4. Accounting for Limited Companies

limited company = an artificial person that has been created by the law; has many of the rights and obligations that real people have; it is separated by other types of businesses simply because they have no separate legal identity

All companies are created by registration. A limited company may be owned by just one person, but most have more than one owner and some have many owners, which are called ***members*** or ***shareholders***. The ***ownership of a company*** is normally ***divided into a number of shares***, each of ***equal size***. Each owner or shareholder owns one or more shares in the company.

Since a limited company has its own legal identity, it is regarded as being quite separate from those that own and manage it. This has no connection with the business entity convention. This accounting convention applies to all businesses types. The legal separateness of the limited company leads to two important features.

PERPETUAL LIFE – a company is normally granted a ***perpetual existence***; the life of a company is quite separate from the lives of those individuals who own or manage it; it is possible for the shareholders to bring this existence to an end; when this happens, ***assets are sold*** and funds are used to ***pay the outstanding liabilities***; any ***remaining amounts*** are then ***distributed to the shareholders***; a company may be brought to an end because it has achieved its purpose or when it has no future; ***voluntary liquidation*** means that the shareholders agree to end the life of a company

LIMITED LIABILITY – since the company is a legal person in its own right, it must ***take responsibility*** for its own debts and losses; it ***limits the shareholders' losses*** to the amount they have paid for their shares; although it is a benefit to providers of equity finance, it ***allows shareholders to walk away*** from any unpaid debts of the company if the amount they invested is not enough to meet those debts; consequently, this is ***a problem for smaller, less established companies***, as other individuals or businesses may be wary of entering into a contract with a limited company

Safeguards (protect the ones that deal with a limited company)

- a requirement to indicate limited liability status
- restrictions placed on the ability of the owners to withdraw their equity
- a requirement to produce annual financial statements and make them public

public limited company = can offer its shares for sale to the general public; must signal its status to all interested parties by the words 'public limited company' or **'plc'**;