7

BUY BACK OF EQUITY SHARE

Unit Structure

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7.0 OBJECTIVES :

After studying this unit the students will be able to

- Know the Concept of Buy-Back of Shares
- Understand the Legal provision for Buy-Back of Shares
- Explain the Limits for Buy-Back of own Shares
- Elaborate the Methods of Buy-Back
- Do the Accounting procedure for Buy-Back

7.1 INTRODUCTION

The term Buy Back of Shares means buying or purchasing by a company of it own Shares / Securities.

U/s 77 of the Companies Act, 1956, a company limited by shares and a company limited guarantee and having a Share Capital cannot buy it own shares unless the consequent reduction

of capital is effected and sanctioned in accordance with provisions of the Act.

The Companies (Amendment) Act 1999 introduced section 77A, 77AA and 77B, now permits to Buy Back its own Shares subject to fulfillment of certain conditions.

7.2 PURPOSES OF BUY-BACK OF OWN SHARES

Buying back of Equity Shares may be carried out, with the following purposes:

i) Higher Earnings per Shares for the remaining shareholders.

ii) Reduction of excess Share Capital

iii) Increase in Intrinsic value of Shares

iv) Utilization of Surplus idle funds lying in the company

v) Increase share holding of promoters.

vi) Financial restructuring of the business.

vii) Maintaining market value of Shares in the situation of slow down in economy.

The Buy-Back of Shares leads to the following benefits to the concerned company :

i) Share Capital Structure can be re-organised suitably.

ii) It reduces capital base and thus return on Equity Capital and Earning Per Share can be increases.

iii) By sub-division of shares and Buy-Back of Shares, company can avoid Corporate Divided Tax as cash resources are used for Buy-Back of Share.

iv) Holding of promoters can be increased.

v) Promoters can keep their control on the company due to buy back as less shares available for sale in the market.

vi) Buy-Back helps family rearrangements, as claims dissatisfied members can be settled.

7.3 BUY-BACK OF SHARES V/S REDEMPTION OF PREFERENCE SHARES

Buy-Back of Shares	Redemption of Preference Shares
a) Any share can be bought back.	a) Only Preference Shares can be redeemed.
b) The Buy-Back must be	b) As per Companies Act all

Authorized by its Articles.	Preference Shares are redeemable.
c) Buy-back date is not known on date of issue of shares.	c) Redemption date is known at the time of issue of Preference Shares.
d) Buy-back is governed by S.77A, 77AA, 77B of the Companies (Amendment) Act 1999, and subject to rules by SEBI.	d) Redemption of Preference Shares is governed by Sec.80 and 80A of the Companies Act, 1956.
e) Buy-back of any kind is not allowed out of fresh issue of shares of the same kind.	e) Redemption of Preference Share is possible by issuing new Preference Shares or by converting Preference Shares into Equity / Preference Shares.
f) Buy-back of Equity Shares can be out of Free Reserves, Securities Premium and / or out of proceeds of earlier issue of Preference Shares / Debentures / Specified Securities.	f) Redemption of Preference Shares can be only out of Free Reserves / Profit and / or out of proceeds of fresh issue of Equity / Preference Shares.
g) Premium payable on Buy-Back depends upon Market price / condition and many other factors.	g) Premium payable on Redemption of Preference Share is fixed and known at the time of issue of Preference Shares.
h) C.R.R. can be created out of Revenue Reserves and / or Securities Premium Account.	h) C.R.R. can be created only out of Divisible Profits.
i) Sec. 77A lays down the limits for Buy-Back of shares.	i) Question of limits by Companies Act does not arise, redemption is as per terms of issue of shares.
j) A declarations of solvency of company required to be file with SEBI and ROC.	j) No such declaration is required.
k) A defaulting company can not Buy-Back Shares.	k) Preference Shares required to be redeem as per terms specified at the time of issue

	of Preference Shares.
l) After Buy-Back, Debt : Equity Ratio should not exceeds 2:1.	l) No such condition of Debt : Equity Ratio.
m) If Buy-Back is less than 10% of total Paid-up Capital then Board Resolution is necessary. However, if it more than 10% special Resolution is mandatory. Maximum buy back permissible in a year is 25% of Paid-up Capital.	m) Only Board Resolution is necessary for Redemption of Preference Share Capital.

7.4 LEGAL PROVISIONS FOR BUY-BACK OF EQUITY SHARES UNDER COMPANIES (AMENDMENTS) ACT 1999

7.4.1 CONDITIONS OF BUY-BACK (U/S 77A)

Section 77A permits Buy-Back of own Shares only if following conditions are fulfilled.

1) The Buy-Back is authorized by the Articles of Association of the Company.

2) A special resolution has been passed in a General Meeting of the shareholders wherein such Buy-Back is authorized. Companies (Amendment) Act 2001 permits Board of Directors to Buy-Back upto 10% of total Equity Capital & Reserves of the company, without special resolution.

3) Only fully Paid-up Shares can be bought back.

4) If shares are listed on any stock exchange, then the guidelines of SEBI have to be complied with.

5) The Board of Directors must file a declaration of solvency with SEBI of Registrar of Companies in Form 4A.

6) After Buy-Back is completed, the company shall have to within 15 days extinguish & physically destroy the Securities / Shares so bought back. Buyback of shares for the purpose of investment is not allowed.

7) A further issue of shares of same kind is not permitted within a period of 6 months. The exception is a) Bonus issue, b) Discharge of obligation such as issue for conversion of securities or warrant, stock option scheme.

8) The company has to maintain Register of securities so bough back mentioning the necessary details in the form 4B.

9) Purchase of its own share, may be in the form of buy-back from existing shareholders on proportionate basis or purchase from open market or purchase of odd lots or acquisition of stock option or Sweat Equity issued to employees. But purchase of its own Shares through as Subsidiary Company or Investment Company is not allowed.

10) Buy-back of shares by a defaulter company is in matter of repayment of Deposit, Term Loans, Debentures or Preference Shares in pending or Interest / Dividend thereon.

11) A company can buyback its shares out of Free Reserves, Securities Premium Account or proceeds of any shares or other specified Security, but of not the same kind of shares.

7.4.2 LIMITS OF BUY-BACK OF OWN SHARES.

As per section 77A Company can buy back its own shares within the following limits.

1) Buy-back should not exceed more than 25% of the Paid-up Equity Capital in any financial year
2) Buy-back should not exceed 25% of the Paid-up Capital, Free Reserves & Securities Premium of the company. This is the upper limit in any financial year for a company to buyback its own shares.
3) Maximum account payable on buyback is 25% of Paid-up Capital & Free Reserves.
4) After buyback is completed, the Debt Equity Ratio should not be more than 2:1. The word debt includes all Secured and Unsecured Loan or Debts except Working Capital Loan (Short Term Loans).

7.4.3 TRANSFER TO CAPITAL REDEMPTION RESERVE (CRR) [Sec.77AA]

Capital Redemption Reserve should be created to the extent of nominal of own shares brought back out of Free Reserves & Securities Premium.

$$CRR = \left(\begin{array}{c}\text{Nominal Value Bought}\\ \text{Back of own shares}\end{array}\right) - \left(\begin{array}{c}\text{Earlier issue of shares or}\\ \text{Other Specified Securities}\end{array}\right)$$

7.5 SOURCES OF BUY-BACK

As per section 77A(1) buyback or purchase of own shares can be done only out of –

1) Its Free Reserves
2) Securities Premium Account
3) Proceeds of any shares or specified securities

7.5.1 FREE RESERVES

The term Free Reserves are those reserves which as per latest audited Balance Sheet are free for distribution as Dividend & includes balance in Securities Premium Account. Free Reserves should be net amount of Free Reserve after adjusting Fictitious Asset and revaluation was of Long Term Investment and Tangible Assets not provide for.

7.5.2 SECURITIES PREMIUM ACCOUNT

The term Security Premium Account represents premium received on account of shares, debenture & other financial instruments. Security Premium Account after making adjusting in respect of Miscellaneous Expenditure (not written off) forms of Free Reserves for the purpose of buyback.

7.5.3 PROCEEDS OF ANY EARLIER ISSUED OF SHARES OR SPECIFIED SECURITIES

It is provided that buy back of own shares can be made from out of the proceeds of an earlier issue of shares or any specified securities. Buy back of shares of any kind is not allowed out of the fresh issue of shares of same kind. Thus for buy back of Equity Shares, earlier issue of Preference Shares, Debentures etc. would be possible.

7.6 MODES OF BUYBACK

There are three important ways of buy-back.

7.6.1 BUYBACK THROUGH TENDER OFFER

A company can buyback its share from the existing shareholders on proportionate basis. A company has to make a public announcement of buy-back in new papers, or it should

contain information as given, it as requires as per SEBI Buy Back Regulations. A company required to complied with SEBI Buy-back Regulations as follows procedure; within time limits.

7.6.2 BUY-BACK THROUGH OPEN MARKET OPERATIONS

After passing special resolution for buy-back, Maximum price to be offered should be specified. Company's appoints merchant banker for buy-back of shares through stock exchange operations.

7.6.3 ACQUISITION OF STOCK OPTION / SWEAT EQUITY

The buy back of own Equity Shares can be done by acquisition of odd lots (only for quoted shares and / or by acquisition of stock option / sweat shares from employees.

7.7 CALCULATION OF MAXIMUM POSSIBLE BUY-BACK OF SHARES / MAXIMUM OFFER PRICE

Limit I 25% of Paid-up Equity Share Capital can be brought back Total Paid Equity Share Capital X 25% = OR If offer price is given then maximum No. of shares available for buy back X offer price = **Which ever is higher**	 X OR X	 X
Limit II Buy back should not exceeds 25% of paid capital + Free Reserves + Security Premium = own funds X 25%		OR X
Limit III After buy back Debt: Equity Ratio should not exceeds 2:1 Own funds before less Buy-Back amount Buy-Back (Equity shares buy back X offer price) Minimum own funds offer buy back $= \frac{\text{Debts}}{2} = \frac{\text{Secured Loans} + \text{Unsecured Loans}}{2}$ = **Whichever is less**	 X OR X	OR X
Maximum buy back amount available, least of I or II or III		**XX**

A. Maximum No. of Equity Shares buy back (When offer price is given)

$$= \frac{\text{Maximum Buy - back amounts avaialble}}{\text{Offer Price}}$$

25% of No. of Equity Shares

B. Calculation of Maximum offer price

$$= \frac{\text{Maximum Buy - Back amounts avaialble}}{\text{Maximum Buy - Back of shares / Shares to be brought back}}$$

7.8 ACCOUNTING PROCEDURES

The accounting entries for buy back of own shares are similar to the entries for redemption of preference shares.

1)	<u>For issue of Debentures</u> Bank Account …… Dr. To Debentures Account To Securities Premium Account (Being _____Debentures of Rs._____ each issued as per B.O.D. Resolution No.____ dated _____)	XX	 XX XX
2)	<u>For decision of buy back of shares</u> a) At Par (Face Value) Equity Share Capital Account (NV) ……Dr. To Equity Share holders Account (NV) b) At Premium Equity Share Capital Account (NV) ……...Dr. Premium on buy back of share Account (Premium)..Dr. To Equity Shareholders Account (Total Amt. Payable) c) At Discount Equity Share Capital Account (NV).....……...Dr. To Equity Shareholders Account (Amount Payable) To Capital Reserve Account (Discount on buyback) (Being entry for buyback of equity shares at par / premium / discount as case may be.)	 XX XX XX XX	 XX XX XX
3)	<u>For creating Capital Redemption Reserve</u> Securities Premium Account ……...Dr. General Reserve / Profit & Loss Account …. Dr. To Capital Redemption Reserve Account (Being C.R.R. is created to the extent buy-back out of devisable profit / security premium) $CRR = \left(\begin{matrix}\text{Nominal Value of}\\ \text{Share Bought Back}\end{matrix}\right) - \left(\begin{matrix}\text{The proceeds of}\\ \text{fresh issue}\end{matrix}\right)$	XX XX	 XX
4)	<u>For Adjusting premium on buyback</u> Security Premium Account (As per Latest Audited B/s)…Dr. Profit & Loss Account / Revenue Reserves Account (As per Latest Audited B/s) ……Dr. To Premium on buy back of shares Account	XX XX	 XX

	(Being premium on buy back adjusted)		

5)	<u>For payment to equity share holders</u> Equity Share holders Account …….. Dr To Bank Account (Being amount due on buy back of share paid)	XX	XX
6)	<u>For buy back expenses paid OR payable</u> Expenses for buy back of shares Account …… Dr. To Cash / Bank / Creditors for Expenses Account (Being buy back expenses paid / payable.)	XX	XX
7)	<u>For writing off buy back expenses</u> Profit & Loss Account …… Dr To Expense for buy back of shares Account (Being buy back expense written off.)	XX	XX

Note : Some companies treat buy back expenses as deferred revenue expenditure and written off over 3 to 5 years.

8) For any other transaction given, in the problem, usual accounting entry should be passed.

Check Your Progress

- Explain the benefits of Buy Back of Own Shares
- Which are the conditions of Buy Back as per sec. 77A?
- How to calculate the maximum possible Buy Back of Shares?

7.9 ILLUSTRATION :

Illustration 1 : (Various Alternative / option for buy-back)
The undernoted balances were extracted from Balance Sheet of Zee Ltd.

Particulars	Rs.
20,000 Equity Shares of Rs.10 each	2,00,000
Free Reserve	1,50,000
Securities Premium Account	1,00,000
10% Debentures	1,00,000

The directors of Zee Ltd. have decided to buy back Equity Shares. Conditions as per the Companies Act have been complied with. Ascertain the possible buy back of shares of Equity Shares.

(a) Buy back maximum Equity Shares at par.

(b) Buy back 4000 Equity Shares at best possible price.

(c) Buy back maximum Equity Shares at Rs.40/- per share.

(d) Buy back maximum Equity Shares @ 10% Discount.

(e) Maximum no. of Equity Share at Best possible price.

Solution :

Section 77A of Companies Act lays down the following limits of Buy-back of shares.

I) A buy back of share cannot be more than 25% of the paid up Equity Share Capital.

II) The Buy back (Buy-back Amount) does not exceed 25% of the Paid up Capital plus Free Reserves plus Security Premium of the company.

III) After Buy back Debt : Equity Ration should not exceed 2:1.

The applicabilities of the above limits have to be consider in various alternative in the problem.

a) <u>Buy back maximum no. of Equity Share at par.</u>

I) 25% of paid up Equity Capital
= 20,000 X 25% = 5000 Equity Shares at par

II) Buy back cannot exceeds 25% of Paid up Capital + Free Reserves.

Paid up Equity Share Capital	2,00,000
+ Free Reserves	1,50,000
+ Securities Premium	1,00,000
Total	4,50,000

Buy back = 4,50,000 X 25% = 11,250

Maximum no. of Equity Share = $\frac{1,12,500}{10}$ = 11,250

Therefore 11,250 Equity Share can be brought back. However it is limited to 5,000 shares as per Limit I.

III) Debt : Equity ratio after buy back should not exceeds 2:1

$$= \frac{\text{Debt}}{\text{Equity after buy back}}$$

$$= \frac{1,00,000\ (\text{Debentures})}{4,50,000 - \text{Buy back (as per I above)}}$$

$$= \frac{1,00,000}{4,50,000 - 50,000} = \frac{1,00,000}{4,00,000} = 0.25$$

Therefore company can buy back maximum 5,000 Equity Shares at par.

b) Buy back 4,000 Equity Shares at Best possible price

I) Buy back can not exceeds 25% of paid up Equity Share Capital.
= 20,000 X 25% = 5,000 Equity Share
$\therefore$ Buying back 4,000 Equity Shares within limit.

II) Buy back Amount = 4,50,000 X 25%
= 1,12,500

$$\therefore \text{ Buy back price} = \frac{\text{Amt. available for buy back}}{\text{No.of Equity Shares to be bought back}}$$

$$= \frac{1,12,500}{4,000} = \text{Rs.28.12}$$

$\therefore$ 4,000 Equity shares can be brought back at Rs.28.12 per share. (at 18.12 premium)

III) Debt Equity Ratio after buy back

$$= \frac{\text{Debt}}{\text{Equity after buy back}} = \frac{1,00,000}{4,50,000 - 1,12,500}$$

$$= \frac{1,00,000}{3,37,500} = 0.30:1$$

Therefore company can buy back 4,000 Equity Shares @ Rs.28.12.

c) Buy back maximum no. of Equity Share @Rs.40/- per share.

I) Maximum no. of share can be brought back
Maximum = 20,000 X 25% = 5,000 shares

II) Buy back amount = 4,50,000 X 25% = Rs.1,12,500/-
Maximum no. of Equity Shares @ Rs.40/- per shares

$$= \frac{1,12,500}{40} = 2812.50$$

Therefore company can buy back 2,812 Equity Shares.

III) Debt : Equity ratio should not exceed 2:1 – It not exceeding 2:1
Therefore, company can buy back 2,812 equity shares at Rs.40/- per share.

d) Buy back maximum Equity share @ Rs.9/- per share

I) As per above I = 5,000 share

II) Maximum amount of Buy back = 4,50,000 X 25% = Rs.1,12,500/-

Buy back of share possible @ Rs.9/- = $\frac{1,12,500}{9} = 12,500$

However as per I limits it can not exceed 5,000 shares.

$\therefore$ The company can buy back 5,000 Equity Shares at Rs.9/- per share as per limits.

e) Buy back of Maximum no. of Equity Shares at Best possible price

I) Maximum No. of share = 20,000 X 25% = 5,000 shares

II) Maximum amount available = 4,50,000 X 25% = 1,12,500

$\therefore$ Maximum price = $\frac{1,12,500}{5,000}$ = Rs.22.50

III) Debt : Equity Ratio is less than 2:1 (as seen above)
Therefore Company can buy back 5,000 Equity Shares at Rs.22.50 per share.

Illustration 2 (Various option as per Limit u/s 77A)

Balance Sheet of Neena Ltd. as on ……

Liabilities	Rs.	Assets	Rs.
I. Share Capital		I. Fixed Assets	7,55,000
Authorized	?		
Paid up		II. Investment	1,00,000
20,000 10% Pref. shares of Rs.10/- each fully paid up.	2,00,000	III. Current Assets & Loans and Advances	
4,000 Equity shares of Rs.50/- each fully paid up.	2,00,000	a) Current Assets	
		Stock	50,000
		S. Debtor	1,20,000
II. Reserve & Surplus		Bank Bal	40,000
Security Premium	40,000		
General Reserve	1,50,000		
Profit & Loss A/c	2,00,000		
III. Secured Loans			
12% Debentures	1,00,000		
IV. Unsecured Loans			
Bank Loans	1,00,000		
V. Current Liabilities and Provisions	75,000		
	10,65,000		10,65,000

Ascertain the number of equity shares that can be bought back if –

(A) The buy back of maximum no. of shares at par.

(B) The buy back of maximum no. of shares at premium of Rs.25/-.

(C) The buy back of 800 Equity shares at Best possible price.

(D) The buy back of maximum no. of Equity share at Best Possible Price.

Consider above option separately individually.

Solution :

Option A : Buy back of maximum shares at par

i) Maximum No. of Equity share
= 4,000 X 25% = 1,000 Equity shares at par

ii) Total amount of buy back = 1,000 X 50
= Rs.50,000/-

Buy back amount should not exceed 25% of Paid-up Capital & Free Reserves.

Equity Share Capital	2,00,000	
Preference Share Capital	2,00,000	4,00,000
Add : Free Reserves		
General Reserve	1,50,000	
Profit & Loss Account	2,00,000	3,50,000
Security Premium		40,000
	Total	7,90,000

Maximum buy back amount = 7,90,000 X 25%
= 1,97,500

Total amount of buy back Rs.50,000/- is less than maximum amount calculated above.

iii) Debt : Equity ratio after buy back should not exceed 2:1.

Debt = Secured Loans + Unsecured Loans
= 1,00,000 + 1,00,000
= 2,00,000

Equity after buy back = 7,90,000 – 50,000
= 7,40,000

$$\therefore \text{Debt : Equity Ratio} = \frac{\text{Debt}}{\text{Equity after buy back}}$$

$$= \frac{2,00,000}{7,40,000}$$

$$= 0.27$$

Which is less than 2:1.

Conclusion: As per option A, company can buy back 1,000 Equity Shares at par.

Option B: The buy back of maximum shares at premium of Rs.25/-

(Buy back price = FV + Premium on buy back = 50 + 25 = Rs.75/-)

i) Maximum no. of shares = 1,000 shares

ii) Total amount of buy back = 1,000 X 75
= Rs.75,000/-

Buy back amount of Rs.75,000/- does not exceeds 25% of Paid-up Capital plus Free Reserves. (Rs.1,97,500/- as per option A)

iii) Debt : Equity Ratio after buy back $= \frac{2,00,000}{7,90,000 - 75,000}$

$$= \frac{2,00,000}{7,15,000}$$

$$= 0.28:1$$

Conclusion: The company can buy back 1,000 Equity shares at Rs.75/-

Option C: The buy back of 800 Equity shares at best possible price.

i) Maximum no. of share = 1,000 Equity shares
Buy back of 800 Equity shares are within limit.

ii) Maximum buy back = 7,90,000 X 25%
= Rs.1,97,500/-

$$\therefore \text{Best possible buy back price}$$

$$= \frac{\text{Maximum amount available}}{\text{No. of Equity shares for buy back}}$$

$$= \frac{1,97,500}{800}$$

$$= \text{Rs.246.87/-}$$

iii) Debt : Equity Ratio $= \frac{\text{Debt}}{\text{Equity after buy back}}$

$= \frac{2,00,000}{7,90,000 - 1,97,500}$

$= \frac{2,00,000}{5,92,500}$

= 0.34:1

Which is less than 2:1.

Conclusion : The company can buy back 800 Equity shares at Rs. 246.87/-.

Option D:

i) Maximum no. of Equity shares buy back = 1,000 shares

ii) Maximum buy back amount = Rs.1,97,500/-

$\therefore$ Best possible buy back price $= \frac{1,97,500}{1,000}$

= Rs.197.50/-

iii) Debt : Equity Ratio = 0.34:1 (As option C)

Conclusion: The company can buy back 1,000 Equity Shares @ Rs.197.50/-.

Illustration 3: (Buy back at par, out of fresh issue of Preference shares)

Bharat Ltd. decides to buy back 50,000 Equity Shares of Rs.10/- each; for this purpose the company issues 10% Preference Shares of RS.100/- each of the equivalent amount. Assume that the buy back is carried out actually on the legally permissible terms, each Journal entries.

Solution :

Journal in the books of Bharat Ltd.

No.	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
1.	Bank A/c …….. Dr. To 10% Pref. Share Cap. A/c (Being 5,000 Preference Shares of Rs.100/- each issued at par.)		5,00,000	 5,00,000

2.	Equity Share Cap. A/c …….. Dr. To Equity Shareholder's A/c (Being amount payable on buy back.)		5,00,000	 5,00,000
3.	Equity Shareholder's A/c …… Dr. To Bank A/c (Being buy back amount paid to Equity shareholders.)		5,00,000	 5,00,000

Note: CRR is not to be created as buy back is out of proceeds of fresh issue of Preference Shares.

Illustration: 4 (Buy back at premium, out of Divisible profits.)

Z Ltd. decided to buy back 20,000 Equity Shares of Rs.10/-each @ Rs.5/- premium per share. Assume that there is sufficient balance in Securities Premium and Profit and Loss account. Pass journal entries.

Solution :

Journal entries in the books of Z Ltd.

No.	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
1.	Equity Share Capital A/c.....…Dr. Premium on buyback of shares A/c ……..…. Dr. To Equity shareholders A/c (Being amount payable on buy back of 20,000 Equity Shares @ Rs.15/- per share)		2,00,000 1,00,000	 3,00,000
2.	Securities Premium A/c ……. Dr. To Premium on buy back of shares A/c (Being premium on buy back adjusted.)		1,00,000	 1,00,000

3.	Profit & Loss A/c ……..Dr. To Capital Redemption Reserve A/c (Being CRR created to the extent buy back out of Profit)		2,00,000	 2,00,000
4.	Equity share holders A/c …....Dr. To Bank A/c (Being buy back amount paid to Equity shareholders.)		3,00,000	 3,00,000

Illustration: 5 (Buy back at Discount and Issue of 12% Preference shares)

K.T. Ltd. bought back 6,000 Equity shares of Rs.20/- each at Rs.19/- per share. The company had issued 10,000 12% Preference Shares of Rs.10/- each at par, for the purpose of buy back.
Pass Journal entries.

Journal entries in the books of K.T. Ltd.

No.	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
1.	Bank A/c …… Dr. To 12% Pref. share Cap. A/c (Being 10,000 Equity shares of Rs.10/- each issued at par.)		1,00,000	 1,00,000
2.	Equity Share Capital A/c …... Dr. To Equity shareholder's A/c To Capital Reserve A/c (Being 6,000 Equity shares of Rs.20/- each brought back @ Rs.19/- per shares.)		1,20,000	 1,14,000 6,000
3.	Profit & Loss A/c …….. Dr. To Capital Redemption Reserve A/c (Being CRR created to the extent buy back of profit)		20,000	 20,000

4.	Equity Shareholder's A/c …… Dr. To Bank A/c (Being payment on buy back)		1,14,000	 1,14,000

Illustration: 6 (Buy back of shares out of divisible profits.)

A company buy back 25,000 Equity shares of Rs.10/- each at Rs.40/- per share. The reserves of the company are as follows :
The company are as follows :

Security Premium	Rs.20,00,000/-
General Reserve	Rs.30,00,000/-
Profit & Loss A/c	Rs.2,00,000/-

The company sold investment for Rs.16,50,000/- at 10% profit.
Pass the necessary entries in the books of the company for the above.

Solution :

Journal entries in the books of company

No.	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
1.	Bank A/c …… Dr. To Investment A/c To Profit & Loss A/c (Being investment sold at 10% profit) $\left[\text{Cost} = 16,50,000 \times \frac{100}{110}\right]$		16,50,000	 15,00,000 1,50,000
2.	Equity Share Cap. A/c …… Dr. Premium on buy back of share A/c …… Dr. To Equity shareholder's A/c (Being buy back of 25,000 Equity shares of Rs.10/- each at Rs.40/- per shares)		2,50,000 7,50,000	 10,00,000
3.	General Reserve A/c …….. Dr. To Capital Redemption Reserve A/c (Being nominal value of shares brought back transfer of CRR)		2,50,000	 2,50,000

4.	Securities Premium A/c …..… Dr. To premium on buy back of shares A/c (Being premium on buy back adjusted)		7,50,000	7,50,000
5.	Equity Shareholder's A/c …….Dr. To Bank A/c (Being amount paid on buy back of shares)		10,00,000	10,00,000

Illustration: 7 (Maximum buy back of given price)

The Balance Sheet of Ketan Ltd. as on 31st March 2009 is as follows.

Liabilities	Rs.	Assets	Rs.
Equity shares of Rs.10/- each	6,00,000	Fixed Assets	20,90,000
10% Preference Shares of Rs.100/- each	1,50,000	Investments	6,00,000
Securities Premium	1,20,000	Current Assets (including Bank balance Rs.1,25,000/-)	8,10,000
General Reserve	2,00,000		
Profit & Loss A/c	1,80,000		
10% Debentures	10,00,000		
Term Loan from Dena Bank	8,00,000		
Current Liabilities	4,50,000		
	35,00,000		**35,00,000**

Keeping in view all the legal requirements, ascertain the maximum no. of Equity shares that Ketan Ltd. can buy back @ Rs.50/- per shares. Assume that the buy back is actually carried out. Investment costing Rs.3,00,000/- sold for Rs.3,20,000/-.

Pass Journal entries and prepare Balance sheet after buy back.

Solution :

Ascertain maximum no. of shares to be bought back.	**Rs.**
A) Maximum 25% of Paid-up Equity Share Capital can be bought back. Rs.6,00,000 X 25% = Rs.1,50,000/- = 15,000 Equity Shares ∴ Buy back = 15,000 shares X 50 = 7,50,000	7,50,000
OR	
B) Buy back amount can not exceeds 25% Paid-up Capital plus Free Reserve Paid-up Capital (Equity + Preference) 7,50,000 Free Reserves : General Reserve 2,00,000 Profit & Loss A/c 1,80,000 Securities Premium 1,20,000 Total own funds 12,50,000 ∴ Maximum amount of buy back = 12,50,000 X 25% = 3,12,500	3,12,500
OR	
C) After buy back Debt : Equity ratio should not exceed 2:1 ∴ Minimum own funds required after buy back $= \frac{\text{Debt}}{2}$ $= \frac{\text{Debentures} + \text{Bank Term Loan}}{2}$ $= \frac{10,00,000 + 8,00,000}{2}$ = 9,00,000 ∴ Own funds before buy back – Minimum own funds required. = 12,50,000 – 9,00,000	3,50,000
∴ Buy back amount can not exceed, minimum of A OR B OR C	3,12,500

∴ No. of Equity Shares brought back @ Rs.50/- per share.

$= \frac{312500}{50} = 6250$ Equity shares of Rs.10/- each @ Rs.50/- per share.

Journal entries in the books of Ketan Ltd.

No.	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
1.	Bank A/c …….…….. Dr.		3,20,000	
	To Investment A/c			3,00,000
	To Profit and Loss A/c			20,000
	(Being investment sold at profit)			
2.	Equity Share Capital A/c …… Dr.		62,500	
	Premium on buy back of shares A/c ……..…. Dr.		2,50,000	
	To Equity Shareholders A/c			3,12,500
	(Being 6,250 Equity shares of Rs.10/- each to be bought back @ Rs.50/- per shares.)			
3.	Securities Premium A/c …….. Dr.		1,20,000	
	Profit & Loss A/c …….. Dr.		1,30,000	
	To Premium on buy back of shares A/c			2,50,000
	(Being premium payable on buy back adjusted)			
4.	General Reserve A/c …….. Dr.		62,500	
	To Capital Redemption Reserve A/c			62,500
	(Being CRR created to the extent of N.V. of Equity Shares bought back out of divisible profit.)			
5.	Equity shareholders A/c ……..Dr.		3,12,500	
	To Bank A/c			3,12,500
	(Being buy back amount paid to Equity Shareholder's)			

Ketan Ltd.

Balance Sheet (After buy back) as on ……

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
I. Share Capital			I. Fixed Assets		20,90,000
Authorized		?			
			II. Investments		3,00,000
Paid up 1500, 10% Pref. shares of Rs.100/- each fully paid up		1,50,000	III. Current Assets		
			Other Current Assets		6,85,000
53,750 Equity shares of Rs.10/- each fully paid			Bank Balance		
(After buy back & 6250 shares)		5,37,500	Op. Bal.	1,25,000	
			(+) Sale of Invt.	3,20,000	
			(–) Paid for buy back	(3,12,500)	1,32,500
II. Reserves & Surplus					
Capital Redemption Reserve		62,500			
Securities premium (1,20,000 – 1,20,000)		NIL			
General Reserve (2,00,000 – 62,500)		1,37,500			
Profit & loss A/c (1,80,000 + 20,000 – 1,30,000)		70,000			
III. Secured Loan					
10% Debentures		10,00,000			
Term Loan from Dena Bank		8,00,000			
IV. Unsecured Loans		NIL			
V. Current Liabilities		4,50,000			
		32,07,500			**32,07,500**

Illustration : 8 (Maximum buy back at best possible price)

Balance sheet of YES Ltd. as on 31st March 09

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
I. Share Capital			I. Fixed Assets		
Authorized		?	Cost	110,25,000	
			Less : Depn prov.	20,50,000	
Paid up 12% Preference			Net Block		89,75,000
Shares of Rs.5/- each		10,00,000	II. Investment		15,00,000
Equity shares of Rs.2/- each fully paid		20,00,000	III. Current Assets, Loans & Advances		
			a) Current Assets (including Bank bal. Rs.30,000/-)		65,00,000
II. Reserves and Surplus					
Securities Premium		6,00,000	b) Loans & Advances		1,25,000
Capital Reserves		1,00,000			
General Reserves		11,00,000			
Profit & Loss A/c		3,00,000			
III. Secured Loans					
9% Debentures		40,00,000			
IV. Unsecured Loans					
Fixed Deposits		50,00,000			
V. Current Liabilities		25,00,000			
Provision for Taxation		5,00,000			
		171,00,000			171,00,000

1) Fixed Asset costing Rs.20,00,000/- W.D.V. Rs.18,20,000/- sold for Rs.19,00,000/-
2) Investment costing Rs.10,00,000/- sold for Rs.12,50,000/-.
3) 10% Preference shares of Rs.5/- each issued at par, for purposed of buy back of security shares.
4) The company wish to buy back the maximum number of equity shares at maximum price as may be possible. Legal requirements have been complied by the company.

You are required to determine the –

i) Maximum shares can be brought back at best possible price.
ii) Pass journal entries for above transaction (Narration not required)
iii) Balance sheet after buy back.

Solution :

I. Limits of buy back u/s 77A, are with reference to latest audited balance sheet.

A) Buy back can not exceeds 25% of paid Equity share capital 20,00,000 X 25% = Rs.5,00,000/-

Equity shares can be brought back

$= \frac{5,00,000}{2}$

= 2,50,000 Equity Shares

Maximum 2,50,000 Equity shares can be brought back.

B) Buy back amount can not exceeds 25% of paid up share capital plus free Reserves.

Paid up Equity Share Capital	20,00,000	
Paid up Preference Share Capital	10,00,000	30,00,000
Add : Free Reserves		
Securities Premium	6,00,000	
General Reserve	11,00,000	
Profit & Loss Account	3,00,000	20,00,000
Own funds for buy back		50,00,000

Buy back amount = 50,00,000 X 25% = Rs.12,50,000/-

C) After buy back Debt : Equity ratio should not exceeds 2:1.

Debt = Secured Loans + Unsecured Loans
= 40,00,000 + 50,00,000 = 90,00,000

Minimum own funds after buy back

$= \frac{9,00,000}{2}$ = Rs.45,00,000/-

Paid up share capital	30,00,000
Add : Preference share issued	2,00,000
Free Reserves	20,00,000
Add : Capital Reserve	1,00,000
Own funds buy back	53,00,000
Post buy back Equity required	45,00,000

Hence buy back 8,00,000

Equity after buy back = 53,00,000 – 8,00,000 = 45,00,000

Therefore, buy back amount cannot exceed.
Lowest of B and C = Rs.8,00,000/-

Best possible price for buy back

$$= \frac{\text{Amt. available for buy back}}{\text{Maximum no. of Equity Shares for buy back}}$$

$$= \frac{8,00,000}{2,50,000}$$

= Rs.3.20

Conclusion : Company can buy back 2,50,000 Equity share for Rs.2/- each. @ Rs. 3.20 per share.

Journal entries in the books of YES Ltd.

No.	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
1.	Bank A/c ……Dr. Provision for Depreciation A/c..Dr. To Fixed Assets A/c To Profit & Loss A/c		19,00,000 1,80,000	 20,00,000 80,000
2.	Bank A/c …… Dr. To Investment A/c To Profit & Loss A/c		12,50,000	 10,00,000 2,50,000
3.	Bank A/c ……Dr. To 10% Preference Shares Capital A/c		2,00,000	 2,00,000
4.	Equity Share Capital A/c …… Dr. Premium on buy back of shares A/c …… Dr. To Equity shareholders A/c		5,00,000 3,00,000	 8,00,000
5.	Security Premium A/c …… Dr. To Premium on buy back of shares A/c		3,00,000	 3,00,000
6.	General Reserve A/c ……. Dr. To Capital Redemption Reserve A/c		5,00,000	 5,00,000
7.	Equity shareholders A/c …… Dr. To Bank A/c		8,00,000	 8,00,000

Bank A/c

Particulars	Rs.	Particulars	Rs.
To Balance b/d	30,000	By Equity shareholders A/c	8,00,000
To Fixed Assets A/c	19,00,000		
To Investment A/c	12,50,000	By Balance c/d	25,80,000
To 10% Preference Share Capital A/c	2,00,000		
	33,80,000		**33,80,000**

YES Ltd.

Balance sheet as on …… (After buy back)

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
I. Share Capital			I. Fixed Assets		
Authorized		?	Op.Cost		
			Less : cost of FA	10,25,000	
Issued Paid up				20,00,000	
12,00,000, 12% Pref.Shares of Rs.5/- each fully paid		10,00,000	Less : Dep. provision	90,25,000	
			(20,50,000 – 1,80,000)	18,70,000	71,55,000
40,000, 10% Preference shares of Rs.5/- each fully paid		2,00,000	II.Investment		5,00,000
7,50,000 Equity shares of Rs.2/- each fully paid		15,00,000	III. Current Assets, Loans & Advances		
			a) Current Assets		
			Other Current Assets		
II. Reserves and Surplus			Bank bal.	64,70,000	
Securities Premium	6,00,000		b) Loans & Advances	25,80,000	90,50,000
(–) Used for buy back premium	3,00,000	3,00,000			1,25,000
Capital Reserves		1,00,000			
Capital Redemption Reserves		5,00,000			
General Reserve	11,00,000				
(–) used for CRR	5,00,000	6,00,000			
Profit & Loss A/c	3,00,000				

Profit on sale of fixed assets	80,000				
Profit on sale of investment	2,50,000	6,30,000			
Used for					
III. Secured Loans					
9% Debentures		40,00,000			
IV. Unsecured Loans					
Fixed Deposits		50,00,000			
V. Current Liabilities of provisions					
Current liabilities		25,00,000			
Provision for Taxation		5,00,000			
Total Rs.		168,30,000			168,30,000

Illustration : 9 (Maximum buy back at offer price)

The undernoted balances were extracted from the ledger of Delta Ltd.

1,00,000, 9% Preference shares of Rs.10/- each fully paid	10,00,000
4,00,000 Equity shares of Rs.10/- each, Rs.8/- paid up	32,00,000
Reserves Surplus	
Security Premium	8,00,000
General Reserves	12,00,000
Investment Allowance Reserves	4,00,000
Secured & Unsecured Loans	NIL

The company make final call on Equity shares amount of final call duly received.

The company decided to buy back maximum Equity shares as may be permitted by law at a price of Rs.80/- per share.

You are required to find number of Equity shares to be brought back and also pass necessary journal entries. (Narration not required)

Solution :

Share final should be made on only fully paid equity shares can be brought Back. Limits of buy back as per sec.77A of Companies Act (After final call, assuming amount received)

i) Buy back can not exceed 25% of paid up Equity Share Capital.

$\therefore$ 40,00,000 X 25% = Rs.10,00,000 i.e. 1,00,000 shares

$\therefore$ 1,00,000 Equity shares can be brought back

Amount of buy back = 1,00,000 X 80 = 80,00,000

OR

ii) Buy back can not exceeds 25% of paid up capital plus fees reserve

Paid up capital (Preference + Equity)	50,00,000
Add : Reserves	
General Reserve	12,00,000
Security Premium	8,00,000
Own funds for buy back	70,00,000

Buy back amount = 70,00,000 X 25% = 17,50,000

$\therefore$ Buy back amount least of above i.e. Rs.17,50,000/-

$\therefore$ No. of Equity shares brought back

$$= \frac{\text{Maximum amount of buy back}}{\text{offer price}}$$

$$= \frac{17,50,000}{80}$$

= 21,875 Equity shares of Rs.10 @ Rs.80/-

Journal of Delta Ltd.

No.	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
1.	Share Final Call A/c ……... Dr. To Equity Share Capital A/c		8,00,000	 8,00,000
2.	Bank A/c …… Dr. To Share Final Call A/c		8,00,000	 8,00,000
3.	Equity Share Capital A/c ……. Dr. Premium on buy back of shares A/c ……Dr. To Equity Share Capital A/c		2,18,750 15,31,250	 17,50,000
4.	Security Premium A/c …….. Dr. General Reserve A/c ……Dr. To Premium on buy back of shares. A/c		8,00,000 7,31,250	 15,31,250

5.	General Reserve A/c …….. Dr. To Capital Redemption Reserve A/c		2,18,750	 2,18,750
6.	Equity Shareholders A/c ……. Dr. To Bank A/c		17,50,000	 17,50,000

Illustration: 10 (Redemption of Pref. shares, buy of equity shares, sale of investments)

Balance sheet of C Ltd. as at 31st March 08

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
I. Share Capital			I. Fixed Assets		
Authorized		?	Gross Block	92,10,000	
			Less : Depn	(25,65,000)	66,45,000
Issued, Paid up					
1,00,000, 10% Pref. Shares of Rs.100/- each	100,00,000		II. Investment		55,00,000
Less : Calls in arrears (Rs.20/- per shares)	(20,000)	99,80,000	III. Current Assets, Loans & Advances		
			Current Assets (including Bank Balance Rs.45,00,000/-)		265,00,000
5,00,000 Equity shares of Rs.10 each fully paid up		50,00,000	Loans & Advances		5,00,000
II. Reserves & Surplus					
Capital Reserve		2,00,000			
Securities Premium		10,00,000			
General Reserve		50,00,000			
Dividend Equalisation Reserve		25,00,000			
Profit & Loss A/c		120,00,000			
III. Secured Loan					
Term loan from Bank		25,00,000			

IV. Unsecured Loan		5,00,000			
V.Current Liabilities and Provisions		4,65,000			
		391,45,000			391,45,000

The transaction during April, May & June 2009 were as follows –

Date	Transactions
01/04/09	A shareholder holding 600 Preference shares paid off his dues and remaining shares forfeited.
01/04/09	Investments sold for Rs.95,00,000/-
01/04/09	10% Preference shares redeemed @ 5% premium, a shareholder, holding 1,000 Preferences shares were not traceable.
30/04/09	The company brought back 80,000 Equity shares of Rs.10/- each @ Rs.45/- per shares; buy back expenses paid Rs.20,000/-.
30/06/09	Cash profit earned by the company for three months, amounted Rs.15,20,000/- subject to tax provision @ 30%.
30/06/09	The issued of bonus share to Equity shareholders in the ratio of one share for every two shares held by them.

Assume that the buy back is carried out on legally permissible terms.

You are required to –

i) Pass necessary journal entries far above transactions. (Narration not required.)

ii) Prepare Balance sheet as on 30th June 2009.

Solution :

Journal entries in the books of C Ltd.

Date	Particulars	L.F.	Debit (Rs.)	Credit (Rs.)
April,01	Bank A/c …… Dr. To Calls in Arrears A/c (600 X 20)		12,000	 12,000

April,01	10% Preference Share Capital A/c (400 X 20)…….. Dr. To Calls in Arrears A/c To Shares Forfeited A/c		40,000	 8,000 32,000
April,01	Share Forfeited A/c ……. Dr. To Capital Reserve A/c		32,000	 32,000
April,01	Bank A/c ……..……. Dr. To Investment A/c To Profit & Loss A/c		95,00,000	 55,00,000 40,00,000
April,01	10% Preference Share Capital A/c ……..…. Dr. [1,00,000 – 400 forfeited shares) X 100] Premium on Redemption of Preference Shares A/c…... Dr. To Pref. Shareholder's A/c		99,60,000 4,98,000	 104,58,000
April,01	Securities Premium A/c…....Dr. To Premium on Redemption of Preference shares A/c		4,98,000	 4,98,000
April,01	Profit & Loss A/c…….. Dr. To Capital Redemption Reserve A/c		99,60,000	 99,60,000
April,01	Pref. Shareholder's A/c ….. Dr. To Bank A/c [1,00,000 – 400 – 1000) X 105]		103,53,000	 103,53,000
April,30	Equity Share Capital A/c.…Dr. Premium on buy back shares A/c …….. Dr. To Equity Shareholder's A/c		8,00,000 28,00,000	 36,00,000
April,30	Securities Premium A/c .....Dr. Profit & Loss A/c ……..Dr. To Premium on buy back of Shares A/c		5,02,000 22,98,000	 28,00,000

April,30	Dividend Equalisation Reserve A/c ……..……Dr. To Capital Redemption Reserve A/c		8,00,000	 8,00,000
April,30	Equity Shareholder's A/c…..Dr. To Bank A/c		36,00,000	 36,00,000
June,30	Cash/Bank A/c……..Dr. To Profit & Loss A/c		15,20,000	 15,20,000
June,30	Profit & Loss A/c……..… Dr. To Provision for Taxation A/c		4,56,000	 4,56,000
June,30	Capital Redemption Reserve A/c …….. Dr. To Bonus to shareholders A/c		21,00,000	 21,00,000
June,30	Bonus to Shareholders A/c..Dr. To Equity Share Capital A/c		21,00,000	 21,00,000
June,30	Buy back expenses A/c …..Dr. To Bank A/c		20,000	 20,000
June,30	Profit & Loss A/c ……...Dr. To Buy Back expenses A/c		20,000	 20,000

Working Notes :

1) Payments to Pref. shareholders

Total amount payable to Redemption	1, 04, 58,000
Less : Unpaid amount (1,000 X 105)	(1,05,000)
	1,03, 53,000

2) Bonus to Equity Share holders

Original Equity shares	5, 00,000
- Bought back	(80,000)
Bal. Equity Shares	4, 20,000

Bonus = 4, 20,000 X ½ = 2,10,000 shares X Rs.10/-
= 21, 00,000 (out of CRR)

Bank A/c

Dr. **Cr.**

Particulars	Rs.	Particulars	Rs.
To Bal b/d	45,00,000	By Preference Shareholders A/c	103,53,000
To Calls in arrears A/c	12,000	By Equity Shareholders A/c	36,00,000
To Investments	95,000	By Buy-back Expenses A/c	20,000
To Profit & Loss A/c	15,20,000	By Bal c/d	15,59,000
	1,55,32,000		1,55,32,000

Balance sheet of C Ltd. as on 30th June 2009

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
I. Share Capital			I. Fixed Assets		
Authorized :		?	Gross Block	92,10,000	
Issued, paid up :			(-) Depreciation provision	(25,65,000)	66,45,000
6,30,000 Equity Shares of Rs.10/- each fully paid		63,00,000	II. Investment		NIL
(includes of 2,10,000 Equity shares of Rs.10/- each issued as fully paid, by capitalization of CRR)			III. Current Assets & Loans and Advances		
			Other Current Assets	2,20,00,000	
			Bank Balance	15,59,000	2,35,59,000
			Loans & Advances		5,00,000
II. Reserves & Surplus					
Capital Reserve	2,00,000				
(+) Forfeited Shares transfer	32,000	2,32,000			
CRR	99,60,000				
(+) on buy-back of Equity shares	8,00,000				
	1,07,60,000				
(-) Used for Bonus	(21,00,000)	86,60,000			
Securities Premium	10,00,000				
(-) Premium paid on Redemption of Pref. shares	(4,98,000)				
(-) Premium paid on buy-back of Equity shares	(5,02,000)	NIL			
General Reserve		50,00,000			
Dividend Equalisation Reserve	25,00,000				
(-) used for CRR	(8,00,000)	17,00,000			
Profit & Loss A/c	1,20,00,000				

(+) Profit on sale of investment	40,00,000				
(-) CRR	(99,60,000)				
(-) Premium on buy-back	(22,98,000)				
(+) Net Profit	15,20,000				
(-) Provision for taxation	(4,56,000)				
(-) buy-back expenses	(20,000)	47,86,000			
III. Secured Loans					
Term loan from Bank		25,00,000			
IV. Unsecured Loans		5,00,000			
V. Current Liabilities & Provisions		4,65,000			
Amount dues to Pref. Shareholders		1,05,000			
Provision for Taxation		4,56,000			
		3,07,04,000			3,07,04,000

7.10 KEY POINTS / TERMS :

- A company can buy-back its own shares out of Free Reserves, Security Premium and proceeds of an earlier issue of shares other than Equity Shares.
- Free Reserves includes balance in Security Premium.
- For purpose of buy-back a company can issued Preference Shares, Bonds Secured and Unsecured Loans.
- Equity Shares can be brought back at par or at premium or at discount.
- Free Reserve should be Net Reserve after adjusting Miscellaneous Expenses / Loss appearing on Asset side of latest audited Balance Sheet.
- Only fully paid Equity Shares can be brought back, if it is authorized by Article of Association.
- Maximum Buy-back amount.
  a) 25% of fully paid Equity share capital
  b) Own Fund after Buy-back = Debts X 2
  c) 25% of fully paid Equity Shares X offer price

  Whichever is less.

- Offer Price = $\frac{\text{Maximum Buy - Back amt. possible}}{\text{Maximum No. of Shares to be brought back}}$
- Buy-back expenses can be written off in the same year or over period of 2 to 5 years.

7.11 EXERCISES :

7.11.1 OBJECTIVES

A) Multiple Choice Questions :

1) A company can buy back
   a) Partly paid share b) Fully paid share
   c) Partly called up d) None of the above

2) A company can buy back
   a) Preference Shares b) Equity Share
   c) Irredeemable Preference Shares
   d) Preference shares and Equity Shares

3) A company can buy-back Equity Shares out of
   a) Its Free Reserves
   b) The Proceeds of Preference Shares
   c) Its Securities Premium A/c
   d) Any or all of the above

4) No company can buy-back its Equity Shares if
   a) Partly paid shares b) Partly called shares
   c) Defluating company d) All of the above

5) Buy-back of Equity Shares in any financial shares shall not exceeds.
   a) 5% of its total capital
   b) 25% of Nominal Share Capital
   c) 25% of fully paid Equity Shares
   d) None of above

6) For buy-back amount payable by a company can not exceed.
   a) 25% of own funds b) 25% of owed funds
   c) 25% of paid capital plus free reserves
   d) 25% of total liabilities

7) Authorised capital of Z Ltd. 50,000 Equity Shares, issued 40,000 shares subscribed 30,000 shares fully paid up. Company can buy-back
   a) 7,500 shares b) 25% of 40,000 shares
   c) 12,500 shares d) 15,000 shares

[Answers: 1 – b, 2 – d, 3 – d, 4 – d, 5 – c, 6 – c, 7 – a]

B) Fill in Blanks :

1) _____ company can not buy-back its Equity Shares.
2) On buy-back of shares, there is a reduction in the Share Capital to the entire of the _____ value of the shares bought back.
3) Company can not buy-back if Own Equity Shares, out of the proceeds of _____ issue of same kind of shares.
4) Buy-back of Equity Shares shall not exceed _____ % of Paid-up Equity share capital in any Financial Year.
5) Amount payable on Buy-back of Equity shares can not exceed _____ Paid-up Capital plus Free Reserve.
6) For Buy-back of 25% of paid Equity Capital _____ resolution required.
7) If buy-back is at discount, amount of discount should be credited to _____ A/c.
8) Buy-back premium can be provided out of _____ and / or _____ A/c.
9) Buy-back of Equity Shares shall be compled with in _____ months from date of Special Resolution.
10) If a company buy-back 1,000 Equity shares of Rs.10/- each @ Rs.60/-, out of Free Reserve, amount transferred to C.R.R. is Rs. _____ .
11) The buy-back of shares may be from _____ lots.
12) Capital Redemption Reserve can be used only for _____ .

[Answer : 1) Defaulting, 2) Face Value, 3) An earlier, 4) 25%, 5) 25%, 6) Special, 7) Capital Reserve, 8) Security Premium, Divisiable Profit, 9) 12 months, 10) Rs.10,000/-, 11) Odd Lots, 12) Issue of fully paid up Bonus Shares]

C) State whether True or False.

1) Board of Directors can buy-back any member of shares.
2) Premium on buy-back can be provided out of Preference share capital.
3) Before buy-back, debts : Equity ratio should exceeds 2:1.
4) For buy-back of Equity shares, Free Reserves should be only as per latest audited Balance sheet.
5) On buy-back of shares by the company there is reduction in the share capital.
6) Buy-back of shares should be authorized by Articles of Association of the company.

7) After buyback of Equity shares, EPS of the company increases.

8) A defaulting company can buy-back its shares.

9) Only fully called shares can be brought.

10) Premium on buy-back can be provided only from Securities Premium.

11) Profit earned after audited Balance sheet can be used for buy-back.

12) Revalation Profit can not be used from providing premium on buy-back.

[Answer: True: iv, v, vi, vii, ix, xii, False : i, ii, iii, viii, x, xi]

D) Match the columns.

Group "A"	Group "B"
a) Date of buy-back of Equity Shares b) Buy-back Premium paid c) After buy-back Debt – Equity Should not d) Escrow Account	i) Exceeds 2:1 ii) Exceeds 1:2 iii) Security Premium / Free Reserve iv) Net know at time of issue v) Can not buy-back vi) With Bank vii) With Co-op. credit society

[Answer : (a – v), (b – iv), (c – iii), (d – i), (e – iv)]

Group "A"	Group "B"
a) Buy-back of Equity Shares b) Sec.77A, 77B of the Companies Act c) Redemption of Preference share d) Buy-back of party paid Equity Shares e) Buy-back of Equity Shares must be authorized by f) After buy-back of Equity Shares	i) Governs buy-back shares ii) Only fully paid iii) Not allowed iv) Articles of Association v) Out of Free Reserve & Security premium vi) Issue fully paid Bonus Shares vii) Share forfeited shares viii) Profit prior to incorporation

[Answer : (a – v), (b – i), (c – ii), (d – iii), (e – iv), (f – vii)]

7.11.2 THEORY QUESTIONS:

1) What is boy-back of shares?
2) How buy-back of Equity shares differs from Redemption of Preference shares?
3) What are the conditions of bay-back?
4) What are the limits of buy-back of Equity Shares?
5) Explain various sources of buy-back.
6) To the what extent CRR should be created buy-back of Equity Shares.
7) When buy-back of Equity Shares not possible?
8) What are advantages of buy-back of Equity Shares?

7.11.3 PRACTICAL PROBLEMS:

1) From the following find out maximum numbers of shares that can be brought back particulars.

Particulars	Rs.
a) Equity share Capital (Rs.10/- each)	10,00,000
b) Reserves and Surplus	2,00,000
Capital Redemption Reserve	4,00,000
Security Premium	6,00,000
General Reserve	5,00,000
c) Profit & Loss A/c	60,00,000

2) The following is the Balance sheet of O.R.K. Ltd. as on 30/09/2009.

Particulars	Rs.	Rs.
SOURCES OF FUNDS :		
Share Capital		
Authorized :		
Equity shares of Rs.10/- each		15,00,000
Issued :		
96,000 shares of Rs.10/- each (Rs.8/- paid up)		7,68,000
Reserves :		
Securities Premium	3,60,000	
Reserve Fund	1,20,000	
Investment Fluctuation Reserve	60,000	
Balance in Profit & Loss A/c	96,000	6,36,000
Loans :		
Loan from IDBI	4,40,000	
Unsecured loan from directors	1,60,000	6,00,000
Total Rs.		20,04,000

APPLICATIONS OF FUNDS :		
Fixed Assets (at WDV)		12,84,000
Investments		4,80,000
Current Assets		
Less : Current Assets	9,00,000	
Net Current Assets	6,60,000	2,40,000
Total Rs.		20,04,000

The company brought back 18,000 Equity shares at a price of Rs.20/- per share after completing the necessary legal provisions. Pass the necessary journal entries for the same. Assume adequate bank balance.

Also prepare the Balance Sheet after buy-back.

3) From the following find out the maximum no. of shares that are eligible for buy-back :
   a) at a par
   b) at Rs.50/- per share

Particulars	Rs.	Rs.
a) Share capital 4,00,000 Equity Shares of Rs.10/- each fully paid		40,00,000
10,000, 10% Preference shares of Rs.100/- each		10,00,000
b) Reserve & Surplus :		
Securities Premium	25,00,000	
General Reserve	10,00,000	
Profit & Loss A/c	5,00,000	40,00,000
c) Borrowings :		
10% Debentures	15,00,000	
Unsecured Loans	35,00,000	50,00,000
		140,00,000

The following information is available from the books of Raju Ltd.

Particulars	Rs.
Equity Shares Capital (Rs.10/- each)	15,00,000
Securities Premium	5,00,000
P&L A/c	11,00,000
Investments	8,00,000

The company decided to buy back 20% of its shares at Rs.12.50/- per share. For the same, the investment sold at a Profit of 60% of cost.

Pass journal entries in the books of Raju Ltd.

4) The Balance Sheet of Eros Ltd. as an 31st March, 2010

Liabilities	Rs.	Assets	Rs.
Share capital :		Sundry Assets	14,00,000
Issued & Paid up		Bank	6,50,000
10,000 8% Redeemable Pref. Shares of Rs.50/- each	5,00,000		
50,000 Equity Shares of Rs.10/- each	5,00,000		
Capital Reserve	2,50,000		
General Reserve	1,00,000		
P&L A/c	4,00,000		
9% Debentures	3,00,000		
	20,50,000		20,50,000

It was deckled that 5,000 Equity shares to be bought back on 31st March, 2010 at a premium of 30% for this purpose the company decided to issue 800 Preference shares of Rs.50/- each at par, payable in full on application.

Pass necessary journal entries to record the transactions & prepare Balance Sheet after buy back.

5) The Balance Sheet of S.Y. Ltd. as on 31st March, 2010

Liabilities	Rs.	Assets	Rs.
Share Capital :		**Sundry Assets**	2,40,000
Issued & Paid up		Investments	60,000
10,000 Equity Shares of Rs.10/- each fully paid	1,00,000	(market value Rs.1,20,000/-)	
500 Preference Shares of Rs.100/- each fully paid	50,000	**Current Assets :**	
Sinking Fund	50,000	Stock	75,000
Securities Premium	1,00,000	Debtors	60,000
P&L A/c	80,000	Bank Balance	1,65,000
General Reserve	1,00,000		
10% Debentures	50,000		
Current Liabilities	70,000		
	6,00,000		6,00,000

It was decided :

a) to redeem Preference shares at 5% premium.
b) to sale the investment at market price.

c) to buy back maximum No. of Equity shares possible at the maximum price possible under the law.
d) temporary Bank overdraft was arranged if required.

6) Balance sheet M.D.C. Ltd. as on 31.03.10.

Liabilities	Rs.	Assets	Rs.
Share Capital :		Fixed Assets	6,50,000
40,000 Equity Shares of Rs.10/- each	4,00,000	Current Assets	2,90,000
		Bank Balance	4,40,000
6,000 6% Redeemable Pref. Shares of Rs.50/- each Rs.25/- per share paid	1,50,000		
4,000 8% Redeemable Preference Shares of Rs.100/- each fully paid	4,00,000		
Reserves & Surplus :			
Security Premium A/c	1,20,000		
Dividend Equilisation Reserve	2,10,000		
Current Liabilities	1,00,000		
	13,80,000		13,80,000

M.D.C. Ltd. decided to buy-back the maximum number of Equity Shares at best possible price. To enable the buy-back to be carried out the company decides to issue, after carrying out the necessary formalities required under law, minimum number of new Preference shares of Rs.100/- each at par. The buy-back is duly carried out. Show Journal entries relating to the buy-back and new issue and also the balance sheet after redemption.

7) The summarized Balance Sheet of Tata Ltd. as on 31-12-2010 was as follows:

Liabilities	Rs.	Assets	Rs.
Share Capital :		Fixed Assets	21,20,000
Issued and paid up		Investments	14,00,000
20,000 8% Redeemable Pref. Shares of Rs.100/- each	20,00,000	Current Assets	51,00,000
		Bank Balance	13,30,000
4,00,000 Equity Shares of Rs.10/- each	40,00,000		
Capital Reserve	5,00,000		
General Reserve	12,00,000		
P&L A/c	19,50,000		
Creditors	3,00,000		
	91,50,000		**91,50,000**

It was decided that 10,000 Equity shares will be bought back on 31.12.10 at a premium of 20%; for the purpose, the company decided to issue the requisite number of Preference shares of Rs.100/- each at par payable in full on 15 Dec. 2010.

Examine whether the company can do so. If so, record the entries, prepare the post-buy back balance sheet.

8) M. Ltd. had 20,000 Equity Shares of Rs.10/- each fully paid. The company decided to buy-back 5,000 shares of Rs.10/- each at 10% premium. For this purpose company issued 3,000 Preference Shares of Rs.100/- each at 20% premium and received the issue amount in full. The remaining amount of buy-back is taken from Profit & Loss A/c. After the buy-back of shares, company issued bonus shares from the capital redemption Reserve A/c. Pass journal entries.

9) Following is the Balance Sheet of Ketan Ltd.

Balance Sheet as on 31-03-2010

Liabilities	Rs.	Assets	Rs.
Equity Share Capital :		Fixed Assets	10,00,000
20,000 Equity Shares of Rs.10/- each Rs.8/- paid up	1,60,000	Current Assets Bank Balance	8,00,000 2,50,000
Preference Share Capital			
4,000 shares of Rs.100/- each fully paid up	4,00,000		
Security Premium A/c	30,000		
Capital Reserve A/c	2,00,000		
Profit & Loss A/c	4,80,000		
10% Debentures	3,00,000		
Creditors	4,80,000		
	20,50,000		20,50,000

Company made a final call on Equity Shares and it was received fully. The company decided to buy-back 20% of its Equity capital at 20% premium. The company is using its profits for the buy-back. Pass journal entries and prepare the Balance sheet of the company.

10) Following is the Balance Sheet of T.K. Ltd. as on 31-03-2010.

Balance Sheet

Liabilities	Rs.	Assets	Rs.
Share capital		Fixed Assets	10,00,000
50,000 Equity Shares of Rs.10/- each	5,00,000	Current Assets Bank Balance	6,00,000 2,90,000
5,000 Preference Shares of Rs.100/- each	5,00,000		
Security Premium A/c	1,10,000		
Profit & Loss A/c	2,60,000		
Creditors	3,00,000		
Bills Payable	2,00,000		
Outstanding Expenses	20,000		
	18,90,000		18,90,000

Company decided to buy-back 20% of its Equity capital at 20% premium. Not having sufficient profits for buy-back, the company issued as many Equity shares as were necessary for buy-back. The amount is fully received and then the company purchased the shares. Company also issued 1,000 10% Debentures of Rs.100/- each. Pass journal entries and prepare the Balance Sheet of the company.

11) Inter-City Ltd. furnishes you with the following Balance Sheet as on 31st March, 2010.

Particulars	Rs. (in lakhs)	
SOURCES OF FUNDS :		
Share Capital		
Authorized, Issued, Subscribed & Called up :		
10% Preference shares of Rs.100/- each fully paid		200
Equity shares of Rs.10/- each fully paid		100
Reserves & Surplus :		
Capital Reserves	50	
Securities Premium	100	
General Reserve	900	
Profit & Loss A/c	150	1,200
Total Rs.		1,500
APPLICATIONS OF FUNDS :		
Fixed Assets (at cost)	450	
Less : Depreciation Provision	150	300
Investments (at cost, market value Rs.750 lakhs)		450
Net Current Assets		750
Total Rs.		1,500

The company redeemed Pref. Shares on 1st April, 2010. It also bought back 1,00,000 Equity Shares of Rs.10/- each at Rs.30/- per share.

Investment realized at market price.

Pass journal entries & prepare Balance Sheet after redemption of Preference share & buy-back of Equity shares.

