Limited Companies

Definition

A Limited Company is a separate legal entity – seen as a person separate from the shareholders. The Company is owned by Shareholders and managed by Directors.

Comparison of a limited Company to a Partnership

	Limited Company	Partnership
1.	limited liability	unlimited liability
2.	number of members limited by number of shares	limited to 20
3.	profits shared by a dividend	agreed profit sharing ratio
4.	pay fixed rate of company tax	tax depending on profit share

Terms used to describe share capital

1. **Authorised Share Capital** – maximum amount of share which a company is allowed to issue

2. **Issued Share Capital** – the amount of shares which have actually been issued to shareholders

3. **Called-up capital** – the money required to be paid by shareholders immediately when they buy shares if the company does not require all the money to be paid in right away

4. **Uncalled Capital** – the amount which has not yet been paid by shareholders for shares bought

5. **Paid-up capital** – the portion of the Called-up capital for which the company has actually received the cash

6. **Calls in advance** – money received from shareholders before a call is made by the company asking for the next amount of money to be paid for the shares.

7. **Calls in Arrear** – money not yet received from shareholders after a call has been made by the company

8. **Forfeited Shares** – shares forfeited by shareholders because they have failed to pay their calls. They may be re-issued to other shareholders.

Types of Shares issued by companies

1. Ordinary Shares
    - Carry voting rights at meetings – one vote per share
    - Ordinary shareholders are the last to receive a dividend
    - In liquidation, ordinary shareholders are the last to receive their capital back
    - The price of these shares is known as the PAR VALUE.
    - Shares sold for a price above par value are sold at a SHARE PREMIUM (the amount above the par value)

2. Preference Shares
    - Receive a fixed dividend
    - Are paid a dividend before ordinary shareholders
    - Can be: a) *cumulative preference shares* (paid arrear dividends)
b) *non-cumulative preference shares* (lose dividends if the directors do not declare)

Reserves

Types of Reserves:

a) Revenue Reserves – are created by ploughing profits back into the company

Examples: Retained Profit – profit not distributed to shareholders
General Reserve – created for general purposes in future
Fixed Asset Reserve – created to purchase fixed assets

Capital Reserves : Share Premium – created when shared are sold above par value
Revaluation Reserve – when assets are revalued
Capital Redemption reserve – when a company buys back shares

Bonus Issue of Shares (also known as a 'Scrip' issue)

If the Directors consider that the Reserves are too high they may transfer some of the reserves to the Ordinary Share Capital account. This means that the shareholders will receive shares (for free). The company does NOT RAISE NEW CAPITAL in this way – no money is received for the shares.

The CAPITAL RESERVES (Share Premium; Capital Redemption and Revaluation Reserve) are usually used to make bonus issues.

Bonus issues may be made when the directors decide not to declare a dividend in order to keep shareholders happy.

Rights Issue

These are shares issued to ***existing shareholders***.

Advantages
- Less expensive than a general issue to the public
- Control remains with existing shareholders

A shareholder may sell his right to purchase additional shares to someone else or he may simply forfeit the right.

Dividend policy

Dividends are paid to shareholders as a way of distributing the profits of the company. Dividends are normally expressed as "cents per share" eg 10 cents for every share held.

Directors decide if a company will be paying out a dividend or not. They look at factors such as:
1. the availability of profits
2. the availability of cash to pay the dividend
3. whether it would be better to keep the profits in the company to allow it to grow
4. whether the market price of the shares will be affected or not

Directors may pay out a dividend more than once per year. A dividend declared during the year is called an INTERIM dividend, and at the end of the year it is called a FINAL dividend.

Debentures

A debenture is a document given to someone who has loaned the company money. It states the amount of the loan, the interest payable each year, and the date on which the loan is to be repaid.

Debenture holders are liabilities of the company – NOT owners as it is with shareholders. The interest must be paid regardless of the profitability of the company.

Debentures due to be paid within a year are shown on the balance sheet as CURRENT LIABILITIES.
Those due to be paid in more than one year are shown as LONG TERM LIABILITIES.

Convertible Loan Stock

These are debentures which give the holder the option to convert the loan amount into shares of the company at a predetermined price on a predetermined date.

When the date arrives, if the market price of the shares is higher than the predetermined price then the holder will find the option very attractive