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What is a Share?

By Colin Nicholson

In trying to understand shares as an investment vehicle, it is important to have a clear idea of what we are talking about. In Australia, there are two interchangeable names – shares and stocks. They mean the same thing. Both terms are used in Australia.

When a company is formed, people need to chip in, or subscribe, some capital to operate the company. In return, they are issued with a number of shares in proportion to the amount of capital they have subscribed. This means that they are part-owners of the company in proportion to the number of shares they own. They also share in the dividends paid out of profits, which are usually paid as so many cents per share.

If the company requires more capital in the future, it can sell more shares to existing shareholders, or to new investors, at a higher or lower price to reflect the changing value of the company.

The companies whose shares are traded on stock exchanges are legal entities known generally as limited liability companies. This simply means that the shareholders have a liability for debts of the company only to the extent of the money subscribed for the shares. Sometimes a company will issue shares that are only partly paid. In this case the shareholders can be called upon in future to subscribe the balance of the fully paid value of the shares. Sometimes, for example Telstra, this is effected by issuing securities called instalment receipts. The holders do not actually own the shares until they have paid all future instalments. They may be paid dividends in the meanwhile.

Colin Nicholson writes on share investing each Tuesday in the Market Wrap section of the Australian Financial Review and each month in Smart Investor magazine. He has also written three books *The Aggressive Investor, The Psychology of Investing* and *Hot Stocks.* Contact him at colin@bwts.com.au or through his web site www.bwts.com.au.