Chapter 8 – Declaration and Payment of Dividend

[Section 123 to 127]

Basics	Provisions	Funds related to Dividend	Punishment for Non-Compliance
↳ Definition u/s 2(35) ↳ **Types** (Final/ Interim)	↳ **Sec. 123:** Declaration of Dividends ↳ **Sec 124:** Unpaid/ Unclaimed Dividend	↳ **Sec. 125:** IEPF ↳ Establishment ↳ Credits to the Fund ↳ Utilization	↳ **Sec. 127:** Punishment for failure to distribute dividend within 30 days

Definition:

Section 2(35) "*dividend*" includes any interim dividend.

Important points relating to dividend:

- It is a distribution of profits
- Final dividend is declared and approved by shareholders (by OR at AGM) on recommendation of Board
- The rate of dividend declared by SH shall not exceed the amount recommended by BOD
- Dividend % is a proportion of nominal value or face value

Concept clarity check:

1. Board recommended 10% dividend. Can SH, by passing unanimous resolution, declare 12% dividend? - No!
2. Calculate the amount of dividend in following case:
   No. of shares held = 50
   Face Value = Rs. 10; Market Value (in stock exchange) – Rs. 200; Purchase price – Rs. 190
   SH approved and declared dividend = 10%
   Amount of dividend = No. of shares * Dividend * Face Value i.e., 50 shares * 10% * Rs. 10 = Rs. 50 (total)

   Note – Market value or purchase price is irrelevant for the calculation of amt. of dividend

Types of dividend:

Classification based on time

Particulars	Interim Dividend	Final Dividend
Announcement	Announced and declared by ~~SH~~ BOD at any time during the FY or from closure of FY till the AGM	Recommended by BoD and declared by shareholders at the AGM of the co.
Provision in AOA	Declared only when the AOA permits the declaration.	Does not require any specific provision in the articles
Source	Out of profits before final adoption of accounts Sources for interim dividend = Surplus in PL or CY profit or Prior Profits	--
Ratification	Shall be ratified at the AGM by the members	Not applicable
Rate of Dividend	If the company has incurred loss during the CY upto preceding quarter • dividend not to be declared at a rate higher • than Avg rate of dividend declared by Co	The rate recommended by the Board cannot be increased by the members

	• during the immediately preceding 3 FYs.	
Revocation	Can be revoked with consent of ALL shareholders	Once declared - cannot be revoked.

The Dividend shall be deposited in a separate A/c of a scheduled bank within 5 days from the date of declaration

Classification of Dividend based on Nature of Shares		
Preference Shares (Sec 43)		Equity Shares
Cumulative	Non-Cumulative (Default)	
Dividend gets accumulated	Dividend is payable only in a year of profit. No accumulation of profit	Equity shares holder do not enjoy any preferential rights for dividends or repayment of capital
Arrears due to insufficiency of profits payable from future profits. Unless this dividend is paid in full (incl. arrears) , no dividend is payable to equity shareholders	Holder not entitled to be paid arrears of dividend out of future years i.e., right to receive dividend expires if not declared in any year.	Rate of dividend depends upon the dividend policy and availability of profits after satisfying Pref. SH rights

Section 123: Declaration of Dividend

(1) **Source**: Dividend shall be declared or paid by a company for any FY out of:

Profits* for that FY (current) arrived at after providing for depreciation (Sch II)	Undistributed profits* of any previous FYs arrived at after providing for depreciation as per Sch II (i.e., credit balance in P&L and free reserves)	Both (a) and (b) [Current + Past Profits]	Money provided by CG/SG for payment of div. in pursuance of guarantee given by the Govt

*Provided that – While calculating profits – exclude:

- unrealised gains, notional gains or revaluation of assets AND
- any change in carrying amount of an asset/liability on measurement at fair value

Transfer to Reserves – A company MAY, before declaration of dividend in any FY, transfer such % of its profits for that FY as it may consider appropriate to reserves of the company.

Conceptual Clarity Check:

1. Can capital reserve be used for payment of dividend? – No! Only free reserves can be used for dividend
2. Carried over previous losses and depreciation not provided in PY has to be set off against CY profits before declaration of dividend
3. Capital profits are not earned in normal course of biz. Hence, not available for distribution as dividend
4. Is it okay if a company decides not to transfer any amount to reserves before dividend? – Yes! Whether or not to transfer and what % to be trf to reserve is left to the discretion of the company.

(2) For the purposes of clause (a) of Sec 123(1) depreciation shall be provided in accordance with Sch II

(3) Rate of Dividend – Interim Dividend in case of loss in recent quarter (not Final Dividend):

Board may declare interim dividend during any FY or at any time from closure of FY till holding of AGM out of:

- Surplus in the P&L account or
- Profits of the FY for which such interim dividend is sought to be declared (past FY), or
- Profits generated in the FY till the quarter preceding the date of declaration of interim dividend

Provided that - In case the co. has incurred loss during the current FY 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 > Average dividends declared by the company during the immediately preceding 3 FY

Concept clarity check:
Is the upper limit on rate of dividend (i.e., not > Avg of preceding 3 FY) also applicable in case if there is profit in the current FY till preceding quarter? – No. In case of profit, the % of dividend can be higher?

Rule 3 Declaration of Dividend out of Reserves: ***[Very imp]***
In the event of inadequacy or absence of profits in any year, a co. may declare dividend out of free reserves subject to the fulfilment of the following 3 conditions, namely:-

Rate shall not exceed Average of dividend of 3 immediately preceeding FY*	Total amount drawn from accumulated profits <= 1/10th of [PUSC + FR] as per latest audited FS Amount drawn shall first be utilised to set off losses of current FY	Balance in reserve after such drawal not < 15% of PUSC as per latest audited FS

* This sub-rule(1) shall not apply if a co. has not declared any dividend in each of the 3 preceding FY.

(4) Dividend amt (incl. interim) – Deposit in separate account with scheduled bank within 5 days from declaration

(5) No dividend shall be paid by a co. 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.

Provided that nothing in this sub-section shall be deemed to prohibit the capitalisation of 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.

Concept clarity check:
1. Mr. Singh has purchased shares of Burraaah Ltd. from Mr. Jai by making full payment. However, the transfer of shares is not yet registered with the company. Meanwhile, the co. announces dividend. Is the company allowed to pay the dividend to Mr. Singh? – No. In such case, the company will keep the dividend till the registration is pending (Discussed in detail in sec 126)

2. Can a company issue bonus shares in lieu of dividend – No. Dividend can only be paid in cash.
3. Can a company pay dividend via bank? – Absolutely Yes. Cash doesn't mean hard cash. It means – Cash, cheque, dividend warrant or via any e-mode.

(6) 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.

Note: Section 8 companies are prohibited from paying any dividend to its members. Its profits are intended to be applied only in promoting the objects for which it is formed. *[Sec 8]*

Bonus Point
What is record date?
Record date is the date announced by the company for determining members who are entitled to dividend. All person whose name is included in the register of members on the record date shall be entitled to dividend.

Section 124: Unpaid Dividend Account

(1) Where a dividend is declared but not paid or claimed within 30 days from the date of declaration,
- the company shall, within 7 days from the expiry of the said 30 days,
- transfer the total unpaid/unclaimed amount of dividend to a special account (with scheduled bank) called the Unpaid Dividend Account (UDA)

(2) Preparing of Statement of the Unpaid Dividend
- Within 90 days of transferring any amount to the Unpaid Dividend Account
- prepare a statement containing the following:

Name	Last known address	Unpaid dividend amount

- and place it on website and on any other website approved by CG for this purpose.

(3) Payment of Interest on default

If default is made in transferring the total amount u/ss (1) to UDA, company shall:
- Pay interest @12% p.a. from the date of such default
- Interest accruing on such amount shall ensure to benefit of members of the co. in proportion to amt. remaining unpaid to them

(4) Claimant to apply for payment of Claimed Amount apply to the Co concerned for payment of the money claimed

(5) Transfer of Unclaimed or unpaid amount to Investor Education and Protection Fund (IEPF)
- If remains unpaid or unclaimed for 7 years from the date of such transfer
- It shall be transferred by the company along with interest to the IEPF, and
- A prescribed statement containing details of such transfer shall be sent to IEPF Authority and
- Authority to issue receipt as an evidence of such transfer

(6) Transfer of Shares to IEPF

All shares in respect of which dividend has not been paid/claimed for >= 7 consecutive years shall be transferred by the company in the name of IEPF along with a statement containing such details.

Author's Note – Note that this section is talking about transfer of the "shares" itself and not the unpaid amount of dividend. The trf. of unpaid amount is already discussed u/ss (5)

Provided that any claimant of shares trfd. above shall be entitled to claim the transfer of shares from IEPF with such procedure and on submission of such documents as may be prescribed.

Explanation:

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.

(7) Punishment for Contravention of this section:

	Company	Officer in default
Penalty	Rs. 1 lakh + Rs. 500/day after first	Rs. 25,000 + Rs. 100/day
Max penalty	Rs. 10 lakhs	Rs. 2 lakhs

Section 125: Investor Education and Protection Fund

(Read with IEPF Authority (Accounting, auditing, transfer and refund) Rules 2016)

(1) The CG shall establish a Fund to be called the Investor Education and Protection Fund (IEPF)

(2) There shall be credited to the Fund—

a) the amount given by the CG 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 u/s 124(5)
d) the amount in general revenue account of the CG which had been transferred to that account u/s 205A (5) of Companies Act, 1956 and remaining unpaid or unclaimed on the commencement of this Act;
e) the amount lying in IEPF u/s 205C of the Companies Act, 1956;
f) the interest or other income received out of investments made from the Fund
g) the amount received under section 38(4);
h) the application money received by companies for allotment of any securities and due for refund;
i) matured deposits with companies other than banking companies;
j) matured debentures with companies;
k) interest accrued on the amounts referred to in clauses (*h*) to (*j*);
l) sale proceeds of fractional shares arising out of bonus shares, merger and amalgamation for >=7 yrs
m) redemption amount of preference shares remaining unpaid or unclaimed for >=7 yrs; and
n) such other amount 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 7 years from the date it became due for payment.

Summary of summary!

CG grants	Donation by CG/SG/Cos.	Amt. of UDA u/s 124	General Revenue A/C	IEPF in Co. Act 1956	Other income from investment
Amount disgorged u/s 38(4)	Application money	Matured deposit or debenture or intt thereon	sale proceeds of fractional shares (>=7 yrs)	Redemption of pref. shares (>=7 yrs)	Other amount

(3) The Fund shall be utilised for: [CD PRO]

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 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 u/s 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, where, as per provision of Sec 205C of Co. Act, 1956, amount is transferred to IEPF, after the expiry of 7 yrs, such person shall be entitled to get refund out of IEPF (constituted under Co. Act 2013)

(4) Any person claiming to be entitled to amt referred u/ss (2) may apply to IEPFA for payment of money claimed

(5) CG to constitute, by notification, an authority for administration of Fund consisting of:

Chairperson [Ex-officio - Secretary, MCA]	a CEO (appt. by CG)	Members not > 7 (including CP)

(6) Manner of administration, appt. of CP, members & CEO, holding of IEPFA meetings– As per prescribed rules

(7) Resources - CG may provide to IEPFA such offices, officers, employees and other resources - as prescribed.

(8) 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 C&AG of India.

(9) It shall be competent for IEPFA to spend money out of the Fund for carrying out the objects of IEPF.

(10) Accounts of the Fund shall be audited by the C&AG of India (at specified intervals). Audited accounts + audit report to be forwarded annually by IEPFA to the CG.

(11) Annual Report:
- IEPFA to prepare its annual report (prescribed form and time for each FY)
- Giving full account of its activities during the FY and
- Forward a copy thereof to the CG and
- CG shall cause annual report + audit report (by C&AG) to be laid before each House of Parliament

126. Right to dividend, rights shares and bonus shares to be held in abeyance pending registration of transfer of shares

- Notwithstanding anything contained in any other provision of this Act,
- Where any instrument of transfer of shares has been delivered to any co. for registration and
- Such transfer has not been registered by the co.,
- Such company shall:

Transfer the dividend w.r.t. such shares to UDA account (unless the co. is authorised, in writing, by registered holder to pay such dividend to transferee specified in transfer instrument)	+	Keep in abeyance - Any offer of right shares u/s 62(1)(a) or issue of fully paid up bonus shares

127. Punishment for failure to distribute dividends

- Where a dividend has been declared
- But, within 30 days of such declaration, it has not been paid or warrant has not been posted, to entitled SH,
- The punishment shall be:

	Every Director who is knowing a party to default (not OID)	Company
Imprisonment	Extend to 2 years AND	NA
Fine – During the period where default continues	Not < Rs. 1k / day – Default continues	Simple Interest 18% p.a.

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

(a) the dividend could not be paid by reason of the operation of any law

(b) SH has given directions to co. regarding payment of dividend and those directions cannot be complied with and the same has been communicated to him (3 conditions – Given directions + Cannot comply + Communicate)

(c) there is a dispute regarding right to receive the dividend;

(d) the dividend has been lawfully adjusted by the company against any sum due from shareholder; (for example – adjustment of calls in arrears), or

(e) 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 default on part of company.

Technique to remember - Law ke Direction mein jaoge toh Dispute nahin hoga. Par agar books mein Adjustment ya payment mein Default karoge toh dikkat hai

Modification for Nidhi Company (w.r.t. Sec 127):

In case of Nidhi Co., where the dividend payable is <= Rs 100, it shall be sufficient compliance of sec 127 if:

- declaration of dividend is announced in local language in one local newspaper of wide circulation
- announcement is also displayed on the notice board of the Nidhis for at least 3 months.

Concept clarity check:

The company is responsible to post the dividend warrant within 30 days of declaration of dividend. However, if such post doesn't reach SH within 30 days, it's not the responsibility of the co. Hence, company cannot be penalised if warrant doesn't reaches before 30 days.