PREFERENCE SHARES

DEFINITION

Capital stock which provides a specific dividend that is paid before any dividends are paid to common stockholders, and which takes precedence over common stock in the event of a liquidation. Like common stock, preference shares represent partial ownership in a company, although preferred stock share holders do not enjoy any of the voting rights of common stockholders. Also unlike common stock, preference shares pay a fixed dividend that does not fluctuate, although the company does not have to pay this dividend if it lacks the financial ability to do so. The main benefit to owning preference shares are that the investor has a greater claim on the company's assets than common stockholders. Preferred shareholders always receive their dividends first and, in the event, the company goes bankrupt, preferred shareholders are paid off before common stockholders. In general, there are four different types of preferred stock: cumulative preferred, non-cumulative, participating, and convertible also called preferred stock.

GUIDE LINE OF PREFERENCE SHARE ON THE BASIS OF INDIAN LAW

1. Issue and Redemption of Preference Shares.

After the commencement of the Companies (Amendment) act, 1988, no company limited by shares shall issue any preference share which is irredeemable or is redeemable after expire of a period of ten years from the date of issue. All existing irredeemable preference shares will be compulsory redeemed within five years after the commencement of the Amendment Act, 1988 and preference shares redeemable after twenty years from the date of issue will either be redeemed as per terms of issue or within twenty years from the date of commencement of Amendment Act 1998 whichever is earlier.


A company may issue redeemable preference shares, if it's Articles of Association so authorize. Redeemable preference shares may be issued stipulating a date on which they would be redeemed or in the alternative, they may be made redeemable at the option of the company. The period of redemption, however cannot exceed ten years from the date of issue of such share by virtue of provision of sub section 5(A).

CONDITIONS GOVERNING RDEMPTION OF SHARES:

The redemption can be effected only on the following conditions.

i. Redemption of such shares must be effected on such terms and in such manner as laid down in the Articles of Association of the Company.

ii. Such Shares can be redeemed out of the profits or out of proceeds of a fresh issue of shares made for this purpose.

iii. Such shares must be fully paid-up.

iv. Premium, if any, payable on redemption of such shares, should be provided from out of the profits or out of company's share premium account and

v. An amount equal to redemption amount must be transferred to Capital Redemption Reserve Account. Where the redemption is effected out of profits, otherwise available for the distribution, as dividend such reserve is a Statutory Capital reserve.
**Sub Section 5(A)**

Notwithstanding anything contained in this Act, no Company limited by shares shall after the commencement of the Companies (Amendment) Act, 1996, issue any preference share, which is Irredeemable or Redeemable after the expiry of a period of 20 years from the date of its issue.

**Source:** An outline of the Company Law, Management and procedure, page 98

Section 80 provides that a Company may issue Redeemable preference shares, which means that capital is refundable at an agreed date or at the Company. The Redeemable preference shares have to be separately so shown in the Balance Sheet with terms of redemption.

**Power to exercise:**

If a Company fails to comply with the provisions of the section (6) the Company, every officer of the company who is in default shall be punishable with fine-which may extend to one thousand rupees or more.

**FROM THE VIEW POINT OF INVESTORS**

**Source:** Fundamental of business management, page 266-267

1) On the liquidation, the preference share holders have the preferential right of getting refund of capital

**Business management page 264 Viewpoint of investors**

2) As there is certainty about getting dividend of fixed amount or at a fixed rate, the risk associated with this investment will be less. The investors can invest without any anxiety in this capital.

**Source** An outline of the Company law, Management and Procedure, page 98 (b)

As a respect capital, a Preferential right to be repaid the amount of capital at the time of winding up of the Company or at the repayment of capital (It means that such shareholders shall get the repayment of capital before any other class of shareholders get it, when the question of repayment of capital arises (i.e., in liquidation)

**Redemption** Fundamental of Business Management, Page 267

In specific cases, the preference shares are redeemed after the maturity period is over.

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**Derived from:** Preference Share at a Glance in Context with Commerce Text Book (ICWAI, ICA)

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