EQUITY SHARES

Equity Shares also known as ordinary shares, which means, other than preference shares. Equity shareholders are the real owners of the company. They have a control over the management of the company. Equity shareholders are eligible to get dividend if the company earns profit. Equity share capital cannot be redeemed during the lifetime of the company. The liability of the equity shareholders is the value of unpaid value of shares.

Features of Equity Shares

Equity shares consist of the following important features:

1. Maturity of the shares: Equity shares have permanent nature of capital, which has no maturity period. It cannot be redeemed during the lifetime of the company.

2. Residual claim on income: Equity shareholders have the right to get income left after paying fixed rate of dividend to preference shareholder. The earnings or the income available to the shareholders is equal to the profit after tax minus preference dividend.

3. Residual claims on assets: If the company wound up, the ordinary or equity shareholders have the right to get the claims on assets. These rights are only available to the equity shareholders.

4. Right to control: Equity shareholders are the real owners of the company. Hence, they have power to control the management of the company and they have power to take any decision regarding the business operation.

5. Voting rights: Equity shareholders have voting rights in the meeting of the company with the help of voting right power; they can change or remove any decision of the business concern. Equity shareholders only have voting rights in the company meeting and also they can nominate proxy to participate and vote in the meeting instead of the shareholder.

6. Pre-emptive right: Equity shareholder pre-emptive rights. The pre-emptive right is the legal right of the existing shareholders. It is attested by the company in the first opportunity to purchase additional equity shares in proportion to their current holding capacity.

7. Limited liability: Equity shareholders are having only limited liability to the value of shares they have purchased. If the shareholders are having fully paid up shares, they have no liability. For example: If the shareholder purchased 100 shares with the face value of Tk. 10 each. He paid only Tk. 900. His liability is only Tk. 100.

Total number of shares 100
Face value of shares Tk. 10
Total value of shares 100 × 10 = 1,000
Paid up value of shares 900
Unpaid value/liability 100

Liability of the shareholders is only unpaid value of the share (that is Tk. 100).

Advantages of Equity Shares

Equity shares are the most common and universally used shares to mobilize finance for the company. It consists of the following advantages.

1. Permanent sources of finance: Equity share capital is belonging to long-term permanent nature of sources of finance, hence, it can be used for long-term or fixed capital requirement of the business concern.

2. Voting rights: Equity shareholders are the real owners of the company who have voting rights. This type of advantage is available only to the equity shareholders.

3. No fixed dividend: Equity shares do not create any obligation to pay a fixed rate of dividend. If the company earns profit, equity shareholders are eligible for profit, they are eligible to get dividend otherwise, and they cannot claim any dividend from the company.

4. Less cost of capital: Cost of capital is the major factor, which affects the value of the company. If the company wants to increase the value of the company, they have to use more share capital because, it consists of less cost of capital (Ke) while compared to other sources of finance.

5. Retained earnings: When the company have more share capital, it will be suitable for retained earnings which is the less cost sources of finance while compared to other sources of finance.

Disadvantages of Equity Shares

1. Irredeemable: Equity shares cannot be redeemed during the lifetime of the business concern. It is the most dangerous thing of over capitalization.

2. Obstacles in management: Equity shareholder can put obstacles in management by manipulation and organizing themselves. Because, they have power to contrast any decision which are against the wealth of the shareholders.

3. Leads to speculation: Equity shares dealings in share market lead to secularism during prosperous periods.

4. Limited income to investor: The Investors who desire to invest in safe securities with a fixed income have no attraction for equity shares.

5. No trading on equity: When the company raises capital only with the help of equity, the company cannot take the advantage of trading on equity.

Preference Shares

The parts of corporate securities are called as preference shares. It is the shares, which have preferential right to get dividend and get back the initial investment at the time of winding up of the company. Preference shareholders are eligible to get fixed rate of dividend and they do not have voting rights.

Features of Preference Shares

The following are the important features of the preference shares:

Maturity period: Normally preference shares have no fixed maturity period except in the case of redeemable preference shares. Preference shares can be redeemable only at the time of the company liquidation.

Residual claims on income: Preferential shareholders have a residual claim on income. Fixed rate of dividend is payable to the preference shareholders.

Residual claims on assets: The first preference is given to the preference shareholders at the time of liquidation. If any extra Assets are available that should be distributed to equity shareholder.

Control of Management: Preference shareholder does not have any voting rights. Hence, they cannot have control over the management of the company.

Preference shares may be classified into the following major types:

1. Cumulative preference shares: Cumulative preference shares have right to claim dividends for those years which have no profits. If the company is unable to earn profit in any one or more years, C.P. Shares are unable to get any dividend but they have right to get the comparative dividend for the previous years if the company earned profit.

2. Non-cumulative preference shares: Non-cumulative preference shares have no right to enjoy the above benefits. They are eligible to get only dividend if the company earns profit during the years. Otherwise, they cannot claim any dividend.

3. Redeemable preference shares: When, the preference shares have a fixed maturity period it becomes redeemable preference shares. It can be redeemable during the lifetime of the company. The Company Act has provided certain restrictions on the return of the redeemable preference shares.

4. Irredeemable Preference Shares: Irredeemable preference shares can be redeemed only when the company goes for liquidator. There is no fixed maturity period for such kind of preference shares.

5. Participating Preference Shares: Participating preference shareholders have right to participate extra profits after distributing the equity shareholders.
6. Non-Participating Preference Shares: Non-participating preference shareholders are not having any right to participate extra profits after distributing to the equity shareholders. Fixed rate of dividend is payable to the type of shareholders.

7. Convertible Preference Shares: Convertible preference shareholders have right to convert their holding into equity shares after a specific period. The articles of association must authorize the right of conversion.

8. Non-convertible Preference Shares: There shares, cannot be converted into equity shares from preference shares.

Advantages of Preference Shares

Preference shares have the following important advantages.

1. Fixed dividend: The dividend rate is fixed in the case of preference shares. It is called as fixed income security because it provides a constant rate of income to the investors.

2. Cumulative dividends: Preference shares have another advantage which is called cumulative dividends. If the company does not earn any profit in any previous years, it can be cumulative with future period dividend.
3. Redemption: Preference Shares can be redeemable after a specific period except in the case of irredeemable preference shares. There is a fixed maturity period for repayment of the initial investment.

4. Participation: Participative preference shareholders can participate in the surplus profit after distribution to the equity shareholders.

5. Convertibility: Convertibility preference shares can be converted into equity shares when the articles of association provide such conversion.

Disadvantages of Preference Shares

1. Expensive sources of finance: Preference shares have high expensive source of finance while compared to equity shares.

2. No voting right: Generally preference shareholders do not have any voting rights. Hence they cannot have the control over the management of the company.

3. Fixed dividend only: Preference shares can get only fixed rate of dividend. They may not enjoy more profits of the company.

4. Permanent burden: Cumulative preference shares become a permanent burden so far as the payment of dividend is concerned. Because the company must pay the dividend for the unprofitable periods also.

5. Taxation: In the taxation point of view, preference shares dividend is not a deductible expense while calculating tax. But, interest is a deductible expense. Hence, it has disadvantage on the tax deduction point of view.