

## JOINT STOCK COMPANY – AN INTRODUCTION

### 26.1 INTRODUCTION

Industrial revolution ushered in a new era of economic development in England during the 18th century. It resulted in a change in the nature of economic activities. The size of market widened from National to international level due to large scale production. It further brought development in Banking, insurance, transport and communication.

As you know that the sole proprietorship form of business organisation could not meet the growing needs of huge capital and managerial skills required for increased scale of production. Partnership, another form of business organisation, emerged as an improvement over sole-proprietorship. But, still it could not cope up with the growth in economic activities. Moreover, partnership, too, has its limitations. The financial resources are limited to the extent of capital provided by its partners and their borrowing capacity. The managerial skills of partners are also limited. Again in sole-proprietorship and partnership, the liability of owner/owners is unlimited. In order to overcome these problems, a new form of business organisation known as company came into existence..

In this lesson, we shall study about Joint Stock Company, its features and the methods of raising capital through issue of shares.

### 26.2 OBJECTIVES

After studying this lesson, you will be able to:-

- state the meaning of company as a form of business organisation;
-

- describe the characteristics of company;
- describe various kinds of companies;
- distinguish between public and private company;
- state the meaning of shares as a source of finance;
- explain various types of shares;
- distinguish between Preference shares and equity shares;
- explain the concept of share capital;
- describe various types of share capital;

### **26.3 COMPANY MEANING AND CHARACTERISTICS**

A company is an association of individuals formed for a common purpose. The common purpose may be carrying on business to earn profits or for charitable purpose.

It is simply stated that a company means "a company formed and registered under the Companies Act." or registered under any previous laws enacted from time to time. The companies Act has defined the company as "an artificial person created by law having a separate entity with perpetual succession and a common seal".

#### **Characteristics of Company**

From the above definition, we can derive the following characteristics of a company:

##### **1. Artificial person**

As such, a company is an artificial person existing in the eyes of law only. It has almost all the rights and powers of a natural person. It can enter into contracts. It can sue in its own name and can be sued.

##### **2. Separate legal entity**

Registered under Companies Act, a company is vested with a corporate personality which is distinct from its members. It has an identity of its own. The capital is contributed by its members called shareholders. The property purchased out of the capital belongs to the company and not to the shareholders.

##### **3. Capital divisible into shares**

The capital of the company is divided into small parts or units called shares. The units of capital are generally of small value, say Rs.10/- or Rs 50/- or Rs 100/-.

---

**4. Transferability of shares**

The shares of the company are easily transferable unless restricted by its Articles of Association. The shareholders can sell their shares and the purchasers become the new members of the company in place of old shareholders.

**5. Perpetual succession**

The company has an independent and separate existence distinct from its shareholders. Therefore a company is a stable organisation or we can say that a company has a perpetual succession. This means that a company continues to exist even after the death of a member or members or on the transfer of shares by one shareholder to another.

**6. Limited liability**

The liability of the shareholders of a company is limited to the extent of full value of shares held by them. The shareholders may be asked to pay the unpaid value of shares if any to the maximum. For example, if the face value of a share is Rs 100 and a shareholder has already paid Rs 80, he cannot be asked to pay more than the balance of Rs 20/- per share.

**7. Representative Management**

A company is an artificial person. For dealing with various matters relating to business, it needs someone to act on its behalf. The number of shareholders is so large that they cannot manage the affairs of the company collectively. For the sake of effective management, shareholders elect some persons from among themselves to manage and administer the company. The management of company is entrusted to the elected representatives of shareholders. They are called the Directors of the company and collectively can be called the Board of Directors.

**8. Common Seal**

A common seal is the official signature of the company. A document not bearing the common seal of the company is not binding on the company. Any document prepared by the directors can be said to belong to the company when it has its common seal.

---

**INTEXT QUESTIONS 26.1**

---

- A. Fill in the blanks with correct word/words relating to the characteristics of company.
- i. A joint stock company exists only in the eyes of law. Hence a company is \_\_\_\_\_.
  - ii. The capital of the company is divided into small parts or units.
-

Such units are called \_\_\_\_\_.

- iii. \_\_\_\_\_ gives an identification in all contracts and is a device required to act as its signature.
- iv. The shareholders elect some persons of their choice to manage the affairs of the company. It explains the \_\_\_\_\_ character of the company.

B. Identify the correct statement by marking (√) and incorrect one by marking (×).

- i. A company ceases to exist on the death of any of shareholders.
- ii. The liability of every member of company is restricted to the face value of shares held by him.
- iii. There is restriction on transfer of shares of a company
- iv. A company can enter into contracts in its own name.

## 26.4 KINDS OF COMPANIES

Various kinds of companies can be classified under the following three heads:

1. On the basis of formation
2. On the basis of liability
3. On the basis of ownership

### 1. On the basis of formation

On the basis of formation, company can be classified as :

#### a) Statutory Company

A company formed by a Special Act passed either by parliament or State Assembly is called a STATUTORY COMPANY. Reserve Bank of India, Industrial Finance corporation of India, Life Insurance corporation are some of its examples. These companies are governed by their respective Acts.

#### b) Registered company

A company formed and registered under Indian companies Act 1956 or earlier Company Act is called Registered company. The working of such companies is regulated by the provisions of Companies Act.

### 2. On the basis of liability

On the basis of liability, company can be classified as :

**a) Company limited by shares**

The liability of the member of such company is limited to the extent of the amount unpaid on the shares held by them.

**(b) Company limited by guarantee**

The liability of each member of such company is limited to the extent of guarantee undertaken by the member voluntarily in the event of its being wound up.

**c) Unlimited Company**

Such a company may or may not have any share capital. The company not having any limit on the liability of its members, is called an unlimited Company. Liability in such a case extends to the personal property of its shareholders. These Companies are not popular in India.

**3. On the basis of Ownership**

**a) Private Company**

A private company is one which by its Articles of Association:

- i. restricts the right of the members to transfer its shares;
- ii. limits the number of its members to 50 (excluding its past and present employees);
- iii. prohibits any invitation to the public to subscribe for its shares or debentures.

The minimum number of shareholders in such a company is 2 and the company has to add the words 'Private Limited' to its name.

**b) Public Company**

A Company which is not a private company is a public company. Its articles do not contain the above mentioned restrictions.

Its main features are:-

- i) The minimum number of members is 7.
- ii) There is no restriction on the maximum number of members.
- iii) It can invite public for subscription to its shares.
- iv) Its shares are freely transferable.
- v) It has to add the word 'Limited' to its name.

**c) Government Company**

A Government Company is one in which not less than 51% of its paid

up Capital is held by State Government, or Central Government or partly by State Government and partly by Central Government for example, Steel Authority of India.

**d) Foreign Company**

A foreign Company is one which is incorporated outside India but has its place of business in India, for example Pepsi Cola

**Difference between Public Company and Private Company**

The differences between Public Company and Private Company are as follows :

Point of difference	Public Company	Private Company
1. Minimum Number of Members	Minimum number of members required is 07.	Minimum number of members required is 2.
2. Maximum number of members	No limit on maximum number of members.	It cannot have more than 50 members.
3. Name	Its name must end with the word 'Limited'.	Its name must end with the words 'Private limited'.
4. Commencement of Business	It can start its business only after getting certificate of commencement of business.	It can commence its business as soon as it gets certificate of Incorporation.
5. Invitation to public	It may invite public to subscribe to its shares.	It cannot extend invitation to public for subscription of its shares.
6. Transfer of shares	There is no restriction on transfer of its shares.	There is restriction on the transfer of its shares.
7. No. of directors	It must have atleast 3 directors.	It must have atleast 2 directors.
8. Statutory Meeting	It must hold statutory meeting.	There is no such obligation on private company.

---

## INTEXT QUESTIONS 26.2

---

- A. Fill in the blanks with correct words/figures from those given in brackets:-
- i. The minimum number of members of a private company is \_\_\_\_\_. (2,5,7)
  - ii. The membership of a private company cannot exceed \_\_\_\_\_. (50,7,100)
  - iii. A Public company \_\_\_\_\_ put restrictions on transfer of shares (can, cannot)
  - iv. In a Government company \_\_\_\_\_ 51% of its paid up capital is held by government. (less than, more than)
  - v. A foreign company is one which has its place of business \_\_\_\_\_ (In India, outside India)
- B. Certain characteristics of different types of companies are given below. Identify and name the company.
- i. It imposes restriction on transfer of its shares.
  - ii. More than 51% of its paid up capital is held by Government.
  - iii. A Company formed by Special Act of Parliament or State Legislature.
  - iv. It has to add 'Private Ltd.' to its name.
  - v. The liability of its members is limited to the extent of the amount unpaid on its shares.
- 

## 26.5 SHARES - MEANING AND ITS KINDS

In order to finance its activities, the company needs capital. The words 'capital' and 'share capital' are synonymous in case of company. The total capital of company is divided in certain small units of one or more denominations. Such units are called 'shares'. A share is an interest of a shareholder in the capital of the company. It expresses the proprietary relationship between the company and the shareholder.

---

## Share Certificate

A certificate is issued by the company to each shareholder specifying the number of shares allotted to him. This certificate is known as 'Share Certificate'. It is the proof of his share holding in the company.

### Kinds of shares

According to the Companies Act, a company can issue the following two types of shares:

- i. Preference shares
- ii. Equity shares

#### i. Preference shares

A preference share is one which carries the following two preferential rights over equity shareholders:

- Payment of dividend at fixed rate
- Repayment of capital at the time of winding up.

#### ii Equity shares

All shares which are not preference shares are equity shares. Holders of these shares receive dividend out of the profit as determined by Board of Directors and declared in the Annual General Meeting of the company. The holders of these shares have ultimate control over the affairs of the company,

They have the privilege of voting for the election of the directors of the company or having elected as directors. Some of the main characteristics of the equity shares are:-

- They are permanent source of capital.
- Once issued they cannot be taken back by the company.
- They confer on the holder a right to attend meetings, vote at the meetings, elect directors and receive dividend.

**Difference between Preference shares and equity shares:-**

Basis of Difference	Preference shares	Equity shares
1. Period of Finance	These shares are sources of medium and long term finance.	These shares are source of long term finance.
2. Control	Management and control of company do not vest with Preference shareholder.	Management and control of company vests with equity shareholders.
3. Rate of dividend	The Preference shareholders receive dividend at fixed rate depending on profits.	Equity shareholders' rate of dividend is not fixed.
4. Payment of Dividend	Preference shareholder have the preference over equity shareholders as to payment of dividend.	Equity shareholders are paid dividend only after dividend has been paid to the preference shareholder.
5. Refund of share capital	Preference shareholders have preference as to refund of share capital in case of winding up of company.	Equity shareholders get refund of capital only after Preference shareholders.

**INTEXT QUESTIONS 26.3**

A. Fill in the blanks with suitable word/words :

- i. Share capital is a main source of finance in a \_\_\_\_\_.
- ii. A \_\_\_\_\_ is a document issued by the company stating the details of shares and the shareholders.
- iii. \_\_\_\_\_ have the preferential right as the payment of dividend over \_\_\_\_\_.
- iv. \_\_\_\_\_ have the right to elect Directors of the company.

- B. Given below are various characteristics relating to equity shares and preference shares. Read them carefully and mark (✓) in appropriate column to which they belong.

Characteristics	Equity shares	Preference shares
i. Holders have the right to vote and elect the directors.		
ii. They are given priority to get the amount of dividend.		
iii. Their rate of dividend is fixed.		
iv. They are paid back capital at last.		
v. They enjoy the success of company.		

## 26.6 SHARE CAPITAL - MEANING AND ITS TYPES

In a company limited by shares, the word capital means share capital. Share capital is the money raised by issue of shares. The share capital of the company is of the following types :-

### 1. Nominal, Authorised or Registered Capital

This is the maximum amount which a company is authorised to raise by issue of shares. It is stated in the Memorandum of Association as capital of the company. It is usually fixed as the amount which the company will need for its present and future requirements.

### 2. Issued Capital

It is that part of the authorised capital which the company offers to the public for purchase or subscription at present. The company may not issue its entire authorised capital at one time. It may be issued from time to time as per needs of the company.

### 3. Subscribed Capital

It is that part of the issued capital which is taken up or subscribed for by the public. Sometimes, there may be overwhelming response to the issue and shares may be over subscribed. While, in other cases the

company may receive applications for less number of shares than the issued shares. In any case the subscribed capital may be equal to or less than the issued capital. Subscribed capital cannot exceed the issued capital.

**4. Called up Capital**

It is that part of the subscribed capital which is called up by the company and is to be paid by the shareholders.

**5. Uncalled capital**

It is the amount which is not called upon by the company on the shares issued.

**6. Unpaid capital**

It is that part of capital which remains unpaid by some shareholders who have subscribed for shares.

**7. Reserve Capital**

You have learnt that company cannot ask its share-holders to pay more than the unpaid value of their shares at the time of winding up. Company may keep some part of the share capital uncalled and keep it in reserve to be called only in case of need upto the time of winding up. It is decided by a special resolution. This part of the capital kept in reserve is known as **Reserve Capital**.

**Example**

Let us take an example to illustrate various kinds of capital.

Suppose a company is registered with Rs.10,00,000 as its Authorised capital divided into 1,00,000 equity shares of Rs10 each. For its present requirement, it issues 80,000 shares of Rs 10/- each and it calls up Rs 8/- per share. Public applied for 60,000 shares. All the called up money was received except that a shareholder holding 200 shares failed to pay Rs.3 per share. The capital would appear in the Balance sheet as under.

Solution :

## Balance Sheet As on .....

Liabilities	Amount Rs.	Assets	Amount Rs.
<b>Authorised capital</b> 1,00,000 equity shares of Rs.10/- each	10,00,000		
<b>Issue Capital</b> 80,000 shares of Rs.10/- each	8,00,000		
<b>Subscribed capital</b> 60,000 shares of Rs.10/- each	6,00,000		
<b>Called up capital</b> 60,000 shares of Rs.8/- per share	4,80,000		
<b>Paid up capital</b> 60,000 shares of Rs.8 per share 4,80,000 (-) unpaid calls (200×3) -600	4,79,400		

**Note:**—Not to be shown in Balance Sheet  
Uncalled capital  
(60,000 shares at Rs 2/- per share 1,20,000)

**INTEXT QUESTIONS 26.4**

- A. Fill in blanks with suitable word/word's :
- \_\_\_\_\_ capital is that part of the authorised capital which is offered to public for subscription.
  - \_\_\_\_\_ capital is that part of uncalled capital which is kept in reserve to be called in the event of winding up.
  - \_\_\_\_\_ capital is that part of issued capital which is applied by the applicants for shares.
  - The registered capital mentioned in the Memorandum of Association is termed as \_\_\_\_\_ capital.
  - Share capital is the amount of capital raised through \_\_\_\_\_.
- B. Identify the correct statements from the following by marking (✓):
- Subscribed capital cannot exceed the issued capital.

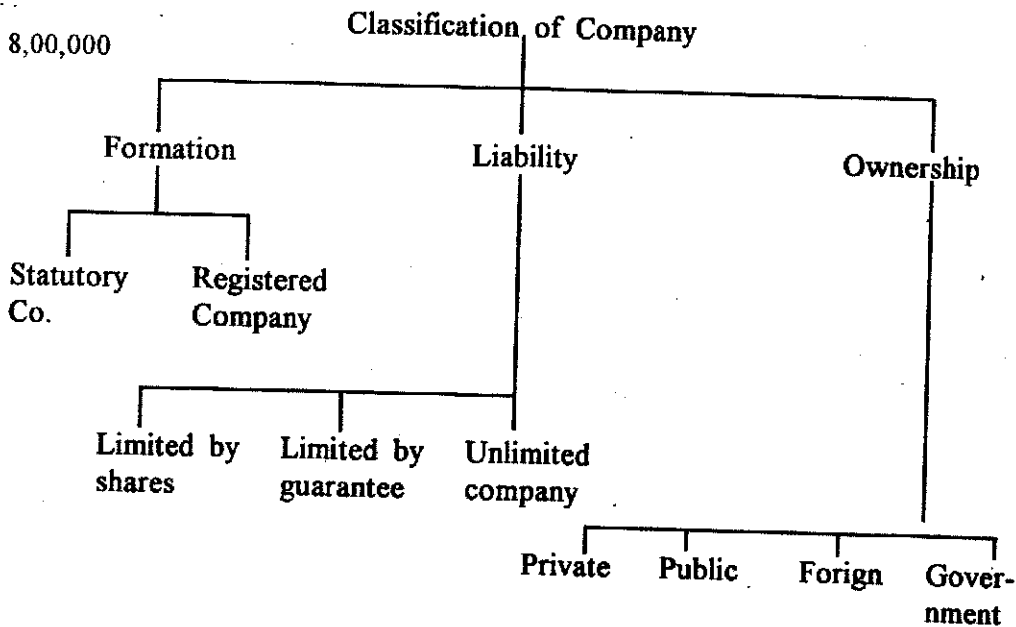
- ii. Face value of the shares held by a shareholder determines his liability.
- iii. Issued capital is mentioned in the document called Memorandum of Association.
- iv. Called up capital is part of the subscribed Capital.

## 26.7 WHAT YOU HAVE LEARNT

1. Inadequacies of the partnership firms to run large size business gave birth to joint stock company. Company form of organisation made it possible to raise huge capital required by large size business and to use developed managerial skills required in modern business.

Through the process of registration, a company is given a separate identity, different from its members.

2. Company is a registered body formed out of voluntary association of persons. Companies in India are formed and controlled under Indian Companies Act. 1956.
3. Important characteristics of a company are separate legal entity, perpetual succession, Common seal, representative management and limited liability.
4. The classification of company can be arranged on the basis of :



5. Private companies are registered with three restrictions:-
  - i maximum number of members restricted to 50;
  - ii restrictions imposed on transferability of shares;
  - iii Inviting public to contribute to the capital restricted.
6. Private company must add the words 'Private limited' after their name.
7. Registered companies other than private companies are public companies.
8. To meet the long term requirements, the company issues shares.
9. A share is a fractional part of the share capital of the company which forms the basis of memberships. Holders of such shares are called shareholders and secures the right to dividend and right to vote.
10. Shares are of two types: equity shares and preference shares. The preference shares are those shares which carry priority over equity shares regarding payment of dividend and return of capital.
11. A certificate issued by the company specifying the details of the holder of shares and the number of shares allotted is known as share certificate.
12. Authorised capital or nominal capital is the registered capital which a company can raise by issue of shares to the maximum.
13. Issued capital is that part of authorised capital which the company offer to the public for purchase or subscription.
14. Subscribed capital is that part of the issued capital which is taken up or subscribed by the public.
15. Called up capital is that part of the subscribed capital which is called up by the company and is to be paid by the shareholders.
16. Uncalled capital is the amount not called upon by the company on its shares.
17. Reserve capital is the uncalled capital kept in reserve to be called up only in case of need at the time of winding up.

## 26.8 TERMINAL QUESTIONS

1. Give brief answers to the following :- (30-50 words)
-



B. Equity Shares		Preference Shares
i)	✓	—
ii)	—	✓
iii)	—	✓
iv)	✓	—
v)	✓	—

- 26.4 A. i. Issued                      ii. Reserve  
 iii. Subscribed                  iv. Authorised or Nominal  
 v. Issue of shares

- B. (i) ✓                  (ii) ✓                  (iii) ×                  (iv) ✓