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शक्तिउत्थानआश्रमलखीसरायबिहार

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Accounting for Share Capital

Question 1:

What is meant by the word 'Company'? Describe its characteristics.

ANSWER:

The Section 3 (1) (i) of the Company Act of 1956 defines an organisation as a company that is formed and registered under the Act or any existing company that is formed and registered under any earlier company laws. In general, a company is an artificial person, created by law that has a separate legal entity, perpetual succession, common seal and has limited liability. It is a voluntary association of person who together contributes in the capital of the company to do business. Generally, the capital of a company is divided into small parts known as shares, the ownership of which is transferable subject to certain terms and conditions. There are two types of company, public company and private company.

Characteristics of Company

1. Association of Person: A company is formed voluntarily by a group of persons to perform a common business. Minimum number of person should be two for formation of a private company and seven for a public company.

2. Artificial Person: Company is an artificial and juristic person that is created by law.

3. Separate Legal Entity: A company has a separate legal entity from its members (shareholders) and Directors. It can open a bank account, sign a contract and can own a property in its own name.

4. Limited Liability: The liability of the members of a company is limited up to the nominal value or the face value of the shares. Unlike a partnership firm, on insolvency of a company, the members and the shareholders are not liable to pay the amount due to the creditors of the company. In fact, the members and the shareholders are only liable to pay the unpaid amount of the shares held by them. For example, if the value of share is Rs 10 and Rs 6 is paid up, then the member is liable to pay only Rs 4.

5. Perpetual Existence: The existence of company is not affected by the death, retirement, and insolvency of its members. That is, the life of a company remains unaffected by the life and the tenure of its members in the company. The life of a company is infinite until it is properly wound up as per the Company Act.

6. Common Seal: The Company is an artificial person and has no physical existence; hence it cannot put its signature. Thus, the Common Seal acts as an official signature of a company that validates the official documents.

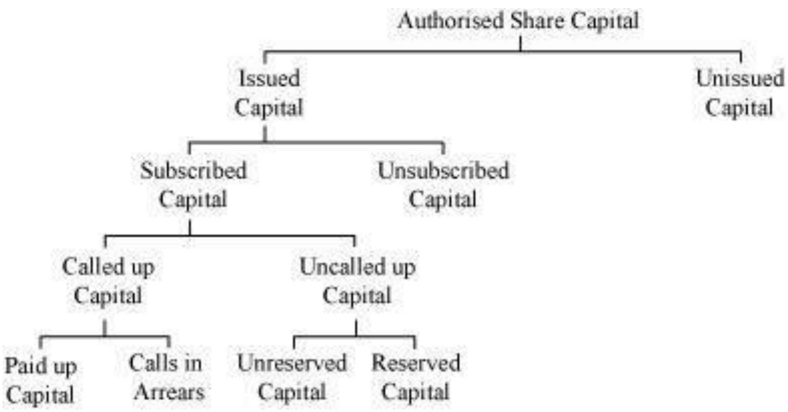
7. Transferability of Shares: The shares of public limited company is easily and freely transferable without any consent from other members. But the share of ownership of a private limited company is not transferable without the consent of the other members.

Question 2:

Explain in brief the main categories in which the share capital of a company is divided.

ANSWER:

The division of the share capital of a company into main categories is diagrammatically explained below.



1. Authorised Capital: It is an amount which is stated in the Memorandum of Association. It is the maximum amount that the company can raise by issuing shares. This maximum amount can be increased as per the procedures laid down in the Company Act.

2. Issued Capital: It is a part of authorised capital which is offered by the company to the general public for subscription. For example, if the authorised capital of a company is Rs 1,00,000 divided into Rs 10 per share, then the issued capital cannot be more than Rs 1,00,000.

3. Unissued Capital: It is a part of authorised capital that is not offered till now but can be offered to the general public in future. In the above example, if the issued capital is Rs 80,000, then the unissued capital is Rs 20,000.

4. Subscribed Capital: It is a part of issued capital that is actually subscribed by the general public. For example, if the company has issued 8,000 shares of Rs 10 per share and public has subscribed for 7,500 shares, then the subscribed share capital of the company amounts to Rs 75,000.

5. Unsubscribed Capital: It is that part of the issued capital that is not subscribed by the public. For example, in the above example, 500 shares were left unsubscribed, making an unsubscribed share capital of Rs 5,000.

6. Called up Capital: It is a part of subscribed capital that is called up by the Directors from the shareholders of a company to pay. For example, if the Directors call up Rs 6 out of Rs 10 (i.e. the face value of the share) from the shareholders of 10,000 to pay, then Rs 60,000 is regarded as called up share capital.

7. Uncalled up Capital: It is that part of subscribed capital which is not called up till now but can be called up in future as per the need of the company. For example, in the above example, Rs 4 were left uncalled from shareholders holding 10,000 shares, so Rs 40,000 is uncalled up share capital.

8. Paid up capital: It is that part of called up share capital which is actually received from the shareholders. If the entire called up money of Rs 4 on 1,000 shares has been received except from a shareholder holding 300 shares, then the paid up share capital is Rs 2,800 (Rs 4,000 − Rs 1,200). The amount of Rs 1,200 is called Call in Arrears that has been called up but is unpaid.

9. Reserved Capital: As per the Section 99 of the Company Act of 1956, a limited company may call up any portion of uncalled share capital in the event of winding up of the company to pay its creditors. This amount of uncalled share capital cannot be used for any other purpose and is reserved for paying back the creditors, that is why, such portion of share capital is called reserve capital.

Question 3:

What do you mean by the term 'share'? Discuss the type of shares, which can be issued under the Companies Act, 2013 as amended to date.

ANSWER:

The total capital of a company is divided into equal units of small denomination termed as shares. The ownership of these shares is easily transferable, from one person to other, subject to certain conditions. The person who is contributing in the capital in the form of shares is known as shareholder. The ownership of a shareholder is limited to the value of the shares held by him/her.

Types of Shares

As per the Section 44 of the Company Act of 2013, there are two types of shares- Preference Shares and Equity Shares (also known as Ordinary Shares)

i) Preference Shares: Section 43 of the Company Act,2013 defines Preference Shares to be featured by the following rights:

a. Preference Shares entitle its holder the right to receive dividend at a fixed rate or fixed amount.

b. Preference Shares entitle its holder the preferential right to receive repayment of capital invested by them before their equity counterparts at the time of winding up of the company.

ii) Equity Shares: Equity Shareholders have a voting right and control the affairs of a company.

As per Section 43 of Companies Act 2013; equity share is a share that is not a preference share. It does not possess any preferential right of payment of dividend or repayment of capital. The rate of dividend is not fixed on equity shares and varies from year to year, depending upon the amount of profit available for distribution after paying dividend to the preference shareholders.

Question 4:

Discuss the process for the allotment of shares of a company in case of over subscription.

ANSWER:

When the total number of applications received for shares exceeds the number of shares offered by the company to the public, the situation of oversubscription arises. A company can opt for any of the three alternatives to allot shares in case of oversubscription of shares.

i) Excess applications are refused and money received on excess applications is returned to the applicants.

The company can refuse excess applications and the money received on these excess applications is returned to the applicants.

Share Application A/c	Dr.
To Share Capital A/c	
To Bank A/c	

(Excess application money returned)

Example: Shares issued 10,000 @ Rs 10 per share and money received for 12,000 shares. Amount is payable Rs 2 on application, Rs 5 on allotment, Rs 3 on first and final call.

Bank A/c	Dr.	24,000	
To Share Application A/c			24,000
(Application money received for 12,000 shares)			

Share Application A/c	Dr.	24,000	
To Share Capital A/c			20,000
To Bank A/c			4,000
(Application money transferred to Share Capital Account and the excess money returned)			

ii) Pro rata Basis

The company can allot shares on pro rata basis to all the share applicants. The excess amount received in the application is adjusted on the allotment.

Share Application A/c	Dr.
To Share Capital A/c	
To Share Allotment A/c	
(Adjustment of application money on allotment)	

Example: Shares issued 10,000 @ Rs 10 per share and money received for 12,000 shares. Amount is payable Rs 2 on application, Rs 5 on allotment, Rs 3 on first and final call.

Bank A/c	Dr.	24,000

To Share Application A/c			24,000
(Application money received for 12,000 shares)			
Share Application A/c	Dr.	24,000	
To Share Capital A/c			20,000
To Share Allotment A/c			4,000
(Application money transferred to Share Capital Account and the balance amount is transferred to Share Allotment Account)			
Share Allotment A/c	Dr.	50,000	
To Share Capital A/c			50,000
(Amount due on allotment of 10,000 shares @ Rs 5 per share)			
Bank A/c	Dr.	46,000	
To Share Allotment			46,000
(Allotment money received, Rs 50,000 – Rs 4,000)			

iii) Pro rata and refund of money

In this case, the company follows a combination of both the method. It may reject some share applications and may allot some applications on the pro rata basis.

Share Application A/c	Dr.		
To Share Capital A/c			
To Share Allotment A/c			
To Bank A/c			

(Application money transferred to Share Capital
Account and the balance amount is transferred to
Share Allotment Account and the excess application
money is refund)

Example: Shares issued 10,000 @ Rs 10 per share and money received for 13,000 shares. Amount is payable Rs 2 on application, Rs 5 on allotment, Rs 3 on first and final call. If the company rejects the applications for 1,000 shares and allots the remaining on the pro rata basis.

Bank A/c	Dr.	26,000	
To Share Application A/c			26,000
(Application money received for 12,000 shares)			

Share Application A/c	Dr.	26,000	
To Share Capital A/c (10,000 × Rs 2)			20,000
To Share Allotment A/c (2,000 × Rs 2)			4,000
To Bank A/c (1,000 × Rs 2)			2,000
(Amount received on share application adjusted to Share Capital and share allotment and balance is refunded)			

Share Allotment A/c	Dr.	50,000	
To Share Capital A/c			50,000
(Amount due on share allotment of 10,000 share @ Rs 5 per share)			

Bank A/c	Dr.	46,000	
To Share Allotment A/c			46,000

(Allotment money received, Rs 50,000 – Rs 4,000)

Question 5:

What is a 'Preference Share'? Describe the different types of preference shares.

ANSWER:

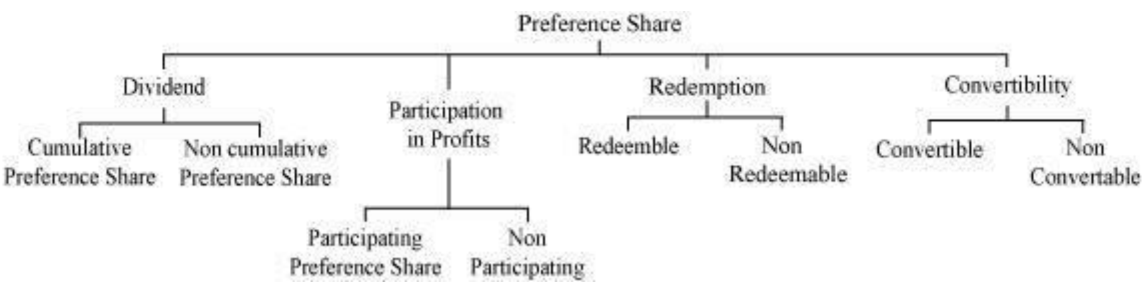
Preference Shares: Section 85 of the Company Act,1956 defines Preference Shares to be featured by the following rights:

a. Preference Shares entitle its holder the right to receive dividend at a fixed rate or fixed amount.

b. Preference Shares entitle its holder the preferential right to receive repayment of capital invested by them before their equity counterparts at the time of winding up of the company.

Types of Preference Shares

The different types of Preference Shares are diagrammatically explained below.



1. On the basis of Dividend:

a) *Cumulative Preference Shares*

When a preference shareholder has a right to recover any arrears of dividend, before any dividend is paid to the equity shareholders, then the type of Preference Shares held by the shareholder is known as Cumulative Preference Shares. All Preference Shares are cumulative unless otherwise expressly stated to be non cumulative.

b) Non Cumulative Preference Share

When a preference shareholder receives dividend only in case of profit and is not entitled any right to recover the arrears of dividend, then the type of Preference Shares held by the shareholder is known as Non Cumulative Preference Shares.

2. On the basis of Participation:

a) Participating Preference Share

When a preference shareholder enjoys the right to participate in the surplus profit (in addition to the fixed rate of dividend) that is left after the payment of dividend to the equity shareholders, the type of shares held by the shareholder is known as Participating Preference Share.

b) Non participating Preference Share

When a preference shareholder receives only a fixed rate of dividend every year and do not enjoy the additional participation in the surplus profit, then the type of shares held by the shareholder is known as Non Participating Preference Shares.

It must be noted that all Preference Shares are non-participating until and unless expressly stated.

3. On the basis of Redemption:

a) Redeemable preference share

When a preference shareholder is repaid by the company after a certain specified period in accordance with the term specified in the Section 80 of Company Act of 1956, then the type of the shares held by him/her is known as Redeemable Preference Shares.

b) Non Redeemable Preference share

These shares are not repaid by the company during its lifetime. As per the Section 80A of the Company Act of 1956, no company can issue Non Redeemable Preference Shares. It is merely a theoretical concept.

4. On the basis of Convertibility:

a) Convertible Preference Share

The shareholders holding Convertible Preference Shares have a right to convert his/her shares into equity shares.

b) Non Convertible Preference Share

Unlike Convertible Preference Shares, the shareholders holding Non Convertible Preference Shares do not enjoy the right to convert their shares into equity shares.