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CENTRE FOR DISTANCE AND ONLINE EDUCATION

B. Com. Part-II

Semester-III

**Accountancy Paper- III
(Corporate Accounting- I)**

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Preface

Corporate Accounting refers to the process of recording, analyzing, and reporting the financial transactions of corporate entities, such as companies registered under the Companies Act. It involves the preparation and presentation of financial statements in accordance with prescribed accounting standards and legal requirements. However, this book is restricted to few introductory topics of corporate accounting such as introduction to company, legal provisions related to corporate accounting, issue of shares and valuation of shares.

This book is divided into four units. The first unit explains meaning, types of companies, concept and types of shares, share capital of a company, features of equity share and preference shares, difference between equity shares and preference shares, memorandum of company, articles of a company, formation of company and Initial Public Offering (IPO). The second unit presents accounts related provisions under Companies Act 2013, key aspects of company accounts, monitoring and regulatory authorities and corporate governance under the Companies Act 2013. The third unit details about issue of shares which includes terms and conditions of issue of shares, issue of shares at par, issue of shares at premium, calls in advance, calls in arrears, journal entries for issue of shares, forfeiture of shares and reissue of forfeited shares. The fourth unit presents accounting about valuation of shares which includes valuation of equity shares, factors affecting valuation of equity shares, methods of valuation of equity shares and valuation of preference shares.

We have tried to keep the standard of the book as per norms of distance and online learning perspective. We appeal all the stakeholders of distance and online education to give their feedback for enriching this self-learning material which will be useful to improve the quality of it in future.

We are grateful to Hon. Vice-Chancellor, Hon. Pro-Vice-Chancellor and Director, Centre for Distance and Online Education. We are also thankful to Dr. V. N. Shinde (Registrar), other officers and staff of the university.

■ Editor ■

Prin. (Dr.) N. L. Kadam

Chairman, BOS Accountancy,
Shivaji University, Kolhapur
Prin. D. R. Mane College, Kagal
Tal. Kagal, Dist. Kolhapur

Prof. (Dr.) S. S. Mahajan

Head of the Department,
Department of Commerce and
Management,
Shivaji University, Kolhapur

Centre for Distance and Online Education
Shivaji University,
Kolhapur.

Accounting Paper - III
(Corporate Accounting)
B. Com. II Semester-III

Writing Team

Author's	Unit No. Sem. III
Prof. (Dr.) Shrikrishna S. Mahajan Dean, Faculty of Commerce and Management, Shivaji University, Kolhapur	1, 3
Dr. S. S. Chile Sadguru Gadage Maharaj College, Karad	2
Prin. (Dr.) N. L. Kadam D. R. Mane College, Kagal	4

■ **Editor** ■

Prin. (Dr.) N. L. Kadam
Chairman, BOS Accountancy,
Shivaji University, Kolhapur
Prin. D. R. Mane College, Kagal
Tal. Kagal, Dist. Kolhapur

Prof. (Dr.) Shrikrishna S. Mahajan
Head of the Department,
Department of Commerce and
Management,
Shivaji University, Kolhapur

B. Com Part-II

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Each Unit begins with the section 'Objectives' -

Objectives are directive and indicative of :

1. What has been presented in the Unit and
2. What is expected from you
3. What you are expected to know pertaining to the specific Unit once you have completed working on the Unit.

The self check exercises with possible answers will help you to understand the Unit in the right perspective. Go through the possible answer only after you write your answers. These exercises are not to be submitted to us for evaluation. These are provided to you as Study Tools to help keep you in the right track as you study the Unit.

Unit 1
Introduction to Company

1.0 Introduction

1.1 Objectives

1.2 Presentation of Subject Matter

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1.5 Answers to Check your progress

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1.0 Introduction

Dear learners, welcome to the course on the introduction to company. There are some activities given in this unit which will keep you active while learning. Do not skip them. Completing those activities will help you for your learning activeness and continuity. You have to also check your progress at different stages which will provide you the feedback through answers at the end of the unit.

Now let us try to understand the initial points of this unit. Before going to understand the issue of shares, you have to revisit your existing knowledge about company and its share capital. A joint stock company is one of the form of organizations. Firstly, see what is a company. It is identical because of its feature of 'share capital'. The capital of a company is called share capital which is divided into shares. Company means an association of persons formed for the economic gain of the members. However, by law, company can be for any legal object not necessary only for economic gain. The Companies Act 2013 defines a company as "a company incorporated under this Act or an existing company." 'An existing company means a company formed and registered under any of the former Companies Act. This unit covers meaning and definition of company, types of companies, concept of share, types of shares, share capital of the company, features of equity share, features of preference share, difference between equity shares and preference shares, Memorandum of Company, Article of Association of company, formation of company, and initial public offering (IPO).

1.1 Objectives

After studying this Unit, you will be able:

1. To describe the meaning, definition and types of company
2. To define the concept of share, types of shares, share capital.
3. To compare between an equity share and a preference share
4. To outline the Memorandum of association, Articles of association and formation of company
5. To describe the Initial Public Offering (IPO)

1.2 Presentation of Subject Matter

Now we are going to learn core points of the subject matter which we want to learn from this unit. It is main part of this unit which includes meaning, definition and types of company, concept of share, types of shares, share capital; difference between an equity share and a preference share; the Memorandum of association, Articles of association and formation of company and the Initial Public Offering (IPO).

1.2.1 Company:

A joint stock company is one of the form of organizations. Firstly, see what is a company. It is identical because of its feature of 'share capital'. The capital of a company is called share capital which is divided into shares. Accounting of valuation of shares as well as share capital are important aspects of corporate accounting. Hence, we as students of accountancy should know about the company as form of business.

1.2.1.1 Meaning and Definition of Company: Company means an association of persons formed for the economic gain of the members. However, by law, company can be for any legal object not necessary only for economic gain. The Companies Act 2013 defines a company as "a company incorporated under this Act or an existing company." 'An existing company means a company formed and registered under any of the former Companies Act. The characteristics of a company includes (a) it is voluntary association, (b) it is independent legal entity, (c) it has perpetual succession, (d) company being artificial entity, has common seal, (e) liability of members is generally limited and (f) shares of company are freely transferable.

Lord Justice Lindley defines it as: 'A company is an association of many persons who contribute money or money's worth to a common stock and employ it in some trade or business and who share the profit and loss arising therefrom. The common stock so contributed is denoted in money and is the capital of the company. The persons who contribute it or to whom it belongs are members. The proportion of capital to which each member is entitled is his share. The shares are always transferable although the right to transfer is often more or less restricted.'

According to Chief Justice Marshall, 'a corporation is an artificial being, invisible, intangible, existing only in corporation of the law. Being a mere creation of law, it possesses only the properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence.'

1.2.1.2 Characteristics of Company: Following are distinguishing characteristics of a company:

- 1) **Incorporated association:** A company is an association of persons who come together voluntarily to carry on business and share profits. It must be incorporated or registered under the relevant Companies Act, which grants it legal recognition and allows it to function as a distinct entity. The minimum number of members required for incorporation varies by jurisdiction and company type, but registration is essential to its existence.
- 2) **Artificial legal person:** A company is considered an "artificial person" or "juridical person." This means it is recognized by law as having rights and obligations similar to those of a natural person, such as entering contracts, owning property, and suing or being sued in its own name. However, unlike a natural person, a company acts through its agents, typically its board of directors.
- 3) **Separate legal entity:** One of the most fundamental characteristics is that a company is a separate legal entity. It has its own identity, distinct from its shareholders or members. This allows the company to own property, incur debts, enter into contracts, and be responsible for its own obligations, independent of its members.
- 4) **Perpetual succession:** Perpetual succession means the company continues to exist regardless of changes in its membership. Death, insolvency, or withdrawal of shareholders or directors does not affect the company's existence. The company only ceases to exist if it is formally wound up according to the law.
- 5) **Limited liability:** Members or shareholders of a company have limited liability. Their responsibility for the company's debts is restricted to the amount they have invested or guaranteed. Personal assets of shareholders are not at risk for the company's liabilities, providing significant financial protection.
- 6) **Transferable shares:** In most companies, especially public ones, shares are freely transferable. This means shareholders can transfer their ownership in the company without affecting its existence or operations. This feature enhances liquidity and makes investment in companies more attractive.

- 7) **Common seal:** Historically, a company could only act through its common seal, which served as its official signature on documents. While the requirement for a common seal has been relaxed in many jurisdictions, it remains a symbol of the company's authority and identity.
- 8) **Separate property:** A company can own, buy, and sell property in its own name. The property of the company is not the property of its shareholders. Even if a shareholder holds all shares, the assets belong to the company, not to the individual.
- 9) **Capacity to sue and being sued:** As a separate legal entity, a company can initiate legal proceedings in its own name and can also be sued. This ensures that the company can enforce its rights and be held accountable independently of its members.

1.2.2 Types of Companies

The companies may be classified into following types:

- 1) **Statutory Companies:** A statutory company, also known as a statutory corporation, is a legal entity created by a special act passed by the Parliament or a state legislature, rather than being incorporated under general company law like the Companies Act. Examples of statutory companies in India include the Reserve Bank of India (RBI), Life Insurance Corporation of India (LIC), and State Bank of India (SBI).
- 2) **Registered Companies:** A registered company is a company that is formed and brought into existence by registering under the relevant Companies Act with the Registrar of Companies. Upon registration, it becomes a legal entity distinct from its members, capable of owning property, entering into contracts, and conducting business in its own name. Such companies can be again divided into:
 - (a) **Companies limited by shares:** A company limited by shares is a type of company in which the liability of its members (shareholders) is limited to the amount unpaid, if any, on the shares they hold in the company. This means shareholders are only responsible for the company's debts up to the value of their shares and are not personally liable beyond that amount
 - (b) **Companies limited by guarantee:** A company limited by guarantee is a type of company where the liability of its members is limited to a specific amount that each member agrees to contribute if the company is wound up. This

amount, known as the "guarantee," is typically nominal and set out in the company's articles or constitution.

- (c) **Unlimited companies:** An unlimited company is a type of company where there is no limit on the liability of its members. This means that if the company faces debts or financial obligations that it cannot meet, the members (shareholders) are personally liable to pay off those debts without any restriction, even if it requires using their personal assets. Unlike limited companies, unlimited companies do not provide limited liability protection to their members.

Or

- (a) **Private limited companies:** A private limited company is a business entity privately owned by a small group of individuals, where the liability of its shareholders is limited to the amount unpaid on their shares. It has a separate legal identity distinct from its members, allowing it to own property, enter contracts, sue, and be sued in its own name. Shares of a private limited company cannot be publicly traded or offered to the general public, and there is a restriction on the maximum number of members (usually up to 200)
- (b) **Public limited companies:** A public limited company is a type of limited liability company that is allowed to offer its shares to the general public and have those shares traded on a stock exchange. It is a separate legal entity distinct from its shareholders, with perpetual succession and limited liability, meaning shareholders are only liable up to the amount they have invested in shares.

Or

- (a) **Unlisted companies:** An unlisted company is a company whose shares are not listed or traded on any recognized stock exchange.
- (b) **Listed companies:** A listed company is a public company whose shares are officially admitted and traded on a recognized stock exchange.
- 3) **Holding Company:** A holding company is a company owns and controls the majority of shares or membership interests in other companies, known as its subsidiaries.
- 4) **Government Company:** A Government Company is a company in which not less than 51% of the paid-up share capital is held by the Government of India,

or by the Government of any State or States, or partly by the Central Government and partly by one or more State Governments.

- 5) **Foreign Company:** A Foreign Company is defined under Section 2(42) of the Companies Act, 2013, as any company or body corporate that is incorporated outside India and (a) has a place of business in India, either by itself or through an agent, physically or through electronic mode; and (b) conducts any business activity in India in any other manner.
- 6) **One-man Companies or Family Companies:** A One Person Company is a type of company introduced under Section 2(62) of the Companies Act, 2013, which is formed and managed by a single individual who acts as the sole member and director of the company.
- 7) **Small Company:** A Small Company is defined under Section 2(85) of the Companies Act, 2013, as a company that is not a public company and meets the following criteria: (a) It has a paid-up share capital that does not exceed Rs.4 crore or such higher amount as may be prescribed, which shall not exceed Rs.10 crore (b) Its annual turnover does not exceed Rs.40 crore or such higher amount as may be prescribed, which shall not exceed Rs.100 crore.
- 8) **Dormant Company:** A Dormant Company is a company that has been registered under the Companies Act, 2013 but is not currently carrying out any significant business activities or operations. It is typically formed for a future project or to hold assets or intellectual property and has no significant accounting transactions for a certain period, usually two consecutive financial years.
- 9) **Associate Company:** An Associate Company is defined under Section 2(6) of the Companies Act, 2013, as a company in which another company has significant influence but which is not a subsidiary of that company. Significant influence generally means holding at least 20% of the total voting power or having control or participation in business decisions under an agreement.
- 10) **Global Company:** A Global Company is an organization that operates in multiple countries around the world, following a unified and standardized strategy across all its markets. Unlike multinational companies that tailor their strategies to individual countries, global companies maintain a consistent brand image, products, and services worldwide.

- 11) **Multinational Company:** A Multinational Company (MNC) is a large corporation that operates in its home country as well as in multiple other countries through subsidiaries, branches, or affiliates. It typically has a centralized decision-making system at its headquarters but allows subsidiaries some operational autonomy to adapt to local markets. MNCs engage in foreign direct investment (FDI) by establishing production, sales, or service facilities abroad.
- 12) **Charitable or Non-Profit Making Companies:** A Charitable or Non-Profit Making Company is an organization established primarily for promoting public welfare or advancing a public benefit without the intention of making profits for its members or shareholders. Such companies operate exclusively for charitable purposes such as education, poverty alleviation, scientific research, religion, health, environment, and other activities serving the public interest or common good. Any surplus or income generated by these companies is reinvested into their objectives rather than distributed as profits. Such companies are registered under Section 8 of Companies Act 2013.

A company is identical form of organization because of its feature of 'share capital'. The capital of a company is called share capital which is divided into shares. In this section we will try to understand the concepts of share, equity shares and preference shares.

1.2.3 Concept of Share: Share capital of a company is divided into parts having equal value is called share. A share has a nominal value or face value. It bears a distinct number. A share is ownership security.

1.2.3.1 Meaning of Share: Share is a part of share capital which has equal value. A share is one unit of share capital in which share capital is divided. According to Section 2 (84) of Companies Act 2013, a share means "share in the share capital of a company and includes stock".

1.2.3.2 Essential Features of Share: The following are the essential features of a share [Section 44]:

- 1) A share has a nominal value and bears a distinct number.
- 2) A share certificate issued under the common seal of the company certifies that the person named herein is a registered holder of a specific number of shares bearing distinct numbers as mentioned in the certificate.

- 3) A share is an ownership security. In other words, a shareholder is a part-owner of the company.
- 4) A share is said to be a bundle of rights as well as liabilities. It secures to its owner the right to receive a proportionate part of the profits, if any, and proportionate part of the assets of the company upon liquidation. On the other hand the shareholder may also be required to pay the full value in winding up.
- 5) Shares may be issued generally at par or premium and at discount only in certain cases.
- 6) A share is considered to be a movable property transferable in the manner provided in the articles of the company.

1.2.3.3 Stock: Fully paid up share capital may, if the Articles so permit, be converted into stock by an ordinary resolution (a resolution by simple majority) of the members. Stock is the aggregate consolidated holdings of the share capital of a person. It can be divided and transferred in any fractions and sub-divisions without regard to the original face value of the share for the purpose of convenient holding into different parts.

Difference between a Share and a Stock:

Sr. No.	Share	Stock
1	A share may not be fully paid up. It may be partly paid up or fully paid up.	Stock is always fully paid up. Only fully paid up shares can be converted into stock.
2	A share has nominal value.	A stock has no nominal value.
3	A share cannot be transferred in small fractions.	A stock can be transferred in any fractions.
4	All shares bear distinct numbers.	Stocks disclose the consolidated value of the share capital. Fractions of the stock do not bear any number.
5	All shares are of equal denomination.	Stock may be of unequal amounts.

6	Shares can be offered to the public.	Stock cannot be directly offered by the company to the public in the first instance.
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1.2.4 Types of Shares:

Shares can be classified in different types as shown below:

- 1) Preference Shares:
- 2) Equity Shares:
 - A) With uniform rights
 - B) With differential rights

1) Preference Shares:

Preference shares are those which carry the following preferential rights over other classes of shares:

- (a) A preferential right in respect of a fixed dividend- it may consist of a fixed amount (say Rs. 30,000 p.a.) or a fixed rate (say 13% p.a.)
- (b) A preferential right as to repayment of the capital in the event of company's winding up.

Types of Preference Shares:

Preference shares are categorized in the following types:

- A) On the basis of Dividend:
 - i) Cumulative Preference Shares
 - ii) Non-cumulative Preference Shares
- B) On the basis of Participation:
 - i) Participatory Preference Shares
 - ii) Non-participatory Preference Shares
- C) On the basis of Redemption:
 - i) Redeemable Preference Shares
 - ii) Non-redeemable Preference Shares

D) On the basis of Convertibility:

- i) Convertible Preference Shares
- ii) Non-convertible Preference Shares

Cumulative Preference Shares: The preference shares in case of which the arrears of dividend are accumulated till they are paid. As per the inherent feature of preference shares, before paying anything else, preference dividend is paid. Preference shares are always cumulative unless otherwise expressly stated in the company's articles.

Suppose, a company has 5,000, 11% preference shares of Rs.100 each. The company has not paid dividend to its preference shareholders for the year 2014-15, 2015-16, 2016-17 and 2017-18. In 2018-19, the company earns adequate profits. In this case the company shall pay dividend for 4 years (including arrears of last 3 years) amounting to Rs.2,20,000 (Rs.55,000 per annum) before paying any dividend to the equity shareholders.

Non-cumulative Preference Shares: The preference shares in which case, the dividend is not allowed to accumulate. In case of such preference shares, the right to claim dividend will lapse if there are not sufficient profits in a particular year.

Suppose, if a company has 5,000, 11% non-cumulative preference shares of Rs.100 each. The company has not paid dividend to its preference shareholders for the year 2014-15, 2015-16, 2016-17 and 2017-18. In 2018-19, the company earns adequate profits. In this case the company shall pay dividend only for one year amounting to Rs.55,000 before paying any dividend to the equity shareholders.

Participatory Preference Shares: The preference shareholders are entitled to (i) a fixed dividend and (ii) a share in the surplus profits, remaining after paying dividend to the equity shareholders upto a certain limit.

Check your progress-1:

(A) State whether the following statement is 'True' or 'False':

1. Share capital of a company is divided into parts having equal value is called share.
2. A share has a nominal value and bears a same number.
3. Shares may be issued generally at par or premium and at discount only in certain cases.

Exhibit-1 What Companies Act 2013 says about Share Capital?

The share capital of a company limited by shares shall be of two kinds, namely:

(a) equity share capital—

(i) with voting rights; or

(ii) with differential rights as to dividend, voting or otherwise in accordance with such rules as may be prescribed; and

(b) preference share capital:

Provided that nothing contained in this Act shall affect the rights of the preference shareholders who are entitled to participate in the proceeds of winding up before the commencement of this Act.

Explanation.—For the purposes of this section,—

(i) “equity share capital”, with reference to any company limited by shares, means all share capital which is not preference share capital;

(ii) “preference share capital”, with reference to any company limited by shares, means that part of the issued share capital of the company which carries or would carry a preferential right with respect to—

(a) payment of dividend, either as a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income-tax; and

(b) repayment, in the case of a winding up or repayment of capital, of the amount of the share capital paid-up or deemed to have been paid-up, whether or not, there is a preferential right to the payment of any fixed premium or premium on any fixed scale, specified in the memorandum or articles of the company;

(iii) capital shall be deemed to be preference capital, notwithstanding that it is entitled to either or both of the following rights, namely:

(a) that in respect of dividends, in addition to the preferential rights to the amounts specified in sub-clause (a) of clause (ii), it has a right to participate, whether fully or to a limited extent, with capital not entitled to the preferential right aforesaid;

(b) that in respect of capital, in addition to the preferential right to the repayment, on a winding up, of the amounts specified in sub-clause (b) of clause (ii), it has a right to participate, whether fully or to a limited extent, with capital not entitled to that preferential right in any surplus which may remain after the entire capital has been repaid.

Source: Companies Act 2013.

1.2.5 Share Capital of the Company:

Capital of a company is divided into number of parts having equal value. Such parts of capital having equal value are called shares. Shareholders are nothing but owners of a company. Hence, share capital is owners' capital of a company. Share capital of a company may be divided into two parts as equity share capital and preference share capital.

Share capital of company may be of two types: Preference share capital and Equity share capital.

- 1) Preference share capital: Preference share capital is shown firstly in the balance sheet. It is a sum total of the nominal value of preference shares of a company. As per Companies Act 2013, "preference share capital", with reference to any company limited by shares, means that part of the issued share capital of the company which carries a preferential right with respect to (a) payment of dividend and (b) repayment of capital.
- 2) Equity share capital: Equity share capital is nothing but a sum total of nominal value of equity shares of a company. Companies Act 2013 says "equity share capital", with reference to any company limited by shares, means all share capital which is not preference share capital.

As per Section 2 of Companies Act 2013, share capital of a company can be classified as shown below:

- 1) Authorized Capital or Nominal Capital: Authorized capital is a capital which is authorized by the company's memorandum of association to be the maximum amount of share capital of the company [Refer Section 2(8)]. It is also called "Nominal capital" or "Registered capital" of a company.
- 2) Issued Capital: It means such capital as the company issues from time to time for subscription [Section 2(50)]. It consists of the shares which are offered for subscription within the authorized limit. It is represented by the nominal value of:
 - (a) The shares allotted for cash.
 - (b) The shares allotted for consideration other than cash.
 - (c) The shares subscribed for by the signatories to the Company's Memorandum.

- 3) **Subscribed Capital:** It means such part the capital which is for the time being subscribed by the members of a company [Section 2(86)]. It represents that portion of the issued capital which has been subscribed and allotted.
- 4) It is possible that all shares offered are not subscribed to and to the extent of unsubscribed portion there will be a difference between shares issued and subscribed. Share capital may not have been allotted because of certain formalities required to be observed by the Shareholder (i.e. in case of right shares). In any case the share capital which could not be finally allotted will be taken as “unissued capital”. Thus, ultimately the subscribed capital and issued capital (in terms of number of shares) are the same because if the number of shares subscribed is less than what is offered, the company can allot only the number of shares for which subscription received. The shares issued but unsubscribed will again be issued whenever a new issue of capital is made. However, at a particular moment of time Issued Capital and Subscribed Capital may be different.
- 5) **Called-up Capital:** It means such part of the capital, which has been called for payment [Section 2(15)].
- 6) **Paid-up Capital:** It means such aggregate amount of money credited as paid-up as is equivalent to the amount received as paid-up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of the company, but does not include any other amount received in respect of such shares (i.e. share premium) by whatever name called [Section 2(64)].

Illustration-1:

Z Company Ltd. is registered with an authorized capital of Rs.2,00,00,000 divided into 10,00,000 equity shares of Rs.10 each and 1,00,000 preference shares of Rs.100 each. Its share capital is being held as under as on 31st March 2025.

- (a) 2,00,000 equity shares of Rs.10 each have been subscribed by subscribers to the Company’s Memorandum.
- (b) 2,00,000 fully paid equity shares have been issued to the equity shareholders as bonus shares.
- (c) 6,00,000 equity shares of Rs.10 each and 60,000 preference shares of Rs.100 each have been offered to the public for subscription.

The Company has called up the entire money due on equity shares and preference shares. All share-holders have paid the calls on due dates except one holder of 2,000 equity shares who could not pay the final call of Rs.3 per share. Show how the capital is to be classified.

Solution:

The different classes of share capital Z Company Ltd. will be as shown below:

Particulars		₹
Authorized Capital		
10,00,000 Equity shares of Rs.10 each		1,00,00,000
1,00,000 Preference shares of Rs.100 each		1,00,00,000
		2,00,00,000
Issued Capital		
8,00,000 Equity shares of Rs.10 each		80,00,000
60,000 Preference shares of Rs.100 each		60,00,000
		1,40,00,000
Subscribed Capital		
7,00,000 Equity shares of Rs.10 each		70,00,000
60,000 Preference shares of Rs.100 each		60,00,000
		1,30,00,000
Called-up Capital		
7,00,000 Equity shares of Rs.10 each		70,00,000
60,000 Preference shares of Rs.100 each		60,00,000
		1,30,00,000
Paid-up Capital		
7,00,000 Equity shares of Rs.10 each fully paid called up	70,00,000	
Less: Calls in arrears on 2,000 shares of Rs.3 per share	6,000	69,94,000
60,000 Preference shares of Rs.100 each fully called and paid up		60,00,000
		1,29,94,000

1.2.6 Features of Equity Share: In Companies Act 2013, it is said that which not preference shares are called equity shares. By this definition, we cannot understand the meaning of equity share. If we know the features of equity shares we can comprehend the meaning of equity shares. Following are the features or characteristics of equity shares which are useful to understand the meaning of equity share in more detail:

1. **Ownership rights:** Equity shares represent ownership in company. Shareholders are partial owners and have a proportional claim on the company's assets and earnings based on the number of shares held.
2. **Voting Rights:** Equity shareholders have the right to vote on important company matters such as electing directors, approving mergers, and making other significant decisions. This gives them a say in the management and direction of the company.
3. **Limited Liability:** Shareholders' liability is limited to the amount they have invested in the shares. They are not personally responsible for the company's debts or obligations beyond their investment.
4. **Dividend Entitlement:** Equity shareholders may receive dividends, which are a share of the company's profits. However, the dividend rate is not fixed and depends on the company's profitability and the discretion of the board of directors.
5. **Residual Claim on Assets:** In the event of liquidation, equity shareholders have a residual claim on the company's assets. They are paid only after all debts and preference shareholders' claims have been settled.
6. **High Liquidity:** Equity shares are highly liquid and can be easily bought or sold on stock exchanges, allowing investors to enter or exit positions quickly.
7. **Permanent Capital:** Equity shares are a permanent source of capital for a company. The invested capital is generally not returned to shareholders during the company's lifetime, except in the case of liquidation.
8. **Fluctuating Market Value:** The market value of equity shares fluctuates based on the company's performance, market conditions, and investor sentiment. This provides the potential for capital appreciation but also involves higher risk.

9. **No Fixed Maturity:** Equity shares do not have a maturity date. Investors can hold them indefinitely or sell them as desired.
10. **Risk Bearing:** Equity shareholders bear the highest risk in the company. In bad years, they may receive low or no dividends, and the value of their shares may decline. In prosperous years, they benefit from higher dividends and capital gains.
11. **Right to Inspect Books and Transfer Shares:** Shareholders have the right to inspect the company's books of account and can freely transfer their shares to others, subject to company policies and regulatory requirements.
12. **Eligibility for Bonus and Rights Issues:** Equity shareholders may receive bonus shares (issued free from accumulated profits) and have the privilege to subscribe to additional shares through rights issues, often at a discounted price.

These features collectively make equity shares an attractive investment for those seeking ownership, voting power, potential for growth, and a share in a company's financial success, while also exposing them to higher risks compared to other forms of investment.

1.2.7 Features of Preference Shares

Preference shares, also known as preferred stock, are a unique class of shares that blend features of both equity and debt instruments. Here are their key features:

1. **Preference in Dividend Payment:** Preference shares carry a preferential right over equity shares when it comes to dividend payments. Dividends are paid to preference shareholders before any dividends are distributed to equity shareholders.
2. **Preference in Repayment of Capital:** In the event of company liquidation, preference shareholders have a higher claim on the company's assets compared to equity shareholders. This makes them less risky than ordinary shares in terms of capital recovery.
3. **Fixed Dividend Rate:** Preference shareholders are entitled to receive dividends at a fixed rate, which is predetermined at the time of issue. This provides shareholders with a steady and predictable income stream, regardless of the company's profitability in a given year, as long as there are distributable profits.

4. **Limited or No Voting Rights:** Generally, preference shareholders do not have voting rights in company meetings, except in matters directly affecting their interests (such as changes to their rights or winding up of the company). This allows companies to raise capital without diluting control.
5. **Hybrid Nature:** Preference shares exhibit characteristics of both equity (ownership in the company) and debt (fixed returns), making them hybrid financial instruments.
6. **Convertibility:** Some preference shares are convertible, meaning they can be converted into a specified number of equity shares after a certain period or under certain conditions. This offers investors the potential for capital appreciation in addition to regular dividends.
7. **Redeemable:** Preference shares may be redeemable. It means the company can buy them back after a specified period or company can repay after a specific period. As per regulations, companies cannot issue irredeemable preference shares; all must be redeemed within a set timeframe.
8. **Cumulative or non-cumulative:** Cumulative preference shares accumulate unpaid dividends, which must be paid out before any dividends to equity shareholders. Non-cumulative shares do not have this feature.
9. **Higher Face Value:** Preference shares are typically issued at a higher face value compared to equity shares, often at denominations like ₹100 per share.
10. **Lower Capital Appreciation:** The market value of preference shares tends to be stable, with lower potential for capital appreciation compared to equity shares, as their returns are primarily from fixed dividends.
11. **No Bonus Shares or Right Issue:** Preference shareholders are generally not entitled to bonus shares or rights issues that may be offered to equity shareholders.

Preference shares are thus attractive to investors seeking stable returns and lower risk, but they typically come with limited control over company decisions and less potential for high capital gains.

1.2.8 Difference between Preference shares and Equity shares:

Dear learners, if you have carefully understand the features of equity shares and preference shares, it explains you how they are different from each other. We

can distinguish between preference shares and equity shares in the following manner:

Sr. No.	Point of difference	Preference Shares	Equity Shares
1.	Fixed rate of dividend	Preference shares are entitled to a fixed rate/amount of dividend.	The rate of dividend on equity share is not fixed. It depends upon the amount of net profit available after payment of dividend to preference shareholders and the fund requirements of the company for future expansion etc.
2.	Priority to pay dividend	Dividend on the preference shares is paid in preference to that on the equity shares.	Dividend on equity shares is paid only after the preference dividend has been paid.
3.	Priority in repayment of capital	The preference shares have preference in repayment of capital.	The equity shares are paid after all payments to third parties and preference shares.
4.	Cumulative dividend	If the preference shares are cumulative, the dividend not paid in any year is accumulated and when profits are available for dividend firstly such arrears of dividend are paid.	The equity shares are not cumulative. Equity dividend can be paid after payment of preference dividend and arrears of preference dividend.
5.	Redemption	Redeemable preference shares are redeemed by the company after expiry of the stipulated period.	The equity shares cannot be redeemed being lifetime capital.
6.	Voting Rights	The voting rights of preference shareholders are restricted. Preference shareholder can vote only when his special rights as a preference shareholder	The equity shareholders can vote on all matters affecting the company.

		are being varied or their dividend is in arrears for at least two years.	
7.	Bonus shares or Right shares	Bonus shares or Right shares are not allowed to preference shareholders.	A company may issue right shares or bonus shares to its existing shareholders.

Check your progress-2:

(A) Fill in the blanks:

- are shares having preferential rights in respect of payment of dividend and repayment of capital.
- is capital of a company but not preference share capital.
- is a capital which is authorized by the company's memorandum of association to be the maximum amount of share capital of the company.
- The rate of dividend is not fixed for shares.

(B) State whether the following statement is true or false:

- The issued capital may be more than authorized capital.
- The called-up capital is a part of subscribed capital.
- The called-up capital is equal to or more than paid-up capital.
- The right shares are issued only to preference shareholders.

1.2.9 Memorandum of Association of a company:

The Memorandum of Association (MoA) is a foundational legal document required for the incorporation of any company under the Companies Act, 2013. This documents acts as the company's charter, defining its scope, powers, and relationship with the external world. It sets out the constitution of the company and establishes its identity and scope of activities.

1.2.9.1 Definition of Memorandum: According to Section 2 (56) of the Companies Act 2013, Memorandum means, “Memorandum of Association as originally framed or as altered from time to time in pursuance of any previous company law

or of this Act.” Any provisions contained in the Memorandum of Association will be void to the extent to which they are repugnant to the provisions of the Companies Act.

Section 4 of the Companies Act, 2013 specifies the requirements for the MoA, and its format is prescribed in Tables A to E of Schedule I, depending on the type of company (e.g., with or without share capital, limited by guarantee, etc.).

It is mandatory for every company to have a MoA, and the company cannot act beyond the powers and objects specified in it. Any act outside its scope is considered ultra vires (beyond powers) and is void. The MoA is a public document, accessible to anyone dealing with the company, thus ensuring transparency and protecting the interests of shareholders, creditors, and other stakeholders. The MoA must be printed, numbered, divided into paragraphs, and signed by the subscribers in the presence of at least one witness.

1.2.9.2 Clauses of Memorandum: Memorandum includes various clauses such as name clause, registered office clause, objects clause, liability clause, capital clause and association clause.

- 1) **Name Clause:** A company being a distinct legal entity must have a name of its own to establish its separate identity. The promoters can choose any suitable name for the company except:
 - (a) A name which is identical with or which closely resembles the name of another company,
 - (b) A name, which in the opinion of the Central Government is undesirable.
 - (c) The last word of the name must be ‘limited’ in the case of public companies and ‘private limited’ in the case of private limited companies. It is not necessary that the word ‘company’ should form part of the name. However, a Company formed for a charitable purpose under section 8 of the Act may not use the word limited or private limited as a part of its name.
- 2) **The Registered Office Clause:** This clause must state the name of the state in which the registered office of the company is to be situated. It will fix up the domicile of the company. It is expected that company’s statutory books must normally be kept at this address of registered office of a company. Notices and other communications can be sent to this address.

- 3) The Object Clause: This clause defines the objects of the company and indicates the sphere of its activities. As per Section 4(1)(c), MoA of every company must state the following things:
- a) The objects for which the company is proposed to be incorporated and
 - b) Any matter considered necessary in furtherance thereof.

This clause defines and limits the scope of the operations of the company. Hence, it is most important clause of MoA.

- 4) Liability Clause: This clause clears the nature of liability of the members. In the case of a company with limited liability, MoA must state that liability of members is limited, whether it be by shares or by guarantee. It means that a shareholder cannot be called upon to pay at any time amount more than the unpaid portion of the shares held by him. We can interpret that if shares are fully paid-up, the liability of shareholders is nil. Suppose, Mr. A, a shareholder of a company holding shares of Rs.10 on which Rs.7 per share has paid-up, he can be called upon to pay the balance of Rs.3 per share. But if he has paid the full value of Rs.10, he cannot be required to pay anything more even if the company owes huge debts to its creditors.

It must further state that each member undertakes to contribute to the assets of the company if wound up while he is a member or within one year after he ceases to be so towards the debts and liabilities of the company as well as the costs and expenses winding up and for the adjustment of the right of the contributory among themselves no exceeding a specified amount [Section 4(1)(d)].

In the case of unlimited liability company, whether having share capital or not, this clause shall state that the liability of its members is unlimited.

- 5) Capital Clause: This clause must indicate the amount of capital with which the company is registered and is known as Registered or Authorized or Nominal capital. As per Section 4 (1) (e), in the case of a company having a share capital, the memorandum must state the amount of share capital with which the company is to be registered and the division thereof into shares of a fixed amount and the number of shares which the subscribers to the memorandum agree to subscribe which shall not be less than one share. This clause shall state the number and value of shares into which the capital of the company is divided. It also shall clear how share capital is divided into preference share capital and equity share capital.

- 6) Association Clause: According to Section 4(1)(e) of Companies Act 2013, It is also called as Subscription clause. This clause is about showing desire of coming in association. As per Section 4(1)(e) of Companies Act 2013, Memorandum of Association must be signed by seven or more persons in the case of a public company and any two or more persons in the case of a private company. At the end of Memorandum, following declaration is made:

“We, the several persons, whose names and addresses are subscribed, are desirous of being formed into a company in pursuance of this memorandum of association, and we respectively agree to take the number of shares in the capital of the company set against our respective names.”

1.2.10 Articles of Association of a company

In a case of a company, the articles of association (AoA) are nothing but a key constitutional document includes bye-laws or rules and regulations.

1.2.10.1 Meaning of AoA: According to Section 2(2) of Companies Act 2013, ‘articles’ means the articles of association of a company as originally framed or as altered from time to time in pursuance of any previous company laws or of the present Act. They regulate the internal management of company. It defines the powers of its officers. They set out provisions for the manner in which the company is to be administered. The AOA governs the conduct of the company’s business, the management of its internal affairs, and the relationship among its members, directors, and the company itself. It covers the matters such as making calls, forfeiture of shares, directors’ qualifications, appointment, powers and duties of auditors, procedures for transfer and transmission of shares and debentures.

1.2.10.2 Provisions regarding AoA: All companies must have Articles which are to be filed at the time incorporation itself- [Section 7(1)(a)]. Under earlier law of 1956, Articles were optional for public limited companies since they could totally adopt Table A, though almost all the companies did have their own Articles.

The articles of a company shall be in respective forms specified below. Schedule I as may be applicable to such company:

Table F: For company limited by shares

Table G: For company limited by guarantee and having share capital

Table H: For company limited by guarantee and not having share capital

Table I: For company unlimited company and having share capital

Table J: For an unlimited company and not having share capital

Section 5 of the Companies Act, 2013, further specifies that the AOA must be in accordance with the provisions of the Act and must be signed by all subscribers to the Memorandum of Association (MOA) in the presence of at least one witness. The articles must be printed, divided into paragraphs, and consecutively numbered.

1.2.10.3 Contents of Articles of Association: The Companies Act, 2013 (particularly Section 5 and Schedule I), prescribes the typical contents of an AOA, which may include the following:

- 1) **Share Capital and Variation of Rights:** Details about classes of shares, their values, rights attached, and procedures for alteration of capital.
- 2) **Transfer and Transmission of Shares:** Rules for transferring shares and procedures in case of death or insolvency of a shareholder.
- 3) **Calls on Shares, Lien and Forfeiture:** Procedures for making calls on shares, company's lien on shares, and forfeiture provisions.
- 4) **Directors:** Appointment, powers, duties, remuneration, and proceedings of the Board of Directors.
- 5) **General Meetings:** Procedures for convening, conducting, and adjourning meetings, including voting rights, proxies, and quorum requirements.
- 6) **Dividends and Reserves:** Rules for distribution of profits and creation of reserves.
- 7) **Accounts and Audit:** Maintenance of books of accounts, audit procedures, and appointment of auditors.
- 8) **Borrowing Powers:** Powers of the Board regarding borrowing on behalf of the company.
- 9) **Winding up:** Procedures for dissolution or winding up of the company.
- 10) **Common Seal:** Rules regarding the use and custody of the company's seal.
- 11) **Indemnity and Secrecy:** Provisions for indemnifying directors/ officers and maintaining confidentiality.
- 12) **Entrenchment Provisions:** Special procedures for amending certain clauses, offering additional protection to key provisions.

1.2.10.4 Alteration of AoA: The AOA can be altered by passing a special resolution in a general meeting, subject to the provisions of the Companies Act, 2013 and the company's own MOA. Certain alterations, especially those converting a public company to a private company or vice versa, require additional approvals, such as from the National Company Law Tribunal (NCLT).

The Articles of Association is legally binding on the company and its members, regulating their rights, duties, and responsibilities. It is essential for effective corporate governance, ensuring smooth internal management and compliance with statutory requirements.

1.2.11 Formation of Company:

A company may be formed as new company or existing business can be taken over by a company. The formation of a company starts with conceiving the idea of forming company and ends with actual commencing business. The formation of a company in India is governed by the Companies Act, 2013. The process is systematic, ensuring compliance with legal and regulatory requirements, and involves several key stages and steps. The procedure for formation of company may divided into main three stages: (a) Promotion stage, (b) Registration stage (c) Incorporation stage, and (d) Commencement of business stage.

1.2.11.1 Promotion Stage: This is the initial phase where the idea of starting a business is developed into concrete plan. In promotion state, it is expected do This stage consists of (i) identifying a business opportunity which assess market needs and decide on the business type; (ii) feasibility study to analyze economic, technical, and legal viability; and (iii) role of promoters includes arranging capital, preparing documents and initiating steps to establish the business.

1.2.11.2 Registration Stage: At this stage, the company is legally recognized under the Companies Act, 2013. The different steps in specific order are undertaken by promoters for the purpose of registration of a company under Companies Act 2013: (a) Approval for Name of company includes proposing a unique name and getting it approved by the Registrar of Companies; (b) Preparation of documents consists of drafting and signing the Memorandum of Association and Article of Association, signatures of minimum seven persons in case of public company, signatures of minimum two persons for a private company and one signature for One Person Company; (c) List of directors includes details of directors and their consent to act as directors; (d) Registered office should be notified to the Registrar of Companies the registered office address; (e) Statutory declaration by a qualified

professional (advocate, company secretary, director) stating all requirements have been met must be filed with the Registrar of Companies.

1.2.11.3 Incorporation stage: This is the stage of incorporation. It brings a company into existence as a separate corporate entity. In this stage, promoters have to take steps such as:

- (a) filing or submitting documents with the Registrar of Companies which includes memorandum of association, articles of association, director details, registered office proof, and statutory declaration. These documents are now submitted through the SPICe+ (Simplified Proforma for Incorporating Company Electronically Plus) form on the Ministry of Corporate Affairs (MCA) portal;
- (b) all proposed directors must obtain a Digital Signature Certificate (DSC) for filing e-forms.
- (c) Obtaining Director Identification Number (DIN) for all proposed directors from the Ministry of Corporate Affairs.
- (d) Once the Registrar of Companies is satisfied with all compliances, a Certificate of Incorporation is issued which proves establishing the company as a legal entity.

1.2.11.3 Commencement of Business Stage: In case of public company, after receiving the Certificate of Incorporation and raising the minimum subscription, a Certificate of Commencement of Business must be obtained before starting operations. In case of private company, it can commence business immediately after incorporation.

The formation of a company under the Companies Act, 2013 is a multi-stage process involving promotion, registration, incorporation, and commencement of business. It requires careful preparation of documents, compliance with legal requirements, and approval from the Registrar of Companies. The process is now largely online, making it more efficient and transparent.

Check your progress-3:

(A) Fill in the blanks:

1. According to Section 2(56) of the Companies Act 2013, “ is originally framed or as altered from time to time in pursuance of any previous company law or of this Act.”

2. As per Clause, the last word of the name must be 'limited' in the case of public companies.
3. Clause of Memorandum of Association fix up the domicile of the company.
4. Is legally binding on the company and its members, regulating their rights, duties and responsibilities.

(B) State whether the following statement is true or false:

1. The Articles of Association cannot be altered as per law.
2. Share capital and various rights are included in the Articles of Association.
3. In the formation of a company, registration stage comes after promotion stage.
4. In case of private company, it can commence business immediately after incorporation.

1.2.12 Initial Public Offering (IPO)

An Initial Public Offering (IPO) under the Companies Act 2013 marks a private company's transition to a publicly traded entity by offering shares to the public for the first time. This process enables capital raising through fresh issuances or existing shareholder sales, governed by SEBI regulations and the Companies Act's disclosure and compliance requirements.

Eligibility of Company for IPO: To launch an IPO in India, a company must: (a) be incorporated under the Companies Act 2013 with a three-year track record of profitability and net tangible of at least Rs.3 crore; (b) maintain a minimum net worth of ₹1 crore in each preceding year; (c) ensure promoters contribute 20% of post-issue capital, locked in for three years; and (d) allocate 75% of net offers to Qualified Institutional Buyers (QIBs) in book-built issues.

1.2.12.1 Meaning of IPO: An Initial Public Offer is the process by which a privately held company offers its shares to the public for the first time, thereby becoming a publicly traded company. This transition is often referred to as "going public."

Features of IPO:

- 1) First-Time Public Sale: The company sells its shares to institutional investors, high-net-worth individuals, and the general public for the first time.

- 2) **Raising Capital:** The primary purpose is to raise equity capital to fund business expansion, pay off debt, or finance other corporate objectives.
- 3) **Ownership Transition:** The company shifts from private ownership (held by founders, early investors, or private equity) to public ownership, allowing anyone to buy and sell shares on the stock exchange.
- 4) **Listing on Stock Exchange:** After the IPO, shares are listed on one or more stock exchanges, making them freely tradable in the open market.
- 5) **Disclosure Requirements:** The company must disclose detailed financial and business information to potential investors in a document called a prospectus.

1.2.12.2 Process of IPO

The process of IPO under the Companies Act 2013 have following stages:

- 1) **Appointment of Intermediaries:** The company hires SEBI-registered merchant bankers, underwriters, and legal advisors to manage due diligence, documentation, and regulatory filings.
- 2) **Draft Red Herring Prospectus (DRHP):** It is prepared with financial data, risk factors and use of proceeds. It is filed with SEBI and stock exchanges for approval. SEBI reviews for compliance and may request revisions before granting in-principle approval.
- 3) **Stock Exchange Application:** The company applies to stock exchanges (e.g. BSE/NSE) for listing, submitting final prospectus and fees.
- 4) **Roadshow and Pricing:** Executives market the IPO to institutional investors through roadshows. Pricing is determined via book-building (price band) or fixed-price method.
- 5) **IPO Launch and Subscription:** Public bidding opens for 3-7 days, with funds blocked via ASBA (Application Supported by Blocked Amount). Minimum 90% subscription required; else, funds are refunded.
- 6) **Allotment and Listing:** Shares are allotted within 15 days post-closure. Mandatory listing within three days of issue closure, followed by trading commencement.

Regulatory Framework for IPO: (a) SEBI ICDR Regulations 2018 govern investor protection, pricing, and allocation; and (b) Companies Act 2013 mandates prospectus disclosures, director accountability, and shareholder resolutions. This

structured approach ensures transparency, protects investor interests, and aligns with India's evolving capital market regulations.

Compliances after IPO: After IPO process is completed, following compliances are to be made: (a) maintain minimum public shareholding of 25% (10% for companies with post-issue capital >Rs.4,000 crore; (b) file Form 23 with the Registrar of Companies for special resolutions; and (c) adhere to SEBI's continuous disclosure norms and quarterly reporting.

IPO is a significant event where a private company offers its shares to the public for the first time, raising capital and enabling public trading of its stock.

Check your progress-4:

State whether the following statement is true or false:

1. Due to Initial Public Offering, private limited company becomes public limited company.
2. IPO is also called as 'going public'.
3. The primary purpose of IPO is making publicity.
4. The company applies to stock exchanges for listing, submitting final prospectus and fees, in the process of IPO.
5. SEBI ICDR Regulations 2018 mandates prospectus disclosures, director accountability, and shareholder resolutions.

1.3 Summary

Company means an association of persons formed for the economic gain of the members. The Companies Act 2013 defines a company as "a company incorporated under this Act or an existing company." 'An existing company means a company formed and registered under any of the former Companies Act. Companies may be private limited companies or public limited companies. The capital of a company is called share capital which is divided into shares. According to Section 2 (84) of Companies Act 2013, a share means "share in the share capital of a company and includes stock". Stock is the aggregate consolidated holdings of the share capital of a person. Shares can be classified in different types such as Preference Shares and Equity Shares. Preference shares are those which carry the following preferential rights over other classes of shares in terms of payment of dividend and repayment of capital. There may be different types of preference shares such as cumulative preference shares, non-cumulative preference shares,

participatory preference shares, non-participatory preference shares, redeemable preference shares, non-redeemable preference shares, convertible preference shares and non-convertible preference shares.

This unit also covered different concept of share capital such as authorized capital, issued capital, subscribed capital, called-up capital and paid-up capital. The share capital of a company can be divided into preference share capital and equity share capital. The features of equity share include ownership rights, voting rights, limited liability, dividend entitlement, residual claim on assets, high liquidity, permanent capital, fluctuating market value, no fixed maturity, risk bearing, right to inspect books and transfer shares, eligibility for bonus and rights issues. The features of preference shares consist of preference in dividend payment, preference in repayment of capital, fixed dividend rate, limited or no voting rights, hybrid nature, convertibility, redeemable, cumulative or non-cumulative, higher face value, lower capital appreciation and no bonus shares or right issue.

This unit explains about Memorandum of Association, Articles of Association and formation of a company. The Memorandum of Association (MoA) is documents acts as the company's charter, defining its scope, powers, and relationship with the external world. It sets out the constitution of the company and establishes its identity and scope of activities. Section 4 of the Companies Act, 2013 specifies the requirements for the MoA, and its format is prescribed in Tables A to E of Schedule I, depending on the type of company (e.g., with or without share capital, limited by guarantee, etc.). Memorandum includes various clauses such as name clause, registered office clause, objects clause, liability clause, capital clause and association clause. The articles of association (AoA) are nothing but a key constitutional document includes bye-laws or rules and regulations. The AOA governs the conduct of the company's business, the management of its internal affairs, and the relationship among its members, directors, and the company itself. It covers the matters such as making calls, forfeiture of shares, directors' qualifications, appointment, powers and duties of auditors, procedures for transfer and transmission of shares and debentures. The formation of a company in India is governed by the Companies Act, 2013. The process is systematic, ensuring compliance with legal and regulatory requirements, and involves several key stages and steps. The procedure for formation of company may divided into main three stages: (a) Promotion stage, (b) Registration stage (c) Incorporation stage, and (d) Commencement of business stage.

An Initial Public Offering (IPO) under the Companies Act 2013 marks a private company's transition to a publicly traded entity by offering shares to the public for the first time. This transition is often referred to as "going public." The process of IPO under the Companies Act 2013 have the stages such as (a) appointment of intermediaries, (b) draft red herring prospectus (DRHP), (c) stock exchange application, (d) roadshow and pricing and (e) IPO launch and subscription. IPO is a significant event where a private company offers its shares to the public for the first time, raising capital and enabling public trading of its stock.

1.4 Terms to Remember:

- 1) **Company:** Company means an association of persons formed for the economic gain of the members. The Companies Act 2013 defines a company as "a company incorporated under this Act or an existing company." 'An existing company means a company formed and registered under any of the former Companies Act. The characteristics of a company includes: it is voluntary association; it is independent legal entity; it has perpetual succession; company being artificial entity, has common seal; liability of members is generally limited; and shares of company are freely transferable.
- 2) **Share Capital:** The capital of a company is called share capital which is divided into shares.
- 3) **Share:** Share capital of a company is divided into parts having equal value is called share. A share has a nominal value or face value. It bears a distinct number. A share is ownership security. According to Section 2 (84) of Companies Act 2013, a share means "share in the share capital of a company and includes stock".
- 4) **Stock:** It is the aggregate consolidated holdings of the share capital of a person. It can be divided and transferred in any fractions and sub-divisions without regard to the original face value of the share for the purpose of convenient holding into different parts.
- 5) **Preference Shares:** Preference shares are those which carry the preferential rights over other classes of shares: A preferential right in respect of a fixed dividend and A preferential right as to repayment of the capital in the event of company's winding up.
- 6) **Equity Shares:** Equity shares are shares of a company which are not preference shares.

- 7) **Preference share capital:** As per Companies Act 2013, “preference share capital”, with reference to any company limited by shares, means that part of the issued share capital of the company which carries a preferential right with respect to the payment of dividend and the repayment of capital.
- 8) **Equity share capital:** Companies Act 2013 says “equity share capital”, with reference to any company limited by shares, means all share capital which is not preference share capital.
- 9) **Authorized Capital:** It is also called Nominal Capital or Registered Capital. It is a capital which is authorized by the company’s memorandum of association to be the maximum amount of share capital of the company [Refer Section 2(8)].
- 10) **Issued Capital:** It means such capital as the company issues from time to time for subscription [Section 2(50)].
- 11) **Subscribed Capital:** It means such part the capital which is for the time being subscribed by the members of a company [Section 2(86)]. It represents that portion of the issued capital which has been subscribed and allotted.
- 12) **Called-up Capital:** It means such part of the capital, which has been called for payment [Section 2(15)].
- 13) **Paid-up Capital:** It means such aggregate amount of money credited as paid-up as is equivalent to the amount received as paid-up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of the company, but does not include any other amount received in respect of such shares (i.e. share premium) by whatever name called [Section 2(64)].
- 14) **Memorandum of Association:** It is a foundational legal document acts as the company's charter, defining its scope, powers, and relationship with the external world. It sets out the constitution of the company and establishes its identity and scope of activities.
- 15) **Articles of Association:** According to Section 2(2) of Companies Act 2013, ‘articles’ means the articles of association of a company as originally framed or as altered from time to time in pursuance of any previous company laws or of the present Act. The AOA governs the conduct of the company’s business, the management of its internal affairs, and the relationship among its members, directors, and the company itself. It covers the matters such as making calls, forfeiture of shares, directors’ qualifications, appointment,

powers and duties of auditors, procedures for transfer and transmission of shares and debentures.

- 16) **Formation of Company:** It is process of establishing a company which include the procedure divided into main three stages: (a) Promotion stage, (b) Registration stage (c) Incorporation stage, and (d) Commencement of business stage.
- 17) **Initial Public Offering:** An Initial Public Offering (IPO) under the Companies Act 2013 is the process by which a privately held company offers its shares to the public for the first time, thereby becoming a publicly traded company. This transition is often referred to as "going public."

1.5 Answers to Check your progress

Check your progress-1: Answers:

- (a) True, (b) False, (c) True

Check your progress-2: Answers:

- (A) 1. Preference Shares, 2. Equity Share Capital, 3. Authorized Capital, 4. Equity
- (B) a) False, b) True, c) True, d) False

Check your progress-3: Answers:

- (A) 1. Memorandum of Association, 2. Name, 3. The Registered Office, 4. Articles of Association
- (B) 1. False, 2. True, 3. True, 4. True

Check your progress-4: Answers:

1. True, 2. True, 3. False, 4. True, 5. False

1.6 Exercise

A) Short Answer Questions

1. What is a company? What are different types of companies?
2. What is a share? What are different types of shares?
3. Distinguish between shares and stock.
4. Distinguish between preference share and equity share.
5. What are features of equity shares?
6. What are features of preference shares?

B) Long Answer Questions

1. Describe different concepts of share capital of a company.
2. What is the Memorandum of association? Describe the different clauses of Memorandum.
3. What is the Articles of association? Explain in details contents of Articles of association.
4. Explain the process of formation of a company.
5. What is Initial Public Offering? Explain the process of IPO.

6. Write short notes on:

- (a) Memorandum of Association
- (b) Articles of Association
- (c) Incorporation Stage
- (d) Commencement Stage
- (e) Initial Public Offering

1.7 Reference for further study

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Unit 2

Legal Provision Related to Corporate Accounting

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2.0 Objectives:

After studying this Unit you will be able to:

1. Understand Accounts related provision under companies Act 2013.
2. Explain Key aspects of company accounts according to the Companies Act. 2013
3. Describe functions of Monitoring and Regulatory Authorities.
4. Understand Corporate Governance under Companies Act, 2013

2.1. Introduction:

Corporate accounting is a specialized area within accounting that emphasizes recording, analyzing, and reporting financial transactions and facts for companies. Its goal is to offer correct and transparent financial statements that mirror the overall financial performance and economic role of an organization. In the previous topic we learn Meaning and Definition of Company, Types of companies, Types of shares, Share capital of the company, Features of Equity share & Preference shares, Memorandum of company, Articles of company, Formation of company, Meaning & Process of Initial Public Offering (IPO). Current topic is mainly focused on legal provisions related accounting of companies in Companies Act. 2013.

2.2. Presentation of Subject Matter.

2.2.1 Accounts related provision under companies Act 2013

The Companies Act, 2013 lays down comprehensive provisions related to the maintenance, preparation, and presentation of company accounts to ensure transparency, accountability, and standardization in financial reporting. Every company is required to keep proper books of accounts at its registered office, which reflect a true and fair view of its financial position and are maintained on an accrual basis using the double-entry system. As per Section 129, the financial statements must comply with the accounting standards notified under the Act and give a true and fair view of the company's affairs. Companies are also required to prepare a Board's Report, and the financial statements must be audited by a qualified Chartered Accountant. Further, companies must file these statements with the Registrar of Companies (RoC) annually. Listed companies and certain other specified companies must also comply with Indian Accounting Standards (Ind AS). These provisions aim to enhance the credibility of financial information disclosed by companies and protect the interest of stakeholders like investors, creditors, and regulators.

a) Books of Accounts to be kept by Company (Section 128):

The books of accounts showing true and fair financial statements and relevant papers shall be kept at the registered address of the company. The books shall be kept on accrual basis and according double entry system of accounting. The books of accounts and relevant papers may be kept at other place in India as BOD may decide. A seven days' notice shall be given to ROC for communication of new address. The accounts can be kept in electronic mode. The books of accounts related to branch office can be kept at the branch however proper summarised returns shall be sent to registered office periodically. The books of accounts shall be open for director's inspection at registered office or other place during business hours. The copies of financial information maintained outside India shall be produced for inspection. The inspection of subsidiary can be done only after authorization from BOD. The books of accounts of the company shall be kept in good order for a period of 8 FYs and in case investigations ordered by CG it may direct a longer period. MD, WTD in charge of finance, CFO and such other person charged by the BOD with compliance of this section, contravenes the provisions shall be punishable with imprisonment for maximum 1 year or with fine (Rs. 50,000 to Rs. 5,00,000).

b) Financial Statements (Section 129):

The financial statement – shall be prepared in Schedule III format, shall comply with the accounting standards specified in section 133 and shall give a true and fair view of the state of affairs of the company shall be laid before AGM by BOD along with the consolidated financials (prepared on the basis of same principles of standalone) in case of subsidiary, associate and JV. if do not comply with accounting standards, shall disclose the deviation, reasons and financial effect Contravention of the provisions of this section; MD, WTD in charge of finance, CFO and such other person charged by the BOD with compliance of this section and in the absence of any such officers all the directors shall be punishable with imprisonment for maximum 1 year or with fine (Rs. 50,000 to Rs. 5,00,000).

c) Reopening of accounts on court's or Tribunal's orders (Sec. 130):

Application made by CG, Income tax authority, SEBI, any other regulatory body, authority or any person concerned and an order made by a court or the tribunal stating that the accounts were prepared in fraudulent manner and the affairs of the company were mismanaged during the relevant period casting a doubt on reliability of financial statements, then a company can re-open and recast its financial statements. Court or Tribunal shall give the notice to the specified authorities and the representations made by the applicant shall be considered before passing the order. The accounts revised or recast shall be final.

d) Voluntary Revision of Financial Statements or Board's Report (Section 131):

If it appears to the directors of a company that the financial statements of the company or the board's report do not comply with the provisions of Section 129 or section 134, financial statements or the board reports for the 3 preceding financial years may be revised. For this purpose company shall make an application to Tribunal and Tribunal will pass an order. The order shall be filed with ROC by the company. Tribunal shall give notice to CG & Income Tax authorities and the representations shall be considered before passing an order by tribunal. Revised financials and report can be filed once in a financial year. Details of reasons for revision shall be stated. If the previous financial statement and board report copies are already sent to the members or ROC or laid in AGM the revision must be confined to the correction and consequential alterations.

e) Constitution of National Financial Reporting Authority (Section 132):

CG may constitute NFRA. NFRA shall – make recommendation to CG on formulation and laying down of accounting and auditing policies and standards for adoption by companies or class of companies or their auditors monitor and enforce compliance with accounting and auditing standards oversee the quality of service of the professionals associated with ensuring compliance with the standards NFRA shall consist 1 chairperson having expertise in the field of accountancy, auditing, finance or law appointed by CG and other members maximum 15. Conflict of interest and lack of independence in respect of appointment shall be declared by the member. Chairperson and members in full time employment shall not be associated with any audit firm (including consultancy firms) during the course of their appointment after ceasing their appointment. Powers of NFRA will be – To investigate professional or other misconduct done by member or firm of CAs. No other body or institute can investigate the same matter. NFRA shall have exclusive jurisdiction. Have the same powers as are vested in a civil court under the Code of Civil Procedures, 1908 while trying a suit To impose penalty (Individual – Rs. 1 Lakhs to 5 times of fees received Firms – Rs. 10 Lakhs to 10 times of fees received) or debar member or firm for a period of 6 months to 10 years, if professional or other misconduct is proved. Any person aggrieved by any order of NFRA may prefer appeal before appellate authority as prescribed.

f) Central Government to Prescribe Accounting Standards (Section 133):

AS shall be prescribed by CG, recommended by ICAI in consultation with and after examination of the recommendations made by NFRA. Financial Statements, board's report etc. FS including CFS (if any) shall be approved by BOD. FS shall be signed at least by the chairperson of the company or by two directors out of which one shall be MD and CEO if he is director , CFO and CS of the company. Auditors' report shall be attached with FS. FS and board's report shall be laid before the company in AGM. Board's report shall include – Extract of annual return Number

of meetings of the board Directors responsibility statement on declaration given by independent directors Company's policy on directors' remuneration Comment on qualifications raised in statutory audit report or secretarial report Particulars of loans, guarantees or investments under section 186 Particulars of contracts or arrangement with related parties mentioned in sec. 188 State of the company's affairs Amounts proposed to be carried forward to reserves Recommended dividend Material changes and commitments affecting the financial position Conservation of energy, technology absorption, foreign exchange earnings and outgo Statement indicating development and implementation of a risk management policy Details of CSR policy developed & implemented Annual evaluation of the board Board report shall be attached to FS. Board report shall be signed by Chairperson if authorised by board otherwise by at least two directors.

g) Corporate Social Responsibility (CSR) (Section 135):

Company having net worth Rs. 500 crores or more, turnover Rs. 1000 crores or more net profit of Rs. 5 crores or more during any financial year shall constitute a CSR Committee of the board consisting of 3 or more directors, one shall be independent director.

h) Right of the Member to Copies of Audited Financial Statement (Section 136)

Financial Statements including Consolidated Financial Statements, auditors' report and other documents which are to be laid down before AGM shall be sent to every member and trustee of debenture holder and all other required persons at least before 21 days of AGM. In case of listed company these documents can be kept for inspection at least before 21 days of AGM.

i) Copy of Financial Statements to be filled with Registrar (Section 137):

The financial statements including consolidated financial statements shall be filed with Registrar within 30 days from the date of AGM.

Check your progress: 1

Choose appropriate alternative :

1. Section 128 of Companies Act 2013 explains regulations related to

- a. Books of accounts to be kept by Company
- b. Financial Statements
- c. Voluntary revision of financial statements
- d. constitution of NFRA

2. As per Section 128, for how many years must a company preserve its books of accounts?

- | | |
|------------|-------------|
| A) 5 years | B) 7 years |
| C) 8 years | D) 10 years |

3. Which body has the power to investigate professional misconduct by chartered accountants under Section 132?

- | | |
|---------|---------|
| A) ICAI | B) SEBI |
| C) NFRA | D) RoC |

4. Voluntary revision of financial statements is allowed for how many preceding financial years under Section 131?

- | | |
|------------|--------------|
| A) 2 years | B) 3 years |
| C) 5 years | D) Unlimited |

5. Who recommends accounting standards to the Central Government under Section 133?

- | | |
|---------|---------|
| A) SEBI | B) NFRA |
| C) ICAI | D) RoC |

6. According to Section 136, financial documents must be sent to members before ----- days of AGM?

- | | |
|------------|------------|
| A) 7 days | B) 14 days |
| C) 21 days | D) 30 days |

7. Which section allows reopening of accounts by a court or tribunal?

- | | |
|----------------|----------------|
| A) Section 130 | B) Section 128 |
| C) Section 133 | D) Section 136 |

2.2.2 Key Aspects of Company Accounts According to the Companies Act 2013

The companies Act 2013, outlines key aspects of company accounting, emphasizing transparency, accuracy & compliance. Key requirements include maintain proper books of accounts, adhering to specific accounting to specific accounting standards & preparing & filling financial statements. Additionally the Act addresses the appointment & responsibilities of auditors, along with provisions for penalties in case of non-compliance.

Key Aspects are as Follows:**a) Maintenance of Books of Accounts (Section 128)**

Every company must maintain proper books of account at its registered office. These should show all money received and spent, sales and purchases, assets and liabilities, and cost records (if applicable). They can be maintained electronically too, but must be accessible in India. The books must provide a true and fair view of the financial position of the company. They must be preserved for at least 8 years. The directors can inspect them during business hours. If a company does not maintain proper books, it can be fined and officers may be punished.

b) Preparation of Financial Statements (Section 129)

Every company must prepare financial statements at the end of each financial year. These include the Balance Sheet, Profit and Loss Account, Cash Flow Statement, Statement of changes in equity, and Notes to Accounts. These must comply with the Accounting Standards notified by the central government. They should reflect the true and fair view of the company's financial affairs. Companies with subsidiaries must prepare consolidated financial statements. Financial statements must be approved by the board and signed by directors.

c) National Financial Reporting Authority (NFRA) (Section 132)

The NFRA is a body established under the Act to oversee compliance with accounting and auditing standards. It has the power to investigate professional misconduct by chartered accountants and auditing firms. It ensures that companies and auditors follow high-quality financial reporting practices. NFRA can impose penalties and take disciplinary action if necessary.

d) Board's Report (Section 134)

The financial statements must be attached with a Board's Report, which is prepared by the directors. This report explains the financial performance, future plans, major decisions, CSR details, and risk management strategies of the company. The Board's Report must be signed by the chairperson or at least two directors (one of them must be the managing director, if any). It helps shareholders understand the company's performance beyond just numbers.

e) Circulation and Filing of Financial Statements (Section 136 & 137)

The company must send financial statements and the Board's Report to all shareholders at least 21 days before the Annual General Meeting (AGM). Listed companies must place these documents on their website. After adoption in the AGM, the company must file the financial statements with the Registrar of Companies (RoC) using Form AOC-4 within 30 days. Delay or failure to file attracts penalties.

f) Auditor's Report (Section 143)

An auditor must examine the financial statements and provide an audit report. This report must state whether the statements give a true and fair view of the company's financial condition. Auditors must also report any frauds found during their work. The Act gives auditors the power to access all books and records. Companies must appoint statutory auditors and rotate them every 5 or 10 years depending on the type of firm.

g) Internal Audit (Section 138)

Certain classes of companies (like listed companies, and large private or public companies) must appoint an internal auditor. Internal audit is done to examine internal controls and ensure efficient operations. The internal auditor may be a chartered accountant, cost accountant, or other professional. This is important for large companies to avoid fraud and improve internal management.

h) Re-opening and Voluntary Revision of Accounts (Section 130 & 131)

Accounts can be reopened only by order of a court or tribunal if there is a fraud or mistake. Voluntary revision is allowed only if the Board feels that the earlier financial statements or Board's Report did not comply with the law. Permission must be taken from the tribunal to revise the documents. This ensures transparency and correction of errors in financial reporting.

i) Maintenance of Cost Records (Section 148)

Certain companies involved in manufacturing, production, or services must maintain cost records. These records track the cost of production, operations, and profit margins. The Cost Audit may also be applicable, and a Cost Auditor must be appointed. The cost audit report must be submitted to the Board and filed with the RoC. This is to ensure that the pricing of goods/services is fair and not manipulated.

j) Penalties for Non-Compliance

If a company fails to maintain books, file returns, or follow accounting standards, it faces heavy penalties. The company and its responsible officers may be fined or even imprisoned. For example, not filing financial statements can lead to daily fines until the default is corrected. These penalties ensure that companies take their accounting responsibilities seriously.

Check your progress: 2

Choose appropriate alternative :

1. Every company must maintain proper books of account at its -----

a. Branch

b. registered office.

c. Director's Office

d. Accountant's Office

2. NFRA has the power to investigate professional misconduct by -----
 - a. Share Holders
 - b. Directors
 - c. Accountants
 - d. chartered accountants and auditing firms.
3. The ----- gives auditors the power to access all books and records.
 - a. Section 143
 - b. Section 138
 - c. Section 129
 - d. Section 140
4. ----- must examine the financial statements and provide an audit report.
 - a. An Accountant
 - b. An auditor
 - c. A Shareholder
 - d. A Director
5. Financial Statement include ----
 - a. Balance Sheet, Profit and Loss Account.
 - b. Cash Flow Statement.
 - c. Statement of changes in equity.
 - d. All the above.

2.2.3 Monitoring and Regulatory Authorities

The Companies Act, 2013, established a robust framework for ensuring transparency and regulatory oversight within the corporate sector in India. Chapter XIV of the Act empowers the government to inspect, inquire, and investigate companies through various statutory authorities such as the Registrar of Companies (ROC), Regional Directors, and the Central Government. For handling serious fraud cases, the Serious Fraud Investigation Office (SFIO) plays a crucial role, with powers to arrest individuals involved in specific offenses.

The purpose of these mechanisms is not only to detect and prevent corporate malpractices but also to safeguard the interests of shareholders, investors, and the general public. By establishing stringent oversight and control, these provisions serve as the backbone of corporate governance and compliance, promoting accountability within the corporate structure.

2.2.3.1. Ministry of Corporate Affairs (MCA)

The Ministry of Corporate Affairs is the governmental agency responsible for corporate governance, company law, and compliance in India. It ensures business is conducted openly, in adherence to the Companies Act, 2013, and in keeping with ethical corporate standards. The MCA also plays a central role in the registration of

companies, oversight of financial disclosures, safeguarding investors, and imposing corporate laws. With the digitalization of corporate services, the MCA introduced online portals like the MCA21 portal, which allows business enterprises to register companies, submit returns, and access corporate documents effectively.

Ministry of Corporate Affairs is an important wing of the Indian Government that regulates corporate entities, implements business laws, and promotes corporate governance. It governs the Companies Act, 2013, the Limited Liability Partnership (LLP) Act, 2008, and other legislation concerning business regulation, financial disclosure, and competition policy. With the growing number of startups, MSMEs, and big businesses, the MCA regulates that companies abide by legal protocols and corporate principles to ensure investor confidence and financial stability. The ministry has also streamlined company registration, compliance filings, and corporate governance monitoring under its MCA21 e-Governance scheme, making it simpler for businesses to conduct their activities in an open manner.

Functions of the Ministry of Corporate Affairs

a) Registration and Compliance of Company

The MCA registers new companies and LLPs under the Companies Act, 2013. Businesses can apply for company incorporation, name approval, and statutory compliance filings through the MCA21 portal. The ministry verifies that companies comply with legal requirements before they begin operations.

b) Corporate Law Enforcement

The MCA imposes corporate legislations to make businesses follow financial, governance, and operational standards. It ensures adherence to laws such as the Companies Act, 2013, the Limited Liability Partnership Act, 2008, and the Insolvency and Bankruptcy Code (IBC), 2016 to prevent fraudulent practices.

c) Regulation of Corporate Governance

For the promotion of ethical business, the MCA sees to it that corporate governance principles, such as board structure, audit requirements, and disclosure guidelines, are met by companies. It monitors corporate behavior to prevent mismanagement, fraud, and financial malpractices.

d) Investor Interest Protection

The MCA protects investors from corporate malpractice and fraud. It enforces regulations regarding issuance of securities, shareholder rights, and fair business practices. It also monitors Corporate Social Responsibility (CSR) activities to ensure that businesses help in the development of society.

e) Dealing with Corporate Insolvency and Liquidation

Under the Insolvency and Bankruptcy Code 2016, the MCA regulates the resolution of financially struggling companies. It enables insolvency proceedings to see that creditors and stakeholders get the dues through defined processes.

f) Digital Transformation of Corporate Services

The MCA launched the MCA21 e-Governance project, under which companies are able to do company registration, annual filings, and compliance submissions online. This has improved transparency, efficiency, and access in corporate governance.

h) Supervising Statutory Bodies and Regulatory Authorities

The MCA regulates major regulatory authorities, namely-

- *Registrar of Companies (ROC)* – Manages the registration of companies and the monitoring of compliance.
- *Serious Fraud Investigation Office (SFIO)* – Investigates company fraud and financial irregularities.
- *National Company Law Tribunal (NCLT)* – Deals with company disputes, mergers, and insolvency cases.

i) Managing Corporate Social Responsibility (CSR) Compliance

Under the Companies Act, 2013, those companies meeting certain financial thresholds are mandated to donate a share of their profits towards CSR. The MCA monitors if the companies are depositing their CSR funds, with donations going into education, healthcare, environmental protection, and social welfare programs.

j) Controlling Corporate Mergers and Acquisitions

The MCA is responsible for imposing sanctions, watching over, and regulating mergers, acquisitions, and demergers to preserve fair business processes. It co-operates with regulatory bodies such as SEBI and CCI to scrutinize monopolistic acts and unfair business practices and certify that corporate transactions are compliant with legal and financial standards.

k) Curbing Corporate Fraud and Financial Misdeeds

By way of investigating agencies such as the Serious Fraud Investigation Office (SFIO), the MCA proactively investigates and acts against corporate fraud, insider trading, false representation of financial statements, and fraudulent trade practices. It keeps the corporates transparent and maintains investor trust in the Indian market.

2.2.3.2. Securities and Exchange Board of India (SEBI)

SEBI plays a crucial role in regulating the securities market, including aspects related to the Companies Act, 2013, specifically concerning the issuance and transfer of securities. While the Companies Act primarily governs the formation and operations of companies, SEBI's role is to ensure fair practices, transparency, and investor protection within the securities market, which includes listed companies.

Functions of SEBI in relation to the Companies Act, 2013:

a) Regulation of Securities Issuance and Transfer:

SEBI regulates the issuance of securities (like shares and debentures) by companies, including initial public offerings (IPOs) and further public offerings, ensuring compliance with regulations and preventing misleading information. It also oversees the transfer of securities, ensuring transparent and lawful procedures are followed. SEBI's regulations provide the procedural and disclosure requirements for these processes.

b) Investor Protection:

A primary function of SEBI is to safeguard investor interests in the securities market. This includes ensuring listed companies provide accurate and timely information to investors, preventing insider trading and fraudulent practices, and taking action against those who violate regulations. SEBI also educates investors about the risks and rewards of investing in securities and provides grievance redressal mechanisms.

c) Market Integrity:

SEBI works to maintain the integrity of the securities market by preventing fraud, market manipulation, and insider trading. It sets regulations and guidelines for market participants, including stock exchanges, brokers, and listed companies, to promote fair and transparent practices.

d) Regulation of Market Intermediaries:

SEBI registers and regulates various market intermediaries such as stockbrokers, merchant bankers, and investment advisors, ensuring their proper functioning and adherence to regulations.

e) Regulation of Takeovers and Acquisitions:

SEBI monitors and regulates substantial acquisitions of shares and takeovers of companies to ensure fair treatment of all shareholders.

f) Enforcement and Oversight:

SEBI has enforcement powers to investigate violations of securities laws and regulations, impose penalties, and take action against those who engage in fraudulent

or unfair practices. It can also conduct inspections, audits, and inquiries to ensure compliance with regulations.

f) **Promoting Development of the Securities Market:**

SEBI also focuses on the development of the securities market by introducing new products and technologies, improving market infrastructure, and promoting investor education. In essence, SEBI acts as a watchdog for the securities market, ensuring its smooth and fair functioning while protecting the interests of investors and promoting market development.

2.2.3.3. National Company Law Tribunal (NCLT)

The National Company Law Tribunal, which is a quasi-judicial body created in India with the purpose of deciding the matters of company law under the Companies Act, 2013, has replaced the Company Law Board (CLB) and absorbed the different functions performed by the High Courts, BIFR, and AAIFR earlier. NCLT plays an important role in law governed by regulating and resolving corporate disputes in India. NCLT has been established to simplify and streamline the law of procedure as it regards companies and to bring efficiency to corporate adjudication. This formation of NCLT meant integrating all the judicial and quasi-judicial authorities, which came under the single roof of an integrated platform to resolve any matters regarding company law. The NCLT, redresses of mergers and demergers, insolvency, shareholder disputes, or mismanagement about companies can be made possible in a more efficient manner as part of the pursuit of improvement in corporate governance through timely adjudication.

Functions of NCLT

a. **Adjudication of Company Law Matters**

NCLT decides cases on corporate governance, shareholder disputes, and directorial misconduct. It applies the Companies Act, 2013 provisions in its judgments on companies.

b. **Approvals for mergers, demergers, and Restructuring**

NCLT approves merger/demerger plans/restructuring schemes and enquires whether such arrangements are per the law and whether the interests of stakeholders are adequately protected. It tests the fairness of such arrangements and safeguards the interests of minority shareholders also in M&A deals.

c. **Insolvency and Bankruptcy Laws**

NCLT is the primary adjudicating authority for corporate insolvency proceedings under the IBC, 2016. It either revives a company or liquidates it to settle creditors' claims.

d. Prevention of Oppression and Mismanagement

NCLT intervenes where minority shareholders or members are oppressed or mismanaged by the majority. It protects the interests of shareholders by having measures like the removal of existing management or reorganization of a company.

e. Winding-Up of Companies

NCLT regulates proceedings for winding up companies: voluntary and on a decree of a court. Liquidation of companies and distribution of assets among all stakeholders with regard to settling debts and liabilities is carried out with perfection.

f. Reduction of Share Capital

Requests relating to reductions in share capital are dealt with by NCLT to ascertain whether the process fulfills legal requirements. It examines whether the reduction affects the rights of the creditors and protects the interests of the stakeholders.

g. Depositor and Creditor Grievance Redress

NCLT hears grievances from the depositors and creditors and renders fair treatment and speedy action against the defaulting companies. It redresses grievances on a non-payment or fraudulent basis.

h. Revival of Dormant Companies

NCLT has the authority to revive companies that have been lodged for strike-off from the register of companies by the Registrar of Companies. It enables dead companies to start working when their essential needs are met.

i. Appeal against Registry of Companies decisions/orders

NCLT disposes of appeals filed against any decision/order made by the Registry of Companies. It provides an opportunity to the companies as well as other individuals to file appeals once wrongful decisions have been meted out.

j. Enquiry of Company Affairs

NCLT can conduct an inquiry about the company's matters if there is a suggestion of fraud or malpractice. It becomes an order to the regulatory authorities, like the Serious Fraud Investigation Office (SFIO), for instance, to carry out an investigation.

2.2.3.4 National Financial Reporting Authority (NFRA)

In the Companies Act, 2013, the National Financial Reporting Authority (NFRA) is an independent regulatory authority established under Section 132. Its primary function is to oversee and ensure the quality of accounting and auditing

standards in India. It acts as a watchdog to enhance investor and public confidence in financial disclosures of companies.

Functions of NFRA

a. Recommend Accounting and Auditing Standards

NFRA recommends accounting and auditing standards to the Central Government for adoption. These standards are crucial because they ensure that all companies follow uniform principles in preparing their financial statements and conducting audits. This helps in making company accounts transparent and comparable across sectors and industries.

b. Monitor and Enforce Compliance

NFRA monitors the compliance of companies and auditors with accounting and auditing standards. If any company or auditor violates the rules, NFRA has the power to investigate and take disciplinary action. This enforcement ensures that the financial data published by companies is reliable and trustworthy.

c. Oversee Quality of Services

It oversees the quality of services provided by professionals like Chartered Accountants in the field of auditing and accounting. NFRA ensures that auditors perform their duties ethically and professionally. Poor quality audits can mislead investors and damage the financial system, so NFRA plays a key role in maintaining high standards.

d. Investigate Misconduct

NFRA can investigate cases of professional misconduct by Chartered Accountants or audit firms. It has the same powers as a civil court for gathering evidence, summoning witnesses, etc. If a professional is found guilty, NFRA can impose penalties and even debar the professional or firm from auditing for up to 10 years.

e. Maintain Data and Records

It maintains detailed data related to companies' financial reporting and auditing. This includes databases of auditors, audit reports, disciplinary actions, etc. Such records are useful for future reference, trend analysis, and policy-making.

f. Promote Awareness and Training

NFRA also works to educate and train auditors and accountants. It may conduct workshops, publish guidance notes, or hold consultations to improve the overall quality of accounting and auditing in India. This helps professionals stay updated with new developments and global best practices.

g. Provide Guidance to the Government

The authority advises the Central Government on matters related to accounting and auditing. For example, if there is a need to change an existing standard or introduce a new one, NFRA can guide the government based on current trends and requirements.

h. Coordinate with International Bodies

NFRA interacts with foreign regulators and international bodies like the International Financial Reporting Standards (IFRS) Foundation. This helps in aligning India's accounting and auditing standards with global norms, making Indian companies more investor-friendly in international markets.

i. Protect Public Interest

By ensuring that financial reports and audits are accurate and honest, NFRA safeguards the interests of investors, creditors, and the general public. It plays a crucial role in maintaining trust in the corporate sector.

j. Disciplinary Powers

NFRA can impose strict disciplinary actions like:

- Monetary penalties (up to ₹25 lakhs for individuals, ₹5 crores for firms)
- Debarring professionals from auditing for a period (up to 10 years)

This authority helps in maintaining accountability among auditors and professionals.

2.2.3.5. Institute of Chartered Accountants of India (ICAI)

The Institute of Chartered Accountants of India (ICAI) is a statutory body established under the Chartered Accountants Act, 1949. Although the Companies Act, 2013 does not directly establish ICAI, the Act recognizes and relies on ICAI in its framework, especially for regulating the profession of Chartered Accountants (CAs), who play a vital role in company audits and financial reporting. ICAI acts as a regulatory authority for Chartered Accountants, and its role and functions support the objectives of the Companies Act, 2013. Below is a detailed explanation of ICAI's role and functions under the Companies Act and in the corporate regulatory system:

Role and Functions of ICAI as a Regulatory Authority in Companies Act, 2013:

a. Regulation of the Chartered Accountancy Profession

ICAI is responsible for licensing and regulating Chartered Accountants (CAs) in India. Under the Companies Act, 2013, only qualified and ICAI-registered CAs are allowed to conduct statutory audits of companies. ICAI ensures that CAs follow ethical standards and professional guidelines while auditing company accounts.

b. Issuing Accounting Standards

ICAI plays a crucial role in formulating Accounting Standards (AS) in India. These standards were earlier notified under the Companies Act, 1956, and now continue under the Companies Act, 2013. Though final approval lies with the Ministry of Corporate Affairs (MCA), ICAI prepares the draft standards which companies must follow while preparing their financial statements.

c. Issuing Auditing Standards

Similarly, ICAI issues Standards on Auditing (SAs), which auditors must follow while conducting audits of company accounts. These standards ensure uniformity, transparency, and reliability in the auditing process as per the requirements of the Companies Act.

d. Providing Guidance on Corporate Financial Reporting

ICAI provides guidance notes, expert opinions, and clarifications on various accounting and auditing issues. These documents help companies and auditors correctly interpret and implement provisions of the Companies Act related to financial reporting.

e. Disciplinary Mechanism

ICAI has the power to discipline its members for misconduct, especially in cases where CAs fail to comply with the Companies Act or auditing standards. Though the National Financial Reporting Authority (NFRA) now investigates serious cases involving listed and large companies, ICAI still handles disciplinary cases of other companies and members.

f. Training and Capacity Building

ICAI organizes training programs, seminars, workshops, and publishes journals to ensure that its members are updated with changes in the Companies Act, accounting standards, auditing techniques, and other corporate laws. This ensures high professional competence among CAs working with companies.

g. Interface with MCA and Other Authorities

ICAI regularly works with the Ministry of Corporate Affairs (MCA) to develop and revise regulations under the Companies Act. It also interacts with SEBI, RBI, and other regulators to ensure integrated development of financial reporting and auditing frameworks.

h. Supporting Implementation of Ind AS

The Companies Act, 2013 provides for the adoption of Indian Accounting Standards (Ind AS), which are converged with IFRS. ICAI plays a major role in formulating, interpreting, and helping companies implement these standards correctly.

i. Certifications and Audit Reports

Many provisions of the Companies Act require certification by a Chartered Accountant. For example:

- Certification of financial statements
- Audit reports on internal controls
- Valuation reports ICAI governs how such certifications and audits are conducted.

j. Upholding Corporate Governance

By ensuring ethical and professional conduct among auditors, ICAI supports the corporate governance framework under the Companies Act. Reliable audits enhance investor confidence and promote transparent corporate behavior.

2.2.3.6. The Registrar of Companies:

The Registrar of Companies (ROC) as the gateway to the corporate world. Every company's journey begins and often ends with this authority. The ROC serves as the primary interface between companies and the government, handling everything from birth certificates (incorporation) to death certificates (winding up) of companies. The ROC operates at the state level, with each state having its own registrar. This decentralized approach ensures that companies can access services locally while maintaining uniform standards across the country. When anyone decides to start a company, the ROC is where he or she'll file their incorporation documents, and throughout the company's life, They'll regularly interact with this office for various compliance requirements.

Functions of the ROC include:

a. Company registration:

Processing incorporation applications and issuing certificates of incorporation

b. Document Filing:

Receiving and processing annual returns, financial statements, and other mandatory filings

c. Name Approval:

Ensuring company names comply with regulations and don't conflict with existing entities

d. Compliance Monitoring:

Tracking whether companies meet their filing obligations and taking action against defaulters

e. **Public Records Maintenance:**

Keeping comprehensive records accessible to the public for transparency

The ROC also has enforcement powers, including the ability to strike off companies that fail to comply with statutory requirements. This makes maintaining a good relationship with your local ROC essential for smooth business operations.

2.2.3.7. Regional Directors:

Regional Directors represent the next level of authority in the corporate hierarchy. While the ROC handles day-to-day administrative functions, Regional Directors focus on supervision, inspection, and ensuring broader compliance with the Companies Act. India is divided into several regions, each headed by a Regional Director who oversees multiple ROCs within their jurisdiction. This structure creates a supervisory layer that can address complex issues requiring higher-level intervention while maintaining the efficiency of local operations.

Powers and Responsibilities of Regional Directors

Regional Directors wield significant authority in corporate governance. They can conduct inspections of companies when irregularities are suspected, investigate complaints about company operations, and take action against companies that violate the Act. Their role becomes particularly important when dealing with inter-state companies or issues that span multiple ROC jurisdictions. These authorities also play a crucial role in approving certain corporate actions that require regulatory clearance. For instance, if a company wants to change its registered office from one state to another, the Regional Director's approval becomes necessary. They also handle appeals against ROC decisions, providing a mechanism for companies to challenge administrative actions.

Functions of Regional Director's:

Choose appropriate alternative :

a. **Supervision of ROCs:**

Ensuring uniform application of laws across different registration offices

b. **Inspection and Investigation:**

Conducting detailed examinations of company affairs when warranted

c. **Approval Functions:**

Sanctioning specific corporate actions that require regulatory consent

d. **Appellate Functions:**

Hearing appeals against ROC decisions and orders

Check your progress: 3

Choose appropriate alternative :

1. Which body is the primary regulator for corporate affairs in India under the Companies Act, 2013?
A. RBI
B. SEBI
C. MCA
D. ICAI
2. Which authority regulates the functioning of Chartered Accountants in India?
A. SEBI
B. MCA
C. ICAI
D. RBI
3. Which authority regulates listed companies and securities market in India?
A. NFRA
B. SEBI
C. ICAI
D. RBI
4. Which of the following is not a function of the Ministry of Corporate Affairs (MCA)?
A. Regulating Company law
B. Administering the LLP Act
C. Monitoring stock market
D. Supervising corporate governance
5. ICAI is primarily responsible for:
A. Issuing securities
B. Framing accounting standards
C. Conducting Company audits
D. Regulating mergers and acquisitions
6. SEBI was established under which act?
A. Companies Act, 2013
B. Securities Contracts Act, 1956
C. SEBI Act, 1992
D. RBI Act, 1934
7. The Registrar of Companies (ROC) works under which authority?
A. RBI
B. SEBI
C. MCA
D. NFRA

2.2.4. Corporate Governance under the Companies Act, 2013

2.2.4.1. Meaning and Definitions

Corporate Governance is a multi-faceted subject and difficult to comprehend in a concise definition. The main theme of corporate governance is to integrate sound management policies in the corporate framework in such a manner to bring economic efficiency in the organization in order to achieve twin goals of profit maximization and shareholder welfare. Few comprehensive definitions on Corporate Governance are discussed below.

- Institute of Company Secretaries of India-

“Corporate Governance is the application of best Management Practices, Compliance of Laws in true letter and spirit and adherence to ethical standards for effective management and distribution of wealth and discharge of social responsibility for sustainable development of all stakeholders.”

- Mathiesen [2002]

“Corporate Governance is a field in economics that investigates how to secure/motivate efficient management of corporations by the use of incentive mechanisms, such as contracts, organizational design and legislation. This is often limited to the question of improving financial performance, for example, how the corporate owners can secure/motivate that the corporate managers will deliver a competitive rate of return.”

- The Cadbury Committee U.K, defined corporate governance as follows-

“It is a system by which companies are directed & controlled.”

2.2.4.2. Emergence of Corporate Governance in India

Corporate Governance is the new golden term coined in the corporate sector in the late 1990's by the industry Association on Confederation of India Institute which Association On Confederation of India Institute which was the first initiative in India as a voluntary measure to be adopted by Indian companies. It has outlined a series of voluntary recommendations to integrate best-in-class practices of corporate governance in listed companies which touches the four cornerstones of fairness, transparency, accountability and responsibility in managing the affairs of the company. The second major initiative was taken by Security Exchange of India (SEBI) as Clause 49 of the Listing Agreement. The third key initiative to effectively introduce Corporate Governance was taken by Naresh Chandra Committee and Narayana Murthy Committee who previewed Corporate Governance model working in companies from the viewpoint of shareholders, investors and other stakeholders of the company. Corporate governance guidelines both mandated and voluntary have evolved since 1998, due to the sincere efforts of several committees appointed by the Ministry of Corporate Affairs (MCA) and the SEBI. The real change in the corporate

sector could be felt with the introduction of 2009 Mandatory Corporate Governance Voluntary Guidelines which has to be comply by companies listed on stock exchange by Clause 49 of Listing Agreement including mandatory codes to be followed by companies pertaining to board of directors, audit committees and various disclosures with respect to related party transaction, whistleblower policies etc. the final assent to Corporate governance practices in the effective management of the company can be seen as introduction to new significant provision introduced in the Companies Act, 2013 in form of independent directors, women directors on the board, corporate social responsibility and mandatory compliance of Secretarial Standards issues by Institute of Company Secretarial Standards issue by Institute of Company Secretaries of India as per Section 118 of Companies Act, 2013.

2.2.4.3. Key Components of Corporate Governance under the Companies Act 2013:

1. Board of Directors:

The companies Act 2013 emphasizes the pivotal role of the board of directors in governing the affairs of a company. It mandates the appointment of independent director and specifies their roles and responsibilities to enhance board effectiveness and decision-making.

2. Audit Committee:

The act mandates the constitution of an audit committee comprising independent directors to oversee financial reporting, internal control, and audit processes. This committee plays a crucial role in ensuring transparency and integrity in financial disclosures.

3. Disclosure and Transparency:

The Companies Act 2013 promotes transparency and disclose essential information to stakeholders, including financial statements, related-party transaction, and corporate governance practices. Such disclosures foster investor confidence and mitigate the risk of corporate malpractices.

4. Shareholder Rights:

The Act recognizes and safeguards the right of shareholders, empowering them to participate in key corporate decisions through voting mechanisms, access to information, and avenues for grievances redress. Shareholder activism is encouraged to hold the management accountable and promote long-term value creation.

2.2.4.4. Significance of Corporate Governance

Effective corporate governance under the Companies Act 2013 is instrumental in achieving the following objective:

1. Enhancing Investor Confidence:

Transparent and accountable corporate governance practices instill trust among investors, fostering capital inflows and market stability.

2. Mitigating Risks:

Robust governance mechanisms mitigate risks associated with fraud, conflicts of interest, and mismanagement, safeguarding the interest of stakeholders.

3. Promoting Sustainable Growth:

Sound governance practices foster sustainable business growth by ensuring ethical conduct, compliance with regulatory requirements and alignment of corporate objective with societal expectations.

4. Fostering Stakeholder Engagement:

Corporate governance facilitates constructive engagement with stakeholder, including shareholders, employee, customer, and communities, thereby promoting stakeholder welfare and inclusive growth.

The Companies Act 2013 represent a significant milestone in India's corporate governance landscape, aiming to instill a culture of transparency, accountability, and integrity in corporate practices. By adhering to the principles outlined in the Act, companies can enhance their competitiveness, mitigate risks, and create long-term value for all stakeholders. Embracing robust corporate governance practices is imperative for organizations aspiring to thrive in today's dynamic business environment.

2.2.4.5. Need of Corporate Governance-

The collapse of international giants like Enron, Worldcom, Tyco, AOL and financial scams like Satyam have been big eye-openers in the corporate arena to make realize the company's management, ownership and stakeholders the emergent need to comply with Corporate Governance principles in order to prevent themselves from paying huge corporate criminal liabilities in the future. These huge corporate giants paid the cost for lack of good corporate governance practices and corrupt. Policies adopted by management of these companies and their financial consulting firms.

The significance of good corporate governance solutions has widened because of the increasing conflict between ownership and management disciplines, the non-compliance of financial reporting by auditors which inflicts heavy losses on investors

and lack of fair and transparent culture in the company which shook's investors trust in the financial viability of the company and its ethical standards.

2.2.4.6. Scope of Corporate Governance-

Corporate governance instils ethical standards in the company. It creates space for open dialogue by incorporating transparency and fair play in strategic operations of the corporate management.

1. Accountability of management to shareholders and other stakeholders.
2. Transparency in basic operations of the company and integrity in financial report produced by the company.
3. Component Board comprising of Executive and Independent Directors
4. Check & balance is an integral part of good corporate governance.
5. Adherence to the rules of the company in law and spirit.
6. Code of responsibility for Directors and employees of the company.
7. Open dialogue between management and stakeholders of the company.
8. Investor loyalty is a guarantor of good corporate governance practices.

A component board comprising of experienced professional and active directorship who brings rich experience and intellectual vision on the board resulting in a greater economic efficiency of the shareholders and key stakeholders of the company as they become trusted market players in the corporate sector enjoying everlasting market repute.

2.2.4.7. Core principles of Corporate Governance-

1. Transparency-

The stakeholders should be informed about the company's activities, financial statements, and the organization's performance and also at the same time it is very important to give accurate and precise information to the shareholders. Poor transparency reduces the ability to raise more capital as the investors will be unaware of vital information. It also leads to less trust among the investor as a company that is financially stable and doing well will not have anything to hide. Moreover, companies that are doing well will like to make the financial statements public to promote themselves. Transparency in financial reporting increase the confidence of the shareholders will help

them. The policies must be formulated in a manner which ensures transparency.

Transparency should also be maintained between directors and employee. The directors should be easily accessible by the employees and directors should be open to ideas of the management and employees. This makes employees more committed to the vision of the company. Lack of transparency will always lead to confusion and it will hinder productivity of the management and employee.

2. Accountability-

To achieve the goals and objective of the company, people should be held accountable at all levels. Employee should be accountable to the management, management should be accountable to the board of directors and the board of directors should be accountable to investors and shareholders. Employee's management staff and directors will learn from the mistakes if they are made accountable and it leads to better utilization of the available resources. In this way the organization will grow faster as the scope for mistake will reduced considerably. It is the duty of directors to encourage accountability in the organization.

3. Responsibility-

The directors of the company are primarily responsible to the shareholders, employees and the whole society. The directors of the company should work in the best interests of the company and its employee. It is the duty of the directors to determine the responsibility of the management and employee. Also management and employee should be held accountable to make sure that responsibilities are carried out properly. Shareholders want directors to be responsible to their needs and maximize the value of the firm.

4. Fairness-

Fairness principle not only enhance corporate value but it also leads to efficiency in resource allocation. All shareholders and investors should receive equal treatment by the company and the directors should try to prevent conflict of interest. It is very important to ensure fairness in the transactions which are entered by the company. For e.g. a company should not enter into related party transactions without getting the approval of the shareholders. Effective communication mechanisms. Should be adopted by the company to make sure policies and financial statements are informed to the shareholders.

5. Shareholders Engagement-

Shareholders should not be kept in the dark must be informed of the financial position and organizational objectives. Minority and majority shareholders should be treated equally. All transaction must be avoided which might lead to conflicts with the shareholders.

6. Leadership-

Board of directors is the brain of any company and it is under their leadership and guidance that any company expands and prospers. The directors should be committed to fulfilling the vision and mission of the company which is mentioned the constitution documents. Leadership also include motivating the employees so that they reach the maximum potential. It also includes effective decision making and capitalize on opportunities to benefit the firm. Poor leadership by the board can create problem for the company and which may eventually end in bankruptcy or shutting down.

2.2.4.8. Corporate Governance Issues in India

Although there are numerous issued in the field of corporate governance, particularly in India, an effort has been made to highlight only the most significant ones here...

1. Performance of the Board:

At least one female director is required, and the balance of executive and non-executive directors is not maintained. Evaluation is not done on a regular basis, and transparency has been lost somewhere. The performance is not oriented toward results. These standards are not always met.

2. Problem pertaining to Independent Directors:

Independent directors are appointed for a reason that does appear to be met in the current situation. Even after SEBI guidelines for the provision of a comprehensive definition of independent directors were issued to corporations, the actual situation appears to be worse.

3. Stakeholder Accountability:

The accountability does not stop with the shareholders or the company, it extends to society as a whole as well as the environment. The directors must consider not only their own interests, but also the interests of the community.

4. Management of Risks:

The risk management techniques must be implemented by the directors in accordance with the Company Law, and they must also be mentioned in their annual report to shareholders. This is not done with the utmost sincerity requires for the job.

Check your progress: 4

Choose appropriate alternative :

1. What does MCA stand for in the context of the Companies Act, 2013?
 - A) Ministry of Corporate Accounting
 - B) Ministry of Corporate Affairs
 - C) Management of Companies Act
 - D) Ministry of Commerce Administration
2. ----- is NOT a function of the Ministry of Corporate Affairs (MCA)?
 - A) Regulating corporate governance
 - B) Registration and regulation of companies
 - C) Laying down tax policies
 - D) Administering the Companies Act, 2013
3. What is the main function of the National Financial Reporting Authority (NFRA)?
 - A) Monitor banking sector compliance
 - B) Recommend taxation reforms
 - C) Regulate accounting and auditing standards
 - D) Issue business licenses
4. Who appoints the Chairperson and members of the NFRA?
 - A) Reserve Bank of India
 - B) SEBI
 - C) Central Government
 - D) ICAI
5. Which regulatory authority is responsible for recommending Accounting Standards to the Central Government?
 - A) MCA
 - B) SEBI
 - C) ICAI
 - D) RBI

6. What is SEBI's primary function in the context of corporate regulation?
- A) Managing government shareholdings
 - B) Regulating insurance companies
 - C) Protecting investors and regulating securities markets
 - D) Approving financial statements

2.3 Summary:

The Companies Act, 2013 provides a comprehensive legal framework for the preparation, maintenance, and presentation of company accounts. Section 128 requires every company to prepare and maintain proper books of account on an accrual basis and double-entry system at its registered office. These books should give a true and fair view of the company's affairs, and they must be kept open for inspection by directors. Section 129 mandates the preparation of financial statements, including balance sheet, profit and loss account, cash flow statement, statement of changes in equity, and notes to accounts, in compliance with prescribed accounting standards. Section 130 allows a company's accounts to be reopened or revised, but only under special circumstances such as fraud, mismanagement, or misrepresentation, and only with prior approval of the Tribunal or relevant authority. Section 131 permits voluntary revision of financial statements by companies when errors are discovered, subject to Tribunal approval. Section 132 establishes the National Financial Reporting Authority (NFRA), which oversees auditing and accounting standards, ensuring professional discipline among auditors. Section 133 empowers the Central Government to prescribe accounting standards recommended by ICAI. Importantly, Section 135 introduces the concept of Corporate Social Responsibility (CSR), making it mandatory for eligible companies to spend at least 2% of average net profits on approved CSR activities. Finally, Sections 136 and 137 ensure shareholder rights and transparency by mandating that audited financial statements be made available to members and filed with the Registrar of Companies within prescribed timelines.

Company accounts under the 2013 Act are designed to ensure accuracy, transparency, and accountability in financial reporting. One of the most important aspects is the requirement for every company to prepare financial statements in a form that gives a true and fair view of its state of affairs. These statements must conform to notified accounting standards, and for companies with subsidiaries, consolidated financial statements are compulsory. This ensures that investors and regulators have a holistic view of a corporate group's financial performance. The Act also emphasizes timely disclosure and audit requirements. All financial statements must be audited by an independent statutory auditor appointed under the Act,

ensuring credibility and reliability. Companies are required to present financial information to shareholders during the annual general meeting (AGM) and file the same with the Registrar of Companies. Provisions relating to auditor rotation, independence, and reporting obligations strengthen trust in corporate reporting. Moreover, CSR obligations, disclosure of related party transactions, and stringent penalties for falsification of accounts highlight the Act's emphasis on ethical and responsible accounting practices.

To safeguard the integrity of financial reporting, the Companies Act, 2013 has established a robust monitoring and regulatory framework. The National Financial Reporting Authority (NFRA) is the apex authority that regulates auditing standards, monitors quality of services of auditors, and investigates cases of professional misconduct. Its establishment reflects the need for independence and accountability in the auditing process. The Registrar of Companies (RoC) acts as the primary regulatory authority responsible for overseeing corporate compliance, ensuring timely filing of accounts, returns, and other statutory documents. In cases of fraud or mismanagement, the Serious Fraud Investigation Office (SFIO) comes into play. It has the power to investigate corporate frauds in depth and recommend prosecution of guilty parties. Alongside these authorities, the Securities and Exchange Board of India (SEBI) also regulates listed companies to protect investor interests by enforcing disclosure norms and governance standards. Together, these regulatory bodies ensure that companies maintain transparency, comply with statutory obligations, and uphold stakeholder trust.

Corporate governance refers to the framework of rules, practices, and processes by which companies are directed and controlled. The Companies Act, 2013 has embedded several provisions to strengthen governance in Indian corporates. It mandates the appointment of independent directors on boards of certain companies to bring objectivity and protect minority shareholder interests. The Act requires the formation of key board committees such as the Audit Committee, Nomination and Remuneration Committee, and Stakeholders' Relationship Committee for effective oversight and accountability. Auditor independence and rotation are also critical governance measures introduced under the Act. This prevents long-term association between companies and auditors, reducing the chances of biased reporting. Furthermore, the Act makes Corporate Social Responsibility (CSR) mandatory for eligible companies, ensuring that corporate profits contribute to social development. Transparency is enhanced through provisions requiring disclosure of related party transactions, directors' remuneration, and key managerial compensation in the board's report. By enforcing such governance practices, the Act seeks to balance the interests of shareholders, employees, customers, and society, thereby promoting sustainable business growth.

2.4 List of Abbreviations used

BOD- Board of Directors

FY – Financial Year

MD – Managing Director

CFO – Chief Finance Officer

CG - Central Government

WTD – Whole Time Director

AGM – Annual General Meeting

CFS – Consolidated Financial Statement

FS – Financial Statements

CEO – Chief Executive Officer

CS – Company Secretary

CSR – Corporate Social Responsibility

MCA- Ministry of Corporate Affairs

SEBI - Securities and Exchange Board of India

NCLT - National Company Law Tribunal

NFRA - National Financial Reporting Authority

ICA - Institute of Chartered Accountants

RoC - The Registrar of Companies

MSMEs – Micro, Small & Medium Enterprises

MCA – Ministry of Corporate Affairs

LLP – Limited Liability Partnerships

CLB – Company Law Board

AAIRFR – Appellate Authority for Industrial and Financial Reconstruction

IFRS – International Financial Reporting Standard

2.5 Answers of Check Your Progression

Check your progress: 1

- 1.: a) Books of accounts to be kept by Company
- 2: C) 8 years
- 3: C) NFRA
- 4: B) 3 years
- 5: C) ICAI
- 6: C) 21 days
- 7: A) Section 130

Check your progress: 2

- 1. b. registered office.
- 2. d. chartered accountants and auditing firms.
- 3. a. Section 143
- 4. b. An auditor
- 5. d. All the above.

Check your progress: 3

- 1: C. MCA
- 2: C. ICAI
- 3: B. SEBI
- 4: C. Monitoring stock market
- 5: B. Framing accounting standards
- 6: C. SEBI Act, 1992
- 7: C. MCA

Check your progress: 4

- 1: B) Ministry of Corporate Affairs
- 2: C) Laying down tax policies
- 3: C) Regulate accounting and auditing standards

- 4: C) Central Government
- 5: C) ICAI
- 6: C) Protecting investors and regulating securities markets

2.6 Exercise:

State True or False

- 1. Section 128 of the Companies Act, 2013 requires every company to maintain books of accounts on an accrual basis and double-entry system.
- 2. Section 131 allows reopening of accounts in case of fraud or mismanagement.
- 3. According to Section 135, every company, irrespective of size, must spend 2% of its average net profits on CSR activities.
- 4. Consolidated financial statements are mandatory for companies having subsidiaries under the Companies Act, 2013.
- 5. Auditor rotation and independence are important corporate governance measures under the Companies Act, 2013.
- 6. The Registrar of Companies (RoC) regulates auditing standards and professional misconduct of auditors.
- 7. The Serious Fraud Investigation Office (SFIO) is empowered to investigate corporate frauds and recommend prosecutions.
- 8. Financial statements under Section 129 include balance sheet, profit and loss account, cash flow statement, and notes to accounts.
- 9. Corporate governance provisions in the Act require the formation of Audit Committee, Nomination Committee, and CSR Committee.
- 10. Section 137 of the Companies Act requires companies to file their audited financial statements with the Income Tax Department.

Answers:

True: 1,4,5,7,8,9

False: 2,3,6,10

Short Notes

- a. Books of accounts to be kept by Company (Section 128)
- b. National Financial Reporting Authority (Section 132)

- c. Ministry of Corporate Affairs (MCA)
- d. Functions of NCLT
- e. The registrar of companies
- f. Regional directors
- g. Significance of Corporate Governance
- h. Components of Corporate Governance under the Companies Act, 2013

Short answer Questions

- a. As per Section 128 of Companies Act 2013, which accounting books must be kept by the companies?
- b. List the functions of Ministry of Corporate Affairs.
- c. What are the functions of SEBI in relation to the Companies Act 2013?
- d. Explain the role of ICAI as a regulatory Authority in Companies Act 2013.
- e. Explain concept of Corporate Governance under the Companies Act. 2013.
- f. Explain Scope of Corporate Governance.
- g. Explain in short Core Principles of Corporate Governance.

Long Answer Questions

- a. Explain Key aspects of company accounts according to the companies Act 2013
- b. What are the Functions of Ministry of Corporate Affairs (MCA)
- c. Explain Functions of Securities and Exchange Board of India (SEBI)
- d. Explain Functions of NFRA
- e. Explain Role and Functions of ICAI as a Regulatory Authority in Companies Act, 2013:
- f. What are the Core principles of Corporate Governance-

2.7 References for further studies.

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Unit 3

Issue of Shares

Index:

- 3.0 Introduction
- 3.1 Objectives
- 3.2 Presentation of Subject Matter
 - 3.2.1 Shares
 - 3.2.2 Terms and Conditions of Issue of Shares
 - 3.2.3 Issue of shares at par
 - 3.2.4 Issue of shares at premium
 - 3.2.5 Calls in Advance
 - 3.2.6 Calls in Arrears
 - 3.2.7 Journal Entries for Issue of Shares
 - 3.2.8 Forfeiture of Shares
 - 3.2.9 Reissue of forfeited shares
- 3.3 Summary
- 3.4 Terms to Remember
- 3.5 Answers to Check your progress
- 3.6 Exercise
- 3.7 Reference for further study

3.0 Objectives:

After studying this Unit, you will be able:

1. To describe the meaning of shares, procedure of issue of shares and its accounting.
2. To differentiate between issue of shares at par and at premium.
3. To define the concepts of calls in advance and calls in arrears.
4. To explain accounting for the forfeiture of shares and its reissue.

3.1 Introduction:

Dear learners, welcome to the course on the issue of shares in corporate sector. There are some activities given in this unit which will keep you active while learning. Do not skip them. Completing those activities will help you for your learning activeness and continuity. You have to also check your progress at different stages which will provide you the feedback through answers at the end of the unit.

Now let us try to understand the initial points of this unit. Before going to understand the issue of shares, you have to revisit your existing knowledge about company and its share capital. A joint stock company is one of the form of organizations. Firstly, see what is a company. It is identical because of its feature of 'share capital'. The capital of a company is called share capital which is divided into shares. Company means an association of persons formed for the economic gain of the members. However, by law, company can be for any legal object not necessary only for economic gain. The Companies Act 2013 defines a company as "a company incorporated under this Act or an existing company." 'An existing company means a company formed and registered under any of the former Companies Act. This unit covers procedure and accounting of issue of shares. It also consists of forfeiture of shares and reissue of shares.

3.2 Presentation of Subject Matter:

Now we are going to learn core points of the subject matter which we want to learn from this unit. It is main part of this unit which includes shares, issue of shares, calls in advance, calls in arrears, forfeiture of shares, effect of forfeiture, reissue of forfeited shares and issue of two classes of shares.

3.2.1 Share: Share capital of a company is divided into parts having equal value is called share. A share has a nominal value or face value. It bears a distinct number. A share is ownership security.

3.2.1.1 Meaning of Share: Share is a part of share capital which has equal value. A share is one unit of share capital in which share capital is divided. According to Section 2 (84) of Companies Act 2013, a share means "share in the share capital of a company and includes stock".

3.2.1.2 Essential Features of Share: The following are the essential features of a share [Section 44]:

- 1) A share has a nominal value and bears a distinct number.
- 2) A share certificate issued under the common seal of the company certifies that the person named herein is a registered holder of a specific number of shares bearing distinct numbers as mentioned in the certificate.
- 3) A share is an ownership security. In other words, a shareholder is a part-owner of the company.
- 4) A share is said to be a bundle of rights as well as liabilities. It secures to its owner the right to receive a proportionate part of the profits, if any, and proportionate part of the assets of the company upon liquidation. On the other hand the shareholder may also be required to pay the full value in winding up.
- 5) Shares may be issued generally at par or premium and at discount only in certain cases.
- 6) A share is considered to be a movable property transferable in the manner provided in the articles of the company.

3.2.1.3 Stock:

Fully paid up share capital may, if the Articles so permit, be converted into stock by an ordinary resolution (a resolution by simple majority) of the members. Stock is the aggregate consolidated holdings of the share capital of a person. It can be divided and transferred in any fractions and sub-divisions without regard to the original face value of the share for the purpose of convenient holding into different parts.

Difference between a Share and a Stock:

Sr. No.	Share	Stock
1	A share may not be fully paid up. It may be partly paid up or fully paid up.	Stock is always fully paid up. Only fully paid up shares can be converted into stock.
2	A share has nominal value.	A stock has no nominal value.
3	A share cannot be transferred in small fractions.	A stock can be transferred in any fractions.
4	All shares bear distinct numbers.	Stocks disclose the consolidated value of the share capital. Fractions of the stock do not bear any number.
5	All shares are of equal denomination.	Stock may be of unequal amounts.
6	Shares can be offered to the public.	Stock cannot be directly offered by the company to the public in the first instance.

3.2.2 Terms and Conditions of Issue of Shares:

1. Shares can be issued at par, at premium (or at discount with rare exceptions).
2. When shares are issued at par, issue price is equal to the face value of the share.
3. When shares are issued at premium, the issue price is higher than the face value. The excess is credited to the securities premium account.
4. The issue of shares at discount is generally prohibited except for sweat equity shares or in specific cases permitted by law.
5. The process of share issuance is governed by the Companies Act 2013 and SEBI regulates public issues and listed companies.

6. The Article of Association must authorize the issue, and shareholder approval by be required for certain types of shares (e.g.- preference shares, shares with differential rights).
7. Minimum 5% of the face value must be collected as application money for each share.
8. Private limited companies cannot issue shares to more than 200 shareholders.
9. As a Right issue, existing shareholders are offered new shares in proportion to their holdings, with a notice period of at least 15 days and not exceeding 30 days.
10. Payment for shares can be collected in instalments (application, allotment, calls) as per the schedule in the Articles of Association.
11. Shares must be allotted and share certificates issued within two months of allotment.
12. The Board may dispose of unsubscribed shares in a manner not disadvantageous to the company or shareholders.
13. Preference shares require a special resolution, must not have pending defaults on existing preference shares, and redemption terms must be clear.
14. Shares with differential voting rights cannot exceed 26% of post-issue paid-up equity capital. The company must have a track record of distributable profits for three years and no defaults on dividends, loans, or statutory payments. Shareholder approval is required via an ordinary resolution.

Activity-1 Read the prospectus for the issue of shares made by any company. (For this purpose you can browse on company's website, broker's website or SEBI's website.)

3.2.3 Issue of Shares at par:

Shares can be issued at par or at premium. As per Section 53 of Companies Act, the issue of shares at discount is prohibited. The procedure of issue of shares has been explained in this section. To raise a capital, it is usually necessary for a public company to issue a prospectus. It is a document or invitation to offer shares to public. It includes information regarding shares offered and number, type and amount of

shares. Generally, shares are issued for cash. The nominal value of shares can be called in different instalments such as application money, allotment money and call money.

Activity-2: Identify which of the following issue is at par.
a) 10000 shares of Rs.100 each issued at Rs.110
b) 10000 shares of Rs.100 each issued at Rs.90
c) 10000 shares of Rs.100 each issued at Rs.100
.....

3.2.3.1 Applications: The company issues a prospectus inviting the public to subscribe for its shares. The prospectus includes the details of the amount which the applicants have to pay as application and allotment money. The company may demand the full value of share on application itself or it may demand only a part of it. However, as stated earlier, the amount payable on application on every security shall not be less than 5% of the nominal price of the security or such other percentage or amount as may be specified by SEBI.

On receipt of application money, the journal entry is passed as follows:

Date	Particulars	L. F.	Debit	Credit
	Bank Account Dr.		*****	
	Share Application Account			*****

3.2.3.2 Allotment: Allotment means allocating or apportioning a certain number of shares to an applicant in response to his application. After receiving the applications by the due date, the directors of the company will get a detailed list of the applicants, prepared. They will call a directors' meeting and take a decision about the persons to whom the shares have to be allotted and the number of shares to be allotted. Applicants to whom the shares are to be allotted will be issued letters termed as "Letter of Allotment" to that effect. They will also be required to pay allotment money as per terms of the prospectus. The journal entries will be as follows:

Date	Particulars	L. F.	Debit	Credit
	Share Application Account Dr. To Share Capital Account (Being transferred application money to Share Capital on allotment of Shares)		*****	*****
	Share Allotment Account Dr. To Share Capital A/c. (Being money due on allotment)		*****	*****
	Bank Account Dr. To Share Allotment Account (Being received allotment money)		*****	*****

Some companies open only one account for application and allotment which called “Share Application and Allotment Account” instead of two separate accounts as mentioned above. In such a situation, the journal entries are made as shown below:

Date	Particulars	L. F.	Debit	Credit
	Bank Account Dr. To Share Application & Allotment A/c. (Being received application money)		*****	*****
	Share Application and Allotment A/c. Dr. To Share Capital A/c. (Being transferred application money)		*****	*****
	Bank A/c. Dr. To Share Application and Allotment A/c. (Being received allotment money)		*****	*****

Pending Allotment of Shares:

If the applications are received however the share are yet to be allotted, the amount of application money is shown in the balance sheet as “Share Application Money Pending Allotment” as per Schedule III to The Companies Act 2013.

3.2.3.3 Calls: After allotment of shares, whenever there will be need, the company may demand money towards payment of the value of shares held by shareholders. Such demands are known as ‘calls’. There can be a maximum of three calls. The journal entries for such calls can be made as follows:

Date	Particulars	L. F.	Debit	Credit
a)	On making the first call: Share First Call A/c. Dr. To Share Capital A/c. (Being made the first call due)		*****	*****
b)	On receipt of the money on first call: Bank A/c. Dr. To Share First Call A/c. (Being received money on the first call).		*****	*****
c)	On making the second call: Share Second Call A/c. Dr. To Share Capital A/c. (Being made the second call due).		*****	*****
d)	On receipt of the money on second call: Bank A/c. Dr. To Share Second Call A/c. (Being received money on second call).		*****	*****
e)	On making the third or final call: Share Final Call A/c. Dr. To Share Capital A/c. (Being made the final call due).		*****	*****

f)	On receipt of money on the third or final call: Bank A/c. Dr. To Share Final Call A/c. (Being received money on the final call).		*****	*****
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If a company collects money on shares on less than three calls, the term 'Final call' is to be used with the call after which no call will be made.

For e.g.- If a company collects money only on one call, the journal entry will be passed as follows:

Date	Particulars	L. F.	Debit	Credit
	Share First and Final Call A/c. Dr. To Share Capital A/c.		*****	*****

Check Your Progress-1:

(A) Whether following statement is true or false:

1. When shares are issued at par, issue price is less than the face value of the share.
2. Payment for shares can be collected in instalments (application, allotment, calls) as per the schedule in the Articles of Association.
3. Applicants to whom the shares are to be allotted will be issued letters termed as "Letter of Application" to that effect.

(B) Fill in the blanks:

1. When shares are issued at premium, the issue price is higher than the face value. The excess is credited to the account.
2. Minimum 5% of the face value must be collected as application money for each share.
3. There can be a maximum of calls.

Illustration-1:

ABC Co. Ltd. offer 10,000 shares of Rs.100 each. They received application for 10,000 shares. Money payable is as follows:

On Application Rs.30 per share

On Allotment Rs.20 per share

On 1st Call Rs.30 per share

On Final Call Rs.20 per share

The shares were duly allotted, calls made and they received money accordingly.

You are required to pass the necessary journal entries.

Solution:

Journal Entries in the books of ABC Co. Ltd.:

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
1	Bank A/c. Dr. To Share Application A/c. (Being received application money on 10,000 shares at Rs.30 per share)		3,00,000	3,00,000
2	Share Application A/c. Dr. To Share Capital A/c. (Being transferred application money to Share Capital A/c.)		3,00,000	3,00,000
3	Share Allotment A/c. Dr. To Bank A/c. (Being allotted 10,000 shares and allotment money due)		2,00,000	2,00,000
4	Bank A/c. Dr. To Share Allotment A/c. (Being received allotment money on 10,000 shares at Rs.20 per share)		2,00,000	2,00,000
5	Share 1 st Call A/c. Dr. To Share Capital A/c. (Being made 1 st call and call money due)		3,00,000	3,00,000

6	Bank A/c. To Share 1 st Call A/c. (Being received money on 1 st Call on 10,000 shares at Rs.30)	Dr.		3,00,000	3,00,000
7	Share Final Call A/c. To Share Capital A/c. (Being made final call and call money due)	Dr.		2,00,000	2,00,000
8	Bank A/c. To Share Final Call A/c. (Being received money on final call on 10,000 shares at Rs.20 per share)	Dr.		2,00,000	2,00,000

3.2.3.4 Under-subscription:

When a company receives applications for the shares less than the shares offered by it to the public, it is called under-subscription. For e.g.- A company offered 10,000 shares to the public but they received applications only for 8,000 shares. Such situation is under-subscription. In this case, journal entries for application, allotment and calls are made only for 8,000 shares. However, when a company receives applications even not for minimum subscription, a company cannot proceed for allotment. It refunds the application money to all applicants.

3.2.3.5 Oversubscription:

When a company receives applications for the shares more than the shares offered by it to the public, it is called oversubscription. For e.g.- A company offered 10,000 shares to the public but they received applications for 12,000 shares. Such situation is oversubscription. In such situation, a company can handle the situation in one or more of the following way:

- (i) A company may reject certain applications straightway (either on the basis of number of shares applied for or any other basis). A company will refund application money to such applicants. The journal entry for this purpose will be as follows:

Share Application A/c.	Dr.
To Bank A/c.	

(Being refund of application money to applicants forshares @ Rs....per share)

- (ii) A company may make partial allotment. It is the allotment of a smaller number of shares than the number of shares applied for. For e.g.- every applicant for 1,000 shares may be allotted 600 shares and every applicant for 2,000 shares be allotted 1,100 shares and so on.
- (iii) A company may make 'Pro-rata Allotment'. It is allotment to be made to each applicant or some applicants on the proportionate basis. For e.g.- a company offers 12,000 shares to the public, and a company received applications for 16,000 shares. No allotment is to be made for 4,000 shares and the rest are allotted shares on a pro rata basis. Here, we can understand, applicants for 16,000 shares will receive 12,000 shares or every applicant of every four shares will get three shares on pro rata basis.

In case of (ii) or (iii), there will be excess application money. Instead of refunding this money, it can be adjusted (used) against allotment money. It means excess application money can be used for money due on allotment. For e.g.- Mr. X applied for 100 shares and paid Rs.20 per share as application money. He got only 80 shares and the money due on allotment is Rs.30 per share. The following journal entry will be passed for transferring excess application money to Share Allotment Account:

Share Application A/c.	Dr.	400
To Share Allotment A/c.		400

Excess money over that due on allotment should be refunded to the allottees, within 15 days from the date of closure of issue or such lessor time as may be specified by SEBI. In case of default, the applicant will be entitled to interest at 15% p.a. for the delayed period besides penalty on both the company and the directors.

Activity-3 Identify which of the following is undersubscription and which of them is oversubscription.
a) A Ltd. issued 90,000 shares of Rs.100 each. They received applications for 1,11,000 shares
b) B Ltd. issued 1,20,000 shares of Rs.100 each. They received applications for 1,11,000 shares

Strike out which is wrong:

Example a) is undersubscription/oversubscription.

Example b) is undersubscription/oversubscription.

Illustration-2:

A company offers 25,000 shares of Rs.100 each to the public. The money payable on shares is as follows:

Rs.20 on Application

Rs.30 on Allotment

Rs.50 on First & Final Call

A company received applications for full 30,000 shares. Applicants for 22,080 shares pay the application money in cash, while the rest pay that money through stockinvests. The shares are allotted on the pro-rata basis. All allottees pay the allotment and final call moneys on due dates.

Pass the necessary journal entries.

Solution:

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
1	Bank A/c. Dr. To Share Application A/c. (Being received application money in cash on 22,000 shares @ Rs.20 per share)		4,41,600	4,41,600
2	Share Application A/c. Dr. To Share Capital A/c. To Share Allotment A/c. (Being transferred application money due on 18,400 shares from applicants who applied for 22,080 shares. Excess application money adjusted towards allotment).		4,41,600	3,68,000 73,600
3	Bank A/c. Dr. To Share Capital A/c. (Being application money received on 2,920 shares @ Rs.20)		58,400	58,400

	per share from persons who applied through stockinvests)			
4	Share Allotment A/c. Dr. To Share Capital A/c. (Being allotment money due on 25,000 shares @ Rs.30 per share)		7,50,000	7,50,000
5	Bank A/c. Dr. To Share Allotment A/c. (Being allotment money received on 25,000 shares)		6,76,400	6,76,400
6	Share First & Final Call A/c. Dr. To Share Capital A/c. (Being 1 st & final call money due on 25,000 shares @ Rs.50 per share)		12,50,000	12,50,000
7	Bank A/c. Dr. To Share First & Final Call A/c. (Being received first & final call money)		12,50,000	12,50,000

3.2.4 Issue of Shares at Premium:

A company can issue its shares at a price more than its nominal value. It is called 'Issue of Shares at Premium'. A company can issue shares at premium without any provision in the Article of Association. However, as per the recent guidelines issued by SEBI, a new company set up by the entrepreneurs without a track record can issue capital to the public only at par. As per Section 52 of the Companies Act, the amount of such premium, shall have to be transferred by the company to the Securities Premium Account. The balance in this account is treated with the same sanctity as the paid up Share Capital of the company.

3.2.4.1 Utilization of Securities Premium Account: The Companies Act 2013 has two provisions regarding utilizing securities premium which are as follows:

1) Section 52 (2): Companies which are not required to follow the accounting standards:

These companies can use the Securities Premium Account for the following purposes:

- a) towards the issue of unissued shares of the company to members of the company as fully paid bonus shares;

- b) in writing off the preliminary expenses of the company;
- c) in writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company;
- d) in providing for the premium payable on the redemption of any redeemable preference shares or of any debentures of the company or
- e) for the purchase of its own shares or other securities under Section 68.

2) Section 52 (3): Companies which are required to follow the accounting standard:

These companies can use the Securities Premium Account for the following purposes:

- a) in paying up unissued equity shares of the company to be issued to members of the company as fully bonus shares; or
- b) in writing off the expenses of, or the commission paid or discount allowed on, any issue of equity shares of the company; or
- c) for the purpose of its own shares or other securities under Section 68.

However, in “Notes to Accounts” the Securities Premium will have to be shown as “Securities Premium Reserve” under the heading Reserve & Surplus as required by the Notes to Accounts given in Schedule III.

The amount of share premium is generally payable in a lump sum on allotment. However, a company may require the applicants to pay premium money with application money or with calls. The accounting entries are made as follows:

(a) When premium money is payable on allotment:

On amount being due:

Share Allotment A/c.

Dr.

To Share Capital A/c.

To Securities Premium A/c.

(Share allotment account will be debited with amount due on account of share capital as well as securities premium)

On receipt of allotment money:

Bank A/c.	Dr.
-----------	-----

To Share Allotment A/c.

(with the amount actually received)

(b) In case premium money is payable on application:

On receipt of application money:

Bank A/c.	Dr.
-----------	-----

To Share Application A/c.

(with money received on account of share capital as well as securities premium)

On transfer of application money:

Share Application A/c.	Dr.
------------------------	-----

To Share Capital A/c.

To Securities Premium A/c.

(c) When premium is received in parts, (say on application as well as allotment or allotment and first call, entries on the same pattern can be passed. For e.g.- if premium is payable in two instalments- on allotment and first call, the following accounting entries will be passed:

For premium due on allotment:

Share Allotment A/c.	Dr.
----------------------	-----

To Share Capital A/c.

To Securities Premium A/c.

For receipt of allotment money:

Bank A/c.	Dr.
-----------	-----

To Share Allotment A/c.

For premium due on first call:

Share First Call A/c.	Dr.
-----------------------	-----

To Share Capital A/c.

To Securities Premium A/c.

For receipt of first call money:

Bank A/c.

Dr.

To Share First Call A/c.

Illustration-3:

A company offers 50000 shares of Rs.10 each to the public for subscription at Rs.12 per share. Money was payable as follows:

Rs.3 on application

Rs.4 on allotment (including Re.1 as premium)

Rs.5 on call (including Re.1 as premium)

Applications are received for 75,000 shares. No allotment was made to applicants for 15,000 shares and their application money is refunded. Rest are allotted shares on a pro rata basis. All allottees pay the money due on shares as and when called up.

Pass journal entries and show how the items will appear in the company's balance sheet.

Solution:

Journal Entries

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
1	Bank A/c. Dr. To Share Application A/c. (Being received application money on 75,000 shares @ Rs.3 per share)		2,25,000	2,25,000
2	Share Application A/c. Dr. To Share Capital A/c. To Bank A/c. To Share Allotment A/c. (Being transferred application money to share capital on 50,000 shares, refunded application money on 15,000 shares and transferred the rest to allotment)		2,25,000	1,50,000 45,000 30,000

3	Share Allotment A/c. To Share Capital A/c. To Securities Premium A/c. (Being allotment money due on 50,000 shares @ Rs.4 per share including Re.1 as share premium)	Dr.	2,00,000	1,50,000 50,000
4	Bank A/c. To Share Allotment A/c. (Being received money on allotment)	Dr.	1,70,000	1,70,000
5	Share First & Final Call A/c. To Share Capital A/c. To Securities Premium A/c. (Being money due on first & final call @ Rs.5 per share including Re.1 as premium)	Dr.	2,50,000	2,00,000 50,000
6	Bank A/c. To First & Final Call A/c. (Being received money on first & final call)	Dr.	2,50,000	2,50,000

Balance Sheet as on ...

Particulars	Note No.	Rs.
<u>Equity & Liabilities</u>		
Share Capital:		
Shareholders' Funds	1	5,00,000
Share Capital		
Reserve & Surplus	2	1,00,000
		6,00,000
<u>Assets</u>		
Current Assets		
Cash & Cash Equivalents	3	6,00,000
		6,00,000

Notes to Accounts

1. Share Capital:		Rs.
Authorized Share Capital		
..... shares of Rs.10 each		
Issued & Subscribed Share Capital		
50,000 shares of Rs.10 each		5,00,000
Subscribed and fully paid up		
50,000 shares of Rs.10 each		5,00,000
2 Reserve & Surplus:		
Securities Premium Reserve		1,00,000
		6,00,000
3 Cash & Cash Equivalents:		
Cash at Bank		6,00,000
		6,00,000

Check your progress-2;

State whether the following statement is 'True' or 'False':

- The nominal value of shares can be called in different installments such as application money, allotment money and call money.
- Allotment of shares is made before receiving applications.
- There can be a maximum of two calls.
- When a company receives applications even not for minimum subscription, a company refunds the application money to all applicants.

3.2.5 Calls in Advance:

If company's Articles allow, a company may accept calls in advance from its shareholders. Table F gives such a power and also provides for payment of interest at a rate not exceeding 12% p.a. The amount received in advance as payment of calls

will be credited to a “Call in Advance Account”. The amount so received will be adjusted towards the payment of calls as and when they become due.

Bank A/c. Dr.

To Call in Advance A/c.

(Being received call in advance)

Share Call A/c. Dr.

To Share Capital A/c.

(Being the amount due on ... call on all shares including those on which call has been received in advance)

Bank A/c. (amount actually received) Dr.

Calls in Advance A/c. Dr.

(amount of call received in advance)

To Call A/c.

(Being received actual ...call money)

3.2.6 Calls in Arrears:

If shareholder does not pay the call money when it becomes due, it is known as ‘Calls in Arrears’. The Article of association of a Company may have provision for charging interest from the defaulting shareholder. Table *F* permits charging of interest on calls in arrears at 10% p.a. The journal entries for calls in arrears are as follows:

When a call become due:

Share ... Call A/c. Dr.

To Share Capital A/c.

When money in response to calls is received:

Bank A/c. Dr.

To Share ... Call A/c.

(with the amount actually received excluding the amount of call in arrear)

At the end of the accounting year, the amount outstanding on account of a call will be transferred to Calls in Arrears A/c.:

Calls in Arrears A/c.	Dr.
To Share ... Call A/c.	

When payment is made of call in arrear with interest:

Bank A/c.	Dr.
To Share ... Call A/c./ Calls in Arrears A/c.	
To Interest A/c.	

Check Your Progress-2

(A) Fill in the blanks:

1. Company B offered 35,000 shares to the public but they received applications for 40,000 shares, such situation is called
2. A company offered 50000 shares to the public but they received applications only for 40,000 shares, such situation is called
3. If company issued 1,00,000 shares of Rs.100 each at Rs.115 per share, then share capital will be Rs.1,00,00,000 and Rs.15,00,000 is called

(B) Choose the most appropriate alternative as an answer:

1. The following accounting entry is passed for at the time of issue of shares:

Share Application A/c.	Dr. *****
------------------------	-----------

To Share Allotment A/c.

- a) Application money
 - b) Excess application money
 - c) Allotment money
 - d) Call money
2. Under section 52 (2) companies which are not required to follow the accounting standards, those companies cannot use the Securities Premium Account for the purpose of
- a) Writing off the preliminary expenses of the company
 - b) For purchase of its own shares or other securities under Section 68
 - c) For personal expenses of manager
 - d) Writing off the commission on any issue of shares
3. If shareholder does not pay the call money when it becomes due, it is known as
- a) Allotment money
 - b) Call money
 - c) Calls in advance
 - d) Calls in arrears

Illustration-4:

XYZ Ltd. offers 20,000 shares to the public. The amount payable was as follows:

On Application Rs.30 per share

On Allotment Rs.20 per share

On 1st Call Rs.30 per share

On Final Call Rs.20 per share

A company received 30,000 shares. The directors make the allotment as follows:

(i) No allotment to applicants for 6,000 shares.

(ii) Rest allotted on a pro rata basis.

All calls were duly made and paid except:

P, a holder of 200 shares paid the two calls with allotment.

Q, a holder of 400 shares fails to pay the 1st & 2nd calls.

R, a holder of 200 shares fails to pay the 2nd call.

Pass the necessary journal entries to record the above transactions in the company's books and show how the share capital will appear in the company's Balance Sheet.

Solution:

Journal Entries in the books of XYZ Ltd.:

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
1	Bank A/c. Dr. To Share Application A/c. (Being received application money 30,000 shares @ Rs.30 per share)		9,00,000	9,00,000
2	Share Application A/c. Dr. To Bank A/c. To Share Allotment A/c. To Share Capital A/c. (Being transferred application money to Share Capital A/c. on 20,000 shares, surplus money on pro rata allotment to share		9,00,000	1,80,000 1,20,000 6,00,000

	allotment account and the balance being refunded)			
3	Share Allotment A/c. Dr. To Share Capital A/c. (Being money due on allotment)		4,00,000	4,00,000
4	Bank A/c. Dr. To Share Allotment A/c. To Calls in Advance A/c. (Being received allotment money and calls in advance)		2,90,000	2,80,000 10,000
5	Shares First Call A/c. Dr. To Share Capital A/c. (Being money due on first call)		6,00,000	6,00,000
6	Bank A/c. Dr. Calls in Advance A/c. Dr. To Share First Call A/c. (Being received the first call money)		5,82,000 6,000	5,88,000
7	Share Second & Final Call A/c. Dr. To Share Capital A/c. (Being money due on second call)		4,00,000	4,00,000
8	Bank A/c. Dr. Calls in Advance A/c. Dr. To Share Second Call A/c. (Being received the second call money)		3,84,000 4,000	3,88,000
9	Calls in Arrears A/c. Dr. To Share First Call A/c. To Share Final Call A/c. (Being transferred first call and final call money)		24,000	12,000 12,000

Extract of Balance Sheet of XYZ Ltd. as on ...

Equity & Liabilities	Note No.	Rs.
Share Capital:		
Shareholders' Funds	1	19,76,000
Share Capital		

Notes to Accounts

1. Share Capital		Rs.
Authorized Share Capital		
..... shares of Rs.100 each		
Issued & Subscribed Share Capital		
Subscribed and Fully Paid up Capital		
19,400 shares of Rs.100 each		19,40,000
Subscribed and not fully paid up		
300 shares of Rs.100 each	60,000	
Less: Calls in Arrears	24,000	36,000
		19,76,000

3.2.8 Forfeiture of Shares:

Forfeiture of shares is nothing but the termination of membership and taking away of the shares because of default in payment of allotment and/or call money by a shareholder. The Companies Act does not contain any specific provision regarding forfeiture of shares. However, Regulation, 28 to 34 of Model Articles of a company limited by shares (as contained in Table F of Schedule I of the Companies Act 2013) make provision forfeiture of shares. These provisions can be summarized as under:

- 1) The power to forfeit shares must be expressly given by the company's Articles.
- 2) There should be a default by the shareholder in payment of a valid call.

- 3) A notice of demand, requiring the shareholder to pay calls of a specified amount within 14 days must be given.
- 4) The Board of Directors must pass a resolution for forfeiture of shares.
- 5) The power to forfeiture must be exercised in good faith and in the interest of the company.
- 6) Forfeited shares may be sold or otherwise disposed of by the Board, as it deems fit. Board can cancel forfeiture on such terms as it deems fit.

3.2.8.1 Effect of Forfeiture: When shares are forfeited, following effects emerge:

- a) A defaulter ceases to be a member of the company.
- b) His shares in the company lapse.
- c) Whatever money paid on the shares prior to forfeiture become the property of the company.
- d) He remains as a contributory past member for the liabilities incurred by the company upto the date of his membership provided the present member is unable to pay and the company goes into liquidation within one year.
- e) If the articles so provide, he will also remain liable for unpaid calls as an ordinary debtor of the company for a period of three years from the date of forfeiture. The ex-shareholder can be put on “List B contributories”.
- f) The company may re-issue the forfeited shares at a discount or at a premium.

3.2.8.2 Forfeiture of Shares issued at par: The following accounting entry is passed for forfeiture of shares basically issued at par:

Share Capital A/c. (with the amount called up) Dr.
 To Unpaid Call A/c. (with the amount remaining unpaid)
 To Forfeited Shares A/c. (with the amount received)

3.2.8.3 Forfeiture of shares issued at premium: There can be two situations:

- (i) The amount of share premium has not been received but it was credited to “Securities Premium Account”, when the amount became due. For this situation, the following journal entry is passed:

Share Capital A/c. (with the amount called up) Dr.

Securities Premium A/c. (with the amount of premium called)

To Unpaid Calls A/c.

To Forfeited Shares A/c.

- (ii) The amount of share premium has either been received or even if not received, the company has given credit to the securities premium account only with the amount of premium received. For this situation, the following journal entry is passed:

Share Capital A/c. (with the amount called up) Dr.

To Unpaid Calls A/c. (with unpaid amount excluding share premium)

To Forfeited Shares A/c. (with the amount received)

Illustration-5:

A company forfeits 500 shares of Rs.100 each fully called up on which the shareholder has failed to pay the allotment money of Rs.20 per share and call money of Rs.30 per share.

Pass journal entry in the books of a company.

Solution:

Journal Entries

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
	Share Capital A/c. Dr.		50,000	
	To Share Allotment A/c.			10,000
	To Share Call A/c.			15,000
	To Share Forfeited A/c.			25,000
	(Being forfeited 500 shares of Rs.100 each failed to pay allotment money of Rs.20 per share and call money of Rs.30 per share)			

Illustration-6:

A company forfeits 500 shares of Rs.10 each issued at Rs.11 per share. The premium was payable on allotment. The shareholder failed to pay allotment money of Rs.3 per share (including premium) and the call money of Rs.2 per share.

Journalize these transactions.

Solution:**Journal Entries**

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
	Share Capital A/c. Dr.		50,000	
	Securities Premium A/c.		500	
	To Share Allotment A/c.			15,000
	To Share Call A/c.			10,000
	To Share Forfeited A/c.			25,500
	(Being forfeited 500 shares of Rs.100 each issued at a premium @ Re.1 per share, failed to pay allotment money of Rs.30 per share and call money of Rs.20 per share)			

3.2.9 Reissue of Forfeited Shares:

After forfeiture of shares, those forfeited sharers will become the property of a company. That company can re-issue those shares at par, at premium or at discount. However, if they are re-issued at discount, the amount of discount cannot exceed the amount that had been received on these shares. In other words, there cannot be any loss on account of re-issue of forfeited shares.

When the forfeited shares are re-issued, the following journal entry is passed:

Bank A/c. (with the amount received) Dr.
 Forfeited Shares A/c. (with the discount allowed) Dr.
 To Share Capital A/c. (with the amount taken as paid up)

If after the re-issue of forfeited shares, there is any balance on Forfeited Shares A/c., it is transferred to Capital Reserve A/c. by passing the following entry:

Forfeited Shares A/c.

Dr.

To Capital Reserve A/c.

Check your progress-3:

- (a)is nothing but the termination of membership and taking away of the shares because of default in payment of allotment and/or call money by a shareholder.
- (b) Before forfeiture of shares, a notice of demand, requiring the shareholder to pay calls of a specified amount within days must be given.
- (c) The forfeited shares can be re-issued at par, at premium or at.....
- (d) If after the re-issue of forfeited shares, there is any balance on Forfeited Shares A/c., it is transferred to

Illustration-7:

A company forfeited 500 shares of Rs.10 each on which Rs.1,500 had been received. The company can allow a maximum discount of Rs.1,500 on these shares. In case these shares are re-issued for Rs.4,500 fully paid. Pass necessary journal entries.

Solution:

Journal Entries

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
	Bank A/c. Dr. Forfeited Shares A/c. To Share Capital A/c. (Being re-issue of 500 forfeited shares)		4,500 500	5,000
	Forfeited Shares A/c. Dr. To Capital Reserve A/c.		1,000	1,000

	(Being profit on re-issue of forfeited shares to capital reserve)			
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Illustration-8:

Wise Ltd. has issued 10000 shares of Rs.20 each on which the amount is payable as follows:

On Application	Rs.5 per share
On Allotment	Rs.4 per share
On 1 st Call	Rs.3 per share
On 2 nd Call	Rs.5 per share
On 3 rd Call	Rs.3 per share

From the particulars given, journalize the transactions in respect of calls, forfeiture & re-issue of shares only.

Name of the Shareholders	Shares held	Amount paid on
Mr. A	200	Application & Allotment
Mr. B	400	Application, Allotment & First Call
Mr. C	600	Application, Allotment, First Call & Second Call

Company made all the calls. The call money was received in full except from the above persons. The directors forfeited the shares of the above shareholders to Mr. X as fully paid up for Rs.22 per share. Mr. X has paid the amount in full.

Solution:

Journal Entries

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
1	Bank A/c. Dr. To Equity Share Application A/c. (Being received application money on 10,000 shares at Rs.5 each)		50,000	50,000

2	Equity Share Application A/c. Dr. To Equity Share Capital A/c. (Being transferred application money to share capital)		50,000	50,000
3	Equity Share Allotment A/c. Dr. To Equity Share Capital A/c. (Being allotment money due on 10,000 shares at Rs.4 per share)		40,000	40,000
4	Bank A/c. Dr. To Equity Share Allotment A/c. (Being received allotment money in full)		40,000	40,000
5	Equity Share First Call A/c. Dr. To Equity Share Capital A/c. (Being first call money due on 10,000 shares at Rs.3 per share)		30,000	30,000
6	Bank A/c. Dr. Calls in Arrears A/c. Dr. To Equity Share First Call A/c. (Being received first call money on 9,800 shares as Mr. A failed to pay on his 200 shares)		29,400 600	30,000
7	Equity Share Second Call A/c. Dr. To Equity Share Capital A/c. (Being second call money due on 10,000 shares at Rs.5 per share)		50,000	50,000
8	Bank A/c. Dr. Calls in Arrears A/c. Dr. To Equity Share Second Call A/c. (Being received second call money on 9,400 shares as Mr. A failed to pay on 200 shares and Mr. B on 400 shares)		47,000 3,000	50,000
9	Equity Share Third Call A/c. Dr. To Equity Share Capital A/c. (Being third call money due on 10,000 shares at Rs.3 per share)		30,000	30,000
10	Bank A/c. Dr.		26,400	
	Calls in Arrears A/c. Dr.		3,600	
	To Equity Share Third Call A/c.			30,000

	(Being received third call money on 8,800 shares as Mr. A, B & C failed to pay on 200, 400 & 600 shares respectively)			
11	Equity Share Capital A/c. Dr. To Calls in Arrears A/c. To Forfeited Shares A/c. (Being forfeited 1,200 shares held by Mr. A, B & C upon failing payment of various calls)		24,000	7,200 16,800
12	Bank A/c. Dr. To Equity Share Capital A/c. To Securities Premium A/c. (Being re-issued 1200 forfeited shares to Mr. X at Rs.22 each i.e. at premium of Rs.2 each)		26,400	24,000 2,400
13	Equity Share Forfeiture A/c. Dr. To Capital Reserve A/c. (Being transferred balance on forfeiture A/c. to Capital Reserve A/c.)		16,800	16,800

Illustration-9:

Glory Health Services Ltd. issued 1,00,000 equity shares of Rs.100 each payable as follows:

Rs.15 with application

Rs.20 on allotment

Rs.30 on first call and

Rs.35 on second and final call

Total Applications received for 93,000 shares.

To applicants of 10,000 shares full allotment

To applicants of 80,000 shares 40,000 shares allotted

To applicants of 3,000 shares No shares allotted

On due dates, the calls were also made. Assuming that all moneys were duly received, journalize the transactions and prepare ledger accounts.

Solution:

Journal Entries

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
1	Bank A/c. Dr. To Equity Share Application A/c. (Being received application money on 93,000 shares at Rs.15 each)		13,95,000	13,95,000
2	Equity Share Application A/c. Dr. To Equity Share Capital A/c. (Being transferred application money to share capital for 50,000 shares)		7,50,000	7,50,000
3	Equity Share Application A/c. Dr. To Equity Share Allotment A/c. (Being transferred excess application money on 40,000 shares)		6,00,000	6,00,000
4	Equity Share Application A/c. Dr. To Bank A/c. (Being refund of application money on 3,000 shares)		45,000	45,000
3	Equity Share Allotment A/c. Dr. To Equity Share Capital A/c.		10,00,000	10,00,000

	(Being allotment money due on 50,000 shares at Rs.20 per share)			
4	Bank A/c. Dr. To Equity Share Allotment A/c. (Being received allotment money Rs.5 remaining on 40,000 shares and Rs.20 per share on 10,000 shares)		4,00,000	4,00,000
5	Equity Share First Call A/c. Dr. To Equity Share Capital A/c. (Being first call money due on 50,000 shares at Rs.30 per share)		15,00,000	15,00,000
6	Bank A/c. Dr. To Equity Share First Call A/c. (Being received first call money on 50,000 shares)		15,00,000	15,00,000
7	Equity Share Second & Final Call A/c. Dr. To Equity Share Capital A/c. (Being second call money due on 50,000 shares at Rs.35 per share)		17,50,000	17,50,000
8	Bank A/c. Dr. To Equity Share Second & Final Call A/c. (Being received second call money on 50,000 shares)		17,50,000	17,50,000

3.2.7 Issue of Two Classes of Shares:

A company can issue two classes of shares i.e. equity shares and preference shares. In this case, two separate capital accounts will be opened i.e. (a) Preference Share Capital Account and (b) Equity Share Capital Account. In the same manner, there will be separate share application accounts, share allotment accounts and share call accounts. Otherwise, all other accounting entries will be similar as we have seen in case of issue of shares. Let us learn accounting treatment in the following illustration regarding issue of two classes of shares.

Illustration-10:

Kavita Steel Ltd. was registered with a capital of Rs.10,00,00,000 divided into 6,00,000 equity shares of Rs.100 each and 2,00,000 7% preference shares of Rs.200 each. The amounts on these shares were payable as follows:

	Equity Shares Rs.	Preference Shares Rs.
On Application	10	30
On Allotment	25	60
On First Call	15	30
On Second Call	30	40
On Third & Final Call	20	40

All the shares were duly subscribed. The final call money on 50 equity shares and 40 preference shares was not received and therefore, the directors decided to forfeit them. After due notice these shares were forfeited. Equity shares, however, were re-issued at Rs.85 per share.

Give the necessary journal entries and prepare Cash book. Create a Reserve account by transferring the balance of forfeited shares account after re-issue of shares.

Solution:

Journal Entries in the books of Kavita Steel Ltd.

Date	Particulars	L. F.	Debit Rs.	Credit Rs.
1	Bank A/c. Dr. To Equity Share Application A/c. To 7% Preference Share Application A/c. (Being received application money on 6,00,000 equity shares at Rs.10 each and on 2,00,000 preference shares at Rs.30 each)		1,20,00,000	60,00,000 60,00,000
2	Equity Share Application A/c. Dr. 7% Preference Share Dr. Application A/c. To Equity Share Capital A/c. To 7% Preference Share Capital A/c. (Being tranferred application money to capital account)		60,00,000 60,00,000	60,00,000 60,00,000
3	Equity Share Allotment A/c. Dr. 7% Preference Share Dr. Allotment A/c. To Equity Share Capital A/c. To 7% Preference Share Capital A/c. (Being made allotment of 6,00,000 equity shares at Rs.25 each and on 2,00,000 preference shares at Rs.60 each)		1,50,00,000 1,20,00,000	1,50,00,000 1,20,00,000
4	Bank A/c. Dr. To Equity Share Allotment A/c. To 7% Preference Share Allotment A/c. (Being received allotment money)		2,70,00,000	1,50,00,000 1,20,00,000
5	Equity Share First Call A/c. Dr. 7% Preference Share Dr. First Call A/c. To Equity Share Capital A/c. To 7% Preference Share Capital A/c. (Being made the first call of 6,00,000 equity shares at		90,00,000 60,00,000	90,00,000 60,00,000

	Rs.15 each and on 2,00,000 preference shares at Rs.30 each)				
6	Bank A/c. To Equity Share First Call A/c. To 7% Preference Share First Call A/c. (Being received first call money)	Dr.		1,50,00,000	90,00,000 60,00,000
7	Equity Share Second Call A/c. 7% Preference Share Second Call A/c. To Equity Share Capital A/c. To 7% Preference Share Capital A/c. (Being made the first call of 6,00,000 equity shares at Rs.30 each and on 2,00,000 preference shares at Rs.40 each)	Dr. Dr.		90,00,000 60,00,000	90,00,000 60,00,000
8	Bank A/c. To Equity Share Second Call A/c. To 7% Preference Share Second Call A/c. (Being received first call money)	Dr.		1,50,00,000	90,00,000 60,00,000
9	Equity Share Final Call A/c. 7% Preference Share Final Call A/c. To Equity Share Capital A/c. To 7% Preference Share Capital A/c. (Being made the first call of 6,00,000 equity shares at Rs.20 each and on 2,00,000 preference shares at Rs.40 each)	Dr. Dr.		1,20,00,000 80,00,000	1,20,00,000 80,00,000
10	Bank A/c. To Equity Share Final Call A/c.* To 7% Preference Share Final Call A/c.# (Being received first call money)	Dr.		1,97,40,000	1,19,00,000 78,40,000

11	Equity Shares Capital A/c. To Equity Shares Forfeited A/c. To Equity Share Final Call A/c. (Being forfeiture of 50 equity shares up on non-payment of final call)	Dr.		5,00,000	4,00,000 1,00,000
12	Bank A/c. Equity Share Forfeiture A/c. To Equity Share Capital A/c. (Being re-issue of 50 equity shares at a discount of Rs.15 each)	Dr. Dr.		4,25,000 75,000	5,00,000
13	Equity Shares Forfeited A/c. To Capital Reserve A/c. (Being transferred the balance on forfeiture account to Capital Reserve A/c.)	Dr.		3,25,000	3,25,000
14	7% Preference Share Capital A/c. To 7% Pref. Shares Forfeited A/c. To 7% Pref. Share Final Call A/c. (Being forfeited 40 7% preference shares upon non-payment of final call)	Dr.		8,00,000	6,40,000 1,60,000

* 1,20,00,000 - 1,00,000 = 1,19,000

80,00,000 - 1,60,000 = 78,40,000

Note: Balance on Preference Shares Forfeited Account can be transferred to Capital Reserve after re-issue of the same.

3.3 Summary:

At the beginning of this unit, we have seen what is company and what are its characteristics. In short we also touched upon types of companies. In the core part of the unit, we have covered shares, issue of shares, forfeiture of shares, effect of forfeiture, reissue of forfeited shares, issue of two classes of shares. In initial state of subject matter, we try to understand the meaning and essential features of share, stock, difference between share and stock. There are two way to issue shares i.e. issue of shares for cash and issue of shares for consideration other than cash.

Terms of issue of shares under consideration for cash are three i.e. (a) issue of shares at par, (b) issue of shares at premium and (c) issue of shares at discount. As per Section 53 of Companies Act, the issue of shares at discount is prohibited. Procedure of issue of shares is divided into instalments like application, allotment and calls. After offer of issue there may be any one of three situations full subscription, oversubscription or under-subscription. Calls in advance and Calls in arrears are also considered for accounting properly.

Forfeiture of shares is nothing but the termination of membership and taking away of the shares because of default in payment of allotment and/or call money by a shareholder. After forfeiture of shares, a company can re-issue those shares at par, at premium or at discount.

3.4 Terms to Remember:

1. **Company:** Company means an association of persons formed for the economic gain of the members. The characteristics of a company includes (a) it is voluntary association, (b) it is independent legal entity, (c) it has perpetual succession, (d) company being artificial entity, has common seal, (e) liability of members is generally limited and (f) shares of company are freely transferable.
2. **Shares:** Share is a part of share capital which has equal value. According to Section 2 (84) of Companies Act 2013, a share means "share in the share capital of a company and includes stock".
3. **Stock:** Stock is the aggregate consolidated holdings of the share capital of a person.
4. **Preference Shares:** Preference shares are those which carry the following preferential rights over other classes of shares: (a) a preferential right in respect of a fixed dividend and (b) a preferential right as to repayment of the capital in the event of company's winding up.
5. **Application:** When company offer issue of shares, people may make application for subscription by paying application money.
6. **Allotment:** Allotment means allocating or apportioning a certain number of shares to an applicant in response to his application.

7. **Calls:** After allotment of shares, whenever there will be need, the company may demand money towards payment of the value of shares held by shareholders. Such demands are known as ‘calls’.
8. **Under-subscription:** When a company receives applications for the shares less than the shares offered by it to the public, it is called under-subscription.
9. **Oversubscription:** When a company receives applications for the shares more than the shares offered by it to the public, it is called oversubscription.
10. **Calls in Advance:** The amount received in advance as payment of calls will be credited to a “Call in Advance Account”.
11. **Calls in Arrears:** If shareholder does not pay the call money when it becomes due, it is known as ‘Calls in Arrears’.
12. **Issue of Shares at par:** When shares are issued at face value, it is the issue of shares at par.
13. **Issue of Shares at premium:** When shares are issued at higher than the face value, it is the issue of shares at a premium.
14. **Share Premium:** The amount a company receives over and above face value of shares at the time of issue of shares. It is accounted for on Securities Premium Account.
15. **Issue of Shares at discount:** When shares are issued at lower than the face value, it is the issue of shares at a discount. According to Companies Act 2013, a company cannot issue shares at a discount except sweat equity shares.
16. **Discount on issue of shares:** When shares are issued at lower than the face value, the difference between face value and issue price is called a discount.
17. **Forfeiture of Shares:** Forfeiture of shares is nothing but the termination of membership and taking away of the shares because of default in payment of allotment and/or call money by a shareholder.
18. **Redemption of Preference Shares:** The redemption of preference shares means the process of repaying the amount of capital to preference share capital after its term.

3.5 Answers to Check your progress:

Answers to Check Your Progress-1:

(A) 1. False 2. True 3 False

(B) Securities Premium 2. Maximum 3. three

Answers to Check Your Progress-2:

(A) 1. Oversubscription, 2. Undersubscription,
3. Share Premium/ Securities Premium

(B) 1. b) Excess application money, 2. c) For personal expenses of manager,
3. d) Calls in arrears

Answers to Check your progress-3:

(a) Forfeiture of shares, (b) 14, (c) Discount, (d) Capital Reserve A/c.

3.6 Exercise:

A) Short Answer Questions :

1. What is the Forfeiture of Shares
2. What is the Re-issue of forfeited shares
3. What is under subscription ?
4. Describe the oversubscription
5. What is call in arrears and its accounting treatment ?
6. What is call in advance and its accounting treatment ?

B) Short Answer Questions :

1. What is the procedure of issue of shares?
2. What is accounting treatment for issue of shares at par and at premium?
3. How does a company deal with the forfeiture and reissue of shares as far as its accounting is concerned?
4. Problems on Issue of shares

5. On 10 January 2016, a company offers 8,000 shares of Rs.10 each. Applications are received for full 8,000 shares. Money is payable as follows:

On Application	Rs.3
On Allotment	Rs.2
On first call	Rs.3
On final call	Rs.2

The shares were duly allotted, calls made and money realized.

You are required to pass the necessary journal entries.

6. Kolhapur Udyog Ltd. issued 1000 Equity shares of Rs.100 each at a premium of Rs. 20 per share. The share amount was collected as follows:

On Application	Rs.15
On Allotment	Rs. 55 including premium
On first call	Rs.25
On final call	Rs.25

Mr. Careless to whom 200 shares were allotted, failed to pay both the calls. Mr. Misfortune failed to pay final call on his 100 shares. Shares were forfeited on which both the calls were not paid. The Directors re-issued these forfeited shares to Mr. Lucky at Rs.80 per share, fully paid.

Give journal entries.

(Clue: 200 shares of Mr. Careless only are forfeited. Capital Reserve Rs.6,000)

7. ABC Co. Ltd. had called up Rs.100 per share on the whole of subscribed capital of 50,000

Equity Shares of Rs.100 payable as follows:

Rs.10 on Application
Rs.20 on Allotment
Rs.30 on first call
Rs.40 on final call

X, Y & Z were the holders of 100 shares, 200 shares & 300 shares respectively in the above company.

X failed to pay the final call, Y failed to pay the first as well as final call while Z failed to pay the amounts on Allotment, first and final calls.

The Directors after giving due notice forfeited all the shares held by X, Y & Z and re-issued all shares to D for cash at a discount of 10%.

Pass the journal entries regarding forfeiture & re-issue only.

Problems on Redemption of Preference Shares:

8. The Dhanpal Ltd. has as a part of share capital, 500 Redeemable Preference Shares of Rs.100 each fully paid up & these have become due for redemption.

The company having Rs. 45,000 to its Reserve Fund, issued Equity Shares of the face value of Rs.30,000 at a premium of 5% specially for the purpose of such redemption and received cash for the full amount of the issue.

The redeemable preference shares are then paid out of the proceeds of the new issue, the balance having been met out the balance to the credit of Reserve Fund.

Pass journal entries.

9. X Co. decided to redeem its 40,000 6% Redeemable Preference Shares of Rs.10 each on which Rs.7 per share have been called up & paid up. The redemption was carried out of profits. Journalize.

3.7 Reference for further study:

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Unit 4

Valuation of Shares

4.0. Objectives

4.1. Introduction

4.2. Valuation of Shares

4.2.1 Valuation of Equity Shares

4.2.1.1 Introduction to Valuation of Equity Shares

4.2.1.2 Need for Valuation of Equity Shares / Circumstances Leading to Valuation of Equity Shares

4.2.1.3 Factors affecting valuation of Equity shares

4.2.1.4 Methods of Valuation of Equity Shares

4.2.1.4.1. Net Assets Method

4.2.1.4.2 Yield Value Method –

4.2.1.4.3. Fair Value Method

4.2.1.5 Illustrations

4.2.2. Valuation of Preference Shares

4.2.2.1 Introduction to Valuation of Preference Shares

4.2.2.2 Factors Influencing Valuation of Preference Shares

4.2.2.3 Calculation of value of Redeemable Preference Shares

4.2.2.4 Illustrations

4.0 Objectives - After studying this unit, you will be able to –

Understand meaning of valuation of equity and preference shares

Explain need for valuation

Find out factors affecting valuation of shares

Find the relationship between earnings of the company and the value of shares

Calculate value of equity shares and preference shares

4.1 Introduction

In the previous you studied meaning of company, types of companies, types of shares – share, features of Equity share & Preference shares, legal provisions related to corporate accounting, issue, forfeiture and reissue of shares. This study will help to understand the valuation of shares i.e. why, when and how the shares are valued.

4.2 Valuation of Shares

4.2.1 Valuation of Equity Shares

4.2.1.1 Introduction to Valuation of Equity Shares

Every limited company has share capital divided in equity shares, preference shares or both. Each share has its face value. The face value is the initial price of the share fixed by the company. Face value never changes. Another value of share is market value. Market value of share means the value which is determined by the market. Market value of equity shares increases or decreases based on company's performance, rate of dividend, demand & supply of the equity shares etc. In general, investors' decision of buying or selling the equity shares is based on the market value. As such, when one company takes over another company, market price of equity shares is the most considerable factor. So, even though, each share is having face value, its valuation becomes essential. Valuation of share is a system of determining the value of a business by estimating the value of its equity shares. It is an evaluation of the net worth of the company's ownership through separate methods and assumptions.

4.2.1.2 Need for Valuation of Equity Shares / Circumstances Leading to Valuation of Equity Shares

1. When companies are amalgamated or absorbed, to know the value of the equity shares held by the shareholders of the liquidating companies and to protect their rights.
2. When a company is reconstructed to ascertain actual value of the equity shares held by the existing shareholders to compensate them.
3. When equity shares are held by the partners jointly and dissolution of the firm or retirement or death of a partner takes place, it is necessary to value the equity shares for proper distribution of partnership property among the partners.
4. When equity shares are given by one member of a private company to other member, it becomes necessary to ascertain fair price of the equity shares.

5. When a loan is advanced on the security of the equity shares, to know the real value of the equity shares.
6. When debentures are converted into equity shares, to ascertain the number of equity shares to be issued to the debenture holders.
7. When preference shares are converted into equity shares, to ascertain the number of equity shares to be issued to the preference shareholders.
8. When a company is nationalised, to determine the compensation to the shareholders.
9. When a company issue equity shares, to take decision whether to issue equity shares at premium or at par.

4.2.1.3 Factors affecting valuation of Equity shares

Principally, the dividend yield is the main factor which affect greatly on the valuation of equity shares. The rate of dividend that the investor expects is the key factor in valuation of equity shares. For small investors the rate of dividend declared by the company plays an important role in valuation of equity shares. Whereas, the investors holding bulk of equity shares total profit or earning capacity is the major factor affecting the valuation of equity shares.

The other factors are –

1. Purpose of valuation of equity shares
2. The nature of the business and of the company
3. Demand and supply of equity shares in the market
4. The Government policy
5. Past performance of the company i.e. Profits earned and dividend paid over the years
6. Potential growth and prospects of the company
7. The management of the company
8. Financial position and accumulated reserves of the company
9. Possibility of bonus or right issue of equity shares
10. Current stock market price of the equity shares
11. Realisable value of the net assets of the company.

12. Current and deferred liabilities for the company.
13. Efficiency, integrity and honesty of Board of Directors and other managerial personnel of the company i.e. quality of top and middle management of the company and their professional competence.

4.2.1.4 Methods of Valuation of Equity Shares

Mainly there are three methods of valuation of equity shares.

1. Net Assets Method
2. Yield Value Method
3. Fair Value Method

4.2.1.4.1. Net Assets Method

This method is also called as Asset Backing Method or Asset-Basis Method or Intrinsic Value Method or Real Value Method.

Since the valuation is made on the basis of the assets of the company, it is called as Net Asset Method or Asset Basis or Assets Backing Method and as the equity shares are valued on the basis of real internal value of the assets of the company, it is called as Intrinsic Value or Real Value Method. Under this method, the net value of assets of the company is divided by the number of equity shares to arrive at the value of each share.

Steps for determining value of each share

Step I – Compute the value of Net Assets

Step II – Compute the value of each share

Step I – Computation of value of Net Assets

A) When the values of assets and liabilities are given – Formula for calculating net assets is -

Net Assets = Revised value of assets – Revised values of liabilities

The following points should be considered while computing net value of assets-

- The goodwill (valued as per the instructions) and non-trading assets (at market values) are to be added to trading assets (with revised values or after depreciation, as the case may be) to get total assets.

- If revised values of some assets are not given, book values of these assets can be considered.
- The fictitious assets such as preliminary expenses, discount on issue of equity shares and debentures, accumulated losses etc. should **not** be considered.
- Provision for bad debts should be deducted from the debtors if it is given.
- All unrecorded assets and liabilities (if any) should be considered.
- The external liabilities i.e. current liabilities such as sundry creditors, bills payable etc. and long term liabilities such as loan, debentures etc. (including outstanding interest) should be deducted from the value of assets for the determination of net value.
- Preference Share Capital including Preference Dividend in arrear (if any) should also be deducted from the total of assets.
- Net Assets are calculated by deducting value of liabilities from value of assets as below –

Computation of Net Assets

	₹
Assets	
Goodwill (Revised value / valued as per instructions)	***
Fixed Assets (Revised Values)	***
Investments (Market Values)	***
Current Assets (Revised / Market Values)	***
Total Assets	***
Liabilities	
Preference Share Capital	***
Arrears of Preference Share Dividend	***
Long Term Liabilities (Debentures, Bank Loan etc.)	***
Current Liabilities (Creditors, Bills Payables etc.)	***
Total Liabilities	***
Net Assets (Total Assets – Total Liabilities)	***

B) When details of values of assets and liabilities are not given, but other required information is provided – Formula for calculating net assets is –

	₹
Equity Share Capital	***
Reserves & Surplus (General Reserve, Reserve Fund, Profit & Loss A/c Balance, Share Premium A/c etc.)	***
Profit on revaluation of assets	***
Profit on revaluation of liabilities	***
Total 'A'	***
Fictitious Assets (Preliminary Expenses, Discount on issue of Equity shares or Debentures etc.)	***
Loss on revaluation of assets	***
Loss on revaluation of liabilities	***
Total 'B'	***
Net Assets (Total 'A' - Total 'B')	***

Step II – Computation of the value of each share

- The value per share can be determined by using the following formula:

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}}$$

Applicability of the Method:

- The investors can determine the value of equity shares under this method to take the decision of purchasing the equity shares.
- The method is applicable in the case of Amalgamation, Absorption and Reconstruction of companies.

4.2.1.4.2 Yield Value Method–

This method is also called as Market Value Method or Profit Basis Method or Income Basis Method or Earning Capacity Method or Price Earning Ratio Method

Yield is the effective rate of return on investments which is invested by the investors. It is also known as Expected Yield / Rate of Return / Earning Rate / Normal Rate / Rate of General Expectation / Estimated Rate for Capitalisation. Under this method, the valuation depends upon the comparison of the company's earning capacity and the normal rate of profit or dividend that is prevailing in the market. Here, the profit means, profit available for equity dividend. It may be termed as average profit or maintainable profit or expected profit. It is always expressed in terms of percentage and calculated as,

$$\text{Yield} = \frac{\text{Profit / Earning (after tax \& Preference Dividend)}}{\text{Equity Share Capital}} \times 100$$

Thus, expected rate of return on investment is denoted by yield. Rate of Return refers to the return which a shareholder earns on his investment. It is also called as Rate of Earning or Rate of Profit or Rate of dividend.

Under this method, equity shares are valued on the basis of expected earning, normal rate of return and price earning ratio. There are different ways for calculation of value per share.

Students can use any one of the following ways considering the information given in the problem.

A) On the basis of expected earnings

Step I – Calculate expected Rate of Earning / Dividend

$$\text{Expected Rate of Earning/Dividend} = \frac{\text{Profit after Tax \& Preference Dividend / Profit available for Equity Dividend}}{\text{Paid up Value of Equity Share Capital}} \times 100$$

Step II – Calculate Value of each share

$$\text{Value per Share} = \frac{\frac{\text{Expected Rate of Earning} / \text{Dividend}}{\text{Normal Rate of Return}} \times \text{Paid up value of Equity Share}}$$

B) On the basis of capitalized value

Step I – Calculate capitalized value

$$\text{Capitalised Value} = \frac{\frac{\text{Average Profit (after tax)} / \text{Profit available for Equity Dividend}}{\text{Normal Rate of Return}} \times 100$$

Step II -Calculate Value of each share

$$\text{Value per Share} = \frac{\text{Capitalised Value}}{\text{Number of Equity Shares}}$$

C) On the basis of normal rate and number of equity shares

$$\text{Value per Share} = \frac{\frac{\text{Average Profit (after tax)} / \text{Profit available for Dividend}}{\text{Normal Rate} \times \text{Number of Equity Shares}} \times 100$$

D) On the basis of Price Earnings Ratio

$$\text{Earnings per Share} = \frac{\text{Profits available for Equity Shareholders}}{\text{No. of Equity Shares}}$$

Market Value per Share = Price Earnings Ratio x Earning per Share

4.2.1.4.3 Fair Value Method -Fair Value Method which is the mean of Intrinsic Value Method and Yield Value Method. As it considers both the values i.e. intrinsic value and yield value, it provides a better indication about the value of equity shares.

$$\text{Fair Value of Equity Share} = \frac{\text{Intrinsic Value} + \text{Yield Value}}{2}$$

4.2.1.5 Illustrations

A) Computation of Intrinsic Value of Share

- When revised values of assets and liabilities are given

Illustration 1: From the following Balance Sheet of Swati Ltd. you are asked to ascertain the value of each Equity Share of the company.

Balance Sheet as on 31/3/2025

Liabilities	₹	Assets	₹
20000 Equity Shares of ₹100 each	2000000	Goodwill	50000
1000 6% Preference shares of ₹100 each	100000	Land & Building	1000000
General Reserve	90000	Plant & Machinery	1200000
7% Debentures	600000	Investments	300000
Sundry Creditors	50000	Stock	50000
Provision for Tax	30000	Sundry Debtors	40000
Bills Payables	20000	Bank Balance	240000
	2890000	Preliminary Expenses	10000
			2890000

1. The assets were revalued as:
Goodwill Rs. 100000, Land and Building at ₹ 1500000,
Plant and Machinery ₹ 960000, Market value of Investments is ₹ 250000,
Debtors after providing for bad debts at 10%
2. Interest outstanding on debentures is ₹21000.
3. Actual tax liability as calculated by the tax consultant is ₹ 25000.
4. Other assets and liabilities have no change in their values.

Solution - In the books of Swati Ltd.

Step I – Computation of Net Assets

Calculation of Net Assets

Particulars	₹
Assets (with revised values)	
Goodwill	100000
Land & Building	1500000
Plant & Machinery	960000
Investments	250000
Stock	50000
Sundry Debtors (40000- 4000)	36000
Bank Balance	240000
Total	3136000
Liabilities (with revised values)	
6% Preference Share Capital	100000
7% Debentures	600000
Outstanding Interest on Debentures (7% on 600000 for half year)	21000
Sundry Creditors	50000
Tax Liability	25000
Bills Payables	20000
Total	816000
Net Assets	2320000

Step II – Computation of value of each share

$$\text{Value Per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{2320000}{20000} = ₹ 116$$

- **When changes in the values of assets are given in percentage**

Illustration 2: Jyoti Ltd. provides you the following -

Balance Sheet as on 31st March 2025

Liabilities	₹	Assets	₹
5000 Equity Shares of ₹100 each	500000	Land & Building	300000
Profit & Loss A/c	450000	Plant & Machinery	600000
Capital Reserve	150000	Investment in Equity shares	250000
General Reserve	180000	Stock	150000
8% Debentures	220000	Sundry Debtors	240000
Sundry Creditors	250000	Bank Balance	210000
	1750000		1750000

Additional Information:

- Land and Building and Plant and Machinery were revalued at 150% and 120%, respectively.
- The value of the equity shares purchased by the company is fallen down by 20% in the market.
- Stock is valued at ₹ 200,000 and Debtors subject to a deduction @ 5% for bad debts.
- Manager's Remuneration ₹ 8,000 is payable.

Ascertain the Intrinsic Value of Equity shares.

Solution - In the books of Jyoti Ltd.

Calculation of Net Assets

Particulars	₹
Assets (with revised values)	
Land & Building	
150	
----- x 300000	
100	450000

Plant & Machinery	
120	
----- x 600000	720000
100	
Investments (250000 – 50000 (20%))	200000
Stock	200000
Sundry Debtors (240000 – 12000 (5%))	228000
Bank Balance	210000
	Total
	2008000
Liabilities (with revised values)	
8% Debentures	220000
Sundry Creditors	250000
Outstanding Remuneration	8000
	Total
	478000
	Net Assets
	1530000

$$\text{Value Per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{1530000}{5000} = ₹ 306$$

- **When information of two companies is given and advise is to be given**
- Illustration 3:** Aarati wants to invest her savings in equity shares of limited companies. She has two options Shridevi Co. Ltd and Mahadevi Co. Ltd. She expects your expert advise that of which company's share she should purchase. She is providing you the following information about these companies.

Balance Sheets as on 31/3/2025

Liabilities	S. Co. ₹	M. Co. ₹	Assets	S. Co. ₹	M. Co. ₹
Equity Shares of ₹100 each	200000	400000	Fixed Assets	425000	730000
Reserves & Surplus	180000	140000	Investment	45000	110000
Secured long term loans	230000	475000	Current Assets	360000	280000
Current Liabilities	220000	105000			
	830000	1120000		830000	1120000

Market values of assets are

Assets	S. Co. ₹	M. Co. ₹
Fixed Assets	439000	660000
Investment	50000	140000
Current Assets	320000	210000

2. Secured loans of Shridevi Ltd. include Bank Loan of ₹ 50000. The bank declared 2% Rebate for timely repayment of instalments.
3. Secured loans of Mahadevi Ltd. include 10% Debentures of ₹ 100000. Interest on these debentures for the year 2018-19 is unpaid.

Solution - In the books of Jyoti Ltd.

Calculation of value of secured loans - Shridevi Ltd. – 230000 – 1000 (2% of 50000)
= 229000

Calculation of current liabilities - Mahadevi Ltd. – 105000 + 10000 (10% of 100000)
= 115000

Calculation of Net Assets

Particulars	S. Co. ₹	M. Co. ₹
Assets (with revised values)		
Fixed Assets	439000	660000
Investment	50000	140000
Current Assets	320000	210000
Total	809000	1010000
Liabilities (with revised values)		
Secured long term loans	229000	475000
Current Liabilities	220000	115000
Total	449000	590000
Net Assets	360000	420000

$$\text{Shridevi Ltd. - Value Per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{360000}{2000} = ₹ 180$$

$$\text{Mahadevi Ltd. - Value Per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{420000}{4000} = ₹ 105$$

Advise – As the intrinsic value of each equity share of Shridevi Ltd. is higher than the intrinsic value of each share of Mahadevi Ltd., so Aarati should invest in equity shares of Shridevi Ltd.

- **When net assets are to be calculated by alternative method Illustration 4.** From the following Balance Sheet and other information of Sangita Ltd. you are asked to ascertain the value of each Equity Share of the company.

Balance Sheet as on 31/3/2025

Liabilities	₹	Assets	₹
700 Equity Equity shares of ₹1000 each	700000	Land & Building	375230
Profit & Loss A/c	57500	Plant & Machinery	657320
Capital Reserve	156000	Investment in Equity shares	258440
General Reserve	89500	Stock	156950
8% Debentures	650000	Sundry Debtors	241250
Sundry Creditors	251800	Bank Balance	203110
		Discount on issue of equity shares	12500
	1904800		1904800

The company revalued the assets to match its real and market values. In this revaluation land & building, investments and stock showed profit totally of ₹ 45750, while plant & machinery showed a loss of ₹ 21250. It is also necessary to create reserve for bad debts at 5%.

Solution – In the books of Sangita Ltd.

Calculation of Net Assets

Particulars	₹
700 Equity Shares of ₹1000 each	700000
Profit & Loss A/c	57500
Capital Reserve	156000
General Reserve	89500
	45750

Profit on Revaluation of assets	1048750
Total	12500
Less – Discount on issue of equity shares	21250
Loss on revaluation of assets	33750
Total	1015000
Net Assets	

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{1015000}{700} = ₹ 1450$$

- **When valuation of goodwill is required**

Illustration 5. Kavita Ltd. presented the following Balance Sheet as on 31st March 2025.

Liabilities	₹	Assets	₹
20000 Equity Shares of ₹100 each	20,00,000	Premises	30,00,000
5000 Preference shares of 100 each	5,00,000	Furniture	7,00,000
Profit & Loss A/c	7,80,000	Investment (Market Value 3,00,000)	3,50,000
Reserve Fund	10,90,000	Stock of goods	15,00,000
8% Debentures	7,00,000	Sundry Debtors	5,40,000
Bank Loan	8,50,000	Bank Balance	2,00,000
Sundry Creditors	4,80,000	Cash in hand	1,10,000
	64,00,000		64,00,000

Additional Information:

- Premises and Furniture were revalued at ₹ 32,00,000 and ₹5,00,000 respectively.
- Investments were brought down to market value.
- Stock to be taken at ₹ 16,00,000.
- Debtors subject to a deduction of ₹ 20,000 for bad debts.
- Net profits for the last five years were ₹1,25,000; ₹2,25,000; ₹2,50,000; ₹1,75,000 and ₹ 2,25,000. Goodwill is to be valued at 3 years' purchase of average Net Profit.

Ascertain the Intrinsic Value of Equity shares.

Solution – In the books of Kavita Ltd.

1. Calculation of Goodwill

$$\text{Average Profit} = \frac{1,25,000 + 2,25,000 + 2,50,000 + 1,75,000 + 2,25,000}{5} = \frac{10,00,000}{5} = 2,00,000$$

$$\text{Goodwill} = 2,00,000 \times 3 = 6,00,000$$

2. Calculation of Net Assets

Particulars	₹
Assets (with revised values)	
Goodwill	6,00,000
Premises	32,00,000
Furniture	5,00,000
Investments	3,00,000
Stock	16,00,000
Sundry Debtors (540000- 20000)	5,20,000
Bank Balance	2,00,000
Cash in hand	1,10,000
Total	70,30,000
Liabilities (with revised values)	
Preference Share Capital	5,00,000
8% Debentures	7,00,000
Bank Loan	8,50,000
Sundry Creditors	4,80,000
Total	25,30,000
Net Assets	45,00,000

3. Calculation of value of each equity share

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{45,00,000}{20,000} = ₹ 225$$

- **When some equity shares are partly paid**

Illustration 6. The following particulars relate to Priya Co. Ltd.

	₹
Total Assets	25,90,000
External liabilities	3,50,000
Share Capital	
14% preference shares of 100 each fully paid	7,00,000
5,600 equity shares of 100 each fully paid	5,60,000
8,400 equity shares of 100 each 75 paid	6,30,000

Calculate the value of each category of equity shares of the company

Solution. Here some equity shares are fully paid and some are partly paid, in this case, partly paid equity shares are to be made fully paid notionally and then value per equity share should be calculated. After valuation, unpaid amount is to be deducted from the calculated value.

1. Calculation of Net Worth

		₹
Total Assets		25,90,000
Less - External liabilities	3,50,000	
14% preference shares capital	7,00,000	10,50,000
Net Worth		15,40,000
Add – Notional call on partly paid equity shares - 8,400 x 25		2,10,000
Adjusted Net Worth		17,50,000

2. Calculation of value of each equity share

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{17,50,000}{14,000 (5600 + 8400)} = ₹ 125$$

- a) Value of fully paid equity share = ₹125
 b) Value of partly paid equity share = $125 - 25 = ₹ 100$

B) Computation of Yield Value of Share

- **When average profit is given**

Illustration 7. From the following information of Jamanadas Co. Ltd. compute the value of its equity share on the basis of – a) Expected earnings, b) Capitalisation and c) Normal rate and number of equity shares

Balance Sheet as on 31/3/2025

Liabilities	₹	Assets	₹
5000 Equity Shares of ₹100 each	5,00,000	Fixed Assets	7,00,000
Reserves and Surplus	1,80,000	Current Assets	4,60,000
10 % Debentures	3,00,000	Discount on issue of Debentures	40,000
Current Liabilities	2,20,000		
	12,00,000		12,00,000

Other information

1. Average profit before tax is ₹2,82,000
2. Rate of Tax is 50%
3. Every year the company transfers ₹24,000 to Reserve Fund.
4. The rate of normal earnings is 12.5%.

Solution – In the books of Jamanadas Co. Ltd.

1. Calculation of Profit available for dividend / equity shareholders / Earnings

	₹
Average Profit	2,82,000
- Tax – 50% of 2,82,000 =	1,41,000
- Transfer to Reserve Fund <u>24,000</u>	1,65,000
Profit available for dividend / Earnings	1,25,000

A) On the basis of earning

Step I – Calculation of Expected Rate of Earning

$$\text{Expected Rate of Earning} = \frac{\text{Profit after Tax \& Preference Dividend}}{\text{Paid up Equity Share Capital}} \times 100$$

$$\text{Expected Rate of Earning} = \frac{1,25,000}{5,00,000} \times 100 = 25\%$$

Step II – Calculation of value of each share

$$\text{Value per Share} = \frac{\text{Rate of Earning}}{\text{Normal Rate of Return}} \times \text{Paid up value of Equity Share}$$

$$\text{Value per Share} = \frac{25}{12.5} \times 100 = ₹200$$

B) On the basis of capitalized value

Step I – Calculation of capitalized value

$$\text{Capitalised Value} = \frac{\text{Average Profit}}{\text{Normal Rate of Return}} \times 100$$

$$\text{Capitalised Value} = \frac{1,25,000}{12.5} \times 100 = ₹10,00,000$$

Step II – Calculation of value of each share

$$\text{Value per Share} = \frac{\text{Capitalised Value}}{\text{Number of Equity Shares}}$$

$$\text{Value per Share} = \frac{10,00,000}{5,000} = ₹200$$

C) On the basis of normal rate and number of equity shares

$$\text{Value per Share} = \frac{\text{Average Profit}}{\text{Normal Rate} \times \text{Number of Equity Shares}} \times 100$$

$$\text{Value per Share} = \frac{1,25,000}{12.5 \times 5,000} \times 100 = ₹200$$

Note – Students can know from this example that, every method gives the same answer, so, they can use any one of the above methods, provided particular basis is not mentioned in the problem.

- **When average profit is to be calculated**

Illustration 8. On March 31, 2025 the Balance Sheet of Mataji Ltd. disclosed the following position.

Liabilities	₹	Assets	₹
Equity Shares of ₹100 each	10,00,000	Goodwill	1,00,000
Reserves	2,25,000	Other Fixed Assets	9,20,000
P. & L. A/c Balance	50,000	Investments	3,30,000
9 % Debentures	2,50,000	Current Assets	5,00,000
Current Liabilities	3,25,000		
	18,50,000		18,50,000

Net Profit for the last 3 years were, 2020-21 – ₹1,29,000, 2021-22 – ₹1,31,500 and 2022-23 – ₹1,29,125, of which 20% was transferred to Reserve. Fair investment return in the industry in which the company is engaged is 10%.

Compute the value of the company's share under yield-basis method.

Solution – In the books of Mataji Ltd.

Note – As any basis is not mentioned in the problem, students can solve this problem by applying any one of the three bases.

1. Calculation of Average Profit available for Equity Share Holders -

		₹
1,29,000 + 1,31,500 + 1,29,125	3,89,625	1,29,875
Average Profit = -----	-----	
3	3	
Less – Transfer to Reserve – 20% of 1,29,875		25,975
Average Profit available for Equity Share Holders		1,03,900

2. Calculation of value per share

$$\text{Value per Share} = \frac{\text{Average Profit}}{\text{Normal Rate} \times \text{Number of Equity Shares}} \times 100$$

$$\text{Value per Share} = \frac{1,03,900}{10 \times 10,000} \times 100 = ₹103.90$$

• **When equity shares are partly paid**

Illustration 9. From the following information of Pitaji Ltd. calculate the value of each Equity Share on the basis of rate of dividend.

- Equity Share Capital – 20,000 equity shares of 100 each, 80% paid up
- 9% Preference Share Capital – 25,000 equity shares of 100 each fully paid
- Net Profit before tax **₹10,00,000**
- Rate of Tax – 40%
- It is the company's policy to transfer 10% of profit to reserves
- Rate of Dividend of other companies working in the same industry is 14%

Solution – In the books of Pitaji Ltd.

1. Calculation of profit available for dividend

	₹
Net Profit before tax	10,00,000
Less – Tax 40% of 10,00,000	4,00,000

Profit after tax	6,00,000
Less – Transfer to Reserve – 10% of 6,00,000 - 60,000	
Preference Dividend – 9% of 25,00,000 – <u>2,25,000</u>	2,85,000
Profit available for equity shareholders	3,15,000

2. Calculation of Rate of Dividend

$$\text{Rate of Dividend} = \frac{\text{Profit after Tax \& Preference Dividend}}{\text{Paid up Equity Share Capital}} \times 100$$

$$\text{Rate of Dividend} = \frac{3,15,000}{16,00,000} \times 100 = 19.69\%$$

3. Calculation of value of each share

$$\text{Value per Share} = \frac{\text{Rate of Dividend}}{\text{Normal Rate of Return}} \times \text{Paid up value of Equity Share}$$

$$\text{Value per Share} = \frac{19.69}{14} \times 80 = ₹112.51$$

• When Profit & Loss A/c is required to prepare

Illustration 10. Gurun and Co. Ltd. is providing you the following information for the financial year 2022-23.

- 6,500 Equity shares of ₹100 each.
- 500 9% Preference shares of ₹1000 each.
- 200 11% Debentures of ₹2000 each.
- Bank loan ₹10,00,000 taken for business expansion. Interest is payable @ 12% annually.
- Net Sales ₹42,35,000
- Operating Expenses ₹35,43,000
- Rate of tax is 50%

8. Transfer to Reserve as per policy of the company ₹24,000 per year.

9. Normal Rate of Return in the industry is 15%.

It is the request of the company to you to calculate value of each equity share by capitalisation method

Solution – In the books of Gurn and Co. Ltd.

1. Calculation of Profit available for Equity Dividend

	₹	₹
Net Sales		42,35,000
Less – Operating Expenses	35,43,000	
Interest on Debentures – 11% on (200 x 2,000)	44,000	
Interest on Bank Loan - 12% on 10,00,000	1,20,000	37,07,000
Net Profit before Tax		5,28,000
Less – Tax – 50% of 5,28,000		2,64,000
Net Profit after Tax		2,64,000
Less – Preference Dividend – 9% on (500 x 1000)	45,000	
Transfer to Reserve	24,000	69,000
Net Profit available for Equity Dividend		1,95,000

2. Calculation of capitalized value

$$\text{Capitalised Value} = \frac{\text{Profit available for Equity Dividend}}{\text{Normal Rate of Return}} \times 100$$

$$\text{Capitalised Value} = \frac{1,95,000}{15} \times 100 = 13,00,000$$

3. Calculation of value of each share

$$\text{Value per Share} = \frac{\text{Capitalised Value}}{\text{Number of Equity Shares}}$$

$$\text{Value per Share} = \frac{13,00,000}{6,500} = ₹200$$

- When values of equity share of two companies are required to calculate

Illustration 11. Compute value of each equity share of the following companies.

	Shree Co. ₹	Sneh Co. ₹
Profit after tax	10,00,000	6,00,000
12% Preference Share Capital in equity shares of ₹1000 each	30,00,000	10,00,000
Equity Share Capital in equity shares of ₹100 each	20,00,000	20,00,000

Market expectation is 15%. Both the companies distribute 75% of their profit as equity dividend.

Solution – 1. Calculation of Profit available for Equity Dividend

	Shree Co. ₹	Sneh Co. ₹
Profit after tax	10,00,000	6,00,000
Less - Preference Dividend – 12%	3,60,000	1,20,000
Profit available for appropriations	6,40,000	4,80,000
Profit available for Equity Dividend – 75%	4,80,000	3,60,000

2. Calculation of Rate of Dividend

$$\text{Rate of Dividend} = \frac{\text{Profit available for Equity Dividend}}{\text{Equity Share Capital}} \times 100$$

Shree Co.	Sneh Co.
4,80,000	3,60,000
----- x 100 = 24%	----- x 100 = 18%
20,00,000	20,00,000

3. Calculation of Value of each Equity Share

$$\text{Value of Equity Share} = \frac{\text{Rate of Dividend}}{\text{Normal Rate of Dividend}} \times \text{Paid up value of Equity Share}$$

Shree Co.	Sneh Co.
24	18
---- x 100 = ₹160	---- x 100 = ₹120
15	15

- **When profit of two companies is same but capital structure is different**

Illustration 12. Two companies, Ajay Ltd. and Vijay Ltd., are doing similar business. Their balance sheet is also similar except the capital structure.

The share capital of Ajay Ltd. is ₹ 18,70,000, divided into 17,000 6% Preference shares of ₹ 100 each and 17,000 Equity Shares of ₹ 10 each.

The share capital of Vijay Ltd. is also ₹ 18,70,000, divided into 1,700, 6% Preference shares of ₹ 100 each and 1,70,000 Equity Shares of ₹ 10 each.

The fair yield in respect of the equity shares of this type of companies is ascertained at 8%.

Both the companies earned same amount of profit during the last two years - 2021-22 ₹ 1,87,000 and 2022-23 ₹ 2,55,000.

Calculate the value of the Equity Shares of each of these two companies on 31.3.2025 on the basis of this information only. Ignore taxation.

Solution – In the books of Ajay Ltd and Vijay Ltd

A) On the basis of earning

Step I – Calculation of Expected Rate of Earning

$$1. \text{ Calculation of Average Profit} = \frac{187000 + 255000}{2} = 221000$$

Ajay Ltd.	Vijay Ltd.
Average Profit 2,21,000	Average Profit 2,21,000
- Preference Dividend <u>1,02,000</u> 1,19,000	- Preference Dividend <u>10,200</u> 2,10,800

$$2. \text{ Expected Rate of Earning} = \frac{\text{Profit after Tax \& Preference Dividend}}{\text{Paid up Equity Share Capital}} \times 100$$

Ajay Ltd.	Vijay Ltd.
Expected Rate of Earning $\frac{1,19,000}{1,70,000} \times 100 = 70\%$	Expected Rate of Earning $\frac{2,10,800}{17,00,000} \times 100 = 12.4\%$

Step II – Calculate Value of each share

$$\text{Value per Share} = \frac{\text{Rate of Earning}}{\text{Normal Rate of Return}} \times \text{Paid up value of Equity Share}$$

Ajay Ltd.	Vijay Ltd.
Value per Share = $\frac{70}{8} \times 10 = ₹ 87.50$	Value per Share = $\frac{12.4}{8} \times 10 = ₹ 15.50$

B) On the basis of capitalized value

Step I – Calculate capitalized value

$$\text{Capitalised Value} = \frac{\text{Average Profit}}{\text{Normal Rate of Return}} \times 100$$

Ajay Ltd.	Vijay Ltd.
Capitalised Value = $\frac{1,19,000}{8} \times 100 = 14,87,500$	Capitalised Value = $\frac{2,10,800}{8} \times 100 = 26,35,000$

Step II - Calculate Value of each share

$$\text{Value per Share} = \frac{\text{Capitalised Value}}{\text{Number of Equity Shares}}$$

Ajay Ltd. 14,87,500 Value per Share = $\frac{14,87,500}{17,000} = 87.50$	Vijay Ltd. 2,10,800 Capitalised Value = $\frac{2,10,800}{8} \times 100 = 15.50$
---	--

C) On the basis of normal rate and number of equity shares

$$\text{Value per Share} = \frac{\text{Average Profit}}{\text{Normal Rate} \times \text{Number of Equity Shares}} \times 100$$

Ajay Ltd. 1,19,000 Value per Share = $\frac{1,19,000}{8 \times 17,000} = 87.50$	Vijay Ltd. 2,10,800 Capitalised Value = $\frac{2,10,800}{8 \times 1,70,000} \times 100 = 15.50$
--	--

Note – students can solve the above problem by applying any of the methods.

- **When average profit and price earning ration is given**

Illustration 13. The capital structure of Ganesh Co. Ltd. is as follows

	₹
12% Preference shares of ₹10 each	250000
Equity shares of ₹10 each	400000
Reserves & Surplus	200000
10% Debentures	300000
11% Term Loan	350000

The average annual profit before payment of tax and interest is ₹328500.

The income tax rate is 50%.

Price earnings ratio is 9.

You are required to calculate valuation of equity shares.

Solution – In the books of Ganesh Co.

1. Calculation of profit available for equity share holders

	₹	₹
Profit before interest and tax		328500
Less - Interest on 10% Debentures	30000	
Interest on 11% Term Loan	38500	68500
Profit after interest		260000
Less – Income Tax – 50%		130000
Profit after interest and tax		130000
Less - 12% Preference shares Dividend		30000
Profit available for equity dividend		100000

$$\text{Earnings per share} = \frac{\text{Profit available for equity shareholders}}{\text{No. of equity shares}} = \frac{1\ 00000}{40000} = ₹2.50$$

$$\begin{aligned} \text{Market Value per share} &= \text{Price Earnings Ratio} \times \text{Earning per Share} = 9 \times 2.50 \\ &= ₹22.50 \end{aligned}$$

- **When price earning ratio is given but average profit is to be calculated**

Illustration 14. Haripriya Ltd. having paid up equity capital of ₹ 6,00,000 divided in equity shares of ₹10 each, decided to sell its business. Net Profits of the company after tax and interest were –

2018 -19- ₹ 1,80,000, 2019 -20 - ₹1,60,000, 2020 -21 – ₹1,95,000,
2021 -22 – ₹1,80,000, 2022 -23 – ₹1,85,000

The applicable price earnings ratio is 8

The company asking you to make an assessment of the price per equity share that a purchaser might be expected to offer.

Solution – In the books of Haripriya Ltd.

1. Calculation of Average Profit-

$$\text{Average Profit} = \frac{(1,80,000 + 1,60,000 + 1,95,000 + 1,80,000 + 1,85,000)}{5} = 1,80,000$$

2. Calculation of Earnings per Share

$$\text{Earnings per share} = \frac{\text{Profit available for equity share holders}}{\text{No. of equity shares}}$$

$$\text{Earnings per share} = \frac{180000}{60000} = ₹3$$

$$\text{Market Value per share} = \text{Price Earnings Ratio} \times \text{Earning per Share} = 8 \times 3 = ₹24$$

C) Computation of Fair Value of Share

- When fair value of share is to be calculated

Illustration 15. The following is the Balance Sheet of Sneh Co. Ltd. as on 31.3.2025

Liabilities	₹	Assets	₹
10,000 Equity Share Capital (Equity shares of ₹10 each)	1,00,000	Building	2,00,000
12% Preference shares of ₹10 each	1,00,000	Plant	1,00,000
General Reserve	60,000	Investment	50,000
Profit & Loss A/c	40,000	Stock	60,000
15% Debentures	1,00,000	Debtors	40,000
Creditors	80,000	Cash	10,000
	4,80,000	Discount on issue of debentures	20,000
			4,80,000

Ascertain the value of each equity share under Fair Value Method on the basis of the above balance sheet and information given below.

Assets are revalued as, Building ₹ 3,20,000, Plant ₹ 1,80,000, Stock ₹ 45,000 and Debtors ₹ 35,000. No change in the values of liabilities.

Average Profit of the company is ₹ 1,20,000 and 12½% of profit is transferred to General Reserve, Rate of taxation being 50%. Normal dividend expected on equity shares is 8% whereas fair return on capital employed is 10%.

Solution - In the books of Sneh Co. Ltd.

A) Calculation of Intrinsic Value

Calculation of Net Assets

Particulars	₹
Assets (with revised values)	
Building	3,20,000
Plant	1,80,000
Investment	50,000
Stock	45,000
Debtors	35,000
Cash	10,000
Total	6,40,000
Liabilities	
12% Preference Share Capital	1,00,000
15% Debentures	1,00,000
Creditors	80,000
Total	2,80,000
Net Assets	3,60,000

$$\text{Intrinsic Value Per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{3,60,000}{10,000} = ₹ 36$$

B) Calculation of Yield Value

a) Calculation of Profit available for equity share holders

Average Profit –	1,20,000
- Tax – 50%	60,000
Net Profit after Tax –	60,000
- Transfer to Reserves – 12.5%	7,500
Profit available for equity share holders	52,500

b) Calculation of capitalized value

$$\text{c) Capitalised Value} = \frac{\text{Profit available for Equity Shareholders}}{\text{Normal Rate of Return}} \times 100$$

$$\text{Capitalised Value} = \frac{52,500}{10} \times 100 = 5,25,000$$

d) Calculation of value of each share

$$\text{Value per Share} = \frac{\text{Capitalised Value}}{\text{Number of Equity Shares}} = \frac{5,25,000}{10,000} = ₹ 52.50$$

e) Calculation of Fair Value

$$\text{Fair Value of Equity Share} = \frac{\text{Intrinsic Value} + \text{Yield Value}}{2}$$

$$\text{Fair Value of Equity Share} = \frac{36 + 52.50}{2} = ₹ 44.25$$

Shivaji University Problems adopted (dates are changed)

Illustration 16. (April 2017) From the following balance sheet of Aba & Baba Ltd. and the additional information given below, ascertain intrinsic value of each share.

Balance Sheet as on 31/3/2025

Liabilities	₹	Assets	₹
Share Capital (Equity shares of ₹ 10 each)	3,00,000	Goodwill	1,20,000
12% Preference shares of ₹10 each	1,00,000	Leasehold Properties	3,50,000
General Reserve	80,000	Fixtures	60,000
Profit & Loss A/c	70,000	Investment	50,000
	1,00,000	Current Assets	75,000
	30,000	Loans & Advances	15,000
		Miscellaneous Expenditures	10,000

Unsecured Loan	6,80,000		6,80,000
Current Liabilities			

Additional Information

- Goodwill should be valued at 3 years purchase of average profits of last 5 years. The profits for the last 5 years are ₹ 70,000, ₹ 90,000, ₹ 75,000, ₹ 85,000 and ₹ 80,000.
- Leasehold property and fixtures are valued at ₹ 4,00,000 and ₹ 50,000 respectively.

Solution – In the books of Aba & Baba Ltd.

1. Calculation of Goodwill

$$\text{Goodwill} = \frac{70,000 + 90,000 + 75,000 + 85,000 + 80,000}{5} \times 3 = 2,40,000$$

2. Calculation of Net Assets

Particulars	₹
Assets (with revised values)	
Goodwill	2,40,000
Leasehold Properties	4,00,000
Fixtures	50,000
Investment	50,000
Current Assets	75,000
Loans & Advances	15,000
Total	8,30,000
Liabilities	
Unsecured Loan	1,00,000
Current Liabilities	30,000
Preference Share Capital	1,00,000
Total	2,30,000
Net Assets	6,00,000

3. Calculation of value of each equity share

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{6,00,000}{30,000} = ₹ 20$$

Illustration 17. (April 2016) Following is the balance sheet of Palus Engineering Ltd. as on 31st March 2025

Balance Sheet

Liabilities	₹	Assets	₹
Share Capital – 5000 Equity Shares of ₹ 100 each	5,00,000	Goodwill	1,20,000
Profit & Loss A/c	50,000	Investment	4,80,000
General Reserve	1,50,000	Stock	5,00,000
10% Debentures	4,50,000	Debtors	3,00,000
Sundry Creditors	1,50,000	Cash at Bank	1,00,000
Workmen's Saving A/c	2,00,000		
	15,00,000		15,00,000

Additional information-

i) The profits for the last 5 years' were -

2018-19 ₹ 25,000, 2019-20 ₹ 35,000, 2020-21 ₹ 50,000,
2021-22 ₹ 60,000, 2022-23 ₹ 80,000

ii) The market value of investment was ₹4,00,000.

iii) Goodwill is to be valued on 3 years purchase of average annual profits for the last 5 years.

Find the intrinsic value of each share.

Solution – In the books of Palus Engineering Ltd.

1. Calculation of Goodwill

$$\text{Goodwill} = \frac{25,000+35,000+50,000+60,000+80,000}{5} \times 3 = 1,50,000$$

2. Calculation of Net Assets

Particulars	₹
Assets (with revised values)	
Goodwill	1,50,000
Investment	4,00,000
Stock	5,00,000
Debtors	3,00,000
Cash at Bank	1,00,000
Total	14,50,000
Liabilities	
10% Debentures	4,50,000
Sundry Creditors	1,50,000
Workmen's Saving A/c	2,00,000
Total	8,00,000
Net Assets	6,50,000

3. Calculation of value of each equity share

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{6,50,000}{5,000} = ₹ 130$$

Illustration 18. Following information pertains to XYZ Co. Ltd.

8% 25,000 preference shares of 10 each.	2,50,000
62,500 equity shares of 100 each	62,50,000
Average annual profit	12,50,000
Income tax	50%
Transfer of General Reserve	25%
Normal return	10%

Mr. Balwant the holder of 200 equity shares in the company assigns you the work of valuing his shareholdings.

Solution

1. Calculation of profit available for equity share holders

	₹	₹
Average annual profit		12,50,000
Income tax - 50%		6,25,000
Profit after Tax		6,25,000
Transfer of General Reserve - 25% of 6,25,000	1,56,250	
Preference Dividend 8% on 2,50,000	20,000	1,76,250
Profit available to equity capital		4,48,750

$$\text{Value per Share} = \frac{\text{Average Profit}}{\text{Normal Rate} \times \text{Number of Equity shares}} \times 100$$

$$\text{Value per Share} = \frac{4,48,750}{10 \times 62,500} \times 100 = ₹ 71.80$$

Illustration 19.(Nov. 2017) Following is the balance sheet of Aditya Ltd. as on 31/3/2025.

Liabilities	₹	Assets	₹
Issued Capital –		Fixed Assets	6,00,000
48000 Equity shares of ₹ 10 each	4,80,000	Current Assets	2,40,000
General Reserve	1,08,000	Goodwill	48,000
Profit & Loss A/c	24,000		
5% Debentures	1,20,000		
Current Liabilities	1,56,000		
	8,88,000		8,88,000

B) Calculation of Market Value of Equity Share

3. Calculation of Profit available for equity share holder

	₹
Average profit 65,000 + 70,000 + 67,500 ----- 3	67500
Transfer to Reserve - 20% of 67500	13500
Profit available for equity share holders	54000

$$\text{Value per Share} = \frac{\text{Profit available for equity share holders}}{\text{Normal Rate} \times \text{Number of Equity Shares}} \times 100$$

$$\text{Value per Share} = \frac{54000}{10 \times 48000} \times 100 = ₹ 11.25 - \text{Market Value}$$

C) Calculation of Fair Value of Equity Share

$$\text{Fair Value} = \frac{\text{Intrinsic Value} + \text{Market Value}}{2}$$

$$\text{Fair Value} = \frac{14.75 + 11.25}{2} = ₹ 13 - \text{Fair Value}$$

Illustration 20. (April 2019) The following is the Balance Sheet of Sujit Company Ltd. as on 31st March 2025.

Liabilities	₹	Assets	₹
Share Capital – 15000		Land & Building	15,40,000
Equity Shares of ₹ 100 each	15,00,000	Plant & Machinery	17,60,000
4000 8% Preference shares		Vehicles	4,50,000
of ₹100 each	4,00,000	Debtors	6,80,000
General Reserve	7,00,000	Stock	4,70,000
Profit & Loss A/c	5,00,000		
	10,00,000		

10% Debentures	8,00,000		
Sundry Creditors	49,00,000		49,00,000

The Land & Building and Plant & Machinery are to be depreciated by 10% and Vehicles by 20%. The Stock was revalued at ₹4,45,000 and Debtors subject to a provision for bad debts of ₹ 80,000.

The profits for the last five years were as –

2018-19 ₹ 4,30,000, 2019-20 ₹ 4,70,000, 2020-21 ₹ 5,00,000,
2021-22 ₹ 6,00,000 and 2022-23 ₹ 6,45,000.

The taxation provision is to be made at 50% and a profit earning capacity of similar companies' show 10%.

Find out I) Intrinsic Value, II) Market Value and III) Fair Value of the Equity Equity shares

Solution – In the books of Sujit Co.

A) Calculation of Intrinsic Value of Equity Share

1. Calculation of Net Assets

Particulars	Calculation	₹
Assets (with revised values)		
Land & Building	15,40,000 – 1,54,000	13,86,000
Plant & Machinery	17,60,000 – 1,76,000	15,84,000
Vehicles	4,50,000 – 90,000	3,60,000
Debtors	6,80,000 – 80,000	6,00,000
Stock		4,45,000
Total		43,75,000
Liabilities		
10% Debentures		10,00,000
Sundry Creditors		8,00,000
8% Preference Share		4,00,000
Total		22,00,000
Net Assets		21,75,000

2. Calculation of value of each equity share

$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{Number of Equity Shares}} = \frac{21,75,000}{15,000} = ₹ 145 - \text{Intrinsic Value}$$

B) Calculation of Market Value of Equity Share

3. Calculation of Profit available for equity share holders

	₹
Average profit 4,30,000 + 4,70,000 + 5,00,000 + 6,00,000 + 6,55,000 ----- 5	5,31,000
Less – Tax - 50% of 5,31,000	2,65,500
Profit available for equity share holders	2,65,500

$$\text{Value per Share} = \frac{\text{Profit available for equity share holders}}{\text{Normal Rate} \times \text{Number of Equity Shares}} \times 100$$

$$\text{Value per Share} = \frac{2,65,500}{10 \times 15000} \times 100 = ₹ 177 - \text{Market Value}$$

B) Calculation of Fair Value of Equity Share

$$\text{Fair Value} = \frac{\text{Intrinsic Value} + \text{Market Value}}{2}$$

$$\text{Fair Value} = \frac{145 + 177}{2} = ₹ 161 - \text{Fair Value}$$

Check your progress -1

Fill in the blanks from the given alternatives and rewrite the sentence

1. Every limited company has----- capital.

- a) share b) personal c) virtual d) notional

2. The face value of the share is -----.
 a) fixed by the company and ever changes
 b) fixed by the company and never changes
 c) fixed by the market and never changes
 d) fixed by the market and ever changes
3. ----- value of equity shares increases or decreases based on company's performance, rate of dividend, demand & supply of the equity shares etc.
 a) Intrinsic b) face c) Market d) Internal
4. ----- value is determined on the basis of values of assets and liabilities.
 a) Yield b) face c) Market d) Intrinsic
5. Under ----- method, the net value of assets of the company is divided by the number of equity shares to arrive at the value of each share.
 a) Asset Backing Method b) Yield Value Method
 c) Fair Value Method d) Price Earning Method
6. Value of Net Assets is determined by deducting revised values of liabilities from ----
 a) book value of assets
 b) revised value of assets
 c) book value of share capital
 d) revised value of share capital
7. If revised values of some assets and liabilities are not given, ---- values of these assets and liabilities are considered while calculating net assets.
 a) market b) book c) original d) replacement
8. The fictitious assets such as preliminary expenses, discount on issue of equity shares and debentures, accumulated losses etc. ----- while calculating net assets.
 a) should be considered b) should be added
 c) should be deducted d) should not be considered

9. While calculating net assets, if there are some unrecorded assets and liabilities, -
-----.
- both should be considered
 - only assets should be considered
 - only liabilities should be considered
 - both should not be considered
10. While calculating net assets, Preference Share Capital and Preference Dividend in arrear should be -----.
- added to the total of assets
 - deducted from the total of assets
 - deducted from total liabilities
 - not be considered
11.
$$\text{Value per Share} = \frac{\text{Net Assets}}{\text{-----}}$$
- Number of Preference shares
 - Preference Share Capital
 - Number of Equity shares
 - Equity Share Capital
12. ----- is the effective rate of return on investments which is invested by the investors.
- Equity value
 - Intrinsic value
 - Fair value
 - Yield value
13.
$$\text{Yield} = \frac{\text{Profit / Earning (after tax \& Preference Dividend)}}{\text{-----}} \times 100$$
- Equity Share Capital
 - Number of Equity Equity shares
 - Net Assets
 - Preference Share Capital
14.
$$\text{Expected Rate of Earning / Dividend} = \frac{\text{-----}}{\text{Paid up Value of Equity Share Capital}} \times 100$$
- Profit available for Preference Dividend
 - Profit available for Equity Dividend
 - Net Assets
 - Profit before tax

15.
$$\text{Value per Share} = \frac{\text{Expected Rate of Earning / Dividend}}{\text{-----}} \times \text{Paid up value of Equity Share}$$
- a) Company's Rate of Return b) Actual Rate of Dividend
c) Normal Rate of Return d) Average Rate of Return
16.
$$\text{Capitalised Value} = \frac{\text{-----}}{\text{Normal Rate of Return}} \times 100$$
- a) Profit after interest but before tax
b) Profit after tax but before Preference Dividend
c) Profit before tax and Preference Dividend
d) Profit after tax and Preference Dividend
17.
$$\text{Value per Share} = \frac{\text{Capitalised Value}}{\text{-----}}$$
- a) Number of Equity Shares b) Equity Share Capital
c) Number of Preference shares d) Preference Share Capital
18. On the basis of Price Earnings Ratio,
$$\text{Market Value per Share} = \text{Price Earnings Ratio} \times \text{-----}$$
- a) Earning on Equity Capital
b) Earnings per Share
c) Profit available for equity dividend
d) Profit before tax and dividend
19. Fair Value of Equity Share is -----
- a) total of Intrinsic Value and Yield Value
b) Intrinsic Value minus Yield Value
c) average of Intrinsic Value and Yield Value
d) Yield Value minus Intrinsic Value

20. ----- value provides a better indication about the value of equity shares.

- a) Intrinsic b) Market c) Face d) Fair

2.2. Valuation of Preference Shares

Important Note –As per section 55 of the Companies Act 2013, no company shall issue preference shares which are irredeemable. A company can issue only redeemable preference shares and these shares must be redeemed within a maximum period of 20 years from the date of issue of such shares. So, no discussion is carried out in the following pages on irredeemable preference shares, as well as, no illustrations are given on valuation of such shares.

2.2.1 Introduction to Valuation of Preference Shares

The shares which enjoy the preferential rights as to dividend at fixed rate and repayment of capital at the time of liquidation over the equity shares are called as Preference shares. Preference shares, often referred to as preferred stock, are a hybrid security that combines features of both equity and debt. They are a form of ownership in a corporation, but they come with specific rights and preferences, such as a fixed dividend payment and priority in receiving assets in case of liquidation. Such shares are generally having no voting right.

The two dominant characteristics of a preference share are that it has a preference regarding both the dividend and capital. Because of this, the considerations applicable for the valuation of equity shares are not wholly applicable to the valuation of preference shares. The risk involved in investment in preference shares is considerably less than that in equity shares. Therefore, the expected rate of return on preference shares is also lower, with the consequent effect upon the rate of capitalisation.

The valuation of such shares depends not only on the percentage of dividend but also on the conditions of redemption and market conditions. It is also necessary to take into consideration, whether the preference shares are cumulative or participating, whether these shares can be converted into equity shares, whether these shares are having voting rights, etc.

Both investors and the companies involved are interested in valuation of preference shares. The values give investors an overview of the worth of the investment before a decision is made. A deep understanding of preference shares

valuation helps to assess financing alternatives and determine their impact on the firm's economic performance. Investing in preference shares can be beneficial as it provides fixed return on holdings and is less risky than equity. However, investors must assess Fixed Returns, Risk and Liquidity. They should analyse the face value of preference share, redemption value (i.e. whether such shares are redeemable at par, discount or premium), market price, rate of dividend and intrinsic value or present value before making decisions.

On the part of the company, it deals with investment appraisal, capital structure and cost of capital. Valuation preference shares help to distinguish between different financing sources, analyse their respective impacts on company valuation and ultimately to make some huge strategic financial decisions.

2.2.2 Factors Influencing Valuation of Preference Shares

Various factors influence preference share prices in the market. These factors help investors to realise a fair valuation for preference shares concerning the investee.

1. **Rates of Interest** - Interest rates have turned out to be one of the chief determinants in determining the value of preference shares. Considering the interest of investors, preference shares would become very attractive when interest rates of deposits and other investments are at a low level. At such time, the value of preference shares increases and vice versa.
2. **Profitability and financial position of the company**- Another factor that affects the price or value of preference shares is the financial condition and profit of the company. If the companies suffer short-term low-profit generation or if the financial position is weak, the price of the preference shares would fall and vice versa.
3. **Dividend Declaration Policy** - Regular dividend payment on preference shares boosts the calculations of yields and thus increases such shares' value and vice versa.
4. **Economic Climate** - The investor's risk appetite may vary with changes in economic conditions. Generally, preference shares preserve their value under normal market conditions. When the economic environment is uncertain, it leads to disruptions in many economic activities and the value of preference shares start to plummet. On the other hand, if economic conditions are very good, value of preference shares start to incline.

5. **Terms of Redemption and Liquidity** - The critical aspect influencing the valuation of redeemable preference shares is the redemption period and the value. Shares with fixed and clear redemption terms will be regarded as best. Liquidity would seriously impact the intrinsic value. If the liquidity of companies is good, price increases and vice versa.
6. **Dividend Rate** - Higher dividend rates typically lead to higher preference share values and vice versa.
7. **Share Market Conditions** - Increase in Sensex increases market prices of preference shares and vice versa.
8. **Credit Risk** - The creditworthiness of the issuing company plays a crucial role. Preference shares issued by financially stable companies are perceived as less risky and tend to have higher valuations and vice versa.
9. **Cumulative vs. Non-** Cumulative Dividends - Preference shares may have cumulative or non-cumulative dividend provisions. Cumulative preference shares accumulate unpaid dividends if the company misses payments, so, the value of such shares are higher.
10. **Dividend Stability-** If the history of the company shows that it is paying dividends on preference shares regularly, the value of such shares increases and vice versa.

2.2.3 Calculation of value of Redeemable Preference Shares

Value of preference shares is also called as Intrinsic Value or Present Value of preference shares. Redeemable preference shares have usually a fixed maturity date and fixed rate of dividend. The valuation considers both the periodic dividend and the redemption price.

The Dividend Discount Model is a common method used to value redeemable preference shares. It involves calculating the present value of expected future dividend payments.

Steps for calculation of value

- Determine the annual preferred dividend, which is usually a fixed percentage of the preference share's face value.

- Choose an appropriate discount rate, which reflects the required rate of return for the preference shareholders. This rate is often a combination of the risk-free rate and a risk premium.
- Discount the expected future dividend payments to their present value using the chosen discount rate.

The sum of the present values of all expected dividend payments represents the fair market value of the preference shares.

The formula is:

$$\text{Value} = \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \frac{D}{(1+r)^3} + \dots + \frac{DD + MV / RV}{(1+r)^n}$$

Where, D = Annual Dividend, MV / RV = Maturity Value / Redemption Value,

r = Discount Rate and n = No. of Years

Calculation of Preference Share Yield

Investors use yield calculations to measure returns. The formula is:

$$\text{Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100$$

2.2.4 Illustrations

Illustration 1. The face value of preference share is ₹ 10,000 and the stated dividend rate is 10%. The shares are redeemable after 3 years. Calculate the value of preference shares if the required rate of return is 12%.

Solution - The formula is:

$$\text{Value} = \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \frac{D}{(1+r)^3} + \dots + \frac{DD + MV}{(1+r)^n}$$

Annual dividend = D = 10% of 10,000 = 1,000 r = 12% = 0.12 Total period – 3 years

$$\text{Value} = \frac{1,000}{(1+0.12)^1} + \frac{1,000}{(1+0.12)^2} + \frac{1,000 + 10,000}{(1+0.12)^3}$$

$$\text{Value} = \frac{1,000}{(1.12)^1} + \frac{1,000}{(1.12)^2} + \frac{11,000}{(1.12)^3}$$

$$\text{Value} = \frac{1,000}{1.12} + \frac{1,000}{1.2544} + \frac{11,000}{1.404928}$$

$$\text{Value} = 892.86 + 797.19 + 7829.58 = 9519.63$$

Illustration 2 - Mr. Rajan, a conservative investor, is evaluating an investment in 10% redeemable preference shares issued by Reliable Ltd. The face value of the preference share is ₹1,000 and it will be redeemed at par after 5 years. The preference dividend is paid annually. The required rate of return by Mr. Rajan is 9%. The current market price of the preference share is ₹950. (The PV factor @ 9% - 1st year – 0.9174, 2nd year – 0.8417, 3rd year – 0.7722,

4th year – 0.7084 and 5th year – 0.6499)

You are required to:

1. Calculate the value of the redeemable preference share.
2. Calculate Preference Share Yield
3. Suggest whether Mr. Rajan should buy the shares or not by comparing the value with market price.

Solution : Given Information - Face value (FV) = ₹1,000 Market Price = ₹950

Dividend p a (D) = 10% of ₹1,000 = ₹100

Redemption period (n) = 5 years

Redemption Value (Maturity Value) = ₹1,000

Required rate of return (rate of discount or discounting factor) (r) = 9%

The value of a redeemable preference share is the present value of all dividends + present value of redemption amount:

Present Value Calculation - Discounting at 9%:

$$\text{Value} = \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \frac{D + MV}{(1+r)^3} + \dots + \frac{D + MV}{(1+r)^n}$$

$$\text{Value} = \frac{100}{(1+0.09)^1} + \frac{100}{(1+0.09)^2} + \frac{100}{(1+0.09)^3} + \frac{100}{(1+0.09)^4} + \frac{1,000 + 100}{(1+0.09)^5}$$

$$\text{Value} = \frac{100}{(1.09)^1} + \frac{100}{(1.09)^2} + \frac{100}{(1.09)^3} + \frac{100}{(1.09)^4} + \frac{1100}{(1.09)^5}$$

$$\text{Value} = \frac{100}{1.09} + \frac{100}{1.1881} + \frac{100}{1.2950} + \frac{100}{1.4116} + \frac{11,000}{1.5386}$$

$$\text{Value} = 91.74 + 84.17 + 77.22 + 70.84 + 714.89 = 1038.86 \text{ ₹}$$

(Note - The present value factor can be calculated by using calculator as – 100 divided by 100 plus discounting rate then press multiple sign button (once or twice), you will get PV Factor for first year, then continue to press equalto sign button for subsequent years)

This calculation can be done by using Present Value Factor @ 9% as below

Year	Cash Flow (₹)	PV Factor @ 9%	Present Value (₹)
1	100	0.9174	91.74
2	100	0.8417	84.17
3	100	0.7722	77.22
4	100	0.7084	70.84
5	1,100	0.6499	714.89
Total Present Value			1038.86

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{100}{950} \times 100 = 10.52\%$$

Suggestion - Present Value = ₹1,038.86 and Market Price = ₹950. Required rate is 9% and preference dividend yield is 10.52%. Since present value is greater than market price and yield is higher than required rate, Mr. Rajan should buy the preference shares.

Illustration 3: Ms. Kavita purchased a 12% redeemable preference share of SafeYield Ltd. in the 2nd year of its 7 years term. The share has a face value of ₹1,000, and it pays annual dividend. The share will be redeemed at par. The required rate of return is 11%. The current market price of the share is ₹980. (The PV factor @ 11% - 1st year – 0.9009, 2nd year – 0.8116, 3rd year – 0.7312, 4th year – 0.6587 and 5th year – 0.5935)

You are required to:

1. Value the preference shares in the 2nd year (i.e., with 5 years remaining).
2. Calculate Preference Share Yield
3. Compare it with the market price and suggest if Ms. Kavita should invest or not.

Solution: Given Information - Face value = ₹1,000

Dividend = 12% of ₹1,000 = ₹120

Remaining life = 5 years

Redemption Value = ₹1,000 Required return = 11%

Market Price = ₹980

Note – As the shares are valuing in the second year, the third year of the term will be the first year for calculation.

Present Value Calculation

Year	Cash Flow (₹)	PV Factor @11%	Present Value (₹)
3	120	0.9009	108.11
4	120	0.8116	97.39
5	120	0.7312	87.74
6	120	0.6587	79.04
7	120	0.5935	71.22
7	1,000	0.5935	593.50
Total Present Value			1,036.99

(Students can use the formula given above instead of this table)

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{120}{980} \times 100 = 12.24\%$$

Suggestion - Intrinsic Value = ₹1,036.99 and Market Price = ₹980. Required return is 11% and yield is 12.24%. As intrinsic value is greater than market price and yield is greater than required rate, Ms. Kavita should invest in this preference share.

Illustration 4: Mr. Dhruv is evaluating the purchase of 9% redeemable preference shares issued by Kinetix Ltd. with a face value of ₹1,000, paying annual dividends. These shares are redeemable after 6 years at a discount of 5%. His required rate of return is 12%. The current market price of the preference share is ₹870.

You are required to: Calculate the intrinsic value of the preference share, preference dividend yield and advise whether Mr. Dhruv should buy the share or not.

Solution: Given Information - Face value = ₹1,000 Dividend = 9% of ₹1,000 = ₹90
Period = 6 years Redemption Value = ₹1,000 – 5% = ₹950,

Required return = 12%, Market Price = ₹870

$$\begin{aligned} \text{Value} &= \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \frac{D}{(1+r)^3} + \frac{D}{(1+r)^4} + \frac{D}{(1+r)^5} + \frac{D + MV}{(1+r)^6} \\ \text{Value} &= \frac{90}{(1+0.12)^1} + \frac{90}{(1+0.12)^2} + \frac{90}{(1+0.12)^3} + \frac{90}{(1+0.12)^4} + \frac{90}{(1+0.12)^5} + \frac{950 + 90}{(1+0.12)^6} \end{aligned}$$

$$\text{Value} = 80.36 + 71.75 + 64.06 + 57.20 + 51.07 + 526.86 = ₹851.30$$

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{90}{870} \times 100 = 10.34\%$$

Suggestion : Intrinsic Value = ₹851.30 and Market Price = ₹870. Required return is 12% and yield is 10.34%. Since intrinsic value is less than market price, as well as, yield is less than required rate, Mr. Dhruv should not invest in the share.

Illustration 5: Dr. Priya is interested in 11% redeemable preference shares of Wellness Ltd., originally issued 4 years ago for a 10-year term. The company has a history of delaying dividend payments but promises to pay 2 years' worth of arrear dividends this year along with regular dividend, and then normal dividends till redemption. The face value is ₹1,000, and dividends are paid annually. The shares are redeemable at par. Dr. Priya requires a 10% return. The current market price is ₹ 950. You are required to:

1. Value the preference shares from today (beginning of Year 5, 6 years left).
2. Compute the rate of yield from dividend
3. Decide whether she should invest or not.

(PV Factor @ 10% are - 0.9091, 0.8264, 0.7513, 0.6830, 0.6209, 0.5645)

Solution: Given Information - Face value = ₹1,000 Dividend rate = 11% - ₹110/year

Arrears for 2 years = ₹220, payable in Year 1 Market price = ₹950

Redemption at par = ₹1,000 after 6 years Required return = 10%

6 years are remaining so, 5th year will be 1st year for calculation

PV Calculations @10%

Year	Cash Flow (₹)	PV Factor	Present Value
5	₹110 (regular) + ₹220 (arrear)= 330	0.9091	300.00
6	110	0.8264	90.90
7	110	0.7513	82.64
8	110	0.6830	75.13
9	110	0.6209	68.30
10	110	0.5645	62.10
10	1,000	0.5645	564.50
Total PV			1,243.57

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{110}{950} \times 100 = 11.58\%$$

Decision - Intrinsic Value = ₹1,243.57 and Market Price = ₹950. Dr. Priya should definitely invest, as intrinsic value exceeds market price by a large margin and the yield is higher than expected rate.

Illustration 6: Mr. Sameer is evaluating an investment in 8% redeemable preference shares of Atlas Ltd. having a face value of ₹1,000, with annual dividends. The share is redeemable at a 10% premium after 5 years. The required rate of return is 9%, and the current market price is ₹920. You are required to:

1. Calculate the intrinsic value of the share.
2. Calculate yield rate of dividend
3. Recommend whether to invest based on market comparison.

Solution - Given Data - Face Value = ₹1,000 Dividend = 8% of ₹1,000 = ₹80

- Redemption Value = ₹1,000 + 10% = ₹1,100 Required Return = 9%
- Term = 5 years Market Price = ₹920

Present Value Calculation - Discounting at 9%:

$$\begin{aligned} \text{Value} &= \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \frac{D}{(1+r)^3} + \frac{D}{(1+r)^4} + \frac{D + MV / RV}{(1+r)^5} \\ \text{Value} &= \frac{80}{(1+0.09)^1} + \frac{80}{(1+0.09)^2} + \frac{80}{(1+0.09)^3} + \frac{80}{(1+0.09)^4} + \frac{1,100 + 80}{(1+0.09)^5} \\ \text{Value} &= \frac{80}{(1.09)^1} + \frac{80}{(1.09)^2} + \frac{80}{(1.09)^3} + \frac{80}{(1.09)^4} + \frac{1,100 + 80}{(1.09)^5} \end{aligned}$$

$$\text{Value} = 73.39 + 67.34 + 61.78 + 56.67 + 766.88 = ₹1,026.06$$

(Students can find PV Factor by using calculator and use the figures for calculation of Present Value)

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{80}{920} \times 100 = 8.70\%$$

Decision: Intrinsic Value = ₹1,026.06 and Market Price = ₹920. Required rate of return is 9% and dividend yield is 8.70%. The intrinsic value exceeds market price and yield is near to required rate. Mr. Sameer can invest considering the intrinsic value.

Illustration 7: Ms. Anjali is considering investing in 15% redeemable preference shares of Legacy Ltd. The shares have a face value of ₹1,000, and only 2 years are left before redemption at par. The company pays annual dividends. Ms. Anjali's required rate of return is 13%. The current market price is ₹1,040. You are required to:

1. Compute the intrinsic value of the share.
2. Calculate the preference share yield.
3. Decide if she should buy the share based on valuation.

Solution – Inputs - Face Value = ₹1,000 Dividend = 15% = ₹150 Term = 2 years

Redemption = ₹1,000 Required Return = 13% Market Price = ₹1,040

Present Value Calculation - Discounting at 13%:

$$\text{Value} = \frac{D}{(1+r)^1} + \frac{D + MV}{(1+r)^2} = \frac{150}{(1+0.13)^1} + \frac{1,000 + 150}{(1+0.13)^2}$$

$$\text{Value} = \frac{150}{(1.13)^1} + \frac{1150}{(1.13)^2} = 132.75 + 900.57 = ₹1,033.32$$

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{150}{1040} \times 100 = 14.42\%$$

Conclusion: Intrinsic Value = ₹1,033.32 and Market Price = ₹1,040. Required rate is 13% and yield is 14.42%. Intrinsic value is less than market price. Though, the yield

is higher than required rate, the remaining period is very less so, it will be better to Ms. Anjali not to buy the shares at this price.

Illustration 8: Mr. Arvind wants to value a 10% redeemable preference share of PrimeCore Ltd. with a face value of ₹1,000, paying semi-annual dividends. The shares are redeemable at par after 4 years, and Mr. Arvind is evaluating them at the end of 2nd year (i.e., 2 years remaining). His required rate of return is 9% per annum, compounded semi-annually. The current market price is ₹970. You are required to:

1. Calculate the intrinsic value of the share.
2. Calculate yield of preference shares
3. Suggest whether he should invest or not.

(Half yearly PV Factor at 4.5% - 0.9569, 0.9155, 0.8763 and 0.8387 respectively)

Solution: Inputs - Face Value = ₹1,000 Market Price = ₹970

Dividend = 10% = ₹100 annually → ₹50 semi-annually

Remaining periods = 2 years × 2 = 4 semi-annual periods

Redemption = ₹1,000 at end of 4th year Required return = 9% p.a. → 4.5% per half-year

PV Table

Year	Half year	Cash Flow (₹)	PV Factor @4.5%	PV (₹)
3	1	50	0.9569	47.85
	2	50	0.9155	45.78
4	1	50	0.8763	43.82
	2	1050	0.8387	880.64
Total Present Value				₹1,018.09

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{100}{970} \times 100 = 10.31\%$$

Conclusion - Intrinsic Value = ₹1,018.09 and Market Price = ₹970. Preference is yield is 10.31% and required rate is 9%. Since intrinsic value is higher than market price and yield is higher than expected rate, Mr. Arvind should invest in these preference shares.

Illustration 9: ABC Ltd. issued 5-year redeemable preference shares of ₹1,000 face value. Dividends are structured as Year 1–2: 8% p.a. and Year 3–5: 12% p.a. Redemption is at a premium of 5% (i.e., ₹1,050) after 5 years. Mr. Manish is evaluating this share at the beginning. His required return is 10% p.a. The share is trading at ₹980. You are required to:

1. Value the preference shares today.
2. Find out the yield of preference shares
3. Decide whether Mr. Manish should invest.

Solution – Inputs - Face Value = ₹1,000 Dividend: Year 1–2: ₹80, Year 3–5: ₹120

Redemption = ₹1,050 Required return = 10% Market price = ₹980

Present Value Table

Year	Cash Flow (₹)	PV Factor @10%	Present Value (₹)
1	80	0.9091	72.73
2	80	0.8264	66.11
3	120	0.7513	90.16
4	120	0.6830	81.96
5	120	0.6209	74.51
5	1,050	0.6209	652.00
Total PV			₹1,037.47

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{80}{980} \times 100 = 8.16\% \text{ - for first two years}$$

$$= \frac{120}{980} \times 100 = 12.24\% \text{ - for next three years}$$

Decision: Intrinsic Value = ₹1,037.47 and Market Price = ₹980. Though, yield is less than expected rate (10%) in the first two years, it will increase in the last three years. So, Mr. Manish should buy the share.

Illustration 10: Ms. Ruchi is considering the valuation of a 6-year, 9% redeemable preference share issued by FinPlus Ltd. on 1/4/2022 with a face value of ₹1,000 and redeemable at par. The company pays annual dividend. She is valuing these shares at the end of 3rd year (i.e., 3 years remaining). Due to recent market volatility, she expects a higher return of 11%. The current market price is ₹945. You are required to:

1. Calculate the intrinsic value as on end of 3rd year.
2. Find out the preference share yield
3. Decide whether she should invest in the preference share or not.

Solution – Inputs - Face Value = ₹1,000 Dividend = 9% = ₹90 annually

Remaining term = 3 years

Required return = 11%

Redemption Value = ₹1,000

Market price = ₹945

Present Value Calculation - Discounting at 11%:

$$\text{Value} = \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \frac{D + MV / RV}{(1+r)^3}$$

$$\text{Value} = \frac{90}{(1+0.11)^1} + \frac{90}{(1+0.11)^2} + \frac{1,000 + 90}{(1+0.11)^3} = 81.08 + 73.04 + 797.01 = ₹ 951.13$$

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{90}{945} \times 100 = 9.52\%$$

Conclusion - Intrinsic Value = ₹951.13 and Market Price = ₹945. Required rate is 11% and yield is 9.52%. Though, intrinsic value is slightly more than market price, yield is less than required rate, so, Ms. Ruchi should not invest in the preference shares.

Illustration 11: Mr. Harsh is evaluating the 10% redeemable preference shares of TrustEdge Ltd. with face value of ₹1,000 and 5 years to maturity. Due to a moderate credit rating, he includes a default risk premium, and hence, his required return is set

at 13%. The shares pay annual dividends and will be redeemed at par. The market price is ₹910. You are required to:

1. Calculate the intrinsic value using the adjusted required return.
2. Advise if Mr. Harsh should invest in these preference shares.

Solution : Inputs - Face Value = ₹1,000 Dividend = 10% of ₹1,000 = ₹100

Required return (adjusted for risk) = 13% Redemption = ₹1,000

Term = 5 years

Market Price = ₹910

Present Value Table

Year	Cash Flow (₹)	PV Factor @13%	PV (₹)
1	100	0.88496	88.50
2	100	0.78315	78.32
3	100	0.69257	69.26
4	100	0.61257	61.26
5	100	0.54276	54.28
5	1,000	0.54276	542.76
Total PV			894.38

$$\text{Preference Share Yield} = \frac{\text{Dividend}}{\text{Market Price}} \times 100 = \frac{100}{910} \times 100 = 10.99\%$$

Conclusion - Intrinsic Value = ₹894.38 and Market Price = ₹910. Expected return is 13% and yield is 10.99%. As intrinsic value is less than market price, also, yield is less than expected earnings, Mr. Harsh should not invest in this share.

Check your progress-2

Multiple Choice Questions

1. Preference shares are considered as --- when they have a mandatory redemption date.

A) Equity
B) Non-current Asset
C) Liability
D) Contingent Liability

Ans: C) Liability

2. When required rate of return increases, the value of preference shares -----.

A) remain constant
B) decrease
C) increase
D) is unaffected if dividends remain the same

Ans: B) decrease

3. --- discounting technique is commonly used when valuing redeemable preference shares?

A) Net Present Value (NPV)
B) Payback Period
C) Future Value Formula
D) Accounting Rate of Return

Ans: A) Net Present Value (NPV)

4. If market interest rates increased in comparison to dividend rate, the value of preference shares will -----

A) increase
B) decrease
C) remain unchanged
D) be equal to face value

Ans: B) decrease

5. ----- affects the valuation of preference shares.

A) The company's net income
B) The dividend payout ratio of equity shares
C) The required rate of return
D) The company's capital expenditure

Ans: C) The required rate of return

6. Decrease in the required rate of return will result in ----- of preference shares.

- | | |
|---------------------------|------------------------------|
| A) Increases the value | B) Decreases the value |
| C) no effect on the value | D) reduces dividend payments |

Ans: A) Increases the value

3. Summary

Every limited company has share capital divided in equity shares, preference shares or both. The face value is the initial price of the share fixed by the company. Face value never changes. Market value of share means the value which is determined by the market. Market value of equity shares increases or decreases based on company's performance, rate of dividend, demand & supply of the equity shares etc. So, even though, each share is having face value, its valuation becomes essential. Valuation of share is a system of determining the value of a business by estimating the value of its equity shares.

The need for Valuation of Equity Shares arises when companies are amalgamated, absorbed, reconstructed, for proper distribution of partnership property among the partners or members, when a loan is advanced on the security of the equity shares, when debentures are converted into equity shares, when preference shares are converted into equity shares, when a company is nationalised, etc.

Principally, the dividend yield is the main factor which affects greatly on the valuation of equity shares. The other factors are, nature of the business and of the company, Government policy, past performance of the company, potential growth, management of the company etc. Mainly there are three methods of valuation of equity shares, Net Assets Method, Yield Value Method and Fair Value Method

The shares which enjoy the preferential rights as to dividend at fixed rate and repayment of capital at the time of liquidation over the equity shares are called as Preference shares. The two dominant characteristics of a preference share are that it has a preference regarding both the dividend and capital. Because of this, the considerations applicable for the valuation of equity shares are not wholly applicable to the valuation of preference shares.

The valuation of such shares depends on the percentage of dividend, the conditions of redemption and market conditions, type of preference shares, convertibility etc. A deep understanding of preference shares valuation helps to

assess financing alternatives and determine their impact on the firm's economic performance. Investors must assess Fixed returns, risk, liquidity, redemption value, market price etc. on the part of the company, valuation preference shares help to distinguish between different financing sources, analyse their respective impacts on company valuation and ultimately to make some huge strategic financial decisions.

Various factors influence preference share prices in the market such as, Rates of Interest, Profitability and financial position of the company, Dividend Declaration Policy, Economic Climate, Terms of Redemption and Liquidity, Dividend Rate, Share Market Conditions, Credit Risk, Cumulative vs. Non-Cumulative Dividends, Dividend Stability etc.

The valuation considers both the periodic dividend and the redemption price. The Dividend Discount Model is a common method used to value redeemable preference shares.

4. Terms to Remember

1. The face value is the initial price of the share fixed by the company.
2. Market value of share means the value which is determined by the market.
3. Valuation of share is a system of determining the value of a business by estimating the value of its shares.
4. Net Asset or Asset Basis or Assets Backing or Intrinsic Value or Real Value Method is the method of valuation of shares where the equity shares are valued on the basis of real internal value of the assets of the company or on the basis of the net assets of the company.
5. Market Value or Profit Basis or Income Basis or Earning Capacity or Price Earnings Ratio Method is the method of valuation of equity shares where the price is determined on the basis of

Expected Yield / Rate of Return / Earning Rate / Normal Rate / Rate of General Expectation / Estimated Rate for Capitalisation. Thus, the valuation depends upon the comparison of the company's earning capacity and the normal rate of profit or dividend that is prevailing in the market.

6. Fair Value Method of valuation of equity shares is the mean of Intrinsic Value Method and Yield Value Method.

7. Preference Shares are the shares which enjoy the preferential rights as to dividend at fixed rate and repayment of capital at the time of liquidation over the equity shares are called as Preference shares.

5. Check your progress-1

A) Valuation of Equity Shares

1. a) share 2. b) fixed by the company and never changes
3. c) Market 4. d) Intrinsic
5. a) Asset Backing Method 6. b) revised value of assets
7. b) book 8. d) should not be considered
9. a) both should be considered 10. b) deducted from the total of assets
11. c) Number of Equity shares 12. d) Yield value
13. a) Equity Share Capital 14. b) Profit available for Equity Dividend
15. c) Normal Rate of Return
16. d) Profit after tax and Preference Dividend
17. a) Number of Equity Shares 18. b) Earnings per Share
19. c) average of Intrinsic Value and Yield Value
20. d) Fair

B) Check your progress-2

1. C) Liability 2. B) decrease
3. A) Net Present Value (NPV) 4. B) decrease
5. C) The required rate of return 6. A) Increases the value

Exercise :

A) Valuation of Equity Shares

Short Answer Questions

1. Explain need of valuation of equity shares
2. List out the Circumstances when valuation of equity shares is made

3. Explain Factors affecting the valuation of equity shares
4. Which Points which are to be considered for determination of Net Assets
5. Present the Chart for calculation of Net Assets assuming at least five assets and three liabilities

Write Short Notes

1. Intrinsic Value Method
2. Yield Value Method
3. Formulae for calculation of Yield Value of Equity shares under different basis

Valuation of Preference Shares

Short Answer Questions

1. What do you mean by valuation of shares? Explain valuation of redeemable preference shares with formula.
2. What are the factors which affect the valuation of preference shares?

Short Notes

1. Valuation of preference shares
2. Steps and formula for calculation of value of redeemable preference share

Practical Questions

Problem 1. Balance Sheet of Suraj Ltd. as on 31/3/2025

Liabilities	₹	Assets	₹
38000 Equity Shares of ₹100 each	3800000	Goodwill	95000
1900 6% Preference shares of ₹100 each		Land & Building	1900000
General Reserve	190000	Plant & Machinery	2280000
7% Debentures	171000	Investments	570000
Sundry Creditors	1140000	Stock	95000
Provision for Tax	95000	Sundry Debtors	76000
Bills Payables	57000	Bank Balance	456000
	38000	Preliminary Expenses	19000
	5491000		5491000

- The assets were revalued as:

Goodwill Rs. 190000, Land and Building at ₹ 2850000,
 Plant and Machinery ₹ 1824000, Market value of Investments is ₹ 475000,
 Debtors after providing for bad debts at 10%

- Interest on debentures is outstanding for 6 months.
- Actual tax liability as calculated by the tax consultant is ₹ 47500.
- Other assets and liabilities have no change in their values.

You are asked to-ascertain the value of each Equity Share of the company.

Problem 2Aarati Ltd. presented the following Balance Sheet as on 31st March 2025:

Liabilities	₹	Assets	₹
9000 Equity Shares of ₹100 each	900000	Land & Building	540000
Profit & Loss A/c	810000	Plant & Machinery	1080000

Capital Reserve	270000	Investment in Equity shares	450000
General Reserve	324000	Stock	270000
8% Debentures	396000	Sundry Debtors	432000
Sundry Creditors	450000	Bank Balance	378000
	3150000		3150000

Additional Information:

- Land and Building and Plant and Machinery were revalued at 150% and 120%, respectively.
 - The value of the equity shares purchased by the company is fallen down by 20% in the market.
 - Stock is valued at ₹ 360000 and Debtors subject to a deduction @ 5% for bad debts.
 - Manager's Remuneration ₹14400 is payable.
- Ascertain the Intrinsic Value of Equity shares.

Problem 3: Pooja wants to invest her savings in equity shares of limited companies. She has two options Dev Co. Ltd and Ishwar Co. Ltd. She expects your expert advise that of which company's share she should purchase. She is providing you the following information about these companies.

Balance Sheets as on 31/3/2025

Liabilities	D. Co. ₹	I. Co. ₹	Assets	D. Co. ₹	I. Co. ₹
Equity Shares of ₹100 each			Fixed Assets	722500	1241000
Reserves & Surplus	340000	680000	Investment	76500	187000
Secured long term loans	306000	238000	Current Assets	612000	476000
Current Liabilities	391000	807500			
	374000	178500			
	1411000	1904000		1411000	1904000

Market values of assets are

Assets	S. Co. ₹	M. Co. ₹
Fixed Assets	746300	1122000
Investment	85000	238000
Current Assets	544000	357000

2. Secured loans of Dev Ltd. include Bank Loan of ₹ 85000. The bank declared 2% Rebate for timely repayment of instalments.
3. Secured loans of Ishwar Ltd. include 10% Debentures of ₹ 170000. Interest on these debentures for the year 2018-19 is unpaid.

Problem 4. From the following Balance Sheet and other information of Sangita Ltd as on 31/3/2025, you are asked to ascertain the value of each Equity Share of the company

Liabilities	₹	Assets	₹
630 Equity Shares of ₹1000 each	630000	Land & Building	337707
Profit & Loss A/c	51750	Plant & Machinery	591588
Capital Reserve	140400	Investment in Equity shares	232596
General Reserve	80550	Stock	141255
8% Debentures	585000	Sundry Debtors	217125
Sundry Creditors	226620	Bank Balance	182799
		Discount on issue of equity shares	11250
	1714320		1714320

The company revalued the assets to match its real and market values. In this revaluation land & building, investments and stock showed profit totally of ₹ 32025, while plant & machinery showed a loss of ₹ 14875. It is also necessary to create reserve for doubtful debts at 5%.

Problem 5. Kavita Ltd. presented the following Balance Sheet as on 31st March 2025.

Liabilities	₹	Assets	₹
8000 Equity Shares of ₹100 each	8,00,000	Premises	12,00,000
		Furniture	280000
		Investment (Market	

2000 Preference shares of 100 each	2,00,000	Value 1,20,000)	140000
Profit & Loss A/c	3,12,000	Stock of goods	600000
Reserve Fund	4,36,000	Sundry Debtors	216000
8% Debentures	2,80,000	Bank Balance	80000
Bank Loan	3,40,000	Cash in hand	44000
Sundry Creditors	1,92,000		
	25,60,000		25,60,000

Additional Information:

- Premises and Furniture were revalued at ₹ 12,80,000 and ₹2,00,000 respectively.
- Investments were brought down to market value.
- Stock to be taken at ₹ 6,40,000.
- Debtors subject to a deduction of ₹ 8,000 for bad debts.
- Net profits for the last five years were ₹50,000; ₹90,000; ₹1,00,000; ₹70,000 and ₹90,000. Goodwill is to be valued at 3 years' purchase of average Net Profit.

Ascertain the Intrinsic Value of Equity shares.

Problem 6. The following particulars relate to Priya Co. Ltd.

	₹
Total Assets	1683500
External liabilities	227500
Share Capital	
14% preference shares of 100 each fully paid	455000
3,640 equity shares of 100 each fully paid	364000
5,460 equity shares of 100 each 75 paid	409500

Calculate the value of each category of equity shares of the company

Problem 7. From the following information of Surdas Co. Ltd. compute the value of its equity share on the basis of – a) Expected earnings, b) Capitalisation and c) Normal rate and number of equity shares

Balance Sheet as on 31/3/2025

Liabilities	₹	Assets	₹
6500 Equity Shares of ₹100 each	6,50,000	Fixed Assets	9,10,000
Reserves and Surplus	2,34,000	Current Assets	5,98,000
10 % Debentures	3,90,000	Discount on issue of Debentures	52,000
Current Liabilities	2,86,000		
	15,60,000		15,60,000

Other information

1. Average profit before tax is ₹3,66,600
2. Rate of Tax is 50%
3. Every year the company transfers ₹26,000 to Reserve Fund.
4. The rate of normal earnings is 12.5%.

Problem 8. On March 31, 2025 the Balance Sheet of Mahalaxmi Ltd. disclosed the following position.

Liabilities	₹	Assets	₹
Equity Shares of ₹100 each	8,00,000	Goodwill	80,000
Reserves	1,80,000	Other Fixed Assets	7,36,000
P. & L. A/c Balance	40,000	Investments	2,64,000
9 % Debentures	2,00,000	Current Assets	4,00,000
Current Liabilities	2,60,000		
	14,80,000		14,80,000

Net Profit for the last 3 years were, 2020-21 – ₹1,03,200, 2021-22 – ₹1,05,200 and 2022-23 – ₹1,03,300, of which 20% was transferred to Reserve. Fair investment return in the industry in which the company is engaged is 10%.

Compute the value of the company's share under yield-basis method.

Problem 9. From the following information of Balaji Ltd. calculate the value of each Equity Share on the basis of rate of dividend.

- Equity Share Capital – 28,000 equity shares of 100 each, 80% paid up
- 9% Preference Share Capital – 35,000 equity shares of 100 each fully paid
- Net Profit before tax ₹ 14,00,000
- Rate of Tax – 40%
- It is the company's policy to transfer 10% of profit to reserves
- Rate of Dividend of other companies working in the same industry is 14%

Problem10. Nandguru Co. Ltd. is providing you the following information for the financial year 2022-23.

1. 5850 Equity Shares of ₹ 100 each.
2. 450 9% Preference shares of ₹1000 each.
3. 180 11% Debentures of ₹ 2000 each.
4. Bank loan ₹ 9,00,000 taken for business expansion. Interest is payable @ 12% annually.
5. Net Sales ₹ 38,11,500
6. Operating Expenses ₹ 31,88,700
7. Rate of tax is 50%
8. Transfer to Reserve as per policy of the company ₹ 21,600 per year.
9. Normal Rate of Return in the industry is 15%.

It is the request of the company to you to calculate value of each equity share by capitalisation method

Problem11. Compute value of each equity share of the following companies.

	Shree Co. ₹	Sneh Co. ₹
Profit after tax	6,50,000	3,90,000
12% Preference Share Capital in equity shares of ₹1000 each	19,50,000	6,50,000
Equity Share Capital in equity shares of ₹100 each	13,00,000	13,00,000

Market expectation is 15%. All the companies distribute 75% of their profit as equity dividend.

Problem 12. Two companies, Amit Ltd. and Shashi Ltd., are doing similar business. Their balance sheet is also similar except the capital structure.

The share capital of Ajay Ltd. is ₹8,41,500, divided into 7,650 6% Preference shares of ₹ 100 each and 7,650 Equity Shares of ₹ 10 each.

The share capital of Vijay Ltd. is also ₹ 8,41,500, divided into 765, 6% Preference shares of ₹ 100 each and 76,500 Equity Shares of ₹ 10 each.

The fair yield in respect of the equity shares of this type of companies is ascertained at 8%.

Both the companies earned same amount of profit during the last two years - 2021-22 ₹ 84,150 and 2022-23 ₹ 1,14,750.

Calculate the value of the Equity Shares of each of these two companies on 31.3.2019 on the basis of this information only. Ignore taxation.

Problem 13. The following is the Balance Sheet of Ashalata Co. Ltd. as on 31.3.2025

Liabilities	₹	Assets	₹
23,000 Equity Share Capital (Equity shares of ₹10 each)	2,30,000	Building	4,60,000
12% Preference shares of ₹10 each	2,30,000	Plant	2,30,000
General Reserve	1,38,000	Investment	1,15,000
Profit & Loss A/c	92,000	Stock	1,38,000
15% Debentures	2,30,000	Debtors	92,000
Creditors	1,84,000	Cash	23,000
	11,04,000	Discount on issue of debentures	46,000
			11,04,000

Ascertain the value of each equity share under Fair Value Method on the basis of the above balance sheet and information given below.

Assets are revalued as, Building ₹ 7,36,000, Plant ₹ 4,14,000, Stock ₹1,03,500 and Debtors ₹80,500. No change in the values of liabilities.

Average Profit of the company is ₹ 2,76,000 and 12½% of profit is transferred to General Reserve, Rate of taxation being 50%. Normal dividend expected on equity shares is 8% whereas fair return on capital employed is 10%.

Problem 14. From the following balance sheet of Alibaba Ltd. and the additional information given below, ascertain intrinsic value of each share.

Balance Sheet as on 31/3/2025

Liabilities	₹	Assets	₹
Share Capital (Equity shares of ₹ 10 each)	6,30,000	Goodwill	252000
12% Preference shares of ₹10 each	2,10,000	Leasehold Properties	735000
General Reserve	1,68,000	Fixtures	126000
Profit & Loss A/c	1,47,000	Investment	105000
Unsecured Loan	2,10,000	Current Assets	157500
Current Liabilities	63,000	Loans & Advances	31500
		Miscellaneous Expenditures	21000
	14,28,000		14,28,000

Additional Information

- Goodwill should be valued at 3 years purchase of average profits of last 5 years. The profits for the last 5 years are ₹ 1,47,000, ₹ 1,89,000, ₹ 1,57,500, ₹ 1,78,500 & ₹ 1,68,000.
- Leasehold property and fixtures are valued at ₹ 8,40,000 and ₹ 1,05,000 respectively.

Problem 15. Following is the balance sheet of Dev Engineering Ltd. as on 31st March 2025

Balance Sheet

Liabilities	₹	Assets	₹
Share Capital – 3750 Equity Shares of ₹ 100 each	375000	Goodwill	90000
Profit & Loss A/c	37500	Investment	360000
General Reserve	112500	Stock	375000
10% Debentures	337500	Debtors	225000
Sundry Creditors	112500	Cash at Bank	75000
Workmen's Saving A/c	150000		
	1125000		1125000

Additional information-

- i) The profits for the last 5 years were 2018-19 ₹ 18,750, 2019-20 ₹ 26,250, 2020-21 ₹ 37,500, 2021-22 ₹ 45,000, 2022-23 ₹ 60,000
- ii) The market value of investment was ₹3,00,000.
- iii) Goodwill is to be valued on 3 years purchase of average annual profits for the last 5 years.

Find the intrinsic value of each share.

Problem 16. Following information pertains to Tejashri Co. Ltd.

8% 20,000 preference shares of 10 each.	2,00,000
50,000 equity shares of 100 each	50,00,000
Average annual profit	10,00,000
Income tax	50%
Transfer of General Reserve	25%
Normal return	10%

Mr. Balasaheb the holder of 200 equity shares in the company assigns you the work of valuing his shareholdings.

Problem 17. Following is the balance sheet of Bhaskar Ltd. as on 31st March 2025.

Liabilities	₹	Assets	₹
Issued Capital – 84000 Equity shares of ₹ 10 each	840000	Fixed Assets	10,50,000
General Reserve	189000	Current Assets	4,20,000
Profit & Loss A/c	42000	Goodwill	84,000
5% Debentures	210000		
Current Liabilities	273000		
	1554000		1554000

On 31st March 2025 the fixed assets were independently valued at ₹11,55,000, current assets at ₹4,62,000 and goodwill at ₹1,05,000. The net profits for the last

three years were ₹1,13,750, ₹1,22,500 and ₹1,18,125 of which 20% was placed to reserve, this proportion being considered reasonable in the industry. The fair investment return may be taken at 10%.

Compute the value of company's share by Intrinsic Value Method and Market Value Method. Also calculate Fair Value of each share.

Problem 18. The following is Balance Sheet of Bahubali Company td. as on 31st March 2025.

Liabilities	₹	Assets	₹
Share Capital – 16500 Equity Shares of ₹ 100 each	1650000	Land & Building	1694000
4400 8% Preference shares of ₹100 each	440000	Plant & Machinery	1936000
General Reserve	770000	Vehicles	495000
Profit & Loss A/c	550000	Debtors	748000
10% Debentures	1100000	Stock	517000
Sundry Creditors	880000		
	5390000		5390000

The Land & Building and Plant & Machinery are to be depreciated by 10% and Vehicles by 20%. The Stock was revalued at ₹4,89,500 and Debtors subject to a provision for bad debts of ₹ 88,000. The profits for the last five years were as – 2018-19 ₹ 4,73,000, 2019-20 ₹ 5,17,000, 2020-21 ₹ 5,50,000, 2021-22 ₹ 6,60,000 and 2022-23 ₹ 7,09,500. The taxation provision is to be made at 50% and a profit earning capacity of similar companies' show 10%.

Find out I) Intrinsic Value, II) Market Value and III) Fair Value of the Equity shares

Practical Problems

Problem 1 - Mrs. Rajani, a conservative investor, is evaluating an investment in 12% redeemable preference shares issued by Reliance Ltd. The face value of the preference share is ₹1,200 and it will be redeemed at par after 5 years. The

preference dividend is paid annually. The required rate of return by Ms. Rajani is 9.5%. The current market price of the preference share is ₹ 1112. You are required to:

1. Calculate the value of the redeemable preference share.
2. Calculate Preference Share Yield
3. Whether Mrs Rajani should buy the shares or not ?

Problem 2. Mr. Kavi purchased a 11% redeemable preference share of South Asia Ltd. in the 3rd year of its 6 years term. The share has a face value of ₹1,500, and it pays annual dividend. The share will be redeemed at par. The required rate of return is 12.5%. The current market price of the share is ₹ 1414. You are required to:

1. Value the preference shares in the 3rd year.
2. Calculate Preference Share Yield
3. Compare it with the market price and suggest if Mr. Kavi should invest or not.

Problem 3. Ms. Dhanwanti is evaluating the purchase of 11% redeemable preference shares issued by Kinetic Ltd. with a face value of ₹ 500, paying annual dividends. These shares are redeemable after 6 years at a discount of 7%. His required rate of return is 12%. The current market price of the preference share is ₹ 475.

You are required to calculate the intrinsic value of the preference share, preference dividend yield and advise whether Ms. Dhanwanti should buy the share or not.

Problem 4. Dr. Priyadarshan is interested in 13% redeemable preference shares of Goodness Ltd., originally issued 5 years ago for a 10-year term. The company has a history of delaying dividend payments but promises to pay 2 years' worth of arrear dividends this year along with regular dividend, and then normal dividends till redemption.

The face value is ₹ 700, and dividends are paid annually. The shares are redeemable at ₹750. Dr. Priyadarshan requires a 14% return. The current market price is ₹650.

You are required to:

1. Value the preference shares from today (beginning of Year 5, 6 years left).

2. Compute the rate of yield from dividend
3. Decide whether he should invest or not.

Problem 5. Mrs. Simran is evaluating an investment in 9% redeemable preference shares of Global Ltd. having a face value of ₹ 900, with annual dividends. The share is redeemable at a 10% premium after 5 years. The required rate of return is 10%, and the current market price is ₹920. You are required to:

1. Calculate the intrinsic value of the share.
2. Calculate yield rate of dividend
3. Recommend whether to invest or not.

Problem 6. Mr. Adnan is considering investing in 14% redeemable preference shares of Royal Ltd. The shares have a face value of ₹ 1100, and only 3 years are left before redemption at par. The company pays annual dividends. Mr. Adnan required rate of return is 15%. The current market price is ₹1,040. You are required to:

1. Compute the intrinsic value of the share.
2. Calculate the preference share yield.
3. Decide if she should buy the share based on valuation.

Problem 7. Miss Arohi wants to value a 10% redeemable preference share of Prince Ltd. with a face value of ₹1,200, paying semi-annual dividends. The shares are redeemable at par after 3 years, and Miss Arohi is evaluating them at the end of 1st year. Her required rate of return is 12% per annum, compounded semi-annually. The current market price is ₹ 1270.

You are required to:

1. Calculate the intrinsic value of the share.
2. Calculate yield of preference shares
3. Suggest whether she should invest or not.

Problem 8. Ambani Ltd. issued 5-year redeemable preference shares of ₹ 2000 face value. Dividends are structured as: Year 1–2: 9% p.a. and Year 3–5: 13% p.a.

Redemption is at a premium of 10%. Ms. Manisha is evaluating this share at the beginning. His required return is 12% p.a. The share is trading at ₹ 1980. You are required to:

1. Value the preference shares today.
2. Find out the yield of preference shares
3. Decide whether Ms. Manisha should invest.

Problem 9. Mr. Rudra is considering the valuation of a 10 year 10% redeemable preference share issued by Fintec Ltd. on 1/4/2022 with a face value of ₹ 5,000 and redeemable at par. The company pays annual dividend. She is valuing these shares at the end of 7th year (i.e., 3 years remaining). Due to recent market volatility, he expects a higher return of 12%. The current market price is ₹ 4945. You are required to:

1. Calculate the intrinsic value as on end of 3rd year.
2. Find out the preference share yield
3. Decide whether she should invest in the preference share or not.

Problem 10. Mrs. Harsha is evaluating the 10% redeemable preference shares of Trustworthy Ltd. with face value of ₹ 3,000 and 5 years to maturity. Due to a moderate credit rating, she includes a default risk premium, and hence, his required return is set at 13%.

The shares pay annual dividends and will be redeemed at par. The market price is ₹ 2910.

You are required to:

1. Calculate the intrinsic value using the adjusted required return.
2. Advise if Mrs. Harsha should invest in these preference shares.

◆◆◆