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BONUS ISSUE

6.1 Introduction

A bonus issue as the name suggests is something which is given free or gratuitously. Companies may, reward their shareholders by way of a bonus issue. Normally, in a bonus issue, the shareholders are given additional shares in a specified ratio, without being asked to pay for the additional shares. Companies may issue bonus shares by capitalising their free reserves out of General Reserves, Profit & Loss Balance, etc. A bonus issue is often called a "zero-sum game" since there is no outflow to the company nor is the shareholder paying for anything. All that the company is doing is converting its free reserves into equity capital.

6.2 Companies Act

The important provisions in the Companies Act relating to the issue of bonus shares are as follows:

(a) The Act does not contain any definition of the term bonus shares.

(b) Schedule I - Table A, which provides for the model Articles of Association of a Limited Company provides that the bonus issue can be made by capitalising free reserves.

(c) Fully paid-up bonus shares can also be issued from the Capital Redemption Reserve and the Share Premium Account.

(d) The Articles of Association of the Company must provide for issue of bonus shares. If the Articles do not provide for a Bonus issue, then they must first be amended.

(e) Bonus shares can also be issued by paying up any amount remaining unpaid on existing shares.

(f) An unlisted public company and a private limited company can issue bonus shares even out its revaluation reserve. The recent Supreme Court decision in the case of Bhagwati Devlopers v. Peerless General Finance & Investment Company (2005) 62 SCL 574 (SC) has laid the controversy over this issue to rest.

6.3 SEBI Guidelines

6.3.1 The SEBI DIP Guidelines contain certain additional provisions for the issue of bonus shares by a listed company. The important provisions may be summarised as follows:

(a) If any FCDs/ PCDs are pending conversion, then a bonus issue cannot be made unless a similar benefit is extended to the holders of such FCDs/ PCDs.

(b) The bonus issue shall be made out of free reserves built out of the genuine profits or out of share premium collected in cash only. Thus, if shares are issued for consideration other than cash, then premium on such shares would not be considered.

(c) Bonus shares cannot be issued out of revaluation reserves by a listed company.

(d) Bonus, in lieu of dividend, is not allowed.

(e) The bonus issue is not made unless the existing partly-paid shares are made fully paid-up.

(f) The Company:
- has not defaulted in payment of interest or principal on fixed deposits and interest or principal on existing debentures and
- has sufficient reason to believe that it has not defaulted in respect of the payment of statutory dues of the employees such as contribution to provident fund, gratuity, bonus etc.

(g) Once the approval of the Board of Directors for the bonus issue is received, the company must implement the proposal within 6 months from the date of such approval and it shall not have the option of changing the decision.

6.3.2 Practice Pointer: The Company and its Auditor or a practising Company Secretary must certify compliance with the Guidelines. There is no specified format for the same. A copy of such Certificate must be forwarded to SEBI.

6.4 FEMA Guidelines

The FEMA Regulations permit an Indian company to issue bonus shares to its non-resident shareholders, subject to the following conditions:

(a) the original are acquired or held by the non-resident shareholder in accordance with the FEMA Rules/ Regulations applicable to such acquisition;

(b) the bonus shares acquired by the non-resident shareholder shall be subject to the same conditions including restrictions in regard to repatriability as are applicable to the original shares.