## Issue of shares:

A company is a voluntary association of persons formed for the purpose of carrying on a business for profit, with contributed by the members comprising it, and divisible into shares.

## Characteristics of a company:

I. Separate legal entity
II. Limited liability
III. Perpetual succession and a common seal
IV. Transferability of shares
V. Voluntary association for profits.

## Prospectus:

Prospectus is a document which invites deposits from the public or invites offers from the public for purchasing shares or debentures of a company. It is an invitation to the public for contribution to capital.

## KINDS OF SHARES:

Shares may be two types.

i) Preference shares.
ii) Equity shares.

### i) Preference shares:

Preference shares are those shares which enjoy the following two preferential rights.

i) Rights as to the payment of a fixed rate of dividend during the life time of the company.

ii) right as to the return of capital on winding up of the company.

### ii) Equity shares:

Equity shares are those shares which are not preference shares. That is, these do not carry the preferential rights.

## Different component of share capital:

The following are the different types of shares capital

i) Authorized capital

ii) Issued share capital
iii) Subscribed capital
iv) Called up capital
v) Paid up capital
vi) Reserve capital

**i) Authorised capital:**

Authorised share capital is the amount of share capital which is authorised in the Memorandum of Association of the company. It is also as known as **Nominal capital or Registered Capital.**

**ii) Issued Share Capital:**

Issued share capital means the amount as share capital issued to the public through prospectus.

**iii) Subscribed share capital:**

Subscribed share capital means the amount of share capital subscribed by the public out of the issue of share capital.

**iv) Called up capital:**

Generally the share capital of a company may be collected in different installments (ie) Application money, allotment, call money etc.

**v) Paid up share capital:**

Paid up share capital is the amount of capital which is paid by the share holders of a company. Generally, the amount of paid up capital must be equal to the amount of called up capital.

**vi) Reserve capital:**

Reserve capital is the portion of authorized capital which is reserved for certain purposes. It is a portion of the subscribed capital not already called becomes the reserve capital.

**Meaning of Debenture:**

The companies Act defines, a debenture as one which includes debenture stock, bonds and any other securities of a company, whether constituting a change on the assets of the company or not.

**Debenture contains the following information:**

i) Name of the company.
ii) Serial number of the debenture.
iii) Name of the debenture holder.
iv) Date of redemption of debenture.
v) Company's seal.
vi) Kinds of assets mortgaged to the debenture holders.
vii) Authorized signatories' signatures.

**Different types of debenture:**Debenture may be grouped into the following types;

1) Unsecured debentures
2) Bearer debentures
3) Secured debentures
4) Registered debentures
5) Redeemable debentures
6) Irredeemable debentures
7) Convertible debentures

**Issues of debentures:**

Debentures may be issued from consideration point of view in the following three ways.

I. For cash.
II. For consideration other than cash.
III. As a collateral security

# VALUATION OF GOOFWILL AND SHARES

**Goodwill – Meaning:**

Goodwill is something which will bring to the firm in future profits almost without efforts. Goodwill is the reputation earned by a business.

**Circumstances under which goodwill may be valued:**

Goodwill of a company may be valued under the following circumstances.

i) When two or more firms decided to amalgamate
ii) When a company takes over another.
iii) When there is external reconstruction of a company.
iv) When a partnership business is sold to a company.
v) When there is exchange of shares
vi) When a new partner is admitted.
vii) When a partner is retired.
viii) When the Government takes over the business of a company.

**Different methods of valuation of goodwill:**

Goodwill of a concern is valued in the following five methods.

i) Average profit method
ii) Super profit method
iii) Capitalization of super profit method
iv) Annuity method
v) Capitalization method

**i) Average profit method:**

Under this method the average profit for

**Goodwill = Average profit × Number of years**

**ii) Super profit method:**

Under this method, super profit is multiplied by the number of years of purchases. Super profit is the difference between average profit and normal profit of a concern

**Super profit = Average profit – normal profit**

**iii) Capitalization method:**

Under this method, the average super profit of the business is capitalized at the normal rate of return. The capital value of the business is known as goodwill.

$$\textbf{Goodwill} = \frac{\textbf{Super profit} \times 100}{\textbf{Normal rate of return}}$$

**iv) Annuity method:**

Goodwill is calculated on the basis of reference to annuity table.

**Goodwill= super profit × Reference to annuity table**

**v) Capitalisation method:**

Under capitalization method, the value of the business is determined by capitalizing the expected average profits on the basis of normal rate of return.

$$\textbf{Total value of the business} = \frac{\textbf{Average Profit} \times 100}{\textbf{Normal rate of return}}$$

**Net assets = Total assets – Liabilities**

**Goodwill = Total value of the business – Net assets**

**VALUATION OF SHARES:**

**Meaning of the term share:**

Every business will have its own capital. Like this, a company will have its own capital. The share capital of a company is divided into units of small denomination.

**Kinds of Shares:**

Shares may be of two types.

1) Preference shares
2) Equity shares

**Types of value shares:**

Value of shares may be of the following types.

i) Par value
ii) Book value
iii) Market value

iv) Purchase value
v) Capitalized value
vi) Intrinsic value
vii) Fair value

**Different methods of valuing shares of a company:**

The following are the three methods of valuation of shares.

i) Net assets method
ii) Yield method
iii) Fair value method

**i) Net assets methods:**

Valuation of assets on the basis of net assets available to equity shares holders is known as net assets method. This method is also as intrinsic value method.

**ii) Income or yield method:**

Valuation of assets on the basis of expected rate of return and normal rate of return is known as yield method.

**iii) Fair value method:**

Under this method, value of a share is obtained by the simple average of value as per net asset method and value as per yield method.

$$\textbf{Value per share} = \frac{\textbf{Value as per net asset method + value as per yield method}}{\textbf{2}}$$

**Final accounts of companies:**

Final accounts of a company include trading accounts, profit and loss account, profit and loss appropriation account and balance sheet but now trading account, profit and loss account, and profit and loss appropriation account are combined and are known as profit and loss account.

Final accounts of a registered company consist of

i) Profit and loss account and
ii) Balance sheet.

**Some special points to be considered:**

i) Interest on debentures
ii) Discount on issue of debentures
iii) Preliminary expenses
iv) Political expenses
v) Dividend expenses
vi) Provision of taxation

**i) Interest on debentures:**

Interest on debenture is an expense of a company. It is a charge against the profit of the company.

**ii) Discount on issue of debentures:**

This amount is shown in the asset side of the balance sheet under the head 'miscellaneous expenditure'. This amount is written off out of the profits of the company and hence debited to profit and loss account.

**iii) Preliminary expenses:**

Preliminary expenses are those expenses which are incurred at the time of formation of a company.

**iv) Political expenses:**

This amount is debited to profit and loss account.

**v) Dividend expenses:**

Some time, a company may receive dividend from other companies. The amount of gross dividend will be credited to profit and loss account.

**vi) Provision of taxation:**

Provision of taxation is debited to profit and loss account. This amount appears in the balance sheet under the head "current liabilities and provisions" .

**Methods of calculating purchase consideration:**

There are two methods of calculating purchase consideration.

1) Net asset method.
2) Net payment method.

1) **Net Asset method:**

Under this method, purchase consideration is the sum of all assets and liabilities which are agreed to be taken over by the purchasing company at an agreed value.

2) **Net payment method:**

Purchase consideration is the aggregate of amount paid to the verified company in the form cash, shares and debentures.

**Meaning of amalgamation:**

When two or more companies go into liquidation and a new company is formed to take over the business of the above two or more companies, it is said to be amalgamation. To avoid competition and to fix the price of an article, amalgamation takes places.

**Absorption:**

When one or more companies g into liquidation and some existing company takes over the business, it is said to be absorption. That is, the business of a small company is absorbed by the big company.

**Reconstruction:**

Reconstruction refers to the reconstruction of a company's financial structure. It may take places with or without the liquidation of the company. If a company goes into liquidation for reconstruction, then it is known as internal reconstruction.

Reconstruction may be of two types;

i) External Reconstruction and
ii) Internal Reconstruction.

**Comparison:**

| **Amalgamation** | **Absorption** | **External Reconstruction** |
|---|---|---|
| i) Two or more companies go into liquidation. | Small company goes into liquidation. | One company goes into liquidation |
| ii) New company is formed. | New company is not formed. | New company is formed. |