1. Details of Module and its structure

Module Detail	
Subject Name	Accountancy
Course Name	Accountancy 04 (Class XII, Semester – 2)
Module Name/Title	Accounting for Share Capital – An Introduction – Part 1
Module Id	leac_20101
Pre-requisites	Knowledge about Journal entries and Ledgers.
Objectives	After going through this lesson, the learners will be able to: • Define a Company and state it's features • Explain different types of companies • Describe the types of shares issued by a company • Make accounting treatment of issue of shares for cas lump sum
Keywords	Types of Companies, Shares, Equity shares, Preference Shares, Par, Premium, Minimum Subscription

2. Development Team

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1.1 Meaning of a Company

A company form of organisation is the third stage in the evolution of forms of organisation. It's capital is contributed by a large number of persons called shareholders who are the real owners of the company.

But neither it is possible for all of them to participate in the management of the company nor considered desirable. Therefore, they elect a Board of Directors as their representative to manage the affairs of the company. In fact, all the affairs of the company are governed by the provisions of the Companies Act, 2013.

A company means a company incorporated or registered under the Companies Act, 2013 or under any other earlier Companies Acts.

According to Chief Justice Marshal, "a company is a person, artificial, invisible, intangible and existing only in the eyes of law. Being a mere creation of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence".

Image 1.

1.2 Features of a Company

A company may be viewed as an association of person who contribute money or money's worth to a common inventory and use it for a common purpose. It is an artificial person having corporate legal entity distinct from its members (shareholders)and has a common seal used for its signature.

Thus, it has certain special features which distinguish it from the other forms of organisation. These are as follows:

- **Body Corporate**: A company is formed according to the provisions of Law enforced from time to time. Generally, in India, the companies are formed and registered under Companies Law except in the case of Banking and Insurance companies for which a separate Law is provided for.
- **Separate Legal Entity**: A company has a separate legal entity which is distinct and separate from its members. It can hold and deal with any type of property. It can enter into contracts and even open a bank account in its own name.
- **Limited Liability**: The liability of the members of the company is limited to the extent of unpaid amount of the shares held by them. In the case of the companies limited by guarantee, the liability of its members is limited to the extent of the guarantee given by them in the event of the company being wound up.
- **Perpetual Succession**: The company being an artificial person created by law continues to exist irrespective of the changes in its membership. A company can be terminated only through law. The death or insanity or insolvency of any member of the company in no way affects the existence of the company. Members may come and go but the company continues.
- **Common Seal**: The company being an artificial person, cannot sign its name by itself. Therefore, every company is required to have its own seal which acts as official signatures of the company. Any document which does not carry the common seal of the company is not binding on the company.
- **Transferability of Shares**: The shares of a public limited company are freely transferable. The permission of the company or the consent of any member of the company is not necessary for the transfer of shares. But
- the Articles of the company can prescribe the manner in which the transfer of shares will be made.

- **May Sue or be Sued**: A company being a legal person can enter into contracts and can enforce the contractual rights against others. It can sue and be sued in its name if there is a breach of contract by the company.

1.3 Kinds of Companies

Companies can be classified either on the basis of the liability of its members or on the basis of the number of members. On the basis of liability of its members the companies can be classified into the following three categories:

(i) Companies Limited by Shares: In this case, the liability of its members is limited to the extent of the nominal value of shares held by them. If a member has paid the full amount of the shares, there is no liability on his part whatsoever may be the debts of the company. He need not pay a single paise from his private property. However, if there is any liability involved, it can be enforced during the existence of the company as well as during the winding up.

(ii) Companies Limited by Guarantee: In this case, the liability of its members is limited to the amount they undertake to contribute in the event of the company being wound up. Thus, the liability of the members will arise only in the event of its winding up.

(iii) Unlimited Companies: When there is no limit on the liability of its members, the company is called an unlimited company. When the company's property is not sufficient to pay off its debts, the private

property of its members can be used for the purpose. In other words, the creditors can claim their dues from its members. Such companies are not found in India even though permitted by the Companies Act.

On the basis of the number of members, companies can be divided into three categories as follows:

(i) Public Company: A public company means a company which

(a) is not a private company;

(b) is a company which is not a subsidiary of a private company.

- Indian Oil Corporation Ltd.
- Bharat Petroleum Corporation Ltd.
- State Bank of India
- Hindustan Petroleum Corporation Ltd.

(ii) Private Company: A private company is one which by its articles:

(a) Restricts the right to transfer its shares;

(b) A private company must have at least 2 persons, except in case of one-person company;

(c) Limits the number of its members to 200 (excluding its employees);

Image 2

(iii) One Person Company (OPC): Sec. 2 (62) of the companies Act, 2013, defines OPC as a "company which has only one person as a member".

Rule 3 of the Companies (Incorporation) Rules, 2014 provides that:

a) Only a natural person being an Indian citizen and resident in India can form one-person company,
b) It cannot carry out non-banking financial investment activities.
c) Its paid up share capital is not more than Rs. 50 Lakhs
d) Its average annual turnover of three years does not exceed Rs. 2 Crores.

1.4 Share Capital of a Company

A company, being an artificial person, cannot generate its own capital which has necessarily to be collected from several persons. These persons are known as shareholders and the amount contributed by them is called share capital. Since the number of shareholders is very large, a separate capital account cannot be opened for each one of them. Hence, innumerable streams of capital contribution merge their identities in a common capital account called as 'Share Capital Account'.

Categories of Share Capital

From accounting point of view, the share capital of the company can be classified as follows:

• **Authorised Capital:** Authorised capital is the amount of share capital which a company is authorised to issue by its Memorandum of Association. The company cannot raise more than the amount of capital
as specified in the Memorandum of Association.
It is also called Nominal or Registered capital. The authorised capital can be increased or decreased as per the procedure laid down in the Companies Act.
It should be noted that the company need not issue the entire authorised capital for public subscription at a time. Depending upon its requirement, it may issue share capital but in any case, it should not be more than the amount of authorised capital.

• **Issued Capital:** It is that part of the authorised capital which is actually issued to the public for subscription including the shares allotted to vendors and the signatories to the company's memorandum. The authorised capital which is not offered for public subscription is known as 'unissued capital'. Unissued capital may be offered for public subscription at a later date.

• **Subscribed Capital:** It is that part of the issued capital which has been actually subscribed by the public. When the shares offered for public subscription are subscribed fully by the public the issued capital and subscribed capital would be the same. It may be noted that ultimately, the subscribed capital and issued capital are the same because if the number of share, subscribed is less than what is offered, the company allot only the number of shares for which subscription has been received. In case it is higher than what is offered, the allotment will be equal to the offer. In other words, the fact of over subscription is not reflected in the books.

• **Called up Capital:** It is that part of the subscribed capital which has been called up on the shares. The company may decide to call the entire amount or part of the face value of the shares. For example, if the face
value (also called nominal value) of a share allotted is Rs. 10 and the company has called up only Rs. 7 per share, in that scenario, the called up capital is Rs. 7 per share. The remaining Rs. 3 may be collected from
its shareholders as and when needed.

• **Paid up Capital:** It is that portion of the called up capital which has been actually received from the shareholders. When the shareholders have paid all the call amount, the called up capital is the same to the paid up capital. If any of the shareholders has not paid amount on calls, such an amount may be called as ‘calls in arrears’. Therefore, paid up capital is equal to the called-up capital minus call in arrears.

• **Uncalled Capital:** That portion of the subscribed capital which has not yet been called up. As stated earlier, the company may collect this amount any time when it needs further funds.

• **Reserve Capital:** A company may reserve a portion of its uncalled capital to be called only in the event of winding up of the company. Such uncalled amount is called ‘Reserve Capital’ of the company. It is available only for the creditors on winding up of the company.

1.5 Nature and Classes of Shares

Shares, refer to the units into which the total share capital of a company is divided. Thus, a share is a fractional part of the share capital and forms the basis of ownership interest in a company. The persons who contribute money through shares are called shareholders.

The amount of authorised capital, together with the number of shares in which it is divided, is stated in the Memorandum of Association but the classes of shares in which the company’s capital is to be divided, along with their respective rights and obligations, are prescribed by the Articles of Association of the company.

As per The Companies Act, a company can issue two types of shares:

(1) Preference Shares, and

(2) Equity Shares (also called ordinary shares).

1.5.1 Preference Shares

According to Section 43 of The Companies Act, 2013, 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.

1.5.2 Equity Shares

According to Section 43 of The Companies Act, 2013, 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/ordinary shares.

The equity shareholders are entitled to share the distributable profits of the company after satisfying the dividend rights of the preference shareholders. 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.

1.6 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.
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 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. The company has to get minimum subscription 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 allotment has been made. When allotment is made, it results in a valid contract between the company and the applicants who now became the shareholders of the company.

Minimum Subscription

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)].
Shares of a company are issued either at par or at a premium. Shares are to be 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.

1.7 Accounting Treatment

A company may issue shares either for

(i) Cash and /or

(ii) For consideration other than cash.

(i) For Cash the issue price may be payable either:

Type (a) For cash in lumpsum.

Type (b) In instalments.

Type (a) Journal entries in case of issue of shares in lump sum are:

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Bank A/c **Dr.** **To Shares Application and Allotment A/c** (Being application and allotment money received on …shares @Rs…. each.)			
	Shares Application and Allotment A/c **Dr.** **To Share Capital A/c** (Being Transfer of application and allotment money to Share Capital Account for amount due on allotment of …. Share @ Rs…. per share).			

Example1. External Ltd. issued 10,000 Equity Shares of Rs.100 each at par payable on application only. Applications were received for all the shares and the shares were allotted. Pass journal entries in the books of External Ltd.

JOURNAL

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Bank A/c **Dr.** **To Shares Application and Allotment A/c** (Being application and allotment money received on 10,000 shares @Rs.100 each.)		10,00,000	10,00,000
	Shares Application and Allotment A/c **Dr.** **To Share Capital A/c.** (Being Transfer of application and allotment money to Share Capital Account for amount due on allotment of 10,000 Share @ Rs.100 per share).		10,00,000	10,00,000