



Question 5. What is a 'Preference Share'? Describe the different types of preference shares.

Answer: Preference share is one which carries the following two rights

(i) They have a right to receive dividend at a fixed rate before any dividend is paid on the equity shares.

(iii) On the winding up of the company, they have right to return of capital before of the capital returned on equity shares.

However, not with standing the above two conditions, a holder of the preference share may have a right to share fully or to a limited extent in the surplus of the company as specified in the Memorandum or Articles of the Company.

Preference shares can be of various types which are as follows

(i) Cumulative Preference Shares If there are no profits in one year and the arrears of dividends are to be carried forward and paid out of the profits of subsequent years, the preference share is said to be cumulative. It is noted that the company should pay dividend out of profits only.

(ii) Non-Cumulative Preference Shares If unpaid dividend lapses, the share is said to be non-cumulative preference share. It means when a preference shareholder receives dividend only in case of profit and is not entitled any right to recover the arrears of dividend, then the type of preference shares held by the shareholder is known as non-cumulative preference shares.

(iii) Redeemable Preference Shares When shares are repaid after some specified time in accordance with the terms of issue they are called redeemable preference shares.

(iv) Non-Redeemable Preference Shares These are the preference shares, which do not carry with them the arrangement regarding redemption. According to Section 80 (54), no company limited by shares shall issue irredeemable preference shares or preference shares redeemable after the expiry of 20 years from the date of issue.

(v) Participating Preference Shares When a preference shareholder enjoys the right to participate in the surplus profit (in addition to the fixed rate of dividend) that is left after the payment of dividend to the equity shareholders, the type of shares held by the shareholder is known as participating preference shares.

(vi) Non-Participating Preference Shares When a preference shareholder receives only a fixed rate of dividend every year and do not enjoy the additional participation in the surplus profit, then the type of shares held by the shareholder is known as non-participating preference shares.

(vii) Convertible Preference Shares These shares give the right to the holder to get them converted into equity shares at their option according to the terms and conditions of their issue.

(viii) Non-Convertible Preference Shares When the holder of a preference share has not been conferred the right to get his holding converted into equity share, it is called non-convertible preference shares. Preference shares are non-convertible unless otherwise stated.

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