BOD.
- (b) Section 127 of the Companies Act, 2013 requires that dividend once declared must be paid within 30 days of declaration & it also contains certain grounds on which non-payment of dividend does not result in a penalty. However, revocation of dividend is not a ground for non-payment of dividend. Only in following cases, declared dividend may be revoked :
  - (i) Where declaration of dividend is ultra virus.
  - (ii) Where the company ceases to be a going concern.

**Answer:**

Thus GM cannot declare dividend at the rate higher than initiated by BOD.

The BOD do not have right to revoke the dividend declared by GM as per law. However dividend declared by GM at rate more than the rate specified by BOD is ultra-virus thus there is no need to revoke the same.

**123(1)-(2): Declaration of Dividend**
**Why Provision is Made?**

The company shall distribute the net profit among the shareholders as the dividend. But for the payment of such dividend the company shall give effect to all the expenses and shall comply with all conditions. The sections provides the conditions for the same.

In addition to this the sources of the dividend shall also be stated from which the company shall declare the dividend. The section also provides for the sources of dividend.

**Applicability**

To all companies.

**Bare Text Vs Text for Understanding & Writing in Exam**

Bare Text	Text for Understanding
<b>123(1): Sources for declaration of dividend.</b>	
<p>(1) No dividend shall be declared or paid by a company for any financial year except—</p> <p>(a) out of the profits of the company for that year arrived at after providing for depreciation in accordance with the provisions of sub-section (2), or out of the profits of the company for any previous financial year or years arrived at after providing for depreciation in accordance with the provisions of that sub-section and remaining undistributed, or out of both; or</p> <p>(b) out of money provided by the Central Government or a State Government for the payment of dividend by the company in pursuance of a guarantee given by that Government.</p>	<p>The company can declare the dividend out of:</p> <ol style="list-style-type: none"> <li>Current year profit (i.e. profit of last FY audited) derived after providing depreciation; or / and</li> <li>Previous year's profits (i.e. Accumulated profit) derived after providing depreciation of respective years; or / and</li> <li>Money provided by CG or SG for payment of dividend in accordance with the guarantee given by respective Government.</li> </ol> <p>In addition to this (even though not mentioned in bare text) the BOD of the company can declare the dividend out of ongoing years profit suo-moto based on the financial position of the company. The dividend can be called as interim dividend. For such dividend the BOD-OR is sufficient.</p>
<p><b>Provided</b> that a company may, before the declaration of any dividend in any financial year, transfer such percentage of its profits for that financial year as it may consider appropriate to the reserves of the company.</p>	<p>For declaration of the dividend the 2 elements are essential as follows:</p> <ol style="list-style-type: none"> <li>Deduction of depreciation (as discussed above); &amp;</li> <li>Transfer to reserves of the company for the safe future.</li> </ol> <p>In the old Companies Act 1956 there was requirement to mandatorily transfer the minimum amount to reserve in case of declaration</p>

	<p>of dividend. But in new Companies Act 2013 there is no any such requirement.</p> <p>If company wish to transfer the profit to the reserve the amount will be decide by BOD-OR and such amount will be transferred. And if BOD does not wish to transfer to the reserve they can resolve the same.</p>
<p><b>Provided further</b> that where, owing to inadequacy or absence of profits in any financial year, any company proposes to declare dividend out of the accumulated profits earned by it in previous years and transferred by the company to the reserves, such declaration of dividend shall not be made except in accordance with such rules as may be prescribed in this behalf.</p>	<p>If company wishes to declare the dividend out of accumulated profit then company do the same out of following things:</p> <ol style="list-style-type: none"> <li>Profit and loss credit balance (not mentioned in bare text). It is a profit of the past year but company did not transferred the same to the reserve. The profit is freely available for distribution by GM-OR.</li> <li>Out of General Reserve. This is the profit which is accumulated and transferred from the profits of the company for every year. Now if the company wants to declare the dividend out of the General Reserve the company need to comply with the following rules for such declaration.</li> </ol>
<p><b>Provided also</b> that no dividend shall be declared or paid by a company from its reserves other than free reserves.</p>	<p>The company shall not declare the dividend out of any other reserve than the free reserve.</p>
<p><b>Provided also</b> that no company shall declare dividend unless carried over previous losses and depreciation not provided in previous year or years are set off against profit of the company for the current year. (Companies Amendment Act, 2015.)</p>	<p>The company shall not declare dividend unless it set off past year losses or depreciation against the profit of current year.</p>
<p><b>Companies (Declaration &amp; Payment of Dividend) Rules, 2014</b></p> <p><b>Rule 3 :</b> In the event of inadequacy or absence of profits in any year, a company may declare dividend out of free reserves subject to the fulfilment of the following conditions, namely:—</p> <p>(1) The rate of dividend declared shall not exceed the average of the rates at which dividend was declared by it in the three years immediately preceding that year.</p> <p>Provided that this sub-rule shall not apply to a company, which has not declared any dividend</p>	<p>In case of absence of the profit the company can declare the dividend out of free reserve. But for the same the company needs to comply the following conditions.</p> <ol style="list-style-type: none"> <li>Rate of Dividend <math>\leq</math> Average rate of dividend of last 3 years.</li> </ol> <p>In case if the company did not declared any dividend in any of the last 3 FY then such FY shall not be counted for average. For e.g. if the company declared dividend only for last 2 years the average rate only of 2 years shall be derived. If company did not declared the dividend in the last 3 FY this condition will not be applicable in such case.</p>

in each of the three preceding financial years.

(2) The total amount to be drawn from such accumulated profits shall not exceed one-tenth of the sum of its paid-up share capital and free reserves as appearing in the latest audited financial statement.

(3) The amount so drawn shall first be utilised to set off the losses incurred in the financial year in which dividend is declared before any dividend in respect of equity shares is declared.

(4) The balance of reserves after such withdrawal shall not fall below fifteen per cent of its paid up share capital as appearing in the latest audited financial statement.

(5) No company shall declare dividend unless carried over previous losses and depreciation not provided in previous year or years are set off against profit of the company of the current year.

2. The maximum withdrawal i.e.  $W^1$  from the reserve can be  $1/10^{\text{th}}$  of Paid up capital and Free Reserves. i.e.

$$W^1 \leq (PC + FR)/10$$

3. The amount withdrawn shall be utilized to set off the current year losses first. As the dividend is need to be declared from the accumulated profit then there might be chances that the company have incurred the losses in the current year.

4. Reserve after such withdrawal (assume  $W^2$ ) shall be at least 15% of Paid up capital.

$$\text{i.e. } FR - W^2 \geq 15\% \text{ of PC}$$

$$\text{i.e. } W^2 \leq FR - 15\% \text{ of PC}$$

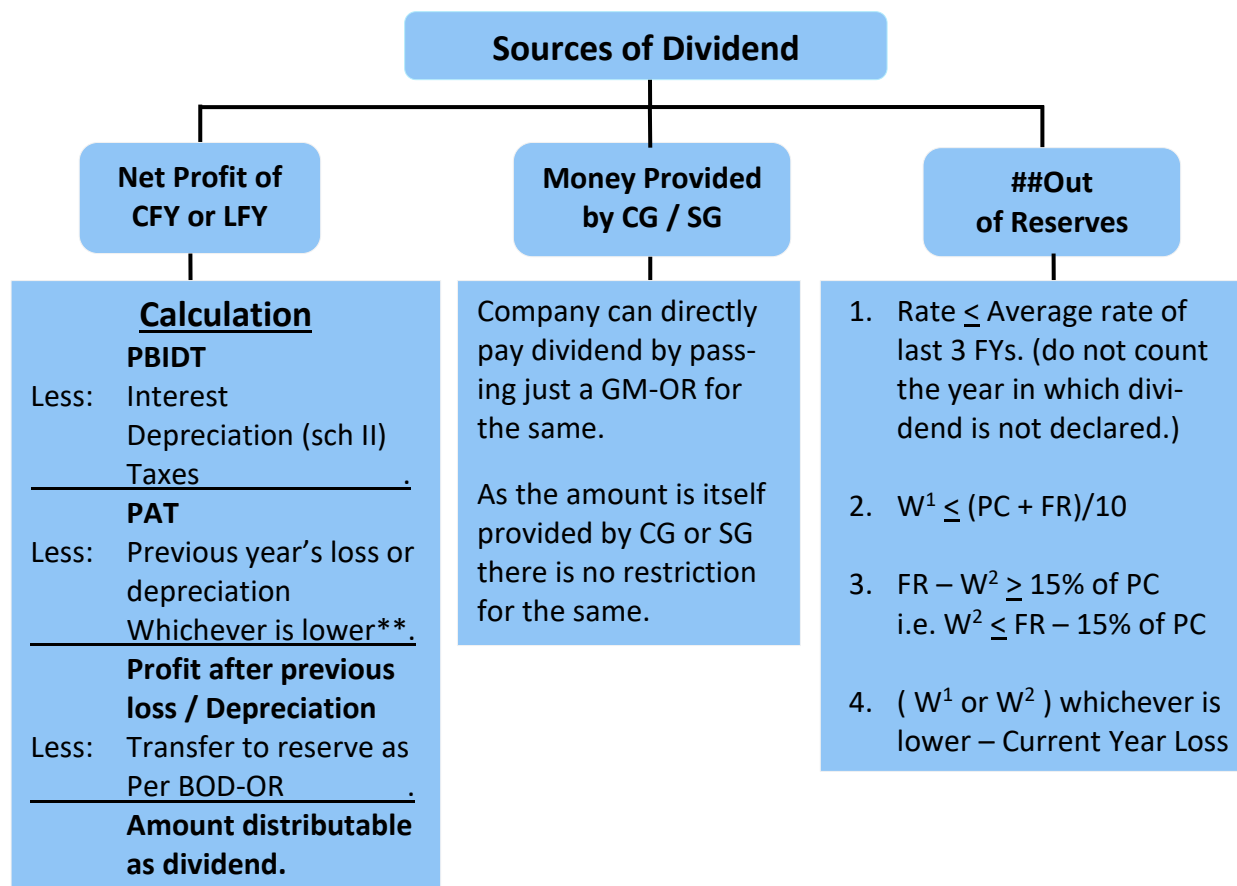
5. The company cannot declare the dividend until all losses or depreciation of the previous years is set off with the profits of current year. This is nothing but the waiting condition for the company. Which means that the company shall not declare the dividend out of accumulate profit if the previous losses are not set off till now. The company shall set off all previous years losses and then it shall think about declaration of the dividend out of accumulate reserve.

**\*In case of inadequate profit in the current year the Government company can declare dividend out of accumulated profit without following the above rules required to declare the dividend out of such accumulated profit.**

### **123(2): Rate of Depreciation**

For the purposes of clause (a) of sub-section (1), depreciation shall be provided in accordance with the provisions of Schedule II.

### **Chart for Understanding**



\*\* Meaning of deduction of previous year's loss or depreciation.

If the Profit for year 25-26 is Rs. 5 lacs and the company wants to declare the dividend then the deduct the following amount from the last column first.

FY	PAT + Depreciation	Depreciation	PAT	Lower of (Loss / Depre)
20-21	90,000	(30,000)	60,000	NA (as there is no loss)
21-22	30,000	(40,000)	(10,000)	(10,000)
22-23	(20,000)	(30,000)	(50,000)	(30,000)
23-24	40,000	(60,000)	(20,000)	(20,000)
24-25	(15,000)	(25,000)	(40,000)	(25,000)

So Rs. 5 lakhs – (10,000 + 30,000 + 20,000 + 25,000) = Rs. 4.15 lakhs.

BOD can transfer the amount to reserve from above amount of Rs. 4.15 lakhs by passing BM-OR. Assuming such amount is of transfer is Rs. 2.15 lakhs, then the distributable profit will be Rs. 2 lakhs for purpose of payment of dividend.

**## The Concept of declaration of Dividend out of Reserve is quite hard to understand with all cumulative conditions. So for the purpose the example is as follows.**

(1) PC	(2) FR	(3) $W^1 = (PC+FR) / 10$	(4) $W^2 = FR - 15\% \text{ of PC}$	(5) Lower of $W^1$ or $W^2$	(6) Current year Loss	(7) (5) Less (6)	(8) Avg Rate of Last 3 yrs (assume)	(9) (8) X (1)	(10) Lower of (7) & (9)
100	60	16	45	16	4	12	15%	15	12
100	40	14	25	14	3	11	8%	8	8



100	20	12	5	5	1	4	13%	13	4
60	80	14	71	14	7	7	25%	15	7
120	70	19	72	19	5	14	8%	9.6	9.6
123.45	98.76	22.22	80.24	22.22	6.7	15.52	12%	14.81	14.81

### Past Exam Questions (PE) / Practice Manual Questions (PM)

**PM:** Advise on the following situations as per the Companies Act, 2013:

- (i) A company wants to transfer more percentage of profits to reserves.
- (ii) A company wants to declare dividends out of past reserves instead of current year profits.
- (iii) A company wants to provide depreciation higher than the rates provided in Schedule II of the Companies Act, 2013.

**Ans:**

**Provision:** [Relevant section 123 of the Companies Act, 2013 as follows]

1. The company can declare the dividend out of:
  - a. Current year profit (i.e. profit of last FY audited) derived after providing depreciation; or / and
  - b. Previous year's profits (i.e. Accumulated profit) derived after providing depreciation of respective years; or / and
  - c. Money provided by CG or SG for payment of dividend in accordance with the guarantee given by respective Government.
2. In addition to this (even though not mentioned in bare text) the BOD of the company can declare the dividend out of ongoing years profit suo-moto based on the financial position of the company. The dividend can be called as interim dividend. For such dividend the BOD-OR is sufficient.
3. For declaration of the dividend the 2 elements are essential as follows:
  - a. Deduction of depreciation (as discussed above); &
  - b. Transfer to reserves of the company for the safe future.
4. In the old Companies Act 1956 there was requirement to mandatorily transfer the minimum amount to reserve in case of declaration of dividend. But in new Companies Act 2013 there is no any such requirement.
5. If company wish to transfer the profit to the reserve the amount will be decide by BOD-OR and such amount will be transferred. And if BOD does not wish to transfer to the reserve they can resolve the same.
6. If company wishes to declare the dividend out of accumulated profit then company do the same out of following things:
  - a. Profit and loss credit balance (not mentioned in bare text). It is a profit of the past year but company did not transferred the same to the reserve. The profit is freely available for distribution by GM-OR.
  - b. Out of General Reserve. This is the profit which is accumulated and transferred from the profits of the company for every year. Now if the company wants to declare the dividend out of the General Reserve the company need to comply with the following rules for such declaration.
7. The company shall not declare the dividend out of any other reserve than the free reserve.
8. In case of absence of the profit the company can declare the dividend out of free reserve. But for the same the company needs to comply the following conditions.

- a. Rate of Dividend  $\leq$  Average rate of dividend of last 3 years. In case if the company did not declared any dividend in any of the last 3 FY then such FY shall not be counted for average. For e.g. if the company declared dividend only for last 2 years the average rate only of 2 years shall be derived. If company did not declared the dividend in the last 3 FY this condition will not be applicable in such case.
  - b. The maximum withdrawal i.e.  $W^1$  from the reserve can be  $1/10^{\text{th}}$  of Paid up capital and Free Reserves. i.e.  $W^1 \leq (PC + FR)/10$
  - c. The amount withdrawn shall be utilized to set off the current year losses first. As the dividend is need to be declared from the accumulated profit then there might be chances that the company have incurred the losses in the current year.
  - d. Reserve after such withdrawal (assume  $W^2$ ) shall be at least 15% of Paid up capital. i.e.  $FR - W^2 \geq 15\% \text{ of PC}$  / i.e.  $W^2 \leq FR - 15\% \text{ of PC}$
  - e. The company cannot declare the dividend until all losses or depreciation of the previous years is set off with the profits of current year. This is nothing but the waiting condition for the company. Which means that the company shall not declare the dividend out of accumulate profit if the previous losses are not set off till now. The company shall set off all previous years losses and then it shall think about declaration of the dividend out of accumulate reserve.
9. For the purposes of declaration of dividend, depreciation shall be provided in accordance with the provisions of Schedule II.

**Explanation:**

The rates contained in Schedule II to the Companies Act, 2013 are the minimum rates below which companies are not permitted to charge for depreciation and therefore there is no bar in providing a higher rate of depreciation. However, it is advisable to give a statement to the effect that the management has estimated life of the asset which requires higher rate of depreciation to be provided than rates prescribed under schedule II to the Companies Act, 2013.

**Answer:**

1. Thus company can transfer the more percentage of the profit to reserve by BM-OR.
2. Company can declare dividend out of past reserve after complying conditions as stated above.
3. The company can provide for higher rate of depreciation than provided in Sch II but not lower than same.

**Transfer to reserve of specific percentage of profit**

**PM,N12:** The Board of Directors of Nimbahera Chemicals Limited proposes to transfer more than 10% of the profits of the company to the reserves for the current year. Advise the Board of Directors of the said company mentioning the relevant provisions of the Companies Act, 2013.

**Ans:**

**Provision:** [Relevant section 123 of the Companies Act, 2013 as follows]

1. For declaration of the dividend the 2 elements are essential as follows:
  - a. Deduction of depreciation; &
  - b. Transfer to reserves of the company for the safe future.
2. In the old Companies Act 1956 there was requirement to mandatorily transfer the minimum amount to reserve in case of declaration of dividend. But in new Companies Act 2013 there is no any such requirement.
3. If company wish to transfer the profit to the reserve the amount will be decide by BOD-OR and such amount will be transferred. And if BOD does not wish to transfer to the reserve



they can resolve the same. The BOD can transfer any amount to reserve as they may thinks fit.

**Answer:**

Thus Board of Directors of Nimbahera Chemicals Limited can transfer more than 10% of the profits of the company to the reserves for the current year.

**Declaration of dividend out of reserves**

**PM:** A Public Company has been declaring dividend at the rate of 20% on equity shares during the last 3 years. The Company has not made adequate profits during the year ended 31st March, 2015, but it has got adequate reserves which can be utilized for maintaining the rate of dividend at 20%. Advise the Company as to how it should go about if it wants to declare dividend at the rate of 20% for the year 2014-15 as per the provisions of the Companies Act, 2013.

**Ans:**

**Provision:** [Relevant section 123 of the Companies Act, 2013 as follows]

1. The company shall not declare the dividend out of any other reserve than the free reserve.
2. In case of absence of the profit the company can declare the dividend out of free reserve. But for the same the company needs to comply the following conditions.
  - a. Rate of Dividend  $\leq$  Average rate of dividend of last 3 years. In case if the company did not declared any dividend in any of the last 3 FY then such FY shall not be counted for average. For e.g. if the company declared dividend only for last 2 years the average rate only of 2 years shall be derived. If company did not declared the dividend in the last 3 FY this condition will not be applicable in such case.
  - b. The maximum withdrawal i.e.  $W^1$  from the reserve can be  $1/10^{\text{th}}$  of Paid up capital and Free Reserves. i.e.  $W^1 \leq (PC + FR)/10$
  - c. The amount withdrawn shall be utilized to set off the current year losses first. As the dividend is need to be declared from the accumulated profit then there might be chances that the company have incurred the losses in the current year.
  - d. Reserve after such withdrawal (assume  $W^2$ ) shall be at least 15% of Paid up capital. i.e.  $FR - W^2 \geq 15\% \text{ of PC}$  / i.e.  $W^2 \leq FR - 15\% \text{ of PC}$
  - e. The company cannot declare the dividend until all losses or depreciation of the previous years is set off with the profits of current year. This is nothing but the waiting condition for the company. Which means that the company shall not declare the dividend out of accumulate profit if the previous losses are not set off till now. The company shall set off all previous years losses and then it shall think about declaration of the dividend out of accumulate reserve.

**Explanation:**

In the given case the average rate of dividend of last 3 years is 20%. Thus company can declare the dividend at the rate of 20%. The only requirement is the withdrawal for the dividend shall not be more than 1/10 of (PC+FR) and the reserve shall remain the 15% of PC.

**Answer:**

Thus the company can declare the dividend of 20% assuming that the required amount is available for withdrawal for declaration of dividend.

**Declaration of dividend out of reserves**

**PM,N11:** The agenda for the meeting of the Board of directors of M/s Brilliant Enterprises Ltd. held on 20-6-2014 for adopting the annual accounts for the year ended 31-3-2014 in-

cluded an item relating to payment of dividend. At the meeting it became apparent that the profits made during the year ended 31-3-2014 were inadequate to declare dividend. The Board was keen to maintain the rate of 20% dividend on the equity shares as declared in the previous years so as to maintain the image of the company. The company has some accumulated profits earned in previous years, which were transferred to reserves. Advise the company as to how it should go about to achieve the objective to pay dividend at the rate of 20% on the equity shares.

**Ans:**

**Provision:** [Relevant section 123 of the Companies Act, 2013 & *Companies (Declaration and Payment of Dividend) Rules*, 2014 as follows]

1. The company shall not declare the dividend out of any other reserve than the free reserve.
2. In case of absence of the profit the company can declare the dividend out of free reserve. But for the same the company needs to comply the following conditions.
  - a. Rate of Dividend  $\leq$  Average rate of dividend of last 3 years. In case if the company did not declared any dividend in any of the last 3 FY then such FY shall not be counted for average. For e.g. if the company declared dividend only for last 2 years the average rate only of 2 years shall be derived. If company did not declared the dividend in the last 3 FY this condition will not be applicable in such case.
  - b. The maximum withdrawal i.e.  $W^1$  from the reserve can be  $1/10^{\text{th}}$  of Paid up capital and Free Reserves. i.e.  $W^1 \leq (PC + FR)/10$
  - c. The amount withdrawn shall be utilized to set off the current year losses first. As the dividend is need to be declared from the accumulated profit then there might be chances that the company have incurred the losses in the current year.
  - d. Reserve after such withdrawal (assume  $W^2$ ) shall be at least 15% of Paid up capital. i.e.  $FR - W^2 \geq 15\% \text{ of PC}$  / i.e.  $W^2 \leq FR - 15\% \text{ of PC}$
  - e. The company cannot declare the dividend until all losses or depreciation of the previous years is set off with the profits of current year. This is nothing but the waiting condition for the company. Which means that the company shall not declare the dividend out of accumulate profit if the previous losses are not set off till now. The company shall set off all previous years losses and then it shall think about declaration of the dividend out of accumulate reserve.

**Answer:**

In the given case therefore, if the company complies with the above conditions, it should have the dividend recommended by the Board and put up for the approval of the members at the AGM as the authority to declare lies with the members of the company.

#### Declaration of dividend out of reserve.

**N09:** A Public Company has been declaring dividend at the rate of 20% on equity shares during the last 3 years. The Company has not made adequate profits during the year ended 31st March, 2015, but it has got adequate reserves which can be utilized for maintaining the rate of dividend at 20%. Advise the Company as to how it should go about if it wants to declare dividend at the rate of 20% for the year 2014-2015. Would your answer be different if the company utilized only the profits made in the previous years and retained in the profit and loss account for the purpose of payment of dividend at the rate of 20% for the year 2014-2015.

**Ans:**

**Provision:** [Relevant section 123 of the Companies Act, 2013 as follows]

1. The company shall not declare the dividend out of any other reserve than the free reserve.
2. In case of absence of the profit the company can declare the dividend out of free reserve. But for the same the company needs to comply the following conditions.
  - a. Rate of Dividend  $\leq$  Average rate of dividend of last 3 years. In case if the company did not declared any dividend in any of the last 3 FY then such FY shall not be counted for average. For e.g. if the company declared dividend only for last 2 years the average rate only of 2 years shall be derived. If company did not declared the dividend in the last 3 FY this condition will not be applicable in such case.
  - b. The maximum withdrawal i.e.  $W^1$  from the reserve can be  $1/10^{\text{th}}$  of Paid up capital and Free Reserves. i.e.  $W^1 \leq (PC + FR)/10$
  - c. The amount withdrawn shall be utilized to set off the current year losses first. As the dividend is need to be declared from the accumulated profit then there might be chances that the company have incurred the losses in the current year.
  - d. Reserve after such withdrawal (assume  $W^2$ ) shall be at least 15% of Paid up capital. i.e.  $FR - W^2 \geq 15\% \text{ of PC}$  / i.e.  $W^2 \leq FR - 15\% \text{ of PC}$
  - e. The company cannot declare the dividend until all losses or depreciation of the previous years is set off with the profits of current year. This is nothing but the waiting condition for the company. Which means that the company shall not declare the dividend out of accumulate profit if the previous losses are not set off till now. The company shall set off all previous years losses and then it shall think about declaration of the dividend out of accumulate reserve.

**Explanation:**

- (a) In the given case the average rate of dividend of last 3 years is 20%. Thus company can declare the dividend at the rate of 20%. The only requirement is the withdrawal for the dividend shall not be more than  $1/10$  of  $(PC+FR)$  and the reserve shall remain the 15% of PC.
- (b) Profits lying in the credit of Profit & Loss account can be utilised for payment of dividend without any restrictions. Such utilisation does not amount to declaration of dividend out of reserves.

**Answer:**

Thus the company can declare the dividend of 20% assuming that the required amount is available for withdrawal for declaration of dividend.

Thus, the company may declare dividend @ 20% for the year 2014-2015 out of accumulated profits retained in the P & L Account without any restriction.

**Declaration of dividend out of reserve**

**M10:** X & Co. Ltd. made a loss of Rs. 20 lakhs after providing for depreciation for the year ended 31st March, 2015 and as a result the company was not in a position to declare any dividend for the said year out of profits. However, the Board of Directors of the company announced the declaration of dividend of 15% on the equity shares payable out of free reserves. The paid up share capital of the company and its free reserves as on 31st March, 2015 are Rs. Two crores and Ten crores respectively. The average dividend declared by the Company in the last five years is 25%. Examine the validity of declaration of dividend.

**Ans:**

**Provision:** [Relevant section 123 of the Companies Act, 2013 & *Companies (Declaration and Payment of Dividend) Rules*, 2014 as follows]

1. The company shall not declare the dividend out of any other reserve than the free re-

serve.

2. In case of absence of the profit the company can declare the dividend out of free reserve. But for the same the company needs to comply the following conditions.
  - a. Rate of Dividend  $\leq$  Average rate of dividend of last 3 years. In case if the company did not declared any dividend in any of the last 3 FY then such FY shall not be counted for average. For e.g. if the company declared dividend only for last 2 years the average rate only of 2 years shall be derived. If company did not declared the dividend in the last 3 FY this condition will not be applicable in such case.
  - b. The maximum withdrawal i.e.  $W^1$  from the reserve can be  $1/10^{\text{th}}$  of Paid up capital and Free Reserves. i.e.  $W^1 \leq (PC + FR)/10$
  - c. The amount withdrawn shall be utilized to set off the current year losses first. As the dividend is need to be declared from the accumulated profit then there might be chances that the company have incurred the losses in the current year.
  - d. Reserve after such withdrawal (assume  $W^2$ ) shall be at least 15% of Paid up capital. i.e.  $FR - W^2 \geq 15\% \text{ of PC}$  / i.e.  $W^2 \leq FR - 15\% \text{ of PC}$
  - e. The company cannot declare the dividend until all losses or depreciation of the previous years is set off with the profits of current year. This is nothing but the waiting condition for the company. Which means that the company shall not declare the dividend out of accumulate profit if the previous losses are not set off till now. The company shall set off all previous years losses and then it shall think about declaration of the dividend out of accumulate reserve.

**Explanation:** The given case is as follows :

(a) Average rate of dividend during the preceding 3 FY is 25%

(b)  $W^1 \leq (2 + 10)/10 = 1.2$  crores.

(c) The amount withdrawn shall be utilized to set off the current year losses of Rs. 20 lakhs first. Thus maximum amount that can be utilized for dividend is 1 crore (1.2cr - 0.20 cr)

(d)  $W^2 \leq FR - 15\% \text{ of PC}$  i.e.  $W^2 \leq 10 - 0.30 = 9.7$  crore

(e) The company cannot declare the dividend until all losses or depreciation of the previous years is set off with the profits of current year.

**Answer :** Thus, the company may distribute dividend at the rate of 25% (i.e. 50 lakhs in total)

### 123(3): Interim Dividend

#### Why Provision is Made?

It is a generalised concept which author thinks that every student shall be aware of and it is just blended with the provision of this section 123 for better understanding.

#### Applicability

To all companies.

#### Bare Text Vs Text for Understanding & Writing in Exam

Bare Text	Text for Understanding
<b>123(3): Interim Dividend</b>	
The Board of Directors of a company may declare interim dividend during any financial year out of the surplus in the profit and loss account and out of profits of the financial year in which such interim dividend is sought to be	The BOD can declare interim dividend by passing BM-OR only out of: <ol style="list-style-type: none"> <li>a. Ongoing Current Year's Profit</li> <li>b. Out of profit of the FY just ended.</li> </ol>

declared.

**Provided** that in case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.

If the company wants to declare dividend in during the ongoing FY and if the company has incurred loss till the end of the last quarter then the company can declare the dividend but at the restricted rate (call R).

Then  $R \leq \text{Average Rate of Dividend of last 3 FY.}$

Now the question arises what if the company did not declared the dividend in last 3 FY?

The answer to the question is ambiguous and the department had not clarified anything till date. But logically speaking the company should not be allowed to pay any rate of dividend in such case. As the company is suffering through losses till last quarter. And as it has not declared any dividend in last 3 year might mean company could have also suffered loss in last 3 FY. So it will be prudential not to pay the dividend.

## 123(4)-(5): Transfer and Payment of Dividend

### Why Provision is Made?

It is a generalised concept which author thinks that every student shall be aware of and it is just blended with the provision of this section 123 for better understanding.

### Applicability

To all companies.

### Bare Text Vs Text for Understanding & Writing in Exam

Bare Text	Text for Understanding
<b>123(4): Transfer of Dividend [*not apply to wholly owned Gov company]</b>	
The amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account within five days from the date of declaration of such dividend.	If company declared any kind of dividend final or interim the company shall transfer the dividend to the separate bank account within the 5 days from the date declaration.
<b>123(5): Payment of Dividend to Specific person.</b>	
No dividend shall be paid by a company in respect of any share therein except to the registered shareholder of such share or to his order or to his banker and shall not be payable except in cash.	The company shall always pay the dividend to: <ul style="list-style-type: none"> <li>a. Registered shareholder; or</li> <li>b. To any person on order of registered shareholder; or</li> <li>c. To banker of registered shareholder.</li> </ul> Such dividend shall be paid in the form of cash and not in kind.
<b>Provided</b> that nothing in this sub-section shall be deemed to prohibit the capitalisation of profits or reserves of a company for the pur-	The above subsection requires the payment of the dividend to registered shareholder by way of cash only. Which might lead to creation of

## Chap 4: Declaration & payment of Dividend

pose of issuing fully paid-up bonus shares or paying up any amount for the time being unpaid on any shares held by the members of the company.

the question that whether company cannot transfer profit to the shareholder in any other form?

The answer is yes, company can transfer the profit to shareholder in other form as follows:

- In the form of bonus shares. And for such purpose the company can capitalise such amount of profit required to reserves.
- Such profit of the company can also be used to make the existing shares fully paid up.

**Provided further** that any dividend payable in cash may be paid by cheque or warrant or in any electronic mode to the shareholder entitled to the payment of the dividend.

The above subsection requires the payment of the dividend in the form of cash only. Now it will be general assumption that dividend can be paid in the form of Cheque, DD or any other electronic means.

### 123(6): Restriction on payment of dividend in case of default in any other section of the Companies Act, 2013.

A company which fails to comply with the provisions of sections 73 and 74 shall not, so long as such failure continues, declare any dividend on its equity shares.

The company shall not pay dividend in case of default in the following.

- If company accepts deposit from the public even when it is prohibited from accepting the same. (sec 73)
- If company fails to repay the deposit accepted on due date. (sec 74)

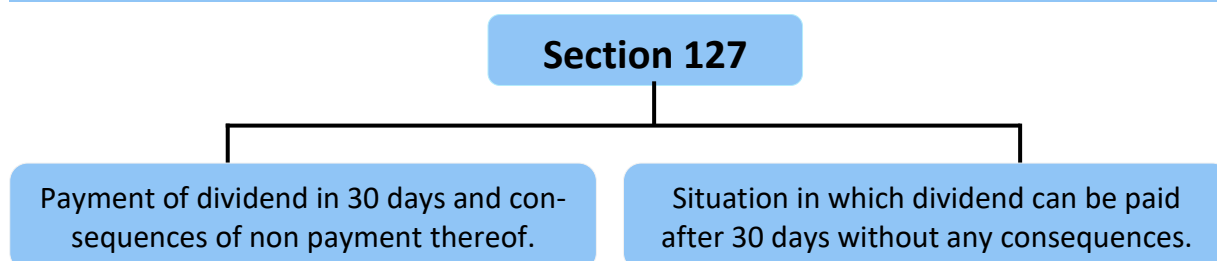
## 127: Dividend shall be paid in 30 days

### Why Provision is Made?

The dividend once declared becomes debt for the company. So it is the duty of the company to pay such dividend as soon as possible. In such situation company may delay the payment of dividend to save itself from the liquidity crunches which arises after declaration of dividend.

In addition to this the dividend payment must not be only a stunt to hike the price of the shares. It shall be executed in the fair manner. Thus the section is prepared to keep watch on the payment of dividend as soon as possible. And in addition to this it suggests the consequences in case of failure of the same.

### Structure of the section



### Applicability

The section is applicable to the all companies.

### Bare Text Vs Text for Understanding & Writing in Exam



**Bare Text**
**Text for Understanding**
**127: Consequences for non payment of dividend within 30 days**

Where a dividend has been declared by a company but has not been paid or the warrant in respect thereof has not been posted within thirty days from the date of declaration to any shareholder entitled to the payment of the dividend, every director of the company shall, if he is knowingly a party to the default, be punishable with imprisonment which may extend to two years and with fine which shall not be less than one thousand rupees for every day during which such default continues and the company shall be liable to pay simple interest at the rate of eighteen per cent per annum during the period for which such default continues.

The company shall pay the dividend in 30 days from declaration in the following manner.

- a. Payment of dividend to shareholders bank account.
- b. Dispatch of dividend warrant in 30 days.

In such situation if the company fails to pay the dividend to any shareholder in the above manner then the consequences will be as follows.

- a. Every Director of the company who is knowingly party to default will be punishable with:
  - (i) Fine of Rs. 1000 per day.
  - (ii) Jail upto 2 years.
- b. Company will be liable to pay the simple interest of 18% per annum to the shareholder for delayed payment. [e.g. If the number of days of delay are 15 days then the interest will be  $(\text{Dividend} \times 18\%) \times 15/365$ ]

In addition to this if the default in payment of the dividend is subsisting for continuous 1 year after end of 30 days all the directors holding the position of the director will be disqualified u/s 164(2) and need to vacate the office u/s 167 immediately after end of such 1 year.

**127: Situation where payment of dividend is allowed after 30 days.**

**Provided** that no offence under this section shall be deemed to have been committed:—

- (a) where the dividend could not be paid by reason of the operation of any law;
- (b) where a shareholder has given directions to the company regarding the payment of the dividend and those directions cannot be complied with and the same has been communicated to him;
- (c) where there is a dispute regarding the right to receive the dividend;
- (d) where the dividend has been lawfully adjusted by the company against any sum due to it from the shareholder; or

The company and the director will not be liable for the above consequences if company fails to pay dividend in 30 days because of following reasons.

- a. Where dividend cannot be paid by operation of law. [e.g. revision of the financial statement resulted in reduction of profit which lead to cancelation of dividend.]
- b. Shareholder requires the payment of the dividend in specific manner and company is unable to comply with such requirements and such inability is communicated by company to shareholder in 30 days.
- c. There is no clarity that to whom the dividend shall be paid or there is dispute between the right to receive the dividend. [e.g. title of the shares is in dispute]

(e) where, for any other reason, the failure to pay the dividend or to post the warrant within the period under this section was not due to any default on the part of the company.

d. The company set off the dividend against the dues from shareholders. [e.g. Company set off dividend against calls in arrears]  
e. Where delay is not due to fault of the company. [e.g. natural calamity, bank strike, fault of post, etc]

### **Past Exam Questions (PE) / Practice Manual Questions (PM)**

**PM:** The Annual General Meeting of ABC Limited declared a dividend at the rate of 30 percent payable on paid up equity share capital of the Company as recommended by Board of Directors on 30th April, 2014. But the Company was unable to post the dividend warrant to Mr. Ranjan, an equity shareholder of the Company, up to 30th June, 2014. Mr. Ranjan filed a suit against the Company for the payment of dividend along with interest at the rate of 20 percent per annum for default period. Decide in the light of provisions of the Companies Act, 2013, whether Mr. Ranjan would succeed? Also state the directors' liability in this regard under the Act.

**Ans:**

**Provision:** [Relevant section 127 of the Companies Act, 2013 as follows]

1. The company shall pay the dividend in 30 days from declaration in the following manner.
  - a. Payment of dividend to shareholders bank account.
  - b. Dispatch of dividend warrant in 30 days.
2. In such situation if the company fails to pay the dividend to any shareholder in the above manner then the consequences will be as follows.
  - a. Every Director of the company who is knowingly party to default will be punishable with:
    - (i) Fine of Rs. 1000 per day.
    - (ii) Jail upto 2 years.
  - b. Company will be liable to pay the simple interest of 18% per annum to the shareholder for delayed payment. [e.g. If the number of days of delay are 15 days then the interest will be (Dividend X 18%) X 15/365]
3. In addition to this if the default in payment of the dividend is subsisting for continuous 1 year after end of 30 days all the directors holding the position of the director will be disqualified u/s 164(2) and need to vacate the office u/s 167 immediately after end of such 1 year.
4. The company and the director will not be liable for the above consequences if company fails to pay dividend in 30 days because of following reasons.
  - a. Where dividend cannot be paid by operation of law. [e.g. revision of the financial statement resulted in reduction of profit which lead to cancelation of dividend.]
  - b. Shareholder requires the payment of the dividend in specific manner and company is unable to comply with such requirements and such inability is communicated by company to shareholder in 30 days.
  - c. There is no clarity that to whom the dividend shall be paid or there is dispute between the right to receive the dividend. [e.g. title of the shares is in dispute]
  - d. The company set off the dividend against the dues from shareholders. [e.g. Company set off dividend against calls in arrears].
  - e. Where delay is not due to fault of the company. [e.g. natural calamity, bank strike, fault of post, etc].

**Explanation:**

The Annual General Meeting of ABC Limited declared a dividend at the rate of 30 percent payable on paid up equity share capital of the Company as recommended by Board of Directors on 30th April, 2014. But the Company was unable to post the dividend warrant to Mr. Ranjan, an equity shareholder of the Company, up to 30th June, 2014. Thus the company will be liable to pay the interest Mr. Ranjan @ 18% pa for the number of days of delay. And the BOD will be liable to pay penalty as stated above.

**Answer:**

1. Thus the Mr. Ranjan will succeed in the suit but for interest of only 18% pa and not for interest of 20%.
2. Every Director of the company who is knowingly party to default will be punishable with:
  - (i) Fine of Rs. 1000 per day.
  - (ii) Jail upto 2 years.

**Revocation of Interim Dividend by BOD.**

**J09,M12:** Board of Directors of M/s. RPP Ltd. in its meeting held on 29th May, 2015 declared an interim dividend payable on paid up Equity Share Capital of the Company. In the Board Meeting scheduled for 10th June, 2015, the Board wants to revoke the said declaration. You are required to state with reference to the provisions of the Companies Act, 1956 whether the Board of Directors can do so.

**Ans :**

**Provision :** [Relevant section 2(35), 127 of the Companies Act, 2013 as follows]

- (a) All the provisions applicable to final dividend shall apply mutatis mutandis to interim dividend.
- (b) Section 127 of the Companies Act, 2013 requires that dividend once declared must be paid within 30 days of declaration & it also contains certain grounds on which non-payment of dividend does not result in a penalty. However, revocation of dividend is not a ground for non-payment of dividend. Only in following cases, declared dividend may be revoked :
  - (i) Where declaration of dividend is ultra virus.
  - (ii) Where the company ceases to be a going concern.

**Explanation:** In the given case, on declaration of interim dividend by M/s. RPP Ltd. in a BM held on 29, May, 2015, the liability of the company to pay the interim dividend has become certain, and the payment of interim dividend must be made within next 30 days, i.e. on or before 28th of June, 2015.

**Answer:** Thus, revocation of interim dividend in the BM held on 10th June, 2015 is not possible.

**124: Unpaid Dividend Account****Why Provision is Made?**

There are lots of situation in the current corporate scenario where company dispatches the dividend warrant and the shareholder does not claims the dividend because of the following reasons:

- a. The amount of dividend is so negligible to claim.
- b. The cost to claim the dividend practically exceeds the amount of dividend.
- c. The dividend warrant have mistake on it in the name of something other which creates hardship for shareholder to claim it and shareholder gives up.
- d. Negligence to claim the dividend.
- e. Any other reasons.

**Chap 4: Declaration & payment of Dividend**

Due to above reasons the large amount of dividend remains unclaimed. Now such amount of dividend is not the income of the company or director or any shareholder it is the money belonging to shareholder. And he shall have chance to claim the same over the period of time. Thus the provision is made in this case to transfer the amount of unclaimed dividend to specific account so it can be claimed over period by rightful shareholder.

**Applicability**

To all the companies.

**Bare Text V/s Text for Understanding & Writing in Exam**

Bare Text	Text for Understanding
<b>124(1): Transfer of dividend to unpaid / unclaimed account</b>	
Where a dividend has been declared by a company but has not been paid or claimed within thirty days from the date of the declaration to any shareholder entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called the Unpaid Dividend Account.	<ol style="list-style-type: none"> <li>1. If the dividend is declared by the company it shall be paid in 30 days u/s 127.</li> <li>2. If the dividend remains unpaid or unclaimed after 30 days, then in next 7 days the company shall transfer the same to unpaid / Unclaimed dividend account.</li> </ol>
<b>124(2): Publication of the details of the Unpaid shareholders</b>	
The company shall, within a period of ninety days of making any transfer of an amount under sub-section (1) to the Unpaid Dividend Account, prepare a statement containing the names, their last known addresses and the unpaid dividend to be paid to each person and place it on the website of the company, if any, and also on any other website approved by the Central Government for this purpose, in such form, manner and other particulars as may be prescribed.	<p>The company shall publish following details regarding unpaid dividend on website of the company and the website approved by CG.</p> <ol style="list-style-type: none"> <li>a. Names of the shareholder who's dividend is unpaid.</li> <li>b. Their address. (in case of change in address then last known address.)</li> <li>c. The amount of unpaid dividend.</li> </ol> <p>The statement for the above particular shall be made in the manner prescribed and the same shall be published.</p> <p>The details have to be posted in 90 days after the transfer has been made to account.</p>
<b>124(3): Delay in transfer of dividend to unpaid account.</b>	
If any default is made in transferring the total amount referred to in sub-section (1) or any part thereof to the Unpaid Dividend Account of the company, it shall pay, from the date of such default, interest on so much of the amount as has not been transferred to the said account, at the rate of twelve per cent per annum and the	<ol style="list-style-type: none"> <li>1. The company needs to transfer the unclaimed / unpaid dividend to unpaid dividend account in the time limit specified above.</li> <li>2. If the company fails to transfer the same to unpaid account within the time specified above then the company shall transfer the interest on the delayed transfer at the rate</li> </ol>

interest accruing on such amount shall endure to the benefit of the members of the company in proportion to the amount remaining unpaid to them.

of 12% per annum.

3. Such amount of dividend shall be transfer do benefit of the shareholder at the time he claims the dividend.

#### **124(4): Claiming the dividend from the unpaid dividend account.**

Any person claiming to be entitled to any money transferred under sub-section (1) to the Unpaid Dividend Account of the company may apply to the company for payment of the money claimed.

The person who is eligible shareholder for the purpose of receiving the dividend can receive the same by applying to the company. The shareholder can also receive the dividend form even unpaid account by making the application to the company.

#### **124(5): Transfer of dividend to IEPF and payment of interest.**

Any money transferred to the Unpaid Dividend Account of a company in pursuance of this section which remains unpaid or unclaimed for a period of seven years from the date of such transfer shall be transferred by the company along with interest accrued, if any, thereon to the Fund established under sub-section (1) of section 125 and the company shall send a statement in the prescribed form of the details of such transfer to the authority which administers the said Fund and that authority shall issue a receipt to the company as evidence of such transfer.

1. After transferring the unclaimed / unpaid dividend to the Unpaid Dividend account, it shall remain in the same account for 7 years.
2. Every shareholder of the company who's dividend is remaining unpaid or who have unclaimed the dividend can claim the same up to the end of such 7 years when dividend is laying in the unpaid account.
3. After expiry of the 7 years from the transfer to unpaid account the dividend together with the interest as per section 124(3) above (12%) shall be transferred to Investor Education Protection Fund (IEPF) maintained in sec 125. (discussed in next section.)
4. The company shall file the details of the transfer to the prescribed authority as per sec 125.

#### **124(6): Transfer of shares on which the dividend is unpaid.**

All shares in respect of which **\*dividend has not been paid or claimed for seven consecutive years or more shall be\*** transferred by the company in the name of Investor Education and Protection Fund along with a statement containing such details as may be prescribed.

\*(Companies Amendment Act, 2015)

1. The company shall transfer those shares to IEPF on which the dividend is unclaimed or unpaid.
2. The company shall file the details of the transfer to the prescribed authority as per sec 125.

**Provided** that any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Education and Protection Fund in accordance with such procedure and on submission of such documents as may be prescribed.

1. If the shares of any shareholder are transferred to IEPF as per above subsection 124(6) then he can reclaim the same on submission of required identification documents and proofs.
2. But this section does not give the power to any shareholder to claim the unpaid / un-

## Chap 4: Declaration & payment of Dividend

claimed dividend from the IEPF. The dividend once transferred to IEPF cannot be claimed in any case.

### 124(7): Contravention and Consequences

If a company fails to comply with any of the requirements of this section, the company shall be punishable with fine which shall not be less than five lakh rupees but which may extend to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees.

The above section can be contravened by way of:

- a. Not transferring the dividend to unpaid account or to IEPF.
- b. Not transferring the interest on the same to unpaid account or to IEPF.
- c. Not transferring the shares on which the dividend is unpaid / unclaimed to IEPF.

If the section is contravened as stated above or in any other manner then the following consequences will be applicable.

- a. The company will be punishable with the fine of Rs. 5 lakhs to Rs. 25 lakhs.
- b. Every officer of the company who is in default will be liable to fine of Rs. 1 lakh to Rs. 5 lakh.

### Mind Benders

**1. What if the company fails to pay dividend due to operation of law in 30 days, whether it requires to transfer the dividend to unpaid account even such case.**

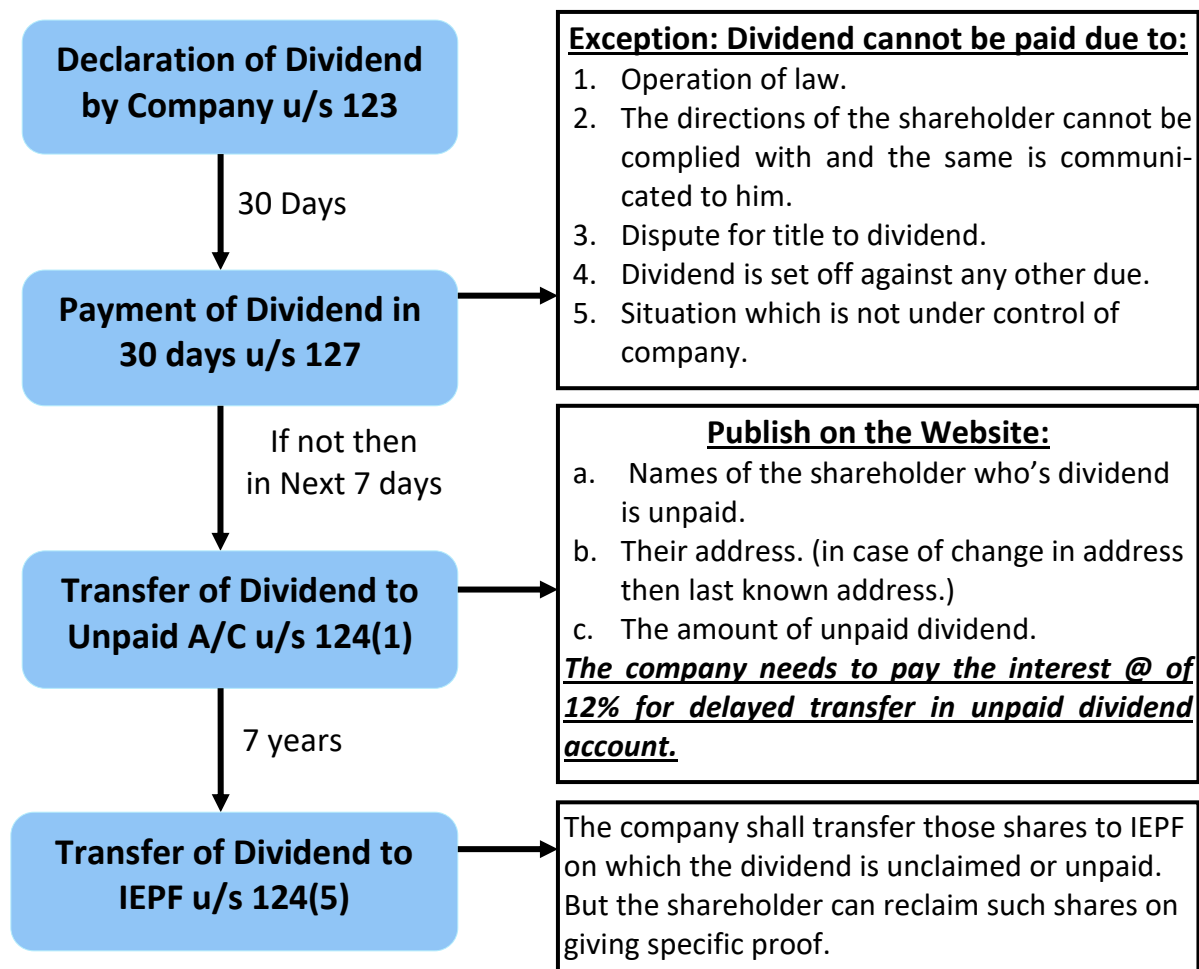
**Ans:** Failure to pay the dividend due to operation of law saves company and the director from the consequences of the section 127. But there is no relief from transferring the dividend to unpaid account.

**2. Whether there is any requirement of the bank in which the Unpaid Dividend A/C shall be opened?**

**Ans:** there is no specific requirement of the bank in which the unpaid dividend account shall be opened. Thus the company can open the unpaid dividend account in any bank.

### Chart for Understanding





## 125: Investor Education & Protection Fund [IEPF]

### Why Provision is Made?

It is being observed in the securities or capital market or even in case of unlisted companies that the lots of amount payable to the shareholders remains unclaimed by shareholders:

- Unpaid dividend accounts of companies;
- Application monies received for allotment of securities and due for refund.
- Matured deposits with companies;
- Matured debentures with companies;
- Interest accrued in respect of the above amounts

Now if we consider the above amount the same does belongs to the shareholders and these are not the profit of the company. Neither company nor BOD have any right on the same. The amount belongs to investor of the company and if the same is not claimed by investor it shall be used for the benefit of the all investors lobby. And with such basic intention the IEPF is formed.

In addition to this the investor in the current market shall be aware of all risk of the securities market and companies working. To make investor aware about the same the authorities needs to conduct the training and awareness session. Thus the expenses of such activity of education and protection of the investor are also incurred from such fund.

### Applicability

To all companies.

**Bare Text √s Text for Understanding & Writing in Exam**

Bare Text	Text for Understanding
<b>125(1): Establishment of IEPF</b>	
The Central Government shall establish a Fund to be called the Investor Education and Protection Fund (herein referred to as the Fund).	
<b>125(2): Deposit to Fund</b>	
There shall be credited to the Fund—	
(a) the amount given by the <u>Central Government</u> by way of <u>grants</u> after due appropriation made by Parliament by law in this behalf for being utilised for the purposes of the Fund; (b) <u>donations</u> given to the Fund by the <u>Central Government, State Governments, companies</u> or any other institution for the purposes of the Fund; (c) the amount in the <u>Unpaid Dividend Account</u> of companies transferred to the Fund under sub-section (5) of section 124; (d) the <u>amount in the general revenue account</u> of the Central Government which had been transferred to that account under sub-section (5) of section 205A of the Companies Act, 1956, as it stood immediately before the commencement of the Companies (Amendment) Act, 1999, and remaining unpaid or unclaimed on the commencement of this Act; (e) the amount <u>lying in the Investor Education and Protection Fund under section 205C</u> of the Companies Act, 1956 (1 of 1956); (f) <u>the interest or other income</u> received out of investments made from the Fund; (g) the amount received under sub-section (4) of section 38; [ <u>Surrender of securities acquired with fraud</u> ] (h) the <u>application money received by companies</u> for allotment of any securities and due for refund; (i) <u>matured deposits</u> with companies other than banking companies; (j) <u>matured debentures</u> with companies; (k) <u>interest accrued</u> on the amounts referred to in clauses (h) to (j); (l) <u>sale proceeds of fractional shares</u> arising out of issuance of bonus shares, merger and amalgamation for seven or more years; (m) <u>redemption amount of preference shares</u> remaining unpaid or unclaimed for seven or more years; and (n) such <u>other amount</u> as may be prescribed:	
Provided that no such amount referred to in clauses (h) to (j) shall form part of the Fund unless such amount has remained unclaimed and unpaid for a period of seven years from the date it became due for payment.	The unclaimed application money or matured deposit or matured debentures will be transferred to IEPF only after expiry of 7 years from the date it is due for payment.
<b>125(3): Utilisation of Fund</b>	
The Fund shall be utilised for—	
(a) the <u>refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money</u> due for refund and interest thereon;	

- (b) promotion of investors' education, awareness and protection;
- (c) distribution of any disgorged amount among eligible and identifiable applicants for shares or debentures, shareholders, debenture-holders or depositors who have suffered losses due to wrong actions by any person, in accordance with the orders made by the Court which had ordered disgorgement;
- (d) reimbursement of legal expenses incurred in pursuing class action suits under sections 37 and 245 by members, debenture-holders or depositors as may be sanctioned by the Tribunal; and
- (e) any other purpose incidental thereto, in accordance with such rules as may be prescribed

**Provided** that the person whose amounts referred to in clauses (a) to (d) of sub-section (2) of section 205C transferred to Investor Education and Protection Fund, after the expiry of the period of seven years as per provisions of the Companies Act, 1956, shall be entitled to get refund out of the fund in respect of such claims in accordance with rules made under this section.

The person was eligible under old law to claim the amount stated above from the IEPF maintained u/s 205C under old Companies Act, 1956.

#### **125(4): Application to Authority to claim the funds**

Any person claiming to be entitled to the amount referred in sub-section (2) may apply to the authority constituted under sub-section (5) for the payment of the money claimed.

The person can claim the funds as stated above only if he makes the application to the authority constituted u/s 125(5) as below.

#### **125(5): Establishment of authority for Refund of claims**

The Central Government shall constitute, by notification, an authority for administration of the Fund consisting of a chairperson and such other members, not exceeding seven and a chief executive officer, as the Central Government may appoint.

The CG can constitute the authority with:

- a. 1 chairman; &
- b. 7 other members; &
- c. CEO

The application for claiming unpaid amounts can be made to such authority.

#### **125(6): The Management and Administration**

The manner of administration of the Fund, appointment of chairperson, members and chief executive officer, holding of meetings of the authority shall be in accordance with such rules as may be prescribed.

The CG have power to decide following things by making new rules:

- a. Administration of fund.
- b. Appointment of chairman.
- c. Appointment of members.
- d. Appointment of CEO
- e. Holding the meetings of authority.

#### **125(7): Resources to Authority**

The Central Government may provide to the authority such offices, officers, employees and other resources in accordance with such rules as may be prescribed.

The CG have power to provide resources to authority by making rules.

## Chap 4: Declaration & payment of Dividend

### 125(8): Administration and Accounts of Fund

The authority shall administer the Fund and maintain separate accounts and other relevant records in relation to the Fund in such form as may be prescribed after consultation with the Comptroller and Auditor-General of India.

The authority shall:

- a. Administer the fund;
- b. Prepare and maintain the records as needed as per CAG.

### 125(9): Power of authority to expend the fund for specific object of sec 125(3)

It shall be competent for the authority constituted under sub-section (5) to spend money out of the Fund for carrying out the objects specified in sub-section (3).

The authority can expend the amount in fund or allocate the same for meeting the objects mentioned in sec 125(3) above.

### 125(10): Audit and Reporting

The accounts of the Fund shall be audited by the Comptroller and Auditor-General of India at such intervals as may be specified by him and such audited accounts together with the audit report thereon shall be forwarded annually by the authority to the Central Government.

1. The audit of the IEPF will be conducted by CAG.
2. CAG will decide the time, frequency and scope of audit.
3. The audited accounts and audit report shall be forwarded by CAG or authority to CG annually or on demand.

### 125(11): Reporting to CG

The authority shall prepare in such form and at such time for each financial year as may be prescribed its annual report giving a full account of its activities during the financial year and forward a copy thereof to the Central Government and the Central Government shall cause the annual report and the audit report given by the Comptroller and Auditor-General of India to be laid before each House of Parliament.

The authority and the CAG shall prepare and present the following documents and reports before the parliament of India.

- a. Annual report;
- b. Audit report by CAG.

The reports shall be first given to the CG and then CG will put the same before the parliament of India.

### Past Exam Questions (PE) / Practice Manual Questions (PM)

**N11:** M/s. USA Industries Limited has constituted "Investor Education and Protection Fund" as required under the Companies Act, 1956 but so far no amounts have been deposited into the said account. Explain with reference to the above said enactment, the amounts payable to the credit, of the said account and the period within which the amounts shall be paid.

**Ans:**

**Provision:** [Relevant section 125 of the Companies Act, 2013 as follows]

The Central Government shall establish a Fund to be called the Investor Education and Protection Fund (herein referred to as the Fund). There shall be credited to the Fund—

1. the amount given by the **Central Government** by way of **grants** after due appropriation made by Parliament by law in this behalf for being utilised for the purposes of the Fund;
2. **donations** given to the Fund by the **Central Government, State Governments, companies** or any other institution for the purposes of the Fund;
3. the amount in the **Unpaid Dividend Account** of companies transferred to the Fund under

sub-section (5) of section 124;

4. the **amount in the general revenue account** of the Central Government which had been transferred to that account under sub-section (5) of section 205A of the Companies Act, 1956, as it stood immediately before the commencement of the Companies (Amendment) Act, 1999, and remaining unpaid or unclaimed on the commencement of this Act;
5. the amount **lying in the Investor Education and Protection Fund under section 205C** of the Companies Act, 1956 (1 of 1956);
6. **the interest or other income** received out of investments made from the Fund;
7. the amount received under sub-section (4) of section 38; [**Surrender of securities acquired with fraud**]
8. the **application money received by companies** for allotment of any securities and due for refund;
9. **matured deposits** with companies other than banking companies;
10. **matured debentures** with companies;
11. **interest accrued** on the amounts referred to in clauses (h) to (j);
12. **sale proceeds of fractional shares** arising out of issuance of bonus shares, merger and amalgamation for seven or more years;
13. **redemption amount of preference shares** remaining unpaid or unclaimed for seven or more years; and
14. such **other amount** as may be prescribed.

The unclaimed application money or matured deposit or matured debentures will be transferred to IEPF only after expiry of 7 years from the date it is due for payment.

The Fund shall be utilised for—

- (a) the **refund in respect of unclaimed dividends, matured deposits, matured debentures, the application money** due for refund and interest thereon;
- (b) **promotion of investors' education, awareness and protection**;
- (c) distribution of **any disgorged amount among eligible and identifiable applicants** for shares or debentures, shareholders, debenture-holders or depositors who have suffered losses due to wrong actions by any person, in accordance with the orders made by the Court which had ordered disgorgement;
- (d) **reimbursement of legal expenses** incurred in pursuing class action suits under sections 37 and 245 by members, debenture-holders or depositors as may be sanctioned by the Tribunal; and
- (e) any other purpose incidental thereto, in accordance with such rules as may be prescribed

## 126: Dividend or Bonus on shares in abeyance.

### Why Provision is Made?

In case of companies when the shares are transferred the company does not register transfer by mistake or by intention in such situation the question arises that to whom the dividend and the bonus shall be paid on the shares; to old shareholder or new shareholder? In such situation sec 126 clarifies the thing that to whom the dividend and the bonus shall be paid logically and ethically.

### Applicability

To all companies.

### Bare Text Vs Text for Understanding & Writing in Exam

**Chap 4: Declaration & payment of Dividend**

Bare Text	Text for Understanding
<b>126: Dividend or Bonus in abeyance</b>	
<p>Where any instrument of transfer of shares has been delivered to any company for registration and the transfer of such shares has not been registered by the company, it shall, notwithstanding anything contained in any other provision of this Act,—</p> <p>(c) transfer the dividend in relation to such shares to the Unpaid Dividend Account referred to in section 124 unless the company is authorised by the registered holder of such shares in writing to pay such dividend to the transferee specified in such instrument of transfer; and</p> <p>(d) keep in abeyance in relation to such shares, any offer of rights shares under clause (a) of sub-section (1) of section 62 and any issue of fully paid-up bonus shares in pursuance of first proviso to sub-section (5) of section 123.</p>	<p>In case of transfer of the shares; if the instrument of transfer is delivered to the company by parties to the transfer then there might be situation that company does not register the transfer due to any problem. In such situation the company shall make following treatment for dividend or bonus.</p> <p>a. The company shall transfer dividend to Unpaid Dividend Account unless company take the written approval of the transferor and then only company can give dividend to transferee.</p> <p>b. If the company have declared right shares in sec 62 or bonus shares in sec 123 then company shall keep such shares in abeyance.</p> <p>Now here question remains to whom the bonus and the right shares shall be transferred? And the department is silent on the same. The logical answer to this is the bonus and the right shares shall be transferred to the transferee. As the section speaks to keep the same in abeyance. If the section required the same to get transferred them to transferor then why it would have said to keep the same in abeyance.</p>

**Mind Benders**

**1. Whether the provisions of this section are also applicable to listed companies in case of shares in D-mat form?**

**Ans:** The company compulsorily needs to transfer the dividend and bonus and right shares for the shares in D-mat form so the provisions on abeyance are not applicable to listed company having shares in D-Mat form.

**Past Exam Questions (PE) / Practice Manual Questions (PM)**

**PM,N04,N09:** SKD an employee of Moreh Ltd. met with an accident and died. The accident occurred when SKD was on Company's duty. He held one hundred shares partly paid. Normally the Company has a first and paramount lien on the shares. The Board of Directors, however, relaxed the said provision with regard to the hundred shares held by SKD as a goodwill gesture on the part of the Company. Is the action of the Company valid? State the reasons. Also state whether the Company's lien can be extended to dividend payable on such shares.

**Ans:**



**Provision:** [Relevant provision of Regulation 9 of Table F of the First Schedule of the Companies Act, 2013 as follows]

1. A Company cannot have lien on shares unless provided in the Articles of Association. Therefore provision to this effect should be in the articles.
2. The company has first and paramount lien on every share (which has not been fully paid up for all monies (whether presently payable or not) called or payable at a fixed time in respect of that share and on all shares which are not fully paid up standing registered in the name of a single person, for all moneys presently payable by him or his estate to the Company.
3. However, companies are free to frame their own Articles of Association and need not follow the Table F. The key point is that lien is permissible only on partly paid shares and only if provided in the Articles of the company.
4. The Board of Directors may, however, at any time declare any share to be wholly or in part exempt from the said lien.
5. Further, the Company's lien is extended to all dividends payable on such shares if provided for in the Articles or if Table F is adopted by the company.

**Explanation:**

In the given case SKD an employee of Moreh Ltd. met with an accident and died. The accident occurred when SKD was on Company's duty. He held one hundred shares partly paid. The lien on his shares is relaxed by BOD. The BOD can do the same as they have right for the same.

**Answer:**

1. Hence the decision of the Board of Directors of M/s Moreh Ltd to relax the provisions of lien in respect of shares held by SKD is in order and valid.
2. The lien on the shares also extends to the dividend as stated above.

### Coverage in the chapter

The following content is covered till now from different chapters of Companies Act, 2013.

Section	Name of Section	Name of Chapter
<b>123</b>	Declaration of dividend	<b>DECLARATION AND PAYMENT OF DIVIDEND</b>
<b>124</b>	Unpaid Dividend Account	-do-
<b>125</b>	Investor Education and Protection Fund	-do-
<b>126</b>	Right to dividend, rights shares and bonus shares to be held in abeyance pending registration of transfer of shares.	-do-
<b>127</b>	Punishment for failure to distribute dividends in 30 days.	-do-

### E-Forms

### Companies (Declaration & Payment of Dividend) Rules, 2014

No E-Forms in this chapter.