Chapter -I

Joint Stock Company

The simplest way to describe a joint stock company is that it is a business organization is owned jointly by all its shareholders. All the shareholders own a certain amount of stock in the company, which is represented by their shares.

Professor Haney defines it as "a voluntary association of persons9. Lol for profit, having the capital divided into some transferable shares, and the ownership of such shares is the condition of membership of the company."

Issue of Shares

The Companies Act 2013 define shares, 'a share in the share capital of a company and includes stock'. Shares is a type of security and in layman's definition it "one of the equal partsinto which a company's capital is divided, entitling the holder to a proportion of the profits"

Issue of Shares is the process in which companies allot new shares to shareholders. Shareholders can be either individuals or corporates. The company follows the rules prescribed by Companies Act 2013 while issuing the shares. Issue of Prospectus, Receiving Applications, Allotment of Shares are three basic steps of the procedure of issuing the shares. The process of creating new shares is known as Allocation or allotment. Let us see the two types of shares of a company and the procedure for issue of shares that a company must follow.

Definition: A share is that smallest part, into which the overall capital of the company is divided. Issue of shares is a process through which the company allocates fresh shares to the new or existing shareholders. The issue of shares is made to both individuals, institutions or body corporates.

Types of capital market

Primary Market

Definition: Primary Market is a form of the capital market wherein new securities are sold by the companies for the very first time to the investors, to raise funds and that is why it is also acknowledged as New Issues Market (NIM).

The process of selling the new securities, in the primary market is called underwriting, which

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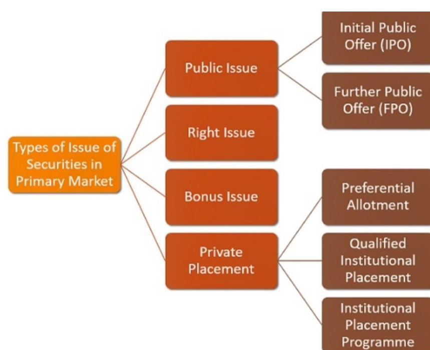
is performed by a group called as underwriters or security dealers.

The underwriting service is offered by financial institutions such as investment banks, insurance companies, etc. The underwriting companies guarantee payment if there is any loss and accepts the risk which occurs as a consequence of such guarantee.

The main function of the primary market is to mobilize the investible money from the savers to the companies or young entrepreneurs who seek funds to set up new businesses or expand the existing venture, by issuing securities.

Types of Issue of Securities in Primary Market

There are several types of issue of securities in the primary market which are discussed as under:Types of Issue of Securities in Primary Market.



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1.**Public Issue:** Public issue is when a company enters the market, to raise money from all kinds of investors. The securities offered for sale to the new investors, so as to become a shareholder in the issuer company, is called Public Issue.

a)Initial Public Offer: Initial Public Offer or IPO, as the name suggests, is the fresh issue of equity shares or convertible securities, or exiting shares or convertible securities by an unlisted company for the very first time i.e. the shares are not previously traded or offered for sale to the general public. This is often followed by listing and trading of the company's securities on the stock exchange.

b)Further Public Offer: Otherwise called as Follow on offer or FPO, refers to the fresh issue of securities to the general public made by a company already listed on the stock exchange, so as to raise additional funds.

2.Right Issue: Right Issue is an offer to the company's existing shareholders to buy further new shares of the company at a discount, as a part of the dividend of pre-emption rights. It helps the firms to raise additional funds, without going to the public. It invites its existing shareholders to subscribe for its fresh issue in the proportion of their shareholdings on the record date in the concern.

3.Bonus Issue: When a company issues fully paid additional shares to the company's existing shareholders for free. The issue is made from the company's free reserves or securities premium account, in a specific proportion to the shareholding on a specific record date.

4.Private Placement: When a company's stocks or bonds are sold directly to a selected group of people, say 50 to 200 people, called as private investors or institutions, instead of offering the same to the general public is called private placement. Hence, in case of a private placement there are only a handful of subscribers to the company's shares. However, it is capable of raising money, more quickly as compared to offering shares for sale in the open market.

a)Preferential Allotment: Preferential Issue is one in which the specified securities are allotted by a listed company to a selected group on a preferential basis. The issuing company needs to adhere to the provisions relating to pricing, lock-in period, disclosures, and so on.

b)Qualified Institutional Placement: When a company, which is already listed in a stock exchange issues shares or debentures (fully or partly convertible) or any other kind of security not including warrants, which are convertible in nature, to Qualified Institutional Buyer (QIB), is called as Qualified Institutional Placement (QIP).

c)Institutional Placement Programme: Institution Placement Programme or IPP implies a further public issue of equity shares by a listed firm or group of promoters of a listed company, wherein the offer and allocation are made to Qualified Institutional Buyers only.
Note: Qualified Institutional Buyers includes mutual fund, venture capital fund, scheduled commercial bank, state industrial development corporation, national investment fund, insurance fund, provident fund, pension fund, etc.

In a nutshell, Primary Market is a market where new long term securities are created and issued to the public for sale through IPO, that helps the company, public sector institutions and governments to raise funds. These funds are injected by the company in new projects and also to expand or upgrade the existing projects.

SECONDARY MARKET

The secondary market is where securities are traded after the company has sold its offering on the primary market. It is also referred to as the stock market. The New York Stock Exchange (NYSE), London Stock Exchange, and Nasdaq are secondary markets.

Small investors have a much better chance of trading securities on the secondary market since they are excluded from IPOs. Anyone can purchase securities on the secondary market as long as they are willing to pay the asking price per share.

A broker typically purchases the securities on behalf of an investor in the secondary market. Unlike the primary market, where prices are set before an IPO takes place, prices on the secondary market fluctuate with demand. Investors will also have to pay a commission to the broker for carrying out the trade.

The volume of securities traded varies from day to day, as supply and demand for the security fluctuates. This also has a big effect on the security's price.

Because the initial offering is complete, the issuing company is no longer a party to any sale between two investors, except in the case of a company stock buyback. For example, after

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Apple's Dec. 12, 1980, IPO on the primary market, individual investors have been able to purchase Apple stock on the secondary market. Because Apple is no longer involved in the issue of its stock, investors will, essentially, deal with one another when they trade shares in the company.

The secondary market is further divided into two kinds of market:

(i**) Auction Market**

An auction market is a place where buyers and sellers convene at a place and announce the rate at which they are willing to sell or buy securities. They offer either the 'bid' or 'ask' prices, publicly. Since all buyers and sellers are convening at the same place, there is no need for investors to seek out profitable options. Everything is announced publicly and interested investors can make their choice easily.

(ii) Dealer Market

In a dealer market, none of the parties convene at a common location. Instead, buying and selling of securities happen through electronic networks which usually fax machines, telephones or custom order-matching machines.

Interested sellers deliver their offer through these mediums, which are then relayed over to the buyers through the medium of dealers. The dealers possess an inventory of securities and earn their profit through the selling. A lot of dealers operate within this market and therefore, a competition exists between them to deliver the best offer to their investors. This makes them deliver the best price to the investors. An example of a dealer market is the NASDAQ.(National Association of Securities Dealers Automated Quotations exchange)

The secondary markets are important for price discovery. The market operations are carried out on stock exchanges.

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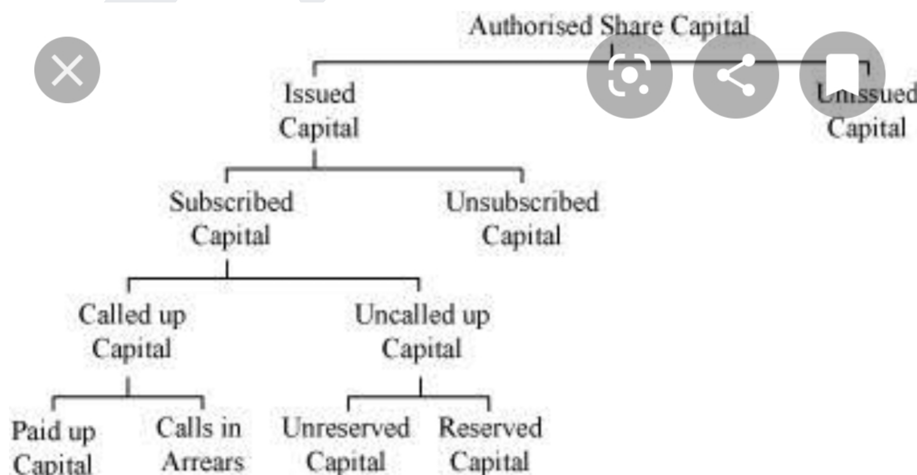
Kinds of share capital



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The share capital of company may be of the following types:

1. Registered, Authorised or Nominal Capital:

The Memorandum of Association of every company has to specify the amount of capital with which it wants to be registered. The capital so stated is called Registered, Authorized or Nominal Capital. The Registered Capital is the maximum amount of share capital which a company can raise by way of public subscription.

2. Issued Capital:

The company may not issue the entire authorised capital at once. It goes on raising the capital as and when the need for additional fund is felt. So, issued capital is that part of Authorised/Registered or Nominal Capital which is offered to the public for subscription in the form of shares.

3. Unissued Capital:

The balance of nominal capital remaining to be issued is called Unissued Capital.

4. Subscribed Capital:

It is that part of "issued capital" for which applications are received from the public. The subscribed capital is allotted to the respective subscribers as per resolution passed by the directors of the company.

5. Called up Capital:

It is that part of subscribed capital which has been called up by the company. A company does not call at once the full amount on each of the shares it has allotted and therefore, calls up only such amount as it needs.

6. Uncalled up Capital:

It is the uncalled portion of the allotted capital and represents contingent liability of the shareholders on the shares.

7. Paid up Capital:

It is that part of called up capital against which payment has been received from the members on their respective shares in response to the calls made by the company.

8. Reserve Capital or Reserve Liabilities:

By Reserve Capital we mean that amount which is not callable by the company except in the event of the company being wound up. The company cannot demand the payment of money on the shares to that extent during its life time. Reserve capital may be created by means of a special resolution passed by the company in its General Meeting by

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three-fourths majority of those voting on it.

When once the Reserve Capital has been so created the company cannot alter its Articles of Association so as to make the reserve liability available at any time. The Reserve Capital cannot be charged as security for loans by the directors. It cannot be turned into ordinary capital without the order of the court. It cannot be cancelled at the time of reduction of capital.

9. Fixed Capital:

The fixed capital of a company is what the company retains in the shape of fixed assets such as land and buildings, plant and machinery, furniture, etc.

10. Circulating Capital:

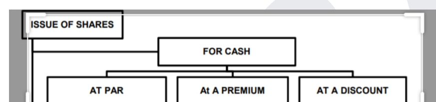
The circulating capital is a part of subscribed capital which is circulated in business in the form of using goods or other assets such as book debts, bill receivables, cash, bank balance, etc.

Classes of Share Capital:

In a company the capital is split into small denominations which are known as shares. Shares can be easily transferred from one person to another and this transfer is bound by certain terms and conditions. Shareholder is that person who is contributing capital in form of shares. Ownership is limited to the value of shares possessed by the shareholder. There are two types of shares:

1. Preference share capital,

2. Equity share capital.



1. Preference Share Capital:

Section 43 of the Company Act, 2013. It means that part of the capital of the company which:

(a) Carries a preferential right as to payment of dividend at fixed rate during the life time of the company.

(b) Carries, on the winding up of the company, a preferential right to be repaid the amount of the capital paid up.

The different types are:

1. Cumulative Preference Share: When arrears of a dividend are cumulative and such

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arrears are paid before paying any dividend to equity shareholders, such shares are known as cumulative shares.

2. Non-Cumulative Preference Share: Shares where the dividend is paid from the net profits earned each year are known as non-cumulative preference share. If the company does not earn profits in any of the year, the arrears of dividend cannot be claimed.

3. Participating preference share: In these type of shares the preference shareholder has the luxury of participating in the surplus profit (i.e. apart from fixed rate of dividend) which is remaining after paying equity shareholders.

4. Non-participating Preference Share: The condition in which the shareholder is entitled only to a fix dividend pay-out and no share in surplus profits is known as non-participating preference share.

5. Convertible Preference Share: Type of shares which can be converted to equity shares within a period of time.

6. Non-Convertible Preference Share: Type of shares which do not have the right to convert into equity shares.

7. Redeemable Preference Shares: Those shares that can be repaid to the shareholders after a certain period as per provisions mentioned in Companies Act, 1956

8. Irredeemable Preference Shares
Irredeemable preference shares are a perpetual liability, which cannot be redeemed during the lifetime of the company.According to the Companies Amendment Act, 1988, no company can issue any preference share which is irredeemable or redeemable after 20 years from the date of the issue.

9. Guaranteed Preference Shares: These shares have the provision of getting fixed dividend, even if the company is making no profits

2. Equity Share Capital:

Equity shareholders manage the affairs of the company and also have a voting right. These type of share do not possess any preferential right for dividend payment or capital repayment. The dividend rate is not fixed and varies year on year which is dependent on available profit left after distributing to preference shareholders.

1. Describe the provision of law relating to 'Calls-in-Arrears' and 'Calls-in-Advance'.

When an investor (shareholder) fails to pay all the instalments for the allotted shares in the due time, the company expects the investor to pay the amount on subsequent calls or

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stages. The amount of money that is paid at later stages is called as Call-in-Arrears. The company is authorized by its Article of Association for charging a interest at a specified rate on the call in arrears amount from due date till the date of payment. If Article of Association does not mention or is silent about such a case, then a 5% charge is levied.

The amount is deducted from called up share capital on the liabilities side of Balance Sheet. If the due amount is not paid the shares can forfeited with proper notice to shareholders.

When the shareholder pays the whole amount before the share payment date becomes due i.e. before the share issuing company makes a call for it. It is known as Calls-in-advance. In case of advance payment the company has provision in their article of association to pay interest to shareholders from date of payment till date of call. If the article of association is silent in this regard, then a default 6% interest is provided.

2.**When can shares be forfeited?**

A shareholder has to pay allotment money for holding the shares and has to pay the calls which are part of share allotment. When a shareholder fails to do so, a 14 days' notice is served to the shareholder, if the shareholder does not pay in these 14 days, the shares will be forfeited.
Table A of the Company Act, 2013 deals with Memorandum of Association for a company limited by shares. It has the following procedure for forfeiting of shares:

1. Notice sent to shareholder for making payment related to call arrears and interest on outstanding call money within a period of 14 days of receipt of the notice.
2. On non-payment of dues, the company can forfeit the share by passing a resolution
3. Forfeit notice resolution sent to the shareholder and a statement published in daily newspaper
4. Name of shareholder removed from registered shareholders list.

Accounting Treatment for Forfeiture of Shares:

i) Forfeiture of Shares that were issued at Par

Share Capital A/c	Dr.	(amount called up)
To Share Allotment A/c		(not received)
To Share Calls A/c		(not received)
To Share Forfeiture A/c		(amount received)
(Shares forfeited)		

ii) Forfeiture of Shares that were issued at Premium
a) If premium is received, then the premium is not shown.

Share Capital A/c	Dr.	(amount called up)
To Share Allotment A/c		(not received)
To Share Calls A/c		(not received)
To Share forfeiture A/c		(amount received)
(Share forfeited)		

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iii) Forfeiture of Shares that were issued at Discount

Share Capital A/c	Dr.	(amount called up, with discount)
To Discount on Issue of Shares A/c		(amount of discount)
To Share Allotment A/c		(not received)
To Share Calls A/c		(not received)
To Share Forfeiture A/c		(amount received)
(Share forfeited)		

3**. What are the uses of securities premium?**

Securities premium can be used for these activities:

1. Issuing fully paid up bonus shares to existing shareholders.

2. Writing off expense of issue of shares and debentures, such as discount given on issue of shares.

3. Writing off preliminary expenses

4. Buying back shares

5. For paying premium payable on redemption of debentures.

4**.**State clearly the conditions under which a company can issue shares at a discount.

Issue at Discount

Under the following conditions a company can issue shares at a discount:

1. The shares issued must belong to a class of shares that are already issued.

2. Shares can be issued at discount after a minimum time frame of 1 year from the date business has started

3. The issue of shares at discount is authorised by a resolution that is passed by the company in general meeting and approved by Company law board.

4. Shares can be issued at discount within two months of obtaining sanction company law board.

5. Maximum rate of discount must not cross 10% of face value or as decided by company law board.

5. Explain the terms ‘Over-subscription’ and ‘Under-subscription’. How are they dealt with in accounting records?

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Over-subscription: It is referred to as the situation where the total number of applications received for share allotment exceeds the available number of shares that are issued by the company for public.

Under-subscription: This is the situation when the number of applications for share allotment are less than the number of shares issued by the company. A 90% subscription of the shares is called as Mini Subscription. If 90% subscription does not take place, the company should refund the money back to applicants.

Pro Rata Allotment

In the case of over-subscription, it is not possible for the company to allot shares to every applicant in the number that he desires. The company needs to allot the shares in a proper manner. The company has the following three alternatives:

Accept some applications in full and reject the others totally.
Make Pro-Rata Allotment.
Adopt a combination of the above two.
Usually, the company does not consider the multiple applications from the same person. Also, generally a company takes the third course of action. The problem of accounting of over-subscription is usually resolved at the time of allotment of shares.

Pro-rata allotment refers to the allotment of shares in proportion of the shares applied for. When a company makes pro-rata allotment, it adjusts the excess money received at the time of application firstly, towards the allotment and then towards calls.

It refunds any surplus left after adjusting the amount towards allotment and calls to the applicants. The company advertises the allotment procedure in the leading newspapers.

For example, AB Ltd. offers 10000 shares to the public. The issue was heavily oversubscribed. It receives applications for 20000 shares.

When the company decides to allot the shares at pro-rata basis, then it has to allot 10000 shares to the applicants of 20000 shares. Thus, the ratio will be 20000:10000 i.e. 2:1. Hence, an applicant for 2 shares will receive 1 share. This is Pro-rata allotment.

II.Redeemable Preference Shares:

Those shares that can be repaid to the shareholders after a certain period as per provisions mentioned in Companies Act, 1956

Conditions for redemption of preference shares

Before going to redeem the preference shares as per section 80 of the Companies Act, 1956, a company should have to follow the conditions:

i) There must be a provision in the Articles of Association regarding the redemption of

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preference shares.

ii) The redeemable preference shares must be fully paid up. If there is any partly paid share, it should be converted in to fully paid shares before redemption.

iii) The redeemable preference shareholders should be paid out of undistributed profit/ distributable profit or out of fresh issue of shares for the purpose of redemption.

iv) If the shares are redeemed at a premium, it should be provided out of securities premium or profit and loss account or general reserve account.

v) The proceeds from fresh issue of debentures cannot be utilized for redemption.

vi) The amount of capital reserve cannot be used for redemption of preference shares.

vii) If the shares are redeemed out of undistributed profit , the nominal value of share capital, so redeemed should be transferred to Capital Redemption Reserve Account. This is also known as capitalization profit.

So, you may understand that a company must follow the above conditions for the purpose of redemption of its redeemable preference shares.

Capital Redemption Reserve (CRR) Account

The preference shares are redeemed out of accumulated profit, it will be necessary to transfer an amount equal to the amount repaid on the redemption to Capital Redemption Reserve Account. If the company issues any fresh shares for redemption purpose, the transferred amount will be the difference between nominal value of shares redeemed and the nominal value of shares issued (i.e. amount transferred to CRR = Nominal value of shares redeemed – Nominal value of shares issued). The capital redemption reserve account can be used for issuing fully paid bonus shares.

The importance of creation of capital redemption reserve account are to

a) protect the interest of creditors

b)maintain working capital. Redemption of preference shares involves repayment of capital before paying creditors of the company. It may affect the interest of creditors. In addition to that the working capital of the company will be depleted as a result of outflow of cash due to redemption. The amount is capitalized by creating the capital redemption reserve account. As a result this amount will not be available for distribution of dividend. It help protect the interest of creditors and on the other hand it replenishes working capital.

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