Date: 01 July 2020

VIRTUAL COACHING CLASSES
ORGANISED BY BOS, ICAI

FOUNDATION LEVEL
PAPER 1: PRINCIPLES AND PRATICE OF ACCOUNTING

Faculty: CA VS Hiranmai

CHAPTER 10-Company Accounts- Unit 2

- This unit deals with the issue, forfeiture and reissue of the shares.
- Where in case of the sole proprietorship, the money invested by the proprietor into the business is termed as capital. Same is with the case of the partners bringing money into the business carried on as partnership firm.
- Incase of company, the money is raised through various sources- internal and external. Examples of the external sources are loans from banks, financial institutions, issue of debt securities.
- When talking of the internal sources of raising capital is by the **issue of shares.** Under this method the capital is termed as share capital. The shares are small divisible units which are distributed to its holders called as the **shareholders**. The liability of the shareholders is only to the extent of the unpaid value of the shares held by them.

CHAPTER 10-Company Accounts- Unit 2

- For ex- A company wants Rs. 1,00,000 as capital for running the business- it will invite public or private people (depending on the co)- to give money (**subscribe**). Since for the ease of carrying out the business, the entire amount is divided into small units- called as **shares.**

- The **face value** of the shares is fixed firstly by the company, which means that each share will have same value. Based on the face value of the shares- we can arrive at the **total number of shares** to be issued.

- Based on the face value- the number of shares to be issued are- **10,000 shares** (1,00,000/10)

- This face value is mentioned in the share certificate given to the shareholders upon becoming the member of the company.

- The liability of the shareholders is limited to the value of the unpaid value of the shares (the value is determined by various process such as book building- which will be explained in the intermediate level)

CHAPTER 10-Company Accounts- Unit 2

- **Share capital of every company is divided in to the following types**-
  - **Authorised share capital**- This is the maximum limit of amount that can be raised by a company as capital from the issue of shares. There can be no money raised beyond this and it is mentioned in the prospectus (invitation to offer) to the public. It is also mentioned in the capital clause of the MOA. It is shown at the face value
  - **Issued share capital**- Out of the total authorized- that amount of shares which are issued to the public for the purpose of raising money is called issued. It deals with the no. of shares issued * face value of the shares.
  - **Subscribed share capital-** Out f the total shares issued above, the no. of shares taken up by the public, meaning the amount paid on the shares is termed as the subscribed share capital. This should meet the criteria of the ***minimum subscription- which means that 90% of the issued share capital shall be subscribed, if not the amount shall be returned to remaining applicants.***

CHAPTER 10-Company Accounts- Unit 2

- **Share capital of every company is divided in to the following types**-
  - **Called up share capital-** This is with regard to the amount called from the members of the company. AS per the SEBI guidelines it is necessary that the total face value of Rs.10 (generally) should be collected in installments. Hence, whenever each instalment money is called- it is referred to as called up capital.
  - **Paid up share capital-** This refers to the amount of calls paid by the members* no. of shares held by them. Where the calls are not being paid by the members it is taken into a separate account called as **calls in arrears**- which is deducted from the called up capital. **Calls in advance** refers to the amount received in advance for the next call with the current call. This is shown as **liability until the actual call is made**.
  - **Reserve capital-** There is a part of the total of the authorized capital which is not called except in case of winding up of the company- which is called as ***reserve capital. This is not shown in the balance sheet.*** This is called only in case of winding up of company to meet its expenses. This is different from the capital reserve.

CHAPTER 10-Company Accounts- Unit 2

- **Formulas for arriving at capital-**
- **Authorized capital**= Issued capital + Unissued (reserve capital) capital
- **Paid up capital**= Called up capital- Calls in arrears + Calls in advance
- **Subscribed capital-** It can be equal or different in 2 cases to Issued capital. Where members pay **more than the issued capital** it is called **over subscription**. When they pay **less than the issued**- it is called **under subscription**
- **Types of shares-**
- **Preference shares-** they have preference over the Equity shares in two things-
  - In the payment of dividend
  - In the prepayment of the capital at he time of winding up
  - But they do not have any voting rights- they are not the owners of the company

CHAPTER 10-Company Accounts- Unit 2

- **Types of shares-**
- **Types of Preference shares-**
  - **Cumulative preference shares-** The return payable to the shareholders is called as dividend and it is appropriation of profits- meaning paid only when there is a profit. Where in one year the co incurs losses- t cannot pay the dividend. If in the next year the co earns profits, and the preference shares are cumulative then the shareholders will be entitled to profits of the previous year as well as the current year also. **Non cumulative preference shareholders** will be entitled only to the current year dividend. Arrears are not payable.
  - **Participating preference shares**- The dividend is first paid to the preference shares, after the payment of dividend to the equity shareholders, if there is any profit left, theses shareholders will participate in remaining profit also. In case of **non participating**, they leave once after their dividend is paid.

CHAPTER 10-Company Accounts- Unit 2

- **Types of shares-**
- **Types of Preference shares-**
  - **Redeemable preference shares-** Redemption means to repay back the amount taken in the form of preference hare capital. Where the terms of redemption are specifically given at the time of issue, they are referred to as the redeemable shares. Irredeemable shares refer to those shares which are not repaid except in case of winding up of company. But in India the maximum years is confined to 20 years.
  - **Convertible preference shares-** Refer to those shares which can be converted into equity shares as per the conditions and terms at the time of issue. Those shares which do not carry a condition for conversion into equity shares are called as **non convertible preference** shares.
  - Unless otherwise mentioned- preference shares are non cumulative, non participating, nonconvertible and redeemable in nature.

CHAPTER 10-Company Accounts- Unit 2

- **Types of shares-**
- **Equity shares-** Those shares which are not preference shares are equity. These shares give decision making power for the major business areas. They are the owners. The rate of dividend is not fixed, but determined each year in the Board meeting. The equity shares can be issued for cash or consideration other than cash.
- Incase of private companies- the shares have to be placed privately, incase of public co- they can be issued to he public for subscription. The shares can be issued for cash and for consideration other than cash.
- First we will try to understand the issue of shares for cash. There are many concepts related to issues of shares for cash-
  - Minimum subscription
  - Issue of shares at par, premium and discount

CHAPTER 10-Company Accounts- Unit 2

- As per the SEBI guidelines the total face value is not collected in one instalment- but it is collected in min of 2 and max being 4-5 calls. So the journal entries to be passed to record the issue of shares for cash are 2 entries for each instalment.
- The **first instalment** is called as **application** meaning the members need to apply for shares along with this instalment called the **application money**. Application money shall be **at least 5% of the nominal value of the shares**.
- The **second instalment** is called as the **allotment** which marks that the person has become the member and is issued the share certificate and his name is entered in the register of members. Then the call is made to the members to remit the allotment money due.
- The **next instalments** are simply called as **calls**- May be 1^{st} and final call or first call, second call or final call respectively based on the company's policy.

CHAPTER 10-Company Accounts- Unit 2

- The two entries can be classified into – Bank entry or **receipt entry** and the **transfer entry.**
- **For the application-** first is the receipt entry and then the bank entry
- **From the allotment till end of calls-** it is first the transfer entry and then the receipt entry
- Bank entry-

Bank A/c Dr (always bank is debited since the money is received)

To Share Application A/c

(or) To Share Allotment A/c

(or) To First call A/c

(or) To Final call A/c

CHAPTER 10-Company Accounts- Unit 2

- The two entries can be classified into – Bank entry or **receipt entry** and the **transfer entry.**
- **For the application-** first is the receipt entry and then the bank entry
- **From the allotment till end of calls-** it is first the transfer entry and then the receipt entry
- **Transfer entry-**

Share Application A/c Dr

(or) To Share Allotment A/c Dr

(or) To First call A/c Dr

(or) To Final call A/c Dr

To Share capital A/c (Always the share capital is credited since the amt is transferred)

CHAPTER 10-Company Accounts- Unit 2

- When the subscribed share capital is different from the issued capital- the following three cases can arise-
  - **Full subscription-** which means that issued capital= subscribed capital
  - **Over subscription-** which means that issued capital< subscribed capital
  - **Under subscription-** which means that issued capital > subscribed capital
- **Full or normal subscription** is a easy question where the entries are passed with the shares subscribed like in a normal case.
- Incase of **under subscription**- the condition of the minimum subscription has to be followed- which is 90% of the issued share capital has to be subscribed else, the money received shall be rejected. So if the shares subscribed is 90% or more, you can go ahead with the journal entries with the subscribed no. of shares.
- Incase of **over subscription-** There can be two options- the excess shares can be rejected or accepted. The entries have to be passed carefully in this case alone. (please follow this in class)

CHAPTER 10-Company Accounts- Unit 2

- Issue price of the shares can be of three types
  - **Issue at par-** which means that Face value= issue price. So changes in entries.
  - **Issue at premium-** which means the company enjoys a great image and can issue the shares at a price higher than the face value.
  - For example if the face value is Rs. 10 and the Issue price is Rs. 15- the higher value is referred to as the **premium amount-** which shall be transferred to a separate account called the **Securities premium account.** This is a liability shown under the **Reserves and Surplus in the balance sheet.**
  - While passing the entries- it shall be written in the transfer entry and on the same side of the share capital (credited). The Securities premium can be used as per Section 52 (pg 10.31)
  - **Issue at discount-**the normal shares cannot be issued at a discount. Only sweat equity shares can be issued at a discount. Hence, there is no need to study this from the accounting perspective.

CHAPTER 10-Company Accounts- Unit 2

- **Calls in arrears and Calls in Advance**
- Where the amount to be paid by the members have not been paid, then the default is recorded in a separate account called as the **calls in arrears.** This is shown as deduction from the called up capital.
- There is **interest to be paid in calls in arrears** to be paid by the members as per **table F is 10%** .
- The calls in arrears will be coming in the receipt entry which is debited alongside with bank A/c
- Where the amount of the next instalment is paid along with the current instalment then it is kept in a separate account called the **calls in advance** account and shown in the receipt entry of the respective account in the credit side.
- The **maximum interest to be paid on the calls in advance** by the company to the members as per **Table F is 12%**.

CHAPTER 10-Company Accounts- Unit 2

- **Calls in arrears and Calls in Advance**
- **Period for calculation** of interest in **calls in arrears** – from the date of the respective call to the date of payment of the amount due.
- **Period for calculation** of interest in **calls in advance** – from the date of the receipt of amount to the date of the respective call.
- Entries for interest on calls in arrears- there are two entries- one is accrual entry and the other one is receipt entry-

Shareholders A/c Dr		(when the interest becomes due)
To Interest on call in Arrears a/c		
Bank a/c Dr		
To Shareholders A/c		(when the interest is received by the co)

CHAPTER 10-Company Accounts- Unit 2

- **Calls in arrears and Calls in Advance**
- Entries for interest on calls in advance- there are two entries- one is accrual entry and the other one is payment entry-

Interest on call in Advance a/c Dr (when the interest is due)

To Shareholders A/c

Shareholders A/c Dr

To Bank A/c (when the interest is paid by the co)

CHAPTER 10-Company Accounts- Unit 2

- **Over subscription and pro rata allotment-** when there is over subscription more than the issued capital- then there is one option to adjust the extra money received. Where the amount is adjusted towards the next instalment due-then it is said to be pro rata allotted or adjusted towards the next instalment due.
- This is one of the most important topic- which needs much attention while passing the application entry and also in the allotment at the time of issue of shares for cash.
- Also if there is calls in arrears where originally there has been over subscription and there has been pro rata allotment done, while calculating the amount paid by them, one should be careful to find it out correctly.

CHAPTER 10-Company Accounts- Unit 2

- **Forfeiture of shares-** When the shares are not being paid by a member repeatedly even after sending various reminders to him, then there is an option for the company to take back the shares from the defaulting member- which is called as the process of forfeiting the shares.

- The entry that will be passed in the case of forfeiture is as follows-

Share capital A/c Dr

Securities premium A/c Dr (this ill come only if the shares are issued at a premium but the premium amount not received)

To Shares forfeiture A/c (This represents the amount paid by the member)

To Calls in arrears A/c (This is the amount unpaid on the shares cancelled)

CHAPTER 10-Company Accounts- Unit 2

- **Reissue of Forfeited shares-** Ultimately it is money which needs to be raised from the issue of shares. Wherein case one member has defaulted, then shares can be cancelled and reissued to another member. Such an issue for the second time is called as reissue.
- he shares can generally be reissued at a lesser value than the original value- which is the loss to company- but this can be set off from the amount paid by the first share holder-since it is loss created out of his negligence.
- If any amount is remaining in the shares forfeited A/c, then such amount should be transferred to capital reserve as the capital profit.
- If in case out of total shares forfeited, only a part of shares is reissued, then in the calculation of the capital profit, there shall be this formula used-

$$\frac{\text{Total shares forfeited amount}}{\text{Total shares forfeited}} * \text{No. of shares reissued} = \text{Shares forfeited amount of shares reissued.}$$

CHAPTER 10-Company Accounts- Unit 2

- **Reissue of Forfeited shares-** Accounting entry for re-issue

Bank A/c Dr

Shares forfeited A/c Dr (to the extent of the loss on re-issue)

To share capital (always the face value)

For the amount to be transferred to Capital reserve-

Shares forfeited A/c Dr (difference between the amount received and amount set off against loss on reissue)

To Capital reserve A/c (shown under reserves and surplus in balance sheet)

If nay amount is remaining in the Shares forfeited account under the liabilities

CHAPTER 10-Company Accounts- Unit 2

- **Issue of shares for consideration other than cash-** In certain cases, the shares can be issued instead of cash being paid. Like against purchase of any assets, or taking over business- the consideration can be discharged in the form of shares.
- Here the computation of the number of shares to be issued shall be found out using the following formula-

$$\text{No of share to be issued} = \frac{\text{Purchase consideration}}{\text{Issue price of shares}}$$

Entry will be – Asset a/c Dr

To share capital A/c

To Securities premium A/c (if issued at premium)

THANK YOU