

A Serious Loss of Capital has occurred when the net assets of the company becomes less than half of its stated capital, usually as a result of a significant accumulated loss that reduces the shareholders equity.

Duties of directors on serious loss of capital

- As per the requirements of the Companies Act, when a Serious Loss of Capital occurs, the board shall within 20 working days of that fact becoming known to the directors, call an EGM of shareholders of the company to address the issue.
- The financial position of the company will be discussed in the EGM, accompanied by a report prepared by the board which advises shareholders of,
 - (a) the nature and extent of the losses incurred by the company
 - (b) the cause or causes of the losses incurred by the company
 - (c) the steps, if any, which are being taken by the board to prevent further such losses or to recover the losses incurred.
- Shareholders will be given adequate opportunity to inquire, discuss and comment on the report and the management of the company. (Source: Companies Act, Section 220, subsection 1&2)

Impact of Serious Loss of Capital

To the
Directors

- If the board of a company fails to comply with the requirements, every director who willfully permits the failure shall be guilty of an offence and be liable. (Source: Companies Act, Section 220, subsection 4)

To the
Company

- The auditor may either emphasis on the matter or even qualify the opinion depending on the severity & non availability of plans to rectify the serious loss of capital situation.
- If the auditor qualifies the financials or submitted an Emphasis of Matter of Going Concern, the Securities of such Listed Entity shall be **transferred to the Watch List** on or before the expiry of five Market Days from the date of submission of such Audited Financial Statements.
- In the event the matters are not resolved within a period of fifteen months from the date of transferring the Securities of the Entity to the Watch List, the trading of **Securities of the Listed Entity shall be suspended**. (Ref note 1, CSE Listing Rules, Section 7)

- In the event the trading suspension continues for a period in excess of twelve months, the **Securities of the Entity shall be delisted** by the Board of Directors of the CSE in terms of Rule 11.3 (a) of the Listing Rules.

- Shareholders may be required to contribute additional capital by **subscribing to the rights issue** to boost the capital.
- In the event the shares get suspended, shareholders **may not be able to trade** on the particular share.
- In the event the company get delisted, due to the company not being able to rectify the Serious Loss of Capital, the shareholders may hold shares that are **difficult to dispose** due to lack of access to the share market.

Rectifying a Serious Loss of Capital

- ✓ Infuse further equity by way of a rights issue. (Refer Scenario 1)
- ✓ Raising funds through a secondary public offer.
- ✓ Identifying assets that could be liquidated in order to restructure the balance sheet.
- ✓ Negotiate with creditors to convert full or part of debt into equity.
- ✓ Restructure the balance sheet by writing off losses against equity/ reserves. (Refer Scenario 2)

Examples for a Serious Loss of Capital & Rectifications

Scenario 1	2018/19	2019/20	2020/21	2021/22	2022/23
Share Capital	800,000,000	800,000,000	800,000,000	800,000,000	1,000,000,000
Retained Earnings	40,000,000	-250,000,000	-440,000,000	-420,000,000	-410,000,000
Net Assets	840,000,000	550,000,000	360,000,000	380,000,000	590,000,000

Serious Loss of Capital Triggered (Net Assets < 50% of stated capital)
After Rectification: Ex: Introduced new capital of 200 Mn by means of a Rights Issue

Scenario 2	2018/19	2019/20	2020/21	2021/22	2022/23
Share Capital	800,000,000	800,000,000	800,000,000	800,000,000	380,000,000
Retained Earnings	40,000,000	-250,000,000	-440,000,000	-420,000,000	50,000,000
Net Assets	840,000,000	550,000,000	360,000,000	380,000,000	430,000,000

Serious Loss of Capital Triggered (Net Assets < 50% of stated capital)
After Rectification: Ex: Balance sheet restructured by writing off losses against equity

Notes

Note 1 (Extracted from CSE Listing Rules, Section 7)

Enforcement Procedure for Independent Auditor's Reports containing a Qualified Audit Opinion and/or an Emphasis of Matter on Going Concern

(A) In respect of Securities Listed on the Main Board and Diri Savi Board in the Main Market Segment

1. This Rule 7.5 (d)(ii)(A) shall not be applicable to Entities which have listed only Debt Securities on the Exchange provided a fresh rating certificate obtained for the relevant financial year is disclosed to the market.
2. In the event the independent auditor's report in the Audited Financial Statements of a Listed Entity submitted to the Exchange contains a qualified audit opinion and/or an emphasis of matter on going concern, it shall be the duty of such Entity to resolve such matters within the time period provided for in these Rules.
3. Until the matters giving rise to the qualified audit opinion and/or emphasis of matter on going concern are resolved and such resolution is independently verified by an auditor within the time periods provided herein, the Listed Entity shall be subjected to the enforcement procedures as specified in this Rule.
4. In the event the independent auditor's report on the Audited Financial Statements submitted to the Exchange contains a qualified audit opinion and/or an emphasis of matter on going concern, the Securities of such Listed Entity shall be transferred to the Watch List on or before the expiry of five (05) Market Days from the date of submission of such Audited Financial Statements to the Exchange.
5. On submission of such Audited Financial Statements to the Exchange, the Entity shall make an announcement to the Market via the Exchange regarding the qualified audit opinion and/or emphasis of matter on going concern (as applicable) and such announcement shall contain the following;
 - a) A Statement that the Securities of the Entity will be or has been (as applicable) transferred to the Watch List by the Exchange within five (5) Market Days from the date of receipt of the Audited Financial Statements of the Entity as it contains a qualified audit opinion and/or an emphasis of matter on going concern (as applicable);
 - b) The remedial action taken or proposed to be taken by the Entity to resolve the matters giving rise to the qualified audit opinion and/or the emphasis of matter on going concern (as applicable);
 - c) The time period within which such remedial action will be taken by the Entity; and
 - d) The following additional statements;
 - i. In the event of any deviation from the proposed remedial action, the extent of the deviation shall be communicated to the investors by way of a subsequent announcement to the Market via the Exchange within one (01) Market Day from the date of obtaining the approval of the Board of Directors of the Entity for such deviation;
 - ii. In the event the matters giving rise to the qualified audit opinion and/or the emphasis of matter on going concern (as applicable) are not resolved within a period of fifteen (15) months from the date of transferring the Securities of the Entity to the Watch List, the trading of Securities of the Listed Entity shall be suspended. In the event the trading suspension continues for a period in excess of twelve (12) months, the securities of the Entity shall be delisted by the Board of Directors of the CSE in terms of Rule 11.3 (a) of the Listing Rules.
 - iii. In the event the matters giving rise to the qualified audit opinion and/or the emphasis of matter on going concern (as applicable) are resolved and such fact is independently verified by an auditor during the period the Securities of the Entity are on the Watch List, it shall be announced to the Market via the CSE forthwith.