FORFEITURE OF SHARES

The Model Articles of Association of a Company Limited by shares as contained in Table-F of the Companies Act, 2013, provide as follows in regard to forfeiture of shares :

1. Article 28 states that if a member fails to pay any call, or instalment of a call, on the day appointed for payment thereof, then at any time thereafter during such time as any part of the call or instalment remains unpaid, the Board may serve a notice on him requiring payment of so much of the call or instalment as is unpaid, together with any interest which may have accrued.

2. Article 29 lays down that the notice as aforesaid shall (a) name a further day (not being earlier than the expiry of 14 days from the date of the service of the notice) on or before which the payment required by the notice is to be made; and (b) state that, in the event of non-payment on or before the day so named, the shares in respect of which the call was made shall be liable to be forfeited.

3. Article 30 says that if the requirements of any such notice as aforesaid are not complied with, then any share in respect of which the notice has been given, at any time thereafter, may be forfeited by a resolution of the Board to that effect, before the payment required by the notice has been made.

4. Article 31 states that (i) A forfeited share may be sold or otherwise disposed of on such terms and in such manner as the Board thinks fit. (ii) At any time before a sale or disposal as aforesaid, the Board may cancel the forfeiture on such terms as it thinks fit.

Article 34 lays down that these provisions of the regulations concerning forfeiture shall apply in the case of non-payment of any sum which, by the terms of issue of a share, becomes payable at a fixed time, whether on account of the nominal value of the share or by way of premium, as if the same had been payable by virtue of a call duly made and notified.

In fact, forfeiture of share means to forfeit that amount of the share which a company has already received from the concerned shareholders.

Normally, rules of forfeiture are mentioned in Articles of Association of the company. If no rules are given in Articles, the provision of Table-F regarding forfeiture applies.

Accounting Treatment : Following entries shall be passed for forfeiture of shares in different cases, *viz.*, forfeiture of shares which were originally issued at par or at premium or at discount.

(1) *Forfeiture of shares which were originally issued at par* : If the shares are issued at par and forfeited due to non-payment of allotment/calls the following entry will be passed :

(a) *If unpaid calls have not been transferred to Calls in Arrears Account :*

Share Capital Account	...Dr.	(No. of shares forfeited × Amount calledup per share)
To Share Forfeiture Account		(Total amount paid by the shareholders on forfeited shares)
To Share Allotment Account		(Amount not paid on allotment, if any)
To Share First Call Account		(Amount not paid on first call, if any)
To Share Second & Final Call Account		(Amount not paid on second & final call, if any)

(Being.....shares forfeited due to non-payment of allotment, first call, second and final call)

(b) *If unpaid calls have been transferred to Calls in Arrears Account or Calls in Arrears Account is maintained* :

Share Capital Account	...Dr.	(No. of shares forfeited × Amount called up per share)
To Share Forfeiture Account		(Total amount paid by the shareholders on forfeited shares)
To Calls in Arrear Account		(Total unpaid amount on various calls)
(Being.....shares forfeited due to non-payment of calls-in-arrears)		

Note : When Calls in Arrears Account was maintained, Calls in Arrears Account is to be credited instead of Share Allotment Account and/or Share Calls Account.

(2) *Forfeiture of Shares which were originally Issued at Premium* : When the shares are issued at premium, then it must be observed whether the premium money has been received or not.

(a) *If the amount of premium has been received on forfeited shares* : If the premium on such shares has already been received, Securities Premium Reserve Account will not be debited or credited or transferred to Share Forfeiture Account, because Companies Act, 2013 does not permit the premium on shares once collected to be refunded or cancelled. According to Section 52 of the *Companies Act,* 2013, *premium once received can be used for specific purpose.*

Accounting treatment (Journal entry) in case of forfeiture of shares if the amount of premium has been received will be same as if the shares were originally issued at par. [as discussed in (1)]

(b) *If the amount of premium has not been received on forfeited shares either wholly or partially* : When a share is forfeited and premium on such share becomes due but not received either wholly or partially, then the *Securities Premium Reserve Account must be debited with the full amount of premium at the time of forfeiture.*

Share Capital Account	...Dr.	(No. of shares forfeited × Amount called-up per share)
Securities Premium Reserve Account	...Dr.	(Amount of premium remaining unpaid on forfeited shares)
To Share Forfeiture Account		(Total amount paid by the shareholders on forfeited shares)
To Share Allotment Account		(Amount not paid on allotment, if any)
To Share First Call Account		(Amount not paid on first call, if any)
To Share Second & Final Call Account		(Amount not paid as second & final call, if any)
(Being.....share forfeited due to non-payment of allotment, first call, second and final call earlier issued at premium)		

(3) *Forfeiture of shares which were originally issued at Discount* : Where shares forfeited were originally issued at a discount, the discount applicable to such shares must be cancelled or written back. Hence, the Discount on Issue of Shares Account should be credited at the time of forfeitures. So, that the balance on 'Discount on Issue of Shares Account' relates only to the remaining shares forming part of share capital :

Share Capital Account	(No. of shares forfeited × Amount called up per share)
To Share Forfeiture Account	(Total amount paid by the shareholders on forfeited shares)
To Discount on Issue of Shares Account	(With the amount of discount allowed originally on forfeited shares)
To Share Allotment Account	(Amount not paid on allotment, if any)
To Share First Call Account	(Amount not paid on first call, if any)
To Share Second & Final Call Account	(Amount not paid on second & final call, if any)
(Being .....shares forfeited due to non – payment of allotment, first call, second and final call earlier issued at discount)	

1,000 shares × ₹ 1 = ₹ 1,000

RE-ISSUE OF FORFEITED SHARES

As per Articles of Association, directors acquire power to reissue forfeited shares, they may do so by selling them to new purchases for any amount they can obtain which together with the amount forfeited on shares is not less than the called up value of the shares on the date when they were reissued. *The liability to pay future calls is taken up by the purchaser*. A resolution is passed for reissue of shares and it is on the basis of this resolution that shares are reissued.

If, after reissue of forfeited shares, some balance is left in Forfeited Shares Account, this balance is transferred to Capital Reserve Account.

However, those forfeited shares which are not reissued the forfeited amount related to them are not transferred to Capital Reverse but are shown in Balance Sheet.

Can Forfeited shares be issued at discount?

Forfeited shares can be issued at a discount. But the discount on the issue of such shares cannot exceed the amount earlier forfeited on such shares. In other words, the amount received on re-issue plus amount already received on forfeited shares must not be less than the paid-up value of such shares.

The maximum amount of discount which may be allowed on re-issue is explained as follows :

Situations	*Maximum Permissible Discount on Re-issue*
(i) When the shares were originally issued at par or at a premium	The amount credited to Share Forfeiture Account.
(ii) When the shares were originally issued at a discount	The amount credited to Share Forfeiture Account plus the amount of original discount.

Accounting Treatment : The following entries will be passed under different situations :

1. For forfeited shares are re-issued at par	Bank A/c (with amount received) ……Dr. To Share Capital A/c (paid or called-up value) (Being forfeited shares re-issued @ ₹ ……each at par)	
2. For forfeited shares are re-issued at premium	Bank A/c (with amount received) ……Dr. To Share Capital A/c (Paid or called-up value) To Securities Premium Reserve A/c (Amount of premium) (Being……forfeited shares re-issued @ ₹ ……each including premium)	
3. For forfeited shares are reissued at discount (If shares were originally issued at par or at premium)	Bank A/c (with amount received) ……Dr. Share Forfeiture A/c ……Dr. (with the amount of discount on re-issue) To Share Capital Account (Paid or called-up value) (Being……forfeited shares re-issued @ ₹ ……each at a discount of ₹ ……each)	
4. For forfeited shares are re-issued at discount (If shares were originally issued at discount)	Bank A/c (with amount received) ……Dr. Share Forfeiture A/c ……Dr. (with the excess of re-issue discount over the original discount) Discount on Issue of Shares A/c ……Dr. (with the amount of discount originally allowed) To Share Capital A/c (Paid or called-up value) (Being……forfeited shares re-issued at a discount of ₹……per share, the advantage of discount allowed)	

Opening of Share Forfeiture Account : When all forfeited shares have been re-issued, the credit balance left in the Forfeited Shares Account being capital profit, is transferred to Capital Reserve Account. For this, entry will be as follows :

5. For transfer of balance of Share Forfeiture Account transferred to Capital Reserve Account	Share Forfeiture A/c ……Dr. To Capital Reserve A/c (Being balance of Share Forfeiture Account transferred to Capital Reserve Account)	

In the context of above entry no. 5, capital profit arises only in respect of the forfeited shares re-issued and not on all forfeited shares. Hence, when a part of the forfeited shares are re-issued, the whole balance of Share Forfeiture Account cannot be transferred to Capital Reserve Account. In such a situation, it is only the *proportionate amount of balance that relates to the forfeited shares re-issued should be transferred to Capital Reserve Account, ensuring that the remaining balance in Share Forfeiture Account is equal to the amount forfeited on shares not yet re-issued.*

Tutorial Notes

1. Capital Reserve is formed on re-issued forfeited shares. When shares are forfeited amount received on these shares is gain to the company and when shares are re-issued, company generally suffers loss (Paid-up Capital *less* Issue Price) by receiving lesser than the paid-up value of shares. In this way, calculate gain per share after forfeiture and re-issue. The gain is multiplied by the number of shares re-issued to ascertain capital reserve.

2. Gain (Profit) on re-issue of shares

$$= \left[\frac{\text{Total Forfeited Amount}}{\text{No. of Forfeited Share}} \times \text{No. of shares reissued}\right] - \left[\begin{array}{c}\text{Amount with which Share Forfeiture}\\ \text{Account was debited at the time of reissue}\end{array}\right]$$

3. In case of partial re-issue, only proportionate amount of Share Forfeiture Account after meeting loss on re-issue of such shall be transferred to Capital Reserve Account.

4. If the forfeited shares have been re-issued on two different dates, there should be separate entries for both the re-issue and transfer to Capital Reserve Account.

ISSUE OF SHARES FOR CONSIDERATION OTHER THAN CASH
Or, ISSUE OF SHARES FOR PURCHASE CONSIDERATION OF ASSETS
Or, ISSUE OF SHARES TO VENDORS

Meaning : Shares are not issued only for cash. It can also be issued for a consideration other than cash. There are instances where a company enters into on arrangement with the vendors from whom it has purchased asset on credit. The vendor agrees to accept the payment in the form of fully paid shares of the company issued to them. Normally, no cash is received for such issue of shares. These shares can also be issued either at par, at premium or at discount. Such issue of shares is called as the issue of shares for consideration other than cash.

Calculation of No. of Shares issued to the Vendors : Number of shares to be issued will depend upon the price at which the shares are issued and the amount payable to the vendor. To find out the number of shares to be issued to the vendor will be calculated as follows :

$$\text{No. of shares to be issued to Vendor} = \frac{\text{Payable Amount}}{\text{Per Share Issue Price}}$$

Explanation : Ashok Limited purchased building from Bittu Limited for ₹ 10,80,000 and the payment is to be made by issue of shares of ₹ 100 each. The number of shares to be issued shall be find out as follows in different situations :

(a) *When shares are issued at par i.e., at* ₹ 100 *per share :*

No. of shares to be issued to Bittu Limited

$$= \frac{\text{Payable Amount or Purchase Consideration}}{\text{Per Share Issue Price at Par}}$$

$$= \frac{₹\ 10,80,000}{₹\ 100} = 10,800 \text{ shares}$$

(b) *When shares are issued at a discount of* 10% *i.e.* ₹ 100 – 10% = ₹ 90 *per share :*

No. of shares to be issued to Bittu Limited

$$= \frac{\text{Payable Amount or Purchase Consideration}}{\text{Per Share Issue Price at Discount}}$$

$$= \frac{₹\ 10,80,000}{₹\ 90} = 12,000 \text{ shares}$$

(c) *When shares are issued at premium of* 20% *i.e.* ₹ 100 + 20% = ₹ 120 *per share :*

No. of shares to be issued to Bittu Limited

$$= \frac{\text{Payable Amount or Purchase Consideration}}{\text{Per Share Issue Price at Premium}}$$

$$= \frac{₹\ 10,80,000}{₹\ 120} = 9,000 \text{ shares}$$

Accounting Treatment : Following Journal entries are passed in case of shares issued for consideration other than cash depending upon the situations :

1. For purchase of assets on credit from the vendor	Assets A/c (write individually)	....Dr.
	To Vendor's A/c	
	(Being assets purchased on credit from vendor)	
2. For issue of shares at par to vendor in purchase consideration	Vendor's A/c	....Dr.
	To Share Capital A/c	
	(Being.....shares of ₹ .....each issued at par in purchase consideration to vendor)	

3. For issue of shares at premium to vendor in purchase consideration	Vendor's A/c To Share Capital A/c To Securities Premium Reserve A/c (Being.....shares of ₹ .....each issued at a premium of ₹....each in purchase consideration to vendor)	....Dr.
4. For issue of shares at discount to vendor in purchase consideration	Vendor's A/c Discount on Issue of Shares A/c To Share Capital A/c (Being.....shares of ₹ ...each issued at a discount of ₹ .....each in purchase consideration to vendor)	....Dr. ....Dr.

Presentation in Balance Sheet : Such shares are disclosed separately under the head 'Share Capital' (Sub-head Subscribed Capital) in the 'Equity and Liabilities' side and assets purchased are disclosed under the head 'Fixed Assets' in the balance sheet of a company.

It should be remembered this payment to vendors will be always equal to its purchase price whether shares are issued at par, at premium or at discount. That is why in case of shares issued at premium number of shares will be less as share value will be more. In case of shares issued at discount number of shares will be more as share value is less.

PRO-RATA ALLOTMENT OF SHARES, FORFEITURE AND RE-ISSUE

MEANING OF *PRO-RATA* ALLOTMENT OF SHARES

When a public issue made by a company is over-subscribed, the problem of allotment of shares arises. The company cannot allot all the shares applied by them. In such a case, the company make *pro-rata* allotment to applications. In case of *pro-rata* allotment each class of applicant receives the shares in proportionate to shares applied for. For example, if shares issued are 40,000 and shares applied are 60,000, then the proportion of shares applied to allotment is 60,000 : 40,000 or 6 : 4 or 3 : 2.

In brief, all allotment is said to be pro-rata allotment when the shares are allotted on proportionate basis i.e., smaller number of shares are allotted to each applicant according to the number of shares applied by him. Pro-rata allotment is made only in case of over-subscription.

In case of *pro-rata* allotment of shares, according to SEBI Guidelines, the company has following two alternatives :

(1) *Company may allot shares to all the applicants proportionately* : After SEBI Guidelines all applications should be categorises according to number of shares applied by them and allotment should be made to them in marketable lots on proportionate basis. This means that all the applicants have been allotted or refused allotment on proportionate basis.

Illustration : If a company issues 10,000 shares, receives applications for 17,000 shares and makes *pro-rata* allotment. This will mean that applicants have been allotted shares in the ratio of 17,000 : 10,000 or 1,700 : 1,000 or 170 : 100 of the shares applied. In other words, applicants for 1,700 shares must have been allotted 1,000 shares. For 170 shares, allotment should have been made for 100 shares and for 85 shares, 50 shares would have been allotted.

(2) *Company may accept some applications in full, reject some applications completely and make proportionate allotment to the remaining applications.*

Accounting Treatment : In case of *pro-rata* allotment excess application money received will be transferred to share allotment and calls accounts according to SEBI Guidelines. While receiving allotment and calls money excess application money received on application is adjusted.

On the basis of above explanation, it can be said that *"Allotment of shares on proportionate basis to the applications is called pro-rata allotment." Pro-rata allotment is made only in case of over-subscription, it is not possible in case of under-subscription.*

USES OF *PRO-RATA* RATIO

In this case, always calculate *pro-rata* ratio (*i.e.*, the ratio of total number of shares applied to total number of shares allotted). This *pro-rata* ratio is used to ascertain :

(a) The number of shares allotted to an applicant; if number of shares applied by him is given;

(b) The number of shares applied by an applicant, if number of shares allotted to him is given.

Ascertainment of number of shares allotted to / applied by an applicant :

(a) No. of shares allotted (if not given)

$$= \frac{\text{Shares allotted under } \textit{pro-rata} \text{ ratio}}{\text{Shares applied under pro-rata ratio}} \times \text{No. of shares applied}$$

(b) No. of shares applied (if not given)

$$= \frac{\text{Shares applied under } \textit{pro-rata} \text{ ratio}}{\text{Shares allotted under } \textit{pro-rata} \text{ ratio}} \times \text{No. of shares allotted}$$