

# **ISSUES WITH DEMATERIALIZATION OF SHARES & FORM PAS-6 AND RECENT UPDATES IN COMPANIES ACT, 2013**





# Law of Dematerialization of Securities



# The Depositories Act, 1996



- ✍ The Depositories Act initially came into force as an Ordinance in January, 1996 to provide a legal framework for establishment of depositories to record ownership details in book entry form.
- ✍ The Act also made consequential amendments in:
  - the Companies Act, 1956;
  - SEBI Act, 1992;
  - the Indian Stamp Act, 1899;
  - the Income tax Act, 1961; and
  - the Benami Transactions (Prohibition) Act, 1988.



## Objective



- ✗ Free transferability of securities with:
  - speed,
  - accuracy, and
  - Security.
- ✗ Dispense with the transfer deed;
- ✗ Dispense with other procedural requirements under the Companies Act.



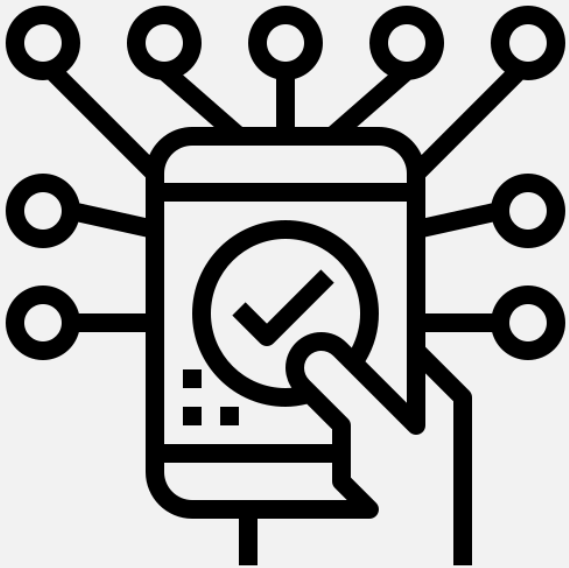
## Revolutionized the Securities Market



Hailed as one of the biggest ever reforms in regulating and developing the securities market in India and for protecting and safeguarding securities holders' interests.



## Applicability to listed companies



- ✍ Mandatory for **listed companies** to issue securities in demat form.
- ✍ All promoter holdings (including past holdings) to be in demat form.
- ✍ Members can still hold shares in physical form but cannot trade without demat.



## Securities of unlisted public companies to be in dematerialized form



- ✍ As per Section 29 of the Companies Act, 2013, every company making public offer and such other class or classes of companies as may be prescribed are required to issue securities only in dematerialized form.
- ✍ Rule 9A of the Companies (Prospectus and Allotment of Securities) Rules, 2014 effective from **2nd October, 2018**, provides that **every unlisted public company** shall-
  - (a) Issue the securities in dematerialized form; and
  - (b) Facilitate dematerialization of all its existing securities.
- ✍ Further any company other than the above mentioned companies has the option to convert securities into dematerialised form or issue its securities in physical form.





## Total no. of Companies



**6,797**

**LISTED COMPANIES**

Source: MCA (as on 31<sup>st</sup> July, 2020)



**57,440**

**UNLISTED PUBLIC COMPANIES**

Source: MCA (as on 31<sup>st</sup> July, 2020)





The background features a white area on the left with faint, light-gray diagonal lines. On the right, there are large, overlapping geometric shapes in black and red. A stylized, dark gray city skyline with various building silhouettes is visible in the lower right quadrant, partially obscured by the red and black shapes.

**COMPULSORY**

**Why mandatory for unlisted companies?**



Multiple sets of same shares were created and pledged with different banks/financial institutions for taking of loans.

Avoidance of payment of capital gains tax

It was a common practice in family run companies either not to issue share certificates or all the share certificates were held in the custody of a single person.

There was a practice to allot shares to dummy/ ghost shareholders.

There were disputes on transfer of shares.

Shares were issued in back date.

## Mal-practices



## Why mandatory for unlisted companies?



- ✍ The underlying intent to make it mandatory for the unlisted public companies to maintain the securities in the dematerialized form is to check these mal-practices and to reap all other benefits associated with dematerialization of securities.
- ✍ These Rules were notified with the primary objective of streamlining the issue and transfer of securities process in unlisted companies by ousting the outdated process of physical certificates of securities.





## Advantages of Dematerialization



# Advantages of Dematerialization



01

Ensures holding of shares in respective shareholder names.



02

Allotment of shares only after a person has complied with KYC norms while opening the demat account. So no more dummy/ghost shareholders.



03

Minimal disputes on transfer of shares.



## Advantages of Dematerialization



04

No risk of loss, mutilation, theft and forgery of physical script.



05

Benami holdings or issue of shares in back date totally eliminated.



06

Pledging of shares will become fraud free.



## Advantages of Dematerialization



07

The State will benefit by way of capital gains tax as it will not be possible to evade payment of capital gains through benami holdings.



08

This will ensure total transparency in shares related transactions thereby causing reduction in disputes/oppression cases.



09

Increased protection of shareholder rights.



# Advantages of Dematerialization



10

Less paperwork and transaction costs.



11

No need to split certificates to sell only a part of securities.



12

Transmission of securities is effected by a depositary participant, no need for the security holder to notify/interact with the company.





## Advantages of Dematerialization



13

Expeditious service to shareholders.



14

Above all, promotes corporate culture, generates confidence in the system and encourages more and more entities to enter organised sector.





## Listed vs Unlisted Public Companies

Basis	Listed Company	Unlisted public company
Fresh issue of securities	In demat only	In demat only
Holding of promoters	In demat only	In demat at the time of issue of new securities
Holding of existing security holders	In demat or in physical	In demat or in physical
Further issue of securities to existing security holders	In demat only	In demat only
Transfer of securities	In demat only	In demat only





## Issues relating to Dematerialization



## Issues relating to Dematerialization: For 'Company'



- ✗ It involves additional cost for the company.
- ✗ More procedural work.
- ✗ Recurring expenses on account of payment of annual charges to the Depository.
- ✗ Payment of charges to the Depository on every corporate action.



## Issues relating to Dematerialization: For 'Shareholders'



- ✍ It involves additional cost.
- ✍ More procedural work in respect of opening of demat account by each subscriber, shareholder.
- ✍ Recurring expenses on account of payment of annual charges to DP.



## General obstacle



- ✍ Depositories Act gives option to hold shares in physical form.
- ✍ Thus, even today all shares of listed companies are not in demat form and SEBI has not been able to enforce this due to the provisions of the Depositories Act.
- ✍ The non-obstante clause contained in section 29 is applicable only in respect of the Companies Act, 2013 and does not override the Depositories Act.





## Suggestions and Way forward



## Suggestions

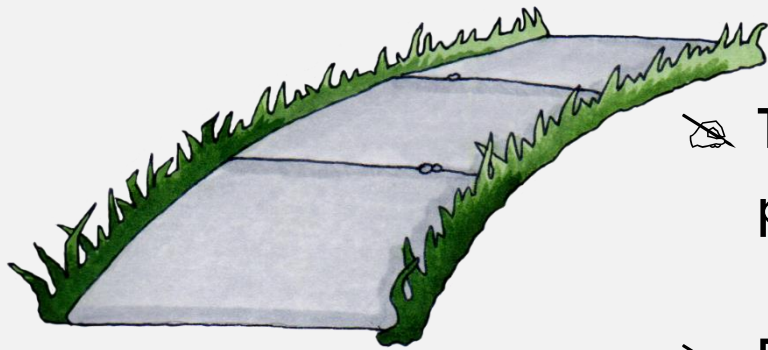


- ✍ Further streamlining of the systems and processes like opening of Bank Account.
- ✍ Streamlining of charges by Depositories in view of higher volume of business on the lines of Jandhan Accounts.





## Way forward



- ✍ Currently, dematerialization of securities is not mandatory for private companies. It may be beneficial to private companies to provide the facility. A few progressive private companies have adopted on voluntary basis.
- ✍ To begin with, the concept may be propagated/extended to private companies which are not small companies.
- ✍ Demat may also be made compulsory in respect of a private companies which take funding from banks/financial institutions or receiving FDI.





# Dematerialization of Securities



## Provisions governing dematerialization



As per section 29 of Companies Act, 2013:,

- a) every company making public offer and such other classes of companies as may be prescribed , shall issue securities in demat form; and
- b) In prescribed classes of unlisted companies , securities can be transferred only in demat form.

In exercise of powers under Section 29, MCA has introduced Rule 9A under Companies (Prospectus and Allotment of Securities) Rules, 2014



## Provisions governing dematerialization



As per Rule 9A, every **unlisted public company** shall –

- a) issue the securities only in dematerialised form; and
- b) facilitate dematerialisation of all its existing securities in accordance with provisions of the Depositories Act, 1996 and regulations made there under.



# Obligations involves



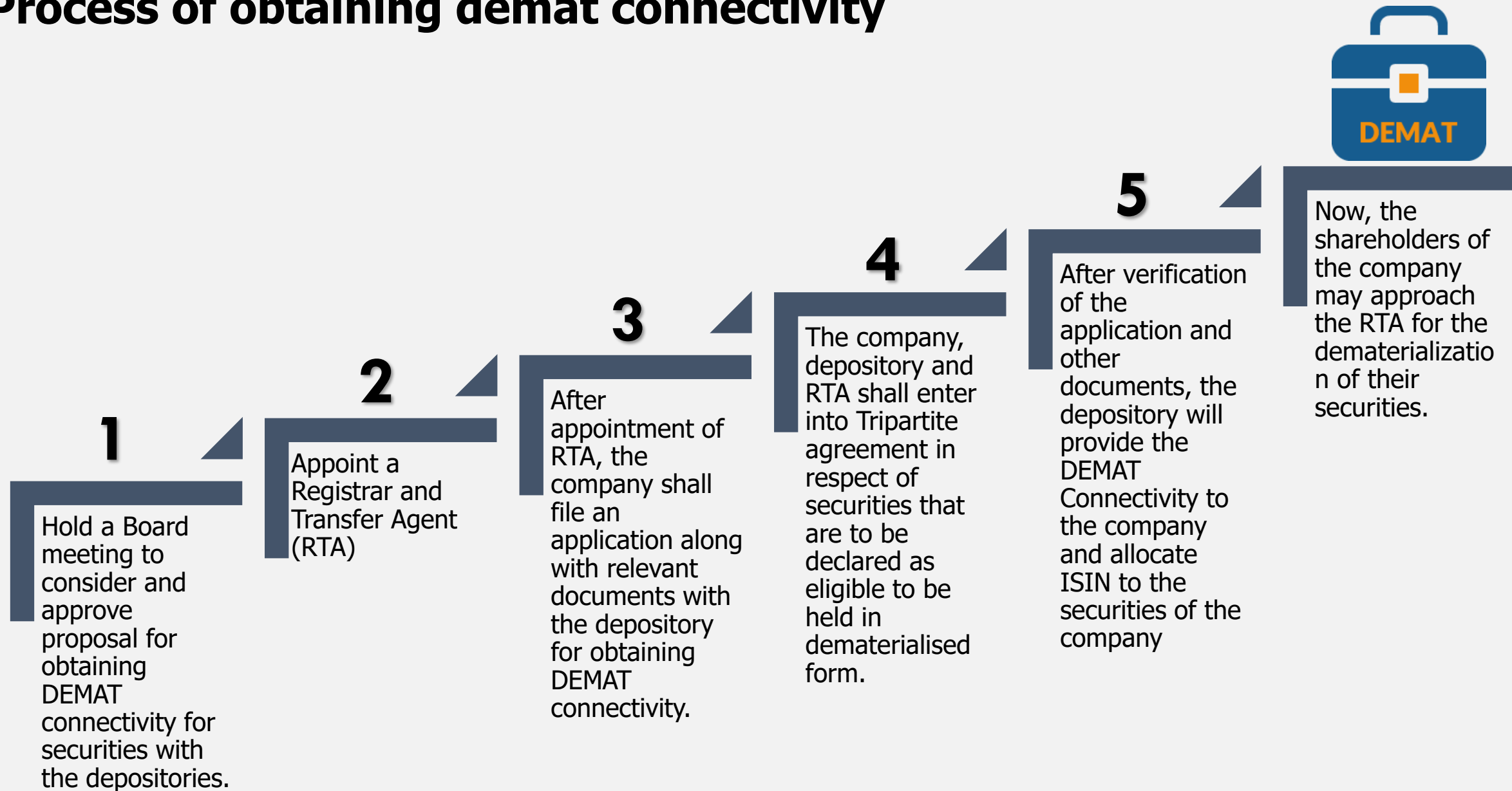
# Impact of Dematerialization



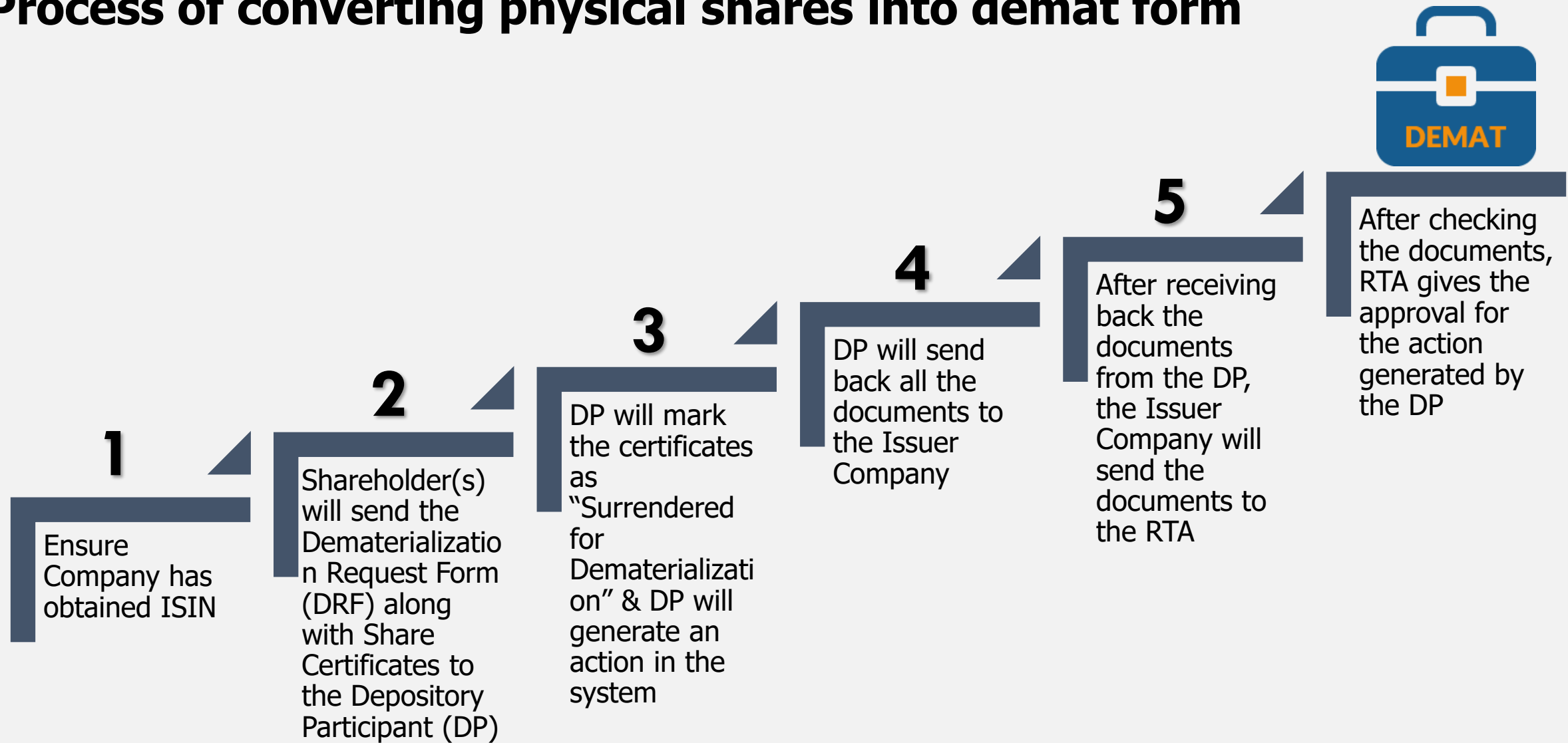
- ✗ As per Section 88, register of index and beneficial owner maintained by depositories shall be register of members for purpose of Section 88.
- ✗ There will be certain restrictions on issuance and transfer of securities .
- ✗ Additional compliance cost in respect of depository and RTA, if appointed and filings.
- ✗ There will be unfettered restriction on transfer of shares in demat form



# Process of obtaining demat connectivity



# Process of converting physical shares into demat form





## Issues related to dematerialization



~~✗~~ **Rules were notified in Sept 2018, can I obtain demat connectivity as on date ?**



# Issues related to dematerialization



~~✗~~ **Whether demat connectivity from both NDSL and CDSL is required?**



# Issues related to dematerialization



~~✗~~ **Whether Company needs to amend its Articles of Association for including clause related to dematerialization?**



# Issues related to dematerialization



 **Whether Company is required to appoint a Registrar & Transfer Agent?**



# Issues related to dematerialization



- ✎ **What are the expected timelines for obtaining demat connectivity**



# Issues related to dematerialization



~~Can a shareholder maintain its holding in form of share certificates?~~



# Issues related to dematerialization



✎ **How can I create a pledge of shares held in demat?**



# Issue of securities in unlisted public company



## Issue of securities or buyback

Entire holding of securities of its promoters, directors and KMP.



## Issue of any securities to existing holders

Entire holding of securities of its promoters, directors and KMP

+

Entire holding of such existing security holders.



## Issue of any securities to new holders

Entire holding of securities of its promoters, directors and KMP

+

Fresh securities to new security holders.





# Issues related issuance of securities



**✗ Can a member, whose shares are not dematerialized, apply for shares in a rights issue?**



# Issues related issuance of securities



- ✗ **Can a member, whose shares are not dematerialized, be allotted bonus shares?**



# Issues related issuance of securities



 **Whether Rule 9A applies to preference shares and debentures?**



# Issues related issuance of securities



- ✗ **Company has issued equity and preference shares, for issuing equity shares , is it necessary all kinds of securities held by promoters, directors, KMP and proposed allottee shall be in demat?**



# Issues related issuance of securities



- ✗ **What remedy is available , if existing promoters are not dematerializing their shares?**



## Issues related issuance of securities



- ✗ **Some of the promoter shareholders are not reachable , the Company wants to issue fresh shares. What options are available ?**



# Issues related issuance of securities



- ✗ **Whether company can split or consolidate shares without having shares of its shareholders in demat form?**



## Restrictions on Transfer of shares



W.e.f. 2nd October, 2018, transfer in unlisted public company is not allowed in physical form





# Restrictions on Transfer of shares



- ✗ **If transfer executed before 02<sup>nd</sup> October, 2018, but documents has not been delivered before such date. Whether the company can be register such transfer after 02<sup>nd</sup> October, 2018?**



# Restrictions on Transfer of shares



**✍ Whether restriction on transfer is applicable on shares received on account of death of registered holder?**



# Restrictions on Transfer of shares



 **Whether transfer of securities in demat is subject to stamp duty?**





## Annual Cost





## Average Annual Cost

Particulars	CDSL/ NSDL
<b>Joining fees (one time)</b>	Rs. 30,000/-
<b>Annual Custody Fee</b>	Rs 10,000/-
<b>Security Deposit</b>	Rs 20,000/-
<b>Annual RTA Cost</b>	Rs 15,000/-
<b>TOTAL COST FOR FIRST YEAR</b>	Rs 75,000/- (plus GST)
<b>ANNUAL TOTAL COST</b>	Rs 25,000 /- (plus GST)



## Standard Annual Cost

Particulars	CDSL/ NSDL		
Joining fees	Rs. 15,000/-		
Annual Custody Fee & Security Deposit	Rs. 11 per folio subject to minimum amount as below:		
	Nominal value of admitted securities	Amount (in Rs.)	Security Deposits (Two Years)
	Upto Rs. 2.5 crore (applicable only for issuer of unlisted shares)	Rs. 5,000/-	Rs. 10,000/-
	Above Rs. 2.5 crores and upto Rs. 5 crore	Rs. 9,000/-	Rs. 18,000/-
	Above Rs. 5 crores and upto Rs. 10 crore	Rs. 22,500/-	Rs. 45,000/-
	Above Rs. 10 crores and upto Rs. 20 crore	Rs. 45,000/-	Rs. 90,000/-
	Above Rs. 20 crore	Rs. 75,000/-	Rs. 1,50,000/-
RTA Cost	Starting from Rs. 10,000/- (Approx) per ISIN.		



## Obligation with respect to payments



- ✍ Company shall make timely payment of fees (admission as well as annual) to the depository and RTA in accordance with the agreement executed between the parties; and
- ✍ Company shall security deposit, at all times, of not less than two years' fees with the depository and RTA, in such form as may be agreed between the parties.
- ✍ Company which has defaulted in aforesaid obligation can't make offer of any securities or buyback its securities or issue any bonus or right shares till the payments to depositories or registrar to an issue and RTA are made





# Reconciliation of Share Capital Audit Report





# Reconciliation of Share Capital Audit Report: Listed Company



- ✍ Regulation 76 of the SEBI (Depositories and Participants) Regulations, 2018.
- ✍ Require to submit quarterly reconciliation of share capital audit report by every listed entity, to the concerned stock exchanges audited by CA or CS in practice.



# Reconciliation of Share Capital Audit Report: PAS-6 (Unlisted Co.)



- ✍ Purpose of **Form PAS-6** is to ensure that shares held physically and in demat form, reconciles with the issued share capital of the Company;
- ✍ While Rule 9A provides for dematerialization of all securities but **Form PAS-6** is only filed for shares and not for debentures, since its capital reconciliation report .
- ✍ **Form PAS-6** shall be certified by either a company secretary in practice or chartered accountant in practice



## Half yearly reconciliation in Form PAS-6

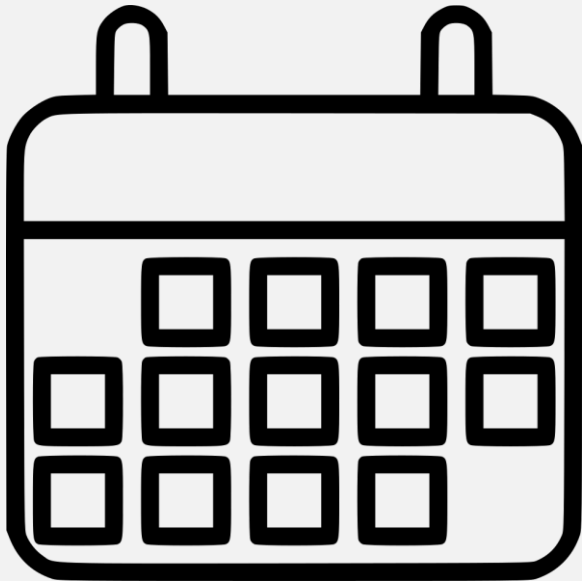


Every unlisted public company shall submit **Form PAS-6** to the Registrar within 60 days from the conclusion of each half year duly certified by a company secretary in practice or chartered accountant in practice.

- ~~✗~~ Half year ended **31st March: 30th May**; and
- ~~✗~~ Half year ended **30th September: 28th November**.



## Due date for filing of PAS-6 for previous periods



- ✍ MCA vide Circular No. 16/2019 dated 28th November, 2019 had stated that the time limit for filing **Form PAS-6 (Half-yearly Reconciliation of Share Capital Audit Report)** without additional fees for the half-year ended on **30th September, 2019** will be 60 days from the date of deployment of this form on MCA-21 portal.
- ✍ Form PAS-6 has been deployed on **15th July, 2020**.
- ✍ Accordingly, the last date for filing the **Form PAS-6** for the half-year ended on **30th September, 2019** and **31st March, 2020** will be **13th September, 2020**.



## Details required in Form PAS-6

Details of demat request accepted within or after 21 days of receipt of request

6

International Security Identification Number (ISIN)

1

Details of shares held by promoters, directors and KMP

5

**Form PAS-6**

Details of capital in demat and physical

2

Details of changes in capital like rights issue, bonus, capital reduction etc.

4

Reason for difference between issued capital and capital in demat & physical

3



## Key Points to be kept in mind



- ✍ ISIN is mandatory to file **Form PAS-6**.
- ✍ The Form is ISIN specific and accordingly, if a company has different types or classes of shares, then **Form PAS-6** will be filed for each of them separately.
- ✍ Since Form is ISIN specific, details of issued capital etc., shall be provided with reference to respective ISIN.
- ✍ If you have different series of preference shares, different ISIN will be required.
- ✍ No separate report as in case of listed entities is required



## Key Issues



**✎ If an unlisted public company has all shares in physical, does it need to file Form PAS-6?**



## Key Issues



**✍ How can a Company who has obtained ISIN now, can file Form PAS-6 for half year ended 30th September, 2019 and 31st March, 2020?**





## Key Issues



~~✎~~ **Whether Form PAS-6 can be filed under CFSS?**



# Suggestions



- ✍ Single **Form PAS-6** shall be allowed to file for all ISIN.
- ✍ Clarification with respect to issued share capital is required
- ✍ There is a validation issue in para 10 and 11.

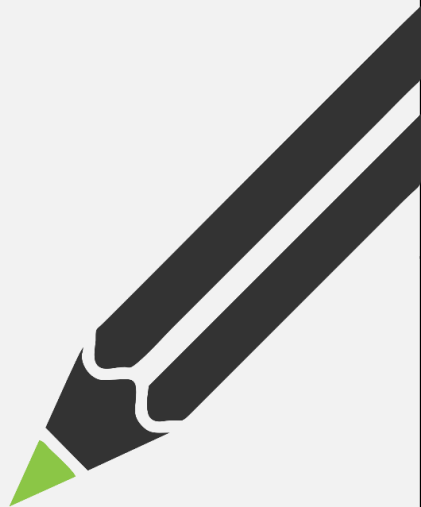




## **Checks to be observed while certifying PAS-6**



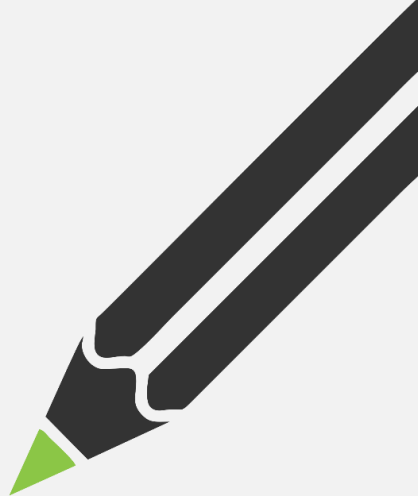
# Checks to be observed while certifying PAS-6 by Practicing CA/CS



<b>1.</b>	Confirm types of shares issued by the Company and their respective ISINs
<b>2.</b>	Check the issued and paid-up with the latest balance sheet as March 2019 and March 2020 and form PAS-3 filed thereafter
<b>3.</b>	For shares in demat, obtain BENPOS/Register of beneficiaries from the concerned depository or RTA
<b>4.</b>	General reasons for difference in issued share capital and shares held in demat and physical <ul style="list-style-type: none"><li>• Forfeiture</li><li>• Shares issued but allotment pending for some reasons</li><li>• Wrong corporate action</li></ul>
<b>5.</b>	Details of changes in share capital during half-year <ul style="list-style-type: none"><li>• Board minutes</li><li>• PAS-3</li><li>• Form INC-28</li><li>• Corporate Action forms for buyback, reduction etc.</li></ul>



# Checks to be observed while certifying PAS-6 by Practicing CA/CS



<b>5.</b>	Details of share held by promoters, directors and KMP <ul style="list-style-type: none"><li>• Check Annual Return- to ascertain promoters</li><li>• List of Directors and KMP as on date of report</li><li>• BENPOS or Individual demat statement</li></ul>
<b>6.</b>	Register of member shall be duly updated: <ul style="list-style-type: none"><li>• Check specific folio for NSDL and CDSL has been created</li><li>• Further allotment of shares have been duly entered in NSDL/CDSL folio</li></ul>
<b>7.</b>	Demat request confirmed before or after 21 days <ul style="list-style-type: none"><li>• Check date of request received and credit from RTA (if appointed) otherwise with Company</li><li>• Obtain necessary undertakings from RTA/ Company, as the case may be</li></ul>
<b>8.</b>	Specific comments of certifying professional , if any, shall be provided in "Any other details that the professional signing this form may like to provide"





# Grievances of security holders



# Grievances of security holders



- ✗ The grievances, if any, of security holders of unlisted public companies under Rule 9A shall be filed before the Investor Education and Protection Fund (IEPF) Authority.
- ✗ The IEPF Authority shall initiate any action against a depository or participant or RTA after prior consultation with the SEBI.
- ✗ It is important to note that neither Section 125 or IEPF Rules , empowers IEPF with such powers.
- ✗ No procedure as on date has been outlined for filing such complaints with IEPF



# Exempted unlisted public companies





## Some Issues



 **Whether a exempted entity, if had dematerialized its securities is required to comply with Rule 9A?**



## Some Issues



 **Whether a wholly owned subsidiary can allot securities , to a third party in physical?**



## Some Issues



 **Whether a holding company of wholly owned subsidiary can transfer shares to a third party in physical?**



# **Dematerialization of shares – a mandatory requirement**



# Key Considerations



- ✗ The Rule creates a mandatory obligation on part of the Company to facilitate dematerialization of shares.
- ✗ There is complete restriction on allotment and transfer of securities in physical.
- ✗ Form PAS-6, which is a mandatory half-yearly filing , can be filed only if ISIN has been obtained.

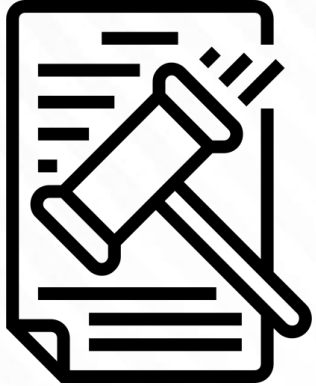


# Key Considerations



~~Can~~ **Can a Company with the consent of shareholders, opt not to obtain demat connectivity?**

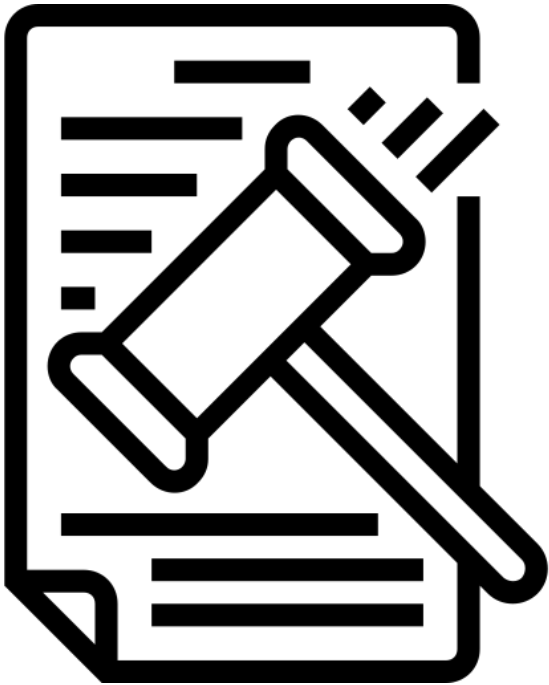




# Penal Provisions



## Penal provisions



- ✍ As there is no penalty prescribed under Section 29 and rule 9A for non-compliance, therefore Section 450 of Companies Act, 2013 (punishment where no specific penalty or punishment is provided) will be applicable.
- ✍ As per Section 450, the company and every officer of the company who is in default or such other person shall be punishable with fine which may extend to Rs. 10 thousand, and where the contravention is continuing one, with a further fine which may extend to Rs. 1 thousand for every day after the first during which the contravention continues.







# **Recent updates in Companies Act, 2013**





## AGM Extension

- ✍ MCA vide General Circular No 28/2020 dated August 17, 2020, has clarified that the companies which are unable to hold their AGM for the financial year ended on 31.03.2020, despite availing the relaxations provided in MCA Circular dated 05.05.2020 ought to file their applications in **form No. GNL-1** for seeking extension of time in holding of AGM for the financial year ended on 31.03.2020 with the concerned Registrar of Companies on or before 29.09.2020.
- ✍ MCA further advised to RoCs to consider all such applications liberally in view of the hardships faced by the stakeholders and to grant extension for the period as applied for (upto three months) in such applications.
- ✍ If approved by ROC, Companies can hold AGM through VC till December , 2020.
- ✍ Kindly note that there is no restriction on holding the AGM physically





## CSR Amendments

MCA vide two Notifications dated 24th August, 2020 has amended the Companies (CSR Policy) Rules, 2014 and Schedule VII of the Companies Act, 2013 to provide for the following amendments:

- ✍ A company which, in its normal course of business, does research and development (R & D) activity of new vaccine, drugs and medical devices is now permitted to incur CSR expenditure to undertake R & D activity of new vaccine, drugs and medical devices related to COVID-19 for financial years 2020-21, 2021-22 and 2022-23 subject to the conditions that-
  - a) such research and development activities are carried out in collaboration with any of the institutes or organisations mentioned in item (ix) of Schedule VII to the Act; and
  - a) details of such activity are disclosed separately in the Annual Report on CSR included in the Board's Report.





# CSR Amendments

- ✍ Companies may also contribute the CSR amount towards the following:
  - a) R & D projects in the field of Science, Technology, Engineering and Medicine funded by the Central Government or State Government or any agency or PSU of the Central Government or State Government; and
  - b) Autonomous Bodies established by the Department of Pharmaceuticals and Ministry of AYUSH, ICMR, CSIR etc., engaged in conducting research in science, technology, engineering and medicine aimed at promoting Sustainable Development Goals .





## Board Report related Amendments

- ✍ MCA has finally notified the long-awaited amendment in section 92 relating to extract of annual return under Companies (Amendment) Act, 2017
- ✍ If a company has its own website, the annual return (**MGT-7**) can be uploaded on the website and the web link of such annual return has been disclosed in the Board's report. In such case extract of annual return in **Form No. MGT.9** will not be required to be attached with the Board's report.
- ✍ Annual Return shall be uploaded for last FY
- ✍ Where accompany has no website, it will continue to attach the extract of annual return with the Board's report in **Form No. MGT.9**.





## Board Report related Amendments

- ✍ It is important to note that while the enabling provisions under Section 92 to provide for extract of **Form MGT-9** has been omitted but the Rules continue to provide for the same.
- ✍ Section 469 of the Act, empowers the Government to make rules in following cases
  - ✍ For carrying out the provisions of Act.
  - ✍ For all or any of the matters, which the Act requires to be prescribed



# THANK YOU

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