

CHAPTER 6 - DISTRIBUTION OF PROFITS

Meaning and Definition of Dividend

Dividend includes any interim dividend [Section 2(35)].

The power to pay dividend is inherent in a company and is not derived from the Companies Act, 2013 or the Memorandum or Articles of Association although the Act and the Articles regulate the manner in which dividends are to be declared.

Right to claim dividend will only arise after a dividend is declared by the company in general meeting and until and unless it is so declared, the shareholder has no claim against the company in respect of it.

Final dividend

Dividend is said to be a final dividend if it is declared at the annual general meeting of the company. Final dividend once declared becomes a debt enforceable against the company. Final Dividend can be declared only if it is recommended by the Board of Directors of the Company.

In accordance with Section 134(3)(k), Board of directors must state in the Directors' Report the amount of dividend, if any, which it recommends to be paid.

Interim dividend

Dividend is said to be an interim dividend, if it is declared by the Board of Directors between two annual general meetings of the company. All the provisions relating to the payment of dividend shall be applicable on the interim dividend also.

Declaration of Dividend (Section 123)

According to Section 51, a company may, if so authorized by its articles, pay dividend in proportion to the amount paid up on each share.

Sources of declaration of dividend

Section 123(1) of Companies Act 2013 provides that no dividend shall be declared or paid by a company for any financial year except—

(a) Out of Profits

- (i) 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
- (ii) 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
- (iii) out of both;

Provided that in computing profits any amount representing unrealised gains, notional gains or revaluation of assets and any change in carrying amount of an asset or of a liability on measurement of the asset or the liability at fair value shall be excluded; or

- (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.

Transfer of profits to reserves

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.

Note:

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.

Dividend in case of absence or inadequacy of profits

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 free reserves,

such declaration of dividend shall not be made except in accordance with such rules as may be prescribed in this behalf.

Note:

- No dividend shall be declared or paid by a company from its reserves other than free reserves.

Rule 3 of Companies (Declaration and Payment of Dividend) Rules, 2014

In the event of adequacy or absence of profits in any year, a company may declare dividend out of surplus subject to the fulfillment of the following conditions, namely:-

- (1) The rate of dividend declared shall not exceed the average of the rates at which dividend was declared by it in the 3 years immediately preceding that year. This condition shall not apply to a company which has not declared any dividend in each of preceding 3 financial years.
- (2) The total amount to be drawn from such accumulated profits shall not exceed 1/10th 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 utilized 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 15% of its paid up share capital as appearing in the latest audited financial statement.

Declaration of interim dividend

According to Section 123(3) of the Companies Act, 2013,

- the Board of Directors of a company may declare interim dividend
 - o during any financial year or
 - o at any time during the period from closure of financial year till holding of the annual general meeting
- out of
 - o the surplus in the profit and loss account or
 - o profits of the financial year for which such interim dividend is sought to be declared or
 - o profits generated in the financial year till the quarter preceding the date of declaration of the interim dividend.

When the company has incurred any 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 the 3 financial years.

Points to Note:

- Amount of Dividend to be deposited in Special Account of a Schedule Bank within 5 days
Section 123(4) provides that the amount of the dividend, including interim dividend, shall be deposited in a scheduled bank in a separate account within 5 days from the date of declaration of such dividend.
- Dividend only to registered shareholder
Section 123(5) explains that 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.
 - o Capitalization of Profits
Company may capitalize the profits or reserves of a company for the purpose 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.
 - o Mode of payment
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.
- No dividend to be declared/paid in case of failure of repayment of deposits [Section 123(6)]
A company which fails to comply with the provisions of sections 73 (prohibition of acceptance of deposits except in the manner provided) and 74 (Repayment of deposits etc. accepted before commencement of Companies Act 2013) shall not declare any dividend on its equity shares (so long as such failure continues).

Unpaid Dividend Account (Section 124)

According to Section 124(1), when a dividend has been declared by a company but has not been paid or claimed within 30 days from the date of the declaration to any shareholder entitled to the payment of the dividend, the company shall, within 7 days from the date of expiry of the said period of 30 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'.

According to Section 124(4), 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.

- (a) Details of unpaid dividend to be placed at the website [Section 124 (2)]
The company shall, within a period of 90 days of making any transfer of an amount under Section 124(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.
- (b) Effect of Non-Transfer of the Dividend – Interest Payable [Section 124(3)]
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, company 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 12% per annum and the interest accruing on such amount shall ensure to the benefit of the members of the company in proportion to the amount remaining unpaid to them.
- (c) Transfer to investor education and protection fund [Section 124 (5)]
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 7 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 Section 125(1) [Investor Education and Protection Fund] 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.
- (d) Shares in respect of unpaid dividend also to be transferred to IEPF [Section 124(6)]

All shares in respect of which dividend has not been paid or claimed for 7 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.

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 (Rule 7 of the Investor Education and Protection Fund Authority (Accounting, Audit, Transfer and Refund) Rules, 2016).

In case any dividend is paid or claimed for any year during the said period of 7 consecutive years, the share shall not be transferred to Investor Education and Protection Fund.

(e) Offence & penalty [Section 124(7)]

If a company fails to comply with any of the requirements of this section, such company shall be liable

- to a penalty of one lakh rupees and in case of continuing failure, with a further penalty of Rs. 500 for each day after the first during which such failure continues, subject to a maximum of Rs. 10 lakh and every officer of the company who is in default shall be liable
- to a penalty of Rs. 25,000 and in case of continuing failure, with a further penalty of Rs. 100 for each day after the first during which such failure continues, subject to a maximum of Rs. 2 lakh.

Investor Education and Protection Fund (Section 125)

The Central Government shall establish a Fund to be called the Investor Education and Protection Fund.

Following amount shall be credited to the Fund—

- (a) 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;
- (b) donations given to the Fund by the Central Government, State Governments, companies or any other institution for the purposes of the Fund;
- (c) the amount in the Unpaid Dividend Account of companies transferred to the Fund under sub section (5) of section 124;
- (d) the amount lying in the Investor Education and Protection Fund under section 205C of the Companies Act, 1956;
- (e) the interest or other income received out of investments made from the Fund;
- (f) the amount received under sub-section (4) of section 38 [Punishment for Personation for Acquisition, etc., of Securities.];
- (g) the application money received by companies for allotment of any securities and due for refund;
- (h) matured deposits with companies other than banking companies;
- (i) matured debentures with companies;
- (j) interest accrued on the amounts referred to in clauses (g) to (i);
- (k) sale proceeds of shares arising out of issuance of bonus shares, merger and amalgamation for 7 or more years;
- (l) redemption amount of preference shares remaining unpaid or unclaimed for 7 or more years; and
- (m) such other amount as may be prescribed.

Provided that no such amount referred to in clauses (g) to (j) shall form part of the Fund unless such amount has remained unclaimed and unpaid for a period of 7 years from the date it became due for payment.

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Utilisation of Investor Education and Protection Fund

Section 125 (3) provides 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.

Right to Dividend, Rights Shares and Bonus Shares to be held in Abeyance Pending Registration of Transfer of Shares

According to Section 126, when 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,—

- (a) 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
- (b) keep in abeyance in relation to such shares, any offer of rights shares under clause (a) of subsection (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.

Punishment for Failure to Distribute Dividends

Section 127 of Companies Act 2013 provides that when a dividend has been declared by a company but has not been paid or the warrant in respect thereof has not been posted within 30 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
 - o with imprisonment which may extend to 2 years and
 - o with fine which shall not be less than Rs. 1,000 for every day during which such default continues and
- the company shall be liable to pay simple interest at the rate of 18% per annum during the period for which such default continues.

Exceptions: Proviso to section 127 has provided a list where 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

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.