# Buy BACK OF SECURITYS

Meaning: Buying back those securites (equity shares) which are issued by the company Previously

Buy back of securities:

a) Applicable only to Equity shares
b) Similar to Redemption
c) A company can buy back its own securities from the following
   1. open market
   2. proportionate basis from Existing Equity share holders.
   3. From the Scheme of Employee Stock option Plan (ESOP)

## Accounting treatment: [Journal Entries]

**Step-1** Matching capital Requirement [To Protect intres of outsiders]

Either through

Fresh issue ↓ other kind ↓ PS/[Fresh issue of Preferance shares] ↓ Direct way of matching capital Requirement.

CRR ↓ created from free Reserves ↓ ~~Indirect~~ way of matching capital Requirement

# Accounting Treatment

| | |
|---|---|
| Cash / Bank A/c Dr xxxx<br>To Preferense Share capital A/c xxxx<br>To Securities Premium A/c xxxx<br>[If any | Free Reserve A/c Dr xxx<br>To CRR A/c xxx |

**Note:** How much amount is to be matched for capital Requirement ?
→ Face value of Equity Share capital to be bought back.

## Step-2 BuyBack

1) Due entry

Equity Share capital A/c Dr [Face Value]
Premium on buyback A/c Dr
To Equity Share buyback A/c [Buyback Price]
To Capital Reserve A/c

Any one will come.

2) Payment entry

Equity share Buyback A/c Dr xxxx
To Cash / Bank A/c xxxx

## Step-3 Closing of Premium of Buyback A/c

Free Reserves A/c Dr xxxx
To Premium on Buyback of Shares A/c xxxx

their names to the Memorandum and
with the requirements of the Act
of persons (Statutory Limit):
One Person Company
Company



# Provisions as per Section 68 of companies Act 2013

1) For Buy Back Existing Shares must be fully Paid up.
2) It is authorised by articals of association (AOA)
3) Resolutions Required
   (a) Board Resolution in Board meeting by board of Directors
   (b) Special Resolution in General meeting by share holders.

Exception: Board Resolution is enough if buyback is $\leq 10\%$ of Paid up Equity share capital + Free Reserves

Note: Free Reserves for the purpose of this chapter includes securities premium.

4) Time limit to complete the entire buyback of securities within 1 year from the date of special Resolution.
5) A share which is bought back has to be Physically destroyed /cancelled within 7days from the date of buy back.
6) A company can go for next by back only after < 1year from the date of closure of previous buy back.
7) A company can issue such kind of shares (same kind) only after 6 months from the date of clousure of previous buyback.

**Exception:** A company can issue Bonus shares (or) Discharge Existing Obligations such as Existing scheme of ESOP [Employees Stock option Plan], conversions of debentures conversion of ~~Pe~~ Preferance shares or Sweat equity shares.

- How many maximum no of shares that a company can Buy Back.

As per companies Act 2013, companies must satisfied all the following 3 tests and consider whichever is lower. [Least of the no. of shares arrived by performing 3 tests]

**Test-1 Shares outstanding tests:**

1) Ascertain the total no of Equity shares outstanding
2) maximum no of shares that can be bought back = 25% of o/s Equity shares

**Test-2 Resource test:**

1) Ascertain share holders Funds [Paid up share capital + Free reserves]
2) maximum Resources can be utilised for buyback = 25% of (Paid up share capital + Free Reserves)
3) Maximum no of shares that can be bought back = $\frac{\text{maximum resources}}{\text{Buy back Prices}}$.

Test-3 Debt Equity test : minimum debt equity ratio to be maintained by company after buy back is 2:1 i.e $\frac{\text{Debt}}{\text{Equity}} = \frac{2}{1}$

minimum equity to be maintained = 1/2 (Debt)

→ To crack this ICAI follows simultaneous method.

Eq① Amt transfered to CRR ($x$) = $\frac{\text{max Permissiable bb equity}}{\text{Buyback Price}} \times$ Face Value

Eq-2 max Permissible Buy back of equity ($y$) = Present Equity − Amt to be transfered to CRR − minimum equity to maintained.

By solveing (1) & (2) we will find $x$ and $y$

★ No. of shares to be bought back = $\frac{\text{max Permissi BB of equity}}{\text{Buy Back Price}}$

→ Example : Nominal value = 10, MV = 15, BB Price = 30
Debt = 1000 cr, present equity = 800 cr

minimum equity to be maintained after BB = 1/2 (Debt)
= 1/2 (1000)
= 500

Maximum Reduction in equity = 800 − 500 cr
= 300 cr

Eq:1 $x = \frac{y}{\text{BB Price}} \times$ Face Value

$x = \frac{y}{30} \times 10$

$y = 3x \rightarrow$ ①

Eq:2 $y = 800\,cr - x - 500\,cr$

$y = 300\,cr - x \rightarrow (2)$

Solve (1) & (2)

$y = 3x$

$300 - x = 3x$

$300 = 4x$

$x = 75\,cr$

$y = 3(75)$

$= 225\,cr.$

maximum no. of shares to be BB $= \dfrac{y}{\text{BB Price}}$

$= \dfrac{225}{30} = 7.5\,cr$

Alternative Approch For the above no of shares to be bought back

case(i)

If entire buyback made from free reserves and securities premium.

No of shares to BB $= \dfrac{\text{Present equity} - \text{min equity to be main;}}{\text{Buyback price} + \text{Face value}}.$

case:2 If entire ~~shares~~ Buy Back made from Proceeds of Fresh issue of shares

No of Shares to BB $= \dfrac{\text{Present Equity} - \text{minimum equity to be maintain}}{\text{Buy Back price}}.$