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Accounting for Share Capital

Preference Shares

According to Section 85 of The Companies Act, 1956, a preference share is one, which fulfils the following conditions :

- a) That it carries a preferential right to dividend to be paid either as a fixed amount payable to preference shareholders or an amount calculated by a fixed rate of the nominal value of each share before any dividend is paid to the equity shareholders.
- b) That with respect to capital it carries or will carry, on the winding-up of the company, the preferential right to the repayment of capital before anything is paid to equity shareholders. However, notwithstanding the above two conditions, a holder of the preference share may have a right to participate fully or to a limited extent in the surpluses of the company as specified in the Memorandum or Articles of the company. Thus, the preference shares can be participating and non-participating. Similarly, these shares can be cumulative or non-cumulative, and redeemable or irredeemable.

Equity Shares

According to Section 85 of The Companies Act, 1956, an equity share is a share which is not a preference share. In other words, shares which do not enjoy any preferential right in the payment of dividend or repayment of capital, are termed as equity shares. The equity shareholders are entitled to share the distributable profits of the company after satisfying the dividend rights of the preference share holders. The dividend on equity shares is not fixed and it may vary from year to year depending upon the amount of profits available for distribution. The equity share capital may be (i) with voting rights; or (ii) with differential rights as to voting, dividend or otherwise in accordance with such rules and subject to such conditions as may be prescribed.

Issue of Shares

A salient characteristic of the capital of a company is that the amount on its shares can be gradually collected in easy instalments spread over a period of time depending upon its growing financial requirement. The first instalment is collected along with application and is thus, known as application money, the second on allotment (termed as allotment money), and the remaining

instalment are termed as first call, second call and so on. The word final is suffixed to the last instalment. However, this in no way prevents a company from calling the full amount on shares right at the time of application. The important steps in the procedure of share issue are :

- **Issue of Prospectus:** The company first issues the prospectus to the public. Prospectus is an invitation to the public that a new company has come into existence and it needs funds for doing business. It contains complete information about the company and the manner in which the money is to be collected from the prospective investors.
- **Receipt of Applications:** When prospectus is issued to the public, prospective investors intending to subscribe the share capital of the company would make an application along with the application money and deposit the same with a scheduled bank as specified in the prospectus. The company has to get minimum subscription (Refer Box 1) within 120 days from the date of the issue of the prospectus. If the company fails to receive the same within the said period, the company cannot proceed for the allotment of shares and application money should be returned within 130 days of the date of issue of prospectus.
- **Allotment of Shares:** If minimum subscription has been received, the company may proceed for the allotment of shares after fulfilling certain other legal formalities. Letters of allotment are sent to those whom the shares have been allotted, and letters of regret to those to whom no

Box 1

Minimum Subscription

It means the minimum amount that, in the opinion of directors, must be raised to meet the needs of business operations of the company relating to:

- the price of any property purchased, or to be purchased, which has to be met wholly or partly out of the proceeds of issue;
- preliminary expenses payable by the company and any commission payable in connection with the issue of shares;
- the repayment of any money borrowed by the company for the above two matters;
- working capital; and
- any other expenditure required for the usual conduct of business operations.

It is to be noted that 'minimum subscription' of capital cannot be less than 90% of the issued amount according to SEBI (Disclosure and Investor Protection) Guidelines, 2000 [6.3.8.1 and 6.3.8.2]. If this condition is not satisfied, the company shall forthwith refund the entire subscription amount received. If a delay occurs beyond 8 days from the date of closure of subscription list, the company shall be liable to pay the amount with interest at the rate of 15% [Section 73(2)].

allotment has been more. When allotment is made, it results in a valid contract between the company and the applicants who now became the shareholders of the company. Shares of a company are issued either at par, at a premium or at a discount. Shares are said to have been issued at par when their issue price is exactly equal to their nominal value according to the terms and conditions of issue. When the shares of a company are issued more than its nominal value (face value), the excess amount is called premium and the issue is said to have been made at a premium. When the shares are issued at a price less than the face value of the share, it is known as shares issued at a discount. Irrespective of the fact that shares are issued at par, premium or discount, the share capital of a company as stated earlier, is collected in instalments to be paid at different stages.