THIRUTHANGAL NADAR COLLEGE

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NAME OF THE DEPARMENT: COMMERCE BM / AF

SUBJECT : CORPORATE ACCOUNTING

TOPIC : ISSUE OF SHARES

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CORPORATE ACCOUNTING

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ISSUE OF SHARES

What is Issue of Shares?

The issue of shares is the procedure in which enterprises allocate new shares to the shareholders. Shareholders can be either corporate or individuals. The enterprise follows the rules stipulated by Companies Act 2013 while circulating the shares. The Issue of Prospectus, Receiving Applications, Allocation of Shares are 3 key fundamental steps of the process of issuing the shares.

SIGNIFICANCE OF ISSUE OF SHARES

- **Issue of Prospectus:** The enterprise initially issues the prospectus to the public generally. The prospectus is an appeal to the public that a new enterprise has come into the presence and it would require funds for operating the trading concern. It comprises of complete data regarding the enterprise and the way in which the money is to be collected from the prospective investors.
- **Receipt of Applications:** When the prospectus is circulated to the public, prospective investors contemplating to sign up and subscribe the share capital of the enterprise would make an application along with the application money and deposit it with a scheduled bank as mentioned in the prospectus.

- **Allocation of shares**
  Once the minimum subscription has been done, the shares can be allocated. Normally, there is always oversubscription of shares, so the allocation is done on pro-rata ground. Letters of Allotment are sent out to those people who have been allocated their part of shares. This results in an authentic contract between the enterprise and the claimant, who will now be a part-owner of the enterprise.

TYPES OF ISSUE OF SHARES

- Ordinary shares. These carry no special rights or restrictions.
- Deferred ordinary shares.
- Non-voting ordinary shares.
- Redeemable shares.
- Preference shares.
- Cumulative preference shares.
- Redeemable preference shares.

PRO RATA ALLOTMENT

A company may receive applications for shares more than the number of shares it has offered to the public. This is known as over-subscription of shares. Usually, the companies that are financially strong, have a good reputation in the market or have profitable future prospects, receive over-subscription of shares. Thus, Pro Rata Allotment becomes necessary.

ISSUE OF PREFERENCE SHARES

Shares which have preference over Equity shares for payment of dividend or return of capital called preference share. Preference shares permit an investor to own a stake in the issuing company with a condition that whenever the company decides to pay dividends, the holders of these shares will be the first to be paid. The dividend payment of the preference shareholders is fixed.

ISSUE OF DEBENTURES

- The issue of Debentures is very similar to the issue of shares by a company. Here to the money can be collected lump sum or in installments. The accounting treatment of the two is also quite similar. Now debentures can be issued for cash or some other consideration. At times issue of debentures is also done as a collateral security. Let us study in detail the issue of debentures.

REDEMPTION OF PREFERENCE SHARES

The Redeemable Preference Shares are those, the amount of which can be paid back to the holders of such shares. That is, the capital raised through the issue of Redeemable Preference Shares can be paid back by the Company to such shares. The paying back of capital is called the Redemption.The redemption of redeemable preference shares does not reduce the Company’s authorized capital. From the Creditors’ point of view the capital remains intact because the share capital redeemed is simply replaced by the nominal value of the new shares issued for the purpose of redemption or by a Capital Redemption Reserve Account, for practical purposes, is equal to the paid up capital of the company

REDEMPTION OF DEBENTURES

Debentures are debt instruments. Hence when their period expires, debenture holders are paid back their principal amount. This process of discharging the company’s debt is known as the redemption of debentures. Let us learn more about the various methods of redemption of debentures and their accounting treatments.

PROFIT PRIOR TO INCORPORATION

- When a running business is taken over from a date prior to its incorporation/commencement, the profit earned up to the date of incorporation/commencement (incorporation, in case of private company; and commencement, in case of public company) is known as 'Pre-incorporation profit'.
- The same is to be treated as capital profit since these are profits which have been earned before the company came into existence. In short, the profit earned after the date of purchase of business is called 'Post-incorporation or Post-acquisition profit' and the profit earned before the date of purchase of business is termed as 'Pre-incorporation profit'.

VALUATION OF SHARES

When a new company is incorporated, it requires the capital for which it issues the shares. The Memorandum of Association has the information on the authorised share capital, number of shares and face value of each share. Authorised capital is defined as the maximum amount of share capital that the company is authorized by its constitutional documents to issue to shareholders. Part of the authorized capital can remain unissued. The authorized capital can be changed with shareholders' approval. The face value is the initial cost of the share fixed by the company. Face Value never changes. The market value of stock however increases or decreases based on company's performance and demand & supply of the share. Market Value usually never goes below Face Value. The difference between what shareholders pay for a share and the face value is referred to as additional paid-in capital or premium. Out of amount you pay, only amount equivalent to face value is your contribution to company and rest goes to seller as premium. That's the reason, company pays dividend on face value amount only.

VALUATION OF GOODWILL

- A well-established firm earns a good name in the market,, builds trust with the customers and also has more business connections as compared to a newly set up business. Thus, the monetary value of this advantage that a buyer is ready to pay is termed as Goodwill. The buyer who pays for Goodwill expects that he will be able to earn super profits as compared to the profits earned by the other firms. Thus, goodwill exists only in the case of firms making super profits and not in the case of firms earning normal profit or or losses.
- Goodwill is recorded in the books only when some consideration in money or money’s worth is paid for it. Thus, in the context of a partnership firm, the need for valuation of goodwill arises at the time