

BONUS ISSUE

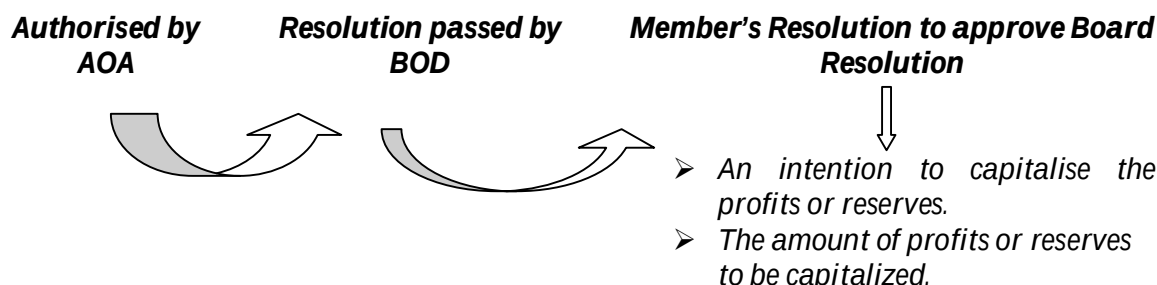
Bonus means Issue of Shares by a Company without any consideration.

Bonus Issue: It is an additional dividend given to the shareholders that can be in cash or in the form of stock. When companies have outstanding performance with surplus profit, they may decide to issue bonus to the shareholders.

Capitalisation of Profits: Process of converting profits or reserves into paid-up capital.

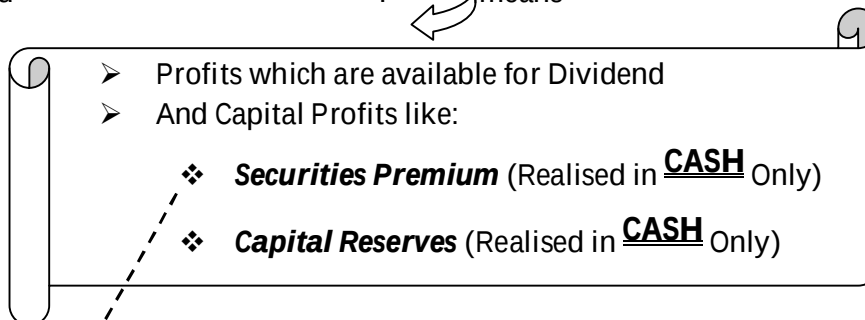
How to Capitalise? Sec. 205(3) of the Companies Act, 1956

1. By paying up amounts unpaid on existing partly paid shares so as to make them fully paid up shares. (Refer P.1 below)
2. By issuing fully paid bonus shares to the existing members. (Refer P.2 below)



SEBI Guidelines:

1. The Company must be **AUTHORISED** by its **(AOA)** Articles of Association. If AOA are not authorised then Resolution shall be passed in General Board Meeting (GBM) to amend the AOA.
2. Bonus Shares are issued to the **FULLY PAID UP Existing Equity Share Holders** only. Partly paid-up Equity Shares can be made fully paid up through Bonus.
3. Bonus must be **ISSUED AT PAR**.
4. Bonus Shares are issued **OUT OF FREE RESERVES**: means



5. Capital Redemption Reserve **(CRR)** shall be **used for FULLY PAID Bonus** Shares only.

6. **STATUTORY RESERVES** shall **not be utilized** for Bonus Issue: - Reserves required by state regulators, and if maintained than used only for specific purpose for which it created. Viz.
- Investment Allowance Reserve
 - Development Rebate Reserve
 - Export Profit Reserve
 - Foreign Project Reserve
7. **REVALUATION RESERVE** shall **not be utilized** for Bonus Issue: - Profit created through Revaluation of Assets Can Not be used to issue the bonus Shares.
8. Bonus Shares Can **NOT BE ISSUED IN LIEU OF DIVIDEND** - The declaration of bonus issue, in lieu of dividend, should not be permitted.
9. **RIGHT OF FCD/PCD HOLDERS**: No company shall pending the conversion of FCDs/PCDs issue any shares by way of bonus unless similar benefit is extended to the holders of FCDs/PCDs, through reservation of shares in proportion to such convertible part of FCDs/PCDs.
The shares so reserved may be issued at the time of conversion of such debentures on the same terms on which the rights or bonus issues were made.
10. A company which **ANNOUNCES** its bonus issue after the approval of the board of directors must implement the proposal within a period of **SIX MONTHS** (6 Months) from the Date of such approval.
11. Consequent upon bonus issue if the **SUBSCRIBED OR PAID UP CAPITAL OF THE COMPANY EXCEEDS THE AUTHORISED CAPITAL**, then a resolution shall be passed by the company at its GBM for increasing its authorised capital to that extent.
12. The company should **NOT BE DEFAULTED** in payment of its **STATUTORY DUES TO THE EMPLOYEES** such as contribution to PF, gratuity, bonus, minimum wages, workmen's compensation, retrenchment, payment to contract labour etc.
13. The company should **NOT HAVE DEFAULTED** in payment of any **INTEREST OR PRINCIPAL** in respect its **fixed deposits** and interest on **debentures** or redemption of debentures.

ACCOUNTING TREATMENT OF BONUS ISSUE**1. To make partly paid Equity Shares Fully Paid up**

Equity Share Final Call A/c	Dr. XXXX	
To Equity Share Capital A/c		XXXX
Bank A/c	Dr. XXXX	
To Equity Share Final Call A/c		XXXX

2. Bonus Announced/Declared

Capital Redemption Reserve A/c	Dr. XXXX	
Capital Reserve/Securities Premium A/c	Dr. XXXX [Cash Only]	
General Reserve/Profit & Loss A/c	Dr. XXXX	
To Bonus to Shareholders		XXXX

Note: Capital Redemption Reserve and Securities Premium cannot be capitalized for converting partly paidup shares into fully paidup.

3. Bonus Paid

Bonus to Shareholders	Dr. XXXX	
To Equity Share Capital A/c		XXXX

CLARIFICATION TO SEBI GUIDELINES

- As per SEBI guidelines, no bonus issue shall be made within 12 months of any ' public/right issue.
- SEBI guidelines are silent on ratio of bonus issue. Therefore, a company can issue bonus shares in any ratio.
- A company issuing bonus shares shall forward a certificate duly signed by the issuer and duly countersigned by its statutory auditor or by a company secretary in practice to the effect that the terms and conditions for issue of bonus shares as laid down in SEBI guidelines, have been complied with.

OTHER POINTS

Bonus paid to the shareholders can be either cash bonus or capital bonus. A company gives cash bonus to its shareholders only when it has larger reserves and sufficient cash to pay bonus. It is also seen that the payment of cash bonus does not affect the working capital of the company. On the other hand, capital bonus is paid when the company wants to share the accumulated reserves with the shareholders but it is not in a position to pay cash bonus because it adversely affects the working capital of the company. Capital bonus is given by making partly paid shares as fully paid without getting cash from the shareholders or it is given by the issue of free fully paid shares known as bonus shares.

Bonus Issue means an offer of free additional shares to existing shareholders. A company may decide to distribute further shares as an alternative to increasing the dividend payout.

Bonus Issue is also known as a "scrip issue" or "capitalization issue".

Circumstances that warrant the Issue of Bonus Shares

1. When a company has accumulated large reserves (whether capital or revenue) and it wants to capitalize these reserves by issuing bonus shares.
2. When the company is not in a position to give cash bonus because it adversely affects its working capital.
3. When the value of fixed assets far exceeds the amount of the capital.
4. When the higher rate of dividend is not advisable for the distribution of the accumulated reserves because shareholders will demand the same rate of dividend in future which the directors may not be able to give. To obviate this difficulty, bonus shares are issued to facilitate the payment of the regular dividend from year to year.
5. When there is a big difference between the market value and paid up value of shares of the company i.e., market value of shares far exceeds the paid up value of shares.

A company issuing bonus shares is better placed in the market. There is a sharp rise in the prices of equity shares following the declaration of bonus issue.

When the companies earn profit in their business, they distribute little profit as cash dividend to its shareholders and retain back larger part of the profit to increase their capital base. The retained profit is used as bonus shares that are issued to the stakeholders. In this way, the company is able to increase their capital-base.

Effects of Bonus Issue

- ☐ Share capital gets increased according to the bonus issue ratio.
- ☐ Liquidity in the stock increases.
- ☐ Effective Earnings per share, Book Value and other per share values stand reduced.
- ☐ Markets take the action usually as a favourable act.
- ☐ Market price gets adjusted on issue of bonus shares.
- ☐ Accumulated profits get reduced.

Purpose of Issuing Bonus Shares

The purpose of a company in issuing bonus shares is to reward or acknowledge the shareholders for being investors in the company. By issuing bonus shares, the company tries to increase the morale of the shareholders. It is a financial reward that the company gives to its shareholders.

Implications of Bonus Shares

- Number of shares for trading increases.
- Management's contribution towards growth of the company and its profits.

Advantages of Issuing Bonus Shares

- Shareholders get their undistributed profits as bonus shares
- Issue of bonus shares keeps the stakeholders happy.
- By issuing bonus shares, the company is able to increase the morale and motivation level of the stakeholders.
- The share capital increases, thus, increasing the security of the creditors.
- By issuing bonus shares, it increases the marketability of the shares

Disadvantages of Issuing Bonus Shares

- Issue of bonus shares declines the rate of dividend in the future.
- The companies encourage speculative dealings in shares by issuing bonus shares.
- Issue of bonus shares is a very lengthy process. It requires the approval of SEBI which might delay in the issue of shares.

Q: What are the Guidelines issued by SEBI for issue of Bonus Shares?

SEBI (i.e., Securities and Exchange Board of India) Guidelines for Issue of Bonus Shares. The company shall, while issuing bonus shares, ensure the following:

- (a) The bonus issue is made out of free reserves built out of the genuine profits or securities premium collected in cash only.
- (b) Reserves created by revaluation of fixed assets are not capitalized.
- (c) The declaration of bonus issue, in lieu of dividend, is not made.
- (d) The bonus issue is not made unless the partly paid shares, if any existing, are made fully paid-up,
- (e) The company has not defaulted in payment of interest or principal in respect of fixed deposits and interest on existing debentures or principal on redemption thereof and has sufficient reason to believe that it has not defaulted in respect of the payment of statutory dues of the employees such as contribution to provident fund, gratuity, bonus etc.
- (f) A company which announces its bonus issue after the approval of the Board of Directors must implement the proposal within a period of six months from the date of such approval and shall not have the option of changing the decision.
- (g) There should be a provision in the Articles of Association of the company for capitalization of reserves, and if not, the company shall pass a resolution at its general body meeting making provisions in the Articles of Association for capitalization.
- (h) Consequent to the issue of bonus shares if the subscribed and paid-up capital exceed the authorized share capital, a resolution shall be passed by the company at its general body meeting for increasing the authorized capital.

(i) The company shall get a resolution passed at its general body meeting for bonus issue and in the said resolution the management's intention regarding the rate of dividend to be declared in the year immediately after the bonus issue should be indicated.

(j) No bonus issue will be made which will dilute the value of rights of the holders of debentures, convertible fully or partly.

(k) No Company shall, pending conversion of fully convertible debentures/partly convertible debentures, issue any shares by way of bonus unless similar benefit is extended to the holders of such fully convertible debentures/partly convertible debentures through reservation of shares in proportion to such convertible part of fully convertible debentures/partly convertible debentures. The shares so reserved may be issued at the time of conversion(s) of such debentures on the same times on which bonus issues were made to shareholders.

Note. Entries for bonus shares reserved for convertible debentures are not to be passed when bonus shares are issued to shareholders. Entries for such reserved shares will be recorded only when these will be issued to convertible debenture holders in the same way as are passed in case of bonus shares issued to shareholders.

Issue of Bonus shares not only increase the capital base of the company, it also increases the morale of the stakeholders which becomes a strong point for the company. The shareholders feel that they are being rewarded and their motivation level increases. But, before the company issues bonus shares, it has to be very careful with the process as it is very complicated.

There are no guidelines for issuing bonus shares by the private companies or unlisted public companies. the listed public companies for issuing bonus shares to the shareholders must comply with the guidelines issued by the SEBI (disclosure and Investor Protection) Guidelines, 2000.

OBJECTIVE TYPE QUESTIONS:

1. Bonus shares can be issued from following :
 - a) General reserves
 - b) Capital Reserve realised in cash
 - c) Securities Premium realised in cash
 - d) All of Above

2. To make partly paid up equity shares as fully paid up the company uses it Revenue Reserves like and Profit and Loss A/c etc.
 - a) General reserves
 - b) Profit & Loss A/c
 - c) Capital Reserves realised in cash
 - d) All of Above

3. Bonus Shares affect the Balance Sheet of the Company?
 - a) Increase Liability and Increase Asset
 - b) Decrease Asset and Decrease Liability
 - c) Decrease Liability and Increase Liability
 - d) Decrease Asset and Increase Asset

Comment: Bonus shares do not affect the balance sheet of the company. They do not have any effect on the assets of the company. It is true that the liability side shows little decrease in reserves but it also increases the capital base of a company.

Q. Which of the following Free Reserves that can be Used for Issue of Bonus Shares? True/False

1. Surplus in Profit and Loss Account (i.e., credit balance of Profit and Loss A/c carried forward).
2. General reserve
3. Dividend equalization reserve.
4. Capital reserve arising from profit on sale of fixed assets received in cash.
5. Balance in debenture redemption reserve after redemption of debentures.
6. Capital Redemption Reserve Account created at the time of redemption of redeemable preference shares out of the profits.
7. Securities Premium collected in cash only.
8. Reserves created by revaluation of fixed assets.
9. If assets are subsequently sold and the profits are realized.

Q. Reserves (i.e., not Free Reserves) not available for Issue of Bonus Shares are: Y/N

1. Capital reserve arising due to revaluation of assets.
2. Securities premium arising on issue of shares on amalgamation or take over.
3. Investment allowance reserve/Development rebate reserve before expiry of 4 years of creation.
4. Balance in debenture redemption reserve account before redemption takes place.
5. Surplus arising from a change in the method of charging depreciation.

Q. Which of the following Reserves are used for Partly Paid-up Bonus Shares? T/F

1. Capital Reserve in Cash.
2. Securities Premium in Cash.
3. Capital Redemption Reserve.
4. Free Reserves etc.
5. Revaluation Reserve.

Questions

P.1 [Bonus by converting partly paid shares into fully paid shares]

Following items appear in the Trial Balance of Tawania Ltd. as at 31st march, 2014.

40,000 Equity Shares of Rs. 10 each, Rs. 7.5 paid up	400,000
Capital Redemption Reserve	30,000
Plant Revaluation Reserve	10,000
Securities Premium Account	35,000
General Reserve	100,000
Profit & Loss Account	50,000
Capital Reserve (including Rs. 25,000 being Profit on Sale of Machinery)	75,000

The company decided to convert the partly paid equity shares into fully paid shares by way of bonus. Pass the Journal entries.

Ans:

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
1.	Equity Share Final Call A/c To Equity Share Capital A/c (Being final call due on 40,000 equity shares @ Rs. 2.50 each to make them fully paid up)	Dr.	100,000	100,000
2.	Capital Reserve A/c General Reserve A/c To Bonus to Shareholders A/c (Being the transfer of Rs. 25,000 from Capital Reserve & Rs. 75,000 from General Reserve to make the partly paid up shares into fully paid up)	Dr. Dr.	25,000 75,000	100,000
3.	Bonus to Shareholders To Equity Share Final Call A/c (Being the amount due on final call adjusted)	Dr.	100,000	100,000

Note: Capital Redemption Reserve, Plant Revaluation Reserve and Securities Premium cannot be capitalised for converting partly paid up shares into fully paid shares. And Capital Reserve realised in cash can be utilised for bonus issue.

P.2 [Bonus by Issue of fully paid shares]

Following items appear in the Trial Balance of Tawania Ltd. as at 31st march, 2014.

40,000 Equity Shares of Rs. 10 each	400,000
Capital Redemption Reserve	30,000
Plant Revaluation Reserve	10,000
Securities Premium Account	35,000
General Reserve	100,000
Profit & Loss Account	50,000
Capital Reserve (including Rs. 25,000 being Profit on Sale of Machinery)	75,000

The company decided to issue bonus shares to its shareholders at the rate of one share for every four shares held. Pass the Journal entries.

Ans:

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
1.	Capital Redemption Reserve A/c	Dr.	30,000	
	Capital Reserve	Dr.	25,000	
	Securities Premium	Dr.	35,000	
	General Reserve A/c	Dr.	10,000	
	To Bonus to Shareholders A/c (Being the bonus declared by issuing one bonus share for every four shares held)			100,000
2.	Bonus to Shareholders	Dr.	100,000	
	To Equity Share Final Call A/c (Being the issue of 10,000 shares of Rs. 10 each by way of bonus)			100,000

Note: Plant Revaluation Reserve cannot be utilised for bonus shares. And Capital Reserve realised in cash can be utilised for bonus issue.

P.3 Following is the extract of the Balance Sheet of Solid Ltd. as at 31st March, 2014.

Authorized capital	Rs.
10,000 12% preference shares of Rs. 10 each	1,00,000
100,000 Equity shares of Rs. 10 each	10,00,000
	11,00,000
Issued and Subscribed capital:	
8,000 12% preference shares of Rs. 10 each fully paid	80,000
90,000 Equity shares of Rs. 10 each, Rs. 8 paid up	7,20,000
Reserves and Surplus:	
General reserve	1,20,000
Capital reserve	75,000
Securities Premium	25,000
Profit and Loss Account	2,00,000
Secured Loan:	
12% Partly Convertible Debentures @ Rs. 100 each	5,00,000

On 1st April, 2014, the Company had made final call @ Rs. 2 each on 90,000 Equity shares. The call money was received by 20th April, 2014. Thereafter the company decided to capitalize its reserves by way of bonus at the rate of one share for every four Shares held. Share premium of Rs. 25,000 includes a premium of Rs. 5,000 for shares issued to vendors pursuant to a scheme of amalgamation. Capital reserves includes Rs. 40,000 being profit on sale of plant and machinery. 20% of 12% debentures are convertible into equity shares of Rs. 10 each fully paid on 1st July, 2014.

Show necessary entries in the company and prepare the extract of the Balance sheet immediately after bonus issue before conversion of debentures. Are the convertible debenture holders entitled to bonus shares?

Ans:

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
2014 Apr-1	Equity Share Final Call A/c To Equity Share Capital A/c (Being final call due on 90,000 equity shares @ Rs. 2 each to make them fully paid up)	Dr.	180,000	180,000

Apr-20	Bank A/c To Equity Share Capital A/c (Being Final Call Money received)	Dr.	180,000	180,000
	Capital Reserve	Dr.	40,000	
	Securities Premium	Dr.	20,000	
	General Reserve A/c	Dr.	120,000	
	Profit & Loss A/c To Bonus to Shareholders A/c (Being the bonus declared by issuing one bonus share for every four shares held by utilizing various reserves)	Dr.	45,000	225,000
Apr-20	Bonus to Shareholders To Equity Share Final Call A/c (Being capitalization of Profit)	Dr.	225,000	225,000

Balance Sheet (Extract) as on 30th April, 2014 (after bonus issue)

	Particulars	Notes	Amount (Rs.)
1	Shareholder's Funds		
a	Share Capital	1	12,05,000
b	Reserves and Surplus	2	195,000
2	Non-Current Liabilities		
a	Long-term Borrowings	3	500,000
	Total		19,00,000

Notes to Accounts**1. Share Capital**

Equity share capital

Authorised share capital

1,25,000 Equity shares of Rs. 10 each 12,50,000

Issued, subscribed and fully paid share capital

1,12,500 Equity shares of Rs. 10 each, fully paid

(Out of above, 22,500 equity shares @ Rs. 10 each were issued by way of bonus)

(A) 11,25,000

Preference share capital

Authorised share capital

10,000 12% Preference shares of Rs. 10 each 1,00,000

Issued, subscribed and fully paid share capital

8,000 12% Preference shares of Rs. 10 each (B) 80,000

Total (A + B) 12,05,000**2. Reserves and Surplus**

Capital Reserves 35,000

Securities Premium Reserves 5,000

Surplus (Profit & Loss Account) 1,55,000

Total 1,95,000

3. Long-term borrowings

Secured

Secured 12% Convertible Debentures @ Rs. 100 each

(Out of above, 1,000 Debentures @ Rs. 100 each to be converted into 10,000 Equity shares @ Rs. 10 each on 1st July, 2014)

5,00,000

Total**500,000****Working Notes**

1. Capital reserve realised in cash can be utilised for issue of fully paid bonus shares.
2. As per SEBI guidelines, securities premium collected in cash can only be utilised for bonus issue.
3. It is assumed that the company will pass necessary resolution at its general body meeting for increasing the authorised capital. In anticipation, the authorised capital has been suitably increased as below:

Existing number of equity shares as authorised	1,00,000*
Add : Issue of bonus shares to equity shareholders	22,500
Add: Number of bonus shares to be issued to debenture holders after conversion	2,500
	1,25,000

*This figure covers the number of shares required for conversion of debentures.

4. As per para (ii) of SEBI guidelines, no company can issue bonus shares to its shareholders without extending similar benefit to convertible debenture holders. Pending such conversion, necessary number of shares should be earmarked for convertible debenture holders. Therefore, convertible debenture holders are also entitled to the bonus shares in the same ratio as the equity shareholders.

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