Chapter 32 BUY BACK OF SECURITIES

NB Pg. No.

Question 1

M Ltd. furnishes the following Balance Sheet as at 31st March, 20X1:

		Particulars	Notes	₹ (in 000)
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	5,000
	B	Reserves and Surplus	2	6,310
2		Non-current liabilities		
		Long term borrowings	3	400
3		Current liabilities		
	A	Trade Payables		40
		Total		**11,750**
		Assets		
1		Non-current assets		
	A	Property, plant and Equipment	4	2,750
	B	Non-Current Investments (at cost)		5,000
2		Current assets		
	A	Inventories		1,000
	B	Trade receivables		2,000
	C	Cash and Cash equivalents		1,000
		Total		**11,750**

Notes to accounts

No.	Particulars	₹ in ('000)
1	Share Capital	
	Authorized, Issued and Subscribed Capital:	
	3,00,000 Equity shares of ₹ 10 each fully paid up	3,000
	20,000 9% Preference Shares of 100 each	2,000
	Total	5,000
2	Reserves and Surplus	
	Capital reserve	10
	Revenue reserve	4,000
	Securities premium	500
	Profit and Loss account	1,800
	Total	6,310
3	Long term borrowings	
	10% Debentures 400	
4	Property, Plant and Equipment (PPE)	

	PPE: Cost	3,000
	Less: Provision for depreciation	(250)
	Net carrying value	2,750

The company passed a resolution to buy-back 20% of its equity capital @ ₹ 15 per share. For this purpose, it sold its investments of ₹ 30 lakhs for ₹ 25 lakhs. You are required to pass necessary Journal entries.

Solution

Journal Entries in the books of M Ltd.

₹ in '000

	Particulars		Dr.	Cr.
1.	Bank A/c	Dr.	2,500	
	Profit and Loss A/c	Dr.	500	
	To Investment A/c			3,000
	(Being investment sold for the purpose of buyback of Equity Shares)			
2.	Equity share capital A/c	Dr.	600	
	Premium payable on buy-back	Dr.	300	
	To Equity shares buy-back A/c			900
	(Being the amount due on buy-back of equity shares)			
3.	Equity shares buy-back A/c	Dr.	900	
	To Bank A/c			900
	(Being payment made for buy-back of equity shares)			
4.	Securities Premium A/c	Dr.	300	300
	To Premium payable on buy-back			
	(Being premium payable on buy-back charged from Securities premium)			
5.	Revenue reserve A/c	Dr.	600	
	To Capital Redemption Reserve A/c			600
	(Being creation of capital redemption reserve to the extent of the equity shares bought back)			

Question 2 (RTP May '23) **NB Pg. No.**

Anu Ltd. (a non-listed company) furnishes you with the following balance sheet as at 31st March, 20X1:

(in crores ₹)

			Particulars	Notes	₹ (in 000)
			Equity and Liabilities		
1			Shareholders' funds		
		A	Share capital	1	100
		B	Reserves and Surplus	2	300

2		Current liabilities		
	A	Trade Payables		40
		Total		440
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	3	-
	B	Non-Current Investments	4	100
2		Current assets		
	A	Trade receivables		140
	B	Cash and Cash equivalents		200
		Total		440

Notes to accounts

No.	Particulars		₹
1	Share Capital		
	Authorized, issued and subscribed share capital:		
	12% Redeemable preference shares of ₹ 100 each, fully paid up		75
	Equity shares of ₹ 10 each, fully paid up		25
	Total		100
2	Reserves and Surplus		
	Capital reserve		15
	Securities premium		25
	Revenue reserves		260
	Total		300
3	Property, Plant and Equipment		
	PPE Cost		100
	Less: Provision for depreciation		(100)
	Net carrying value		NIL
4	Non-Current Investments		
	Non-current investments at cost (Market value ₹ 400 Cr.)		100

The company redeemed preference shares on 1st April, 20X1. It also bought back 50 lakhs equity shares of ₹ 10 each at ₹ 50 per share. The payments for the above were made out of the huge bank balances, which appeared as a part of current assets.

You are asked to:

(i) Pass journal entries to record the above.

(ii) Prepare balance sheet as at 1.4.20X1.

Solution

(i) Journal entries in the books of Anu Ltd.

(in crores ₹)

	Particulars		Dr.	Cr.
1st April, 20X1	12% Preference share capital A/c	Dr.	75	
	To Preference shareholders A/c			75
	(Being preference share capital account transferred to shareholders account)			
	Preference shareholders A/c	Dr.	75	
	To Bank A/c			75
	(Being payment made to shareholders)			
	Shares buy-back A/c	Dr.	25	
	To Bank A/c			25
	(Being 50 lakhs equity shares bought back @ ₹ 50 per share)			
	Equity share capital A/c (50 lakhs x ₹ 10)	Dr.	5	
	Securities premium A/c (50 lakhs x ₹ 40)	Dr.	20	
	To Shares buy-back A/c			25
	(Being cancellation of shares bought back)			
	Revenue Reserve A/c	Dr.	80	
	To Capital Redemption Reserve A/c (75+5)			80
	(Being creation of capital redemption reserve to the extent of the face value of preference shares redeemed and equity shares bought back)			

(ii) Balance Sheet of Anu Ltd as at 1.4.20X1

(in crores ₹)

		Particulars	Notes	₹
		Equity and Liabilities		
1		Shareholders' funds		
	A	Share capital	1	20
	B	Reserves and Surplus	2	280
2		Current liabilities		
	A	Trade Payables		40
		Total		340
		Assets		
1		Non-current assets		
	A	Property, plant and equipment	3	-
	B	Non-Current Investments	4	100
2		Current assets		
	A	Trade receivables		140
	B	Cash and Cash equivalents	5	100
		Total		340

Notes to accounts

No	Particulars		₹
1	Share Capital		
	Authorized, issued and subscribed share capital 200 lakhs Equity shares of ₹ 10 each fully paid		20
	Total		20
2	Reserves and Surplus		
	Capital reserve		15
	Capital redemption reserve		80
	Securities premium	25	
	Less: Utilization for buy-back of shares	(20)	5
	Revenue Reserve	260	
	Less: transfer to Capital redemption reserve	(80)	180
	Total		280
3	Property, plant and Equipment		
	PPE: cost		100
	Less: Provision for depreciation		(100)
	Net carrying value		-
4	Non-Current Investments		
	Non-current investments at cost		100
	(Market value ₹ 400 Crores)		
5	Cash and Cash Equivalents		
	Cash and Cash Equivalents as on 31.3.20X1		200
	Less: Bank payment for redemption and buy-back		(100)
	Total		100

Question 3 (RTP May'24)

NB Pg. No.

KG Limited furnishes the following Balance Sheet as at 31st March, 20X1:

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	**Share capital**		
	B	Reserves and Surplus	1	1,200
2		**Non-current liabilities**	2	810
		Long term borrowings		
3		**Current liabilities**	3	750
	A	Trade Payables		
	B	Other Current Liabilities		745
		Total		195
		Assets		3,700
1		**Non-current assets**		
	A	Property, plant and equipment	4	2,026

	B	Non-current Investments	74
2		Current assets	
	A	Inventories	600
	B	Trade receivables	260
	C	Cash and Cash equivalents	740
		Total	3,700

Notes to accounts

No.	Particulars	₹
1	**Share Capital**	
	Authorized, issued and subscribed capital	
	Equity share capital (fully paid up shares of ₹ 10 each)	1,200
2	**Reserves and Surplus**	
	Securities premium	175
	General reserve	265
	Capital redemption reserve	200
	Profit & loss A/c	170
	Total	810
3	**Long term borrowings**	
	12% Debentures	750
4	**Property, plant and equipment**	
	Land and Building	1,800
	Plant and machinery	226
	Net carrying value	2,026

On 1st April, 20X1, the company announced the buy-back of 25% of its equity shares @ ₹ 15 per share. For this purpose, it sold all of its investments for ₹ 75 lakhs.

On 5th April, 20X1, the company achieved the target of buy-back. On 30th April, 20X1 the company issued one fully paid up equity share of ₹ 10 by way of bonus for every four equity shares held by the equity shareholders.

You are required to:

1) Pass necessary journal entries for the above transactions.

2) Prepare Balance Sheet of KG Limited after bonus issue of the shares.

Solution:

In the books of KG Limited

Journal Entries

Date	Particulars		Dr.	Cr.
20X1			(₹ in lakhs)	
April 1	Bank A/c	Dr.	75	
	To Investment A/c			74
	To Profit on sale of investment			1
	(Being investment sold on profit)			
April 5	Equity share capital A/c	Dr.	300	

	Securities premium A/c	Dr.	150	
	To Equity shares buy-back A/c			450
	(Being the amount due to equity shareholders on buy-back)			
April 5	General reserve A/c	Dr.	265	
	Profit and Loss A/c	Dr.	35	
	To Capital redemption reserve A/c			300
	(Being amount equal to nominal value of buyback shares from free reserves transferred to capital redemption reserve account as per the law)			
April 30	Capital redemption reserve A/c	Dr.	225	
	To Bonus shares A/c (W.N.1)			225
	(Being the utilization of capital redemption reserve to issue bonus shares)			
	Bonus shares A/c	Dr.	225	
	To Equity share capital A/c			225
	(Being issue of one bonus equity share for every four equity shares held)			

Balance Sheet

(After buy-back and issue of bonus shares)

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	1,125
	B	Reserves and Surplus	2	436
2		**Non-current liabilities**		
		Long term borrowings	3	750
3		**Current liabilities**		
	A	Trade Payables		745
	B	Other Current Liabilities		195
		Total		3,251
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	4	2,026
2		**Current assets**		
	A	Inventories		600
	B	Trade receivables		260
	C	Cash and Cash equivalents		365
		Total		3,251

Notes to accounts

No.	Particulars		₹
1	**Share Capital**		
	Authorized, issued and subscribed capital:		
	Equity share capital (fully paid up shares of ₹10 each)		1,125
2	**Reserves and Surplus**		
	General Reserve	265	
	Less: Transfer to CR	(265)	-
	Capital Redemption Reserve	200	
	Add: Transfer due to buy-back of shares from P/L	35	
	Add; Transfer due to buy-back of shares from General Reserve	265	
	Less: Utilisation for issue of bonus shares	(225)	275
	Securities premium	175	
	Less: Adjustment for premium paid on buyback	(150)	25
	Profit & Loss A/c	170	
	Add: Profit on sale of investment	1	
	Less: Transfer to CRR	(35)	136
	Total		436
3	**Long term borrowings**		
	12% Debentures		750
4	**Property, Plant and Equipment**		
	Land and Building		1,800
	Plant and machinery		226
	Net carrying value		2,026

Working Notes:

1) Amount of bonus shares = 25% of (1,200 – 300) lakhs = ₹ 225 lakhs

2) Cash at bank after issue of bonus shares

Particulars	₹ in lakhs
Cash balance as on 1st April, 20X1	740
Add: Sale of investments	75
	815
Less: Payment for buy-back of shares	(450)
	365

Note: In the given solution, it is possible to adjust transfer to capital redemption reserve account or capitalization of bonus shares from any other free reserves or securities premium (to the extent available) also.

NB Pg. No.

Question 4 (RTP Nov'18)

Dee Limited (a non-listed company) furnishes the following Balance Sheet as at 31st March, 20X1:

(in thousand ₹)

		Particulars	Notes	₹
		Equity and Liabilities		

1		Shareholders' funds		
	A	Share capital	1	2,700
	B	Reserves and Surplus	2	9,700
2		Current liabilities		
	A	Trade Payables		1,400
		Total		13,800
		Assets		
1		Non-current assets		
	A	Property, plant and Equipment		9,300
	B	Non-Current Investments		3,000
2		Current assets		
	A	Inventories		500
	B	Trade receivables		200
	C	Cash and Cash equivalents		800
		Total		13,800

Notes to accounts

No.	Particulars		₹
1	Share Capital		
	Authorized, issued and subscribed capital:		
	2,50,000 Equity shares of ₹ 10 each fully paid up		2,500
	2,000, 10% Preference shares of ₹ 100 each		200
	(Issued two months back for the purpose of buy-back)		-----
	Total		2,700
2	Reserves and Surplus		
	Capital reserve		1,000
	Revenue reserve		3,000
	Securities premium		2,200
	Profit and loss account		3,500
	Total		9,700

The company passed a resolution to buy-back 20% of its equity capital @ ₹ 50 per share. For this purpose, it sold all of its investment for ₹ 22,00,000.

You are required to pass necessary journal entries and prepare the Balance Sheet.

Solution

Journal Entries in the books of Dee Limited

(in thousand ₹)

	Particulars	Dr.	Cr.
(i)	Bank Account Dr. Profit and Loss Account Dr. To Investment Account (Being the investments sold at loss for the purpose of buy-back)	2,200 800	 3,000

(ii)	Equity Share buy-back Account	Dr.	2,500	
	To Bank Account			2,500
	(Being the payment made on buy-back)			
(iii)	Equity Share Capital Account	Dr.	500	
	Premium Payable on Buy-Back Account	Dr.	2,000	
	To Equity Shares Buy-Back Account			2,500
	(Being the buy-back amount allocated to equity share capital)			
(iv)	Securities premium Account	Dr.	2,000	
	To Premium payable on buy-back Account			2,000
	(Being the premium payable on buy-back adjusted against securities premium account)			
(v)	Revenue reserve Account	Dr.	300	
	To Capital Redemption Reserve Account			300
	(Being the amount equal to nominal value of equity shares bought back out of free reserves transferred to capital redemption reserve account)			

Balance Sheet of Dee Limited as at 1st April, 20X1

(After buy-back of shares)

(in thousand ₹)

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	2,200
	B	Reserves and Surplus	2	6,900
2		**Current liabilities**		
	A	Trade Payables		1,400
		Total		10,500
		Assets		
1		**Non-current assets**		
	A	Property, plant and Equipment		9,300
2		**Current assets**		
	A	Inventories		500
	B	Trade receivables		200
	C	Cash and Cash equivalents		500
		Total		10,500

Notes to accounts

No.	Particulars		₹
1	Share Capital		
	Authorized, issued and subscribed capital:		

	2,50,000 Equity shares of ₹ 10 each fully paid up		2,000
	2,000, 10% Preference shares of ₹ 100 each		200
	(Issued two months back for the purpose of buyback)		-----
	Total		2,200
2	Reserves and Surplus		
	Capital reserve		1,000
	Capital redemption reserve		300
	Securities Premium	2,200	
	Less: Premium payable on buy-back of shares	(2,000)	200
	Revenue reserve	3,000	
	Less: Transfer to Capital redemption reserve	(300)	2,700
	Profit and loss A/c	3,500	
	Less: Loss on investment	(800)	2,700
	Total		6,900

Question 5

NB Pg. No.

Extra Ltd. (a non-listed company) furnishes you with the following Balance Sheet as at 31st March, 20X1:

(in lakhs ₹)

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	120
	B	Reserves and Surplus	2	118
2		**Non-current liabilities**		
		Long term borrowings	3	4
3		**Current liabilities**		
	A	Trade Payables		70
		Total		312
		Assets		
1		**Non-current assets**		
	A	Property, plant and Equipment		50
	B	Non-current Investments		120
2		**Current assets**		
	A	Cash and Cash equivalents		142
		Total		312

Notes to accounts

No.	Particulars		₹
1	**Share Capital**		
	Authorized, issued and subscribed capital:		
	Equity shares of ₹ 10 each fully paid		100

	9% Redeemable preference shares of ₹ 100 each fully paid		20
	Total		120
2	**Reserves and Surplus**		
	Capital reserves		8
	Revenue reserves		50
	Securities premium		60
	Total		118
3	**Long term borrowings**		
	10% Debentures		4

(i) The company redeemed the preference shares at a premium of 10% on 1st April, 20X1.

(ii) It also bought back 3 lakhs equity shares of ₹ 10 each at ₹ 30 per share. The payment for the above was made out of huge bank balances.

(iii) Included in its investment were "investments in own debentures" costing ₹ 2 lakhs (face value ₹ 2.20 lakhs). These debentures were cancelled on 1st April, 20X1.

(iv) The company had 1,00,000 equity stock options outstanding on the above mentioned date, to the employees at ₹ 20 when the market price was ₹30 (This was included under current liabilities). On 1.04.20X1 employees exercised their options for 50,000 shares.

(a) Pass the journal entries to record the above.

(b) Prepare Balance Sheet as at 01.04.20X1.

Solution

(₹ in lakhs)

Date	Particulars		Debit	Credit
20X1 1st April	9% Redeemable preference share capital A/c	Dr.	20.00	
	Premium on redemption of preference shares A/c	Dr.	2.00	
	To Preference shareholders A/c			22.00
	(Being preference share capital transferred to shareholders account)			
	Preference shareholders A/c	Dr.	22.00	
	To Bank A/c			22.00
	(Being payment made to shareholders)			
	Equity shares buy-back A/c	Dr.	90.00	
	To Bank A/c			90.00
	(Being 3 lakhs equity shares of ₹ 10 each bought back @ ₹ 30 per share)			
	Equity share capital A/c	Dr.	30.00	
	Securities premium A/c	Dr.	60.00	
	To Equity Shares buy-back A/c			90.00
	(Being cancellation of shares bought back)			

	Revenue reserve A/c Dr. To Capital redemption reserve A/c (Being creation of capital redemption reserve account to the extent of the face value of preference shares redeemed and equity shares bought back as per the law)	50.00	50.00
	10% Debentures A/c Dr. To Investment (own debentures) A/c To Profit on cancellation of own debentures A/c (Being cancellation of own debentures costing ₹ 2 lakhs, face value being ₹ 2.20 lakhs and the balance being profit on cancellation of debentures)	2.20	2.00 0.20
	Bank A/c Dr. Employees stock option outstanding (Current liabilities) A/c Dr. To Equity share capital A/c To Securities premium A/c (Being the allotment to employees, of 50,000 shares of ₹ 10 each at a premium of 20 per share in exercise of stock options by employees)	10.00 5.00	5.00 10.00
	Securities premium A/c Dr. To Premium on redemption of preference shares A/c (Being premium on redemption of preference shares adjusted through securities premium)	2.00	2.00

Balance Sheet of Extra Ltd. as at 01.04.20X1

(in lakhs ₹)

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	75.00
	B	Reserves and Surplus	2	66.20
2		**Non-current liabilities**		
		Long term borrowings	3	1.80
3		**Current liabilities**		
	A	Other Current Liabilities	4	65.00
		Total		208
		Assets		
1		**Non-current assets**		
	A	Property, plant and Equipment		50.00
	B	Non-current Investments	5	118.00
2		**Current assets**		
	A	Cash and Cash equivalents	6	40.00
		Total		208

Notes to accounts

No.	Particulars		₹
1	**Share Capital**		
	Equity shares of ₹ 10 each fully paid		100
	Less: Cancellation of bought back shares		(30)
	Add: Shares issued against ESOP		5
	Total		75
2	**Reserves and Surplus**		
	Capital Reserve		
	Opening balance	8.00	
	Add: Profit on cancellation of debentures	0.20	8.20
	Revenue reserves		
	Opening balance	50.00	
	Less: Creation of Capital Redemption Reserve	(50.00)	-
	Securities Premium		
	Opening balance	60.00	
	Less: Adjustment for cancellation of equity shares	(60.00)	
	Less: Adjustment for premium on redemption of preference shares	(2.00)	
	Add: Shares issued against ESOP at premium	10.00	8.00
	Capital Redemption Reserve		50.00
	Total		66.20
3	**Long term borrowings**		
	10% Debentures		4.00
	Less: Cancellation of own debentures		(2.20)
	Total		1.80
4.	**Other Current liabilities**		
	Opening balance		70.00
	Less: Adjustment for ESOP outstanding		(5.00)
	Total		65.00
5.	**Non-current investments**		
	Opening balance		120.00
	Less: Investment in own debentures		(2.00)
	Total		118.00
6.	**Cash and Cash Equivalents**		
	Opening balance		142.00
	Less: Payment to preference shareholders		(22.00)
	Less: Payment to equity shareholders		(90.00)
	Add: Share price received against ESOP		10.00
	Total		40.00

Question 6 (MTP Oct'20, Oct'21, Oct'23, RTP May'20) NB Pg. No.

The following was the summarized balance sheet of Bhoomi Ltd. as on 31st March, 2020:

Equity & liability	Rs (in lakhs)	Assets	Rs (in lakhs)
Authorised Capital:		Property, plant and equipment	1,12,000
Equity shares of Rs 10 each	80,000	Investments	24,000
Issued Capital		Cash at Bank	13,200
Equity Shares of Rs10 each Fully Paid up	64,000		
Trade Receivables	66,000		
10% Redeemable Preference Shares of 10 each, Fully Paid Up	20,000		
Reserves & Surplus:			
Capital Redemption Reserve	8,000		
Securities Premium	6,400		
General Reserve	48,000		
Profit & Loss Account	2,400		
9% Debentures	40,000		
Trade Payables	26,400		
	2,15,200		**2,15,200**

On 1st April,2020 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 25% of its Equity Shares at Rs 20 per Share. In order to make Cash available, the Company sold all the Investments for Rs 25,000 Lakhs and raised a Bank Loan amounting to Rs 16,000 lakh on the Security of the Company's Plant. Give the necessary Journal Entries considering that the buy back is authorized by the articles of company and necessary resolution is passed by the company for this. The amount of Securities premium may be utilized to the maximum extent allowed by law.

(8 Marks)

Solution:

Journal entries In the books of Bhoomi Ltd.

		Dr.	Cr.
		(₹ in lakhs)	
1	Bank A/c Dr.	25,000	
	To Investments A/c		24,000
	To Profit and Loss A/c		1,000
	(Being Investments sold and, profit being credited to Profit and Loss Account)		
2	10% Redeemable Preference Share Capital A/c Dr.	20,000	
	Premium payable on Redemption of Preference Shares A/c Dr.	2,000	
	To Preference Shareholders A/c		**22,000**
	(Being amount payable on redemption of Preference shares, at a Premium of 10%)		
3	Securities Premium A/c Dr.	2,000	

	To Premium payable on Redemption of Preference Shares A/c		2,000
	(Being Securities Premium utilised to provide Premium on Redemption of Preference Shares)		
4	Equity Share Capital A/c Dr.	16,000	
	Premium payable on Buyback A/c Dr.	16,000	
	To Equity Share buy back A/c		32,000
	(Being the amount due on buy-back)		
5	Securities Premium A/c (6,400 - 2,000) Dr.	4,400	
	General Reserve A/c (balancing figure) Dr.	11,600	
	To Premium payable on Buyback A/c		16,000
	(Being premium on buyback provided first out of Securities Premium and the balance out of General Reserves.)		
6	Bank A/c Dr.	16,000	
	To Bank Loan A/c		16,000
	(Being Loan taken from Bank to finance Buyback)		
7	Preference Shareholders A/c Dr.	22,000	
	Equity Shares buy back A/c Dr.	32,000	
	To Bank A/c		54,000
	(Being payment made to Preference Shareholders and Equity Shareholders)		
8	General Reserve Account Dr.	36,000	
	To Capital Redemption Reserve Account		36,000
	(Being amount transferred to Capital Redemption Reserve Account to the extent of face value of preference shares redeemed and equity Shares bought back) (20,000 + 16,000)		

Question 7 (MTP Nov'21, Apr'23) NB Pg. No.

SM Limited gives the following information as on 31st March, 2020:

		Rs
Share capital		
(60,000 Equity Shares of Rs 10 Each)		6,00,000
Reserve & Surplus:		
Security premium		70,000
General reserve		63,000
Profit and Loss		1,40,000
Non-current liability:		
9% debentures (secured)		3,00,000
Current Liabilities:		
Term loan		40,000
Creditors		65,000
Provision for taxation		15,000

Property plant and equipment		6,00,000
Non-current investment		1,50,000
Current assets:		
Stock		2,00,000
Debtors		2,60,000
Bank		83,000

The shareholders adopted the resolution on 31st March, 2020 to:

(i) Buy back 25% of the paid up capital @ Rs 15 each.

(ii) Issue 10% debentures of Rs 60,000 at a premium of 10% to finance the buyback of shares.

(iii) Maintain a balance of Rs 20,000 in General Reserve.

(iv) Sell investments worth Rs 1,00,000 for Rs 80,000.

(v) Buy back expenses were Rs 2,000.

You are required to pass necessary journal entries to record the above transactions and prepare Ledger account of Bank. **(8 Marks)**

Solution:

In the books of SM Limited Journal Entries

Particulars		Dr.	Cr.
		Rs	Rs
1. Equity share capital A/c (15,000 x Rs10)	Dr.	1,50,000	
Premium on buyback A/c (15,000 x Rs5)	Dr.	75,000	
To Equity shares buy back or Equity Shareholders A/c (15,000 x Rs15)			2,25,000
(Being the amount due to equity shareholders on buy back)			
2. Equity shares buy back/Equity shareholders A/c	Dr.	2,25,000	
To Bank A/c			2,25,000
(Being the payment made on account of buy back of 15,000 Equity Shares as per the Companies Act)			
3. Bank A/c	Dr.	66,000	
To 10 % Debentures A/c			60,000
To Securities Premium A/c			6,000
(Being 14 % debentures issued to finance buy back)			
4. Buyback Expenses A/c	Dr.	2,000	
To Bank A/c			2,000
(Buyback expenses paid)			
5. Bank A/c	Dr.	80,000	
Profit and Loss A/c (Loss on sale of investment)		20,000	
To Investment A/c			1,00,000
(Being investment sold at loss)			
6. General reserve	Dr.	43,000	
Profit and Loss A/c	Dr.	1,07,000	
To Capital redemption reserve A/c			1,50,000

(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)		
7. Securities Premium Dr.	75,000	
Profit and Loss A/c Dr.	2,000	
To Premium on buyback		75,000
To Buyback Expenses A/c		2,000
(Being premium on buyback and buyback expenses charged to securities premium and profit and loss account)		

Bank Account

Particulars	Amount (Rs)	Particulars	Amount (Rs)
To Balance b/d To	83,000	By Equity Shareholders A/c	2,25,000
Investment A/c	80,000	By Expenses on buy back of shares	2,000
To 10% Debentures and Securities premium	66,000	By Balance c/d	2,000
Total	2,29,000	Total	2,29,000

Note: It may be noted that as per the provisions of the Companies Act, no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities. Issue of debentures has been excluded for the purpose of "specified securities" and the entire amount of Rs 1,50,000 has been credited to CRR while solving the Question.

Question 8 (PYQ Nov'19) (RTP Nov'21) NB Pg. No.

X Ltd. furnishes the following summarized Balance Sheet as at 31-03-2018.

Liabilities	(in ₹)	(in ₹)
Share Capital		
Equity Share Capital of ₹ 20 each fully paid up	50,00,000	
10,000, 10% Preference Shares of ₹ 100 each fully paid up	10,00,000	60,00,000
Reserves & Surplus		
Capital Reserve	1,00,000	
Security Premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and Loss	20,00,000	
Dividend Equalization Fund	5,50,000	43,50,000
Non-Current Liabilities		
12% Debenture		12,50,000
Current Liabilities and Provisions		5,50,000
Total		1,21,50,000
Assets		
Fixed Assets		
Tangible Assets		1,00,75,000

Current Assets	3,00,000	
Investment	2,00,000	
Inventory	15,75,000	20,75,000
Cash and Bank		1,21,50,000
Total		

The shareholders adopted the resolution on the date of the above mentioned Balance Sheet to:

1) Buy back 25% of the paid up capital and i was decided to offer a price of 20% over market price. The prevailing market value of the company's share is Rs. 30 per share.

2) To finance the buy back of share company :
   a. Issue 3000, 14 % debenture of 100 each at a premium of 20%
   b. Issue 2500, 10 % preference share of Rs. 100 each

3) Sell investment worth Rs. 1,00,000 for Rs. 1,50,000.

4) Maintain a balance of Rs. 2,00,000 in Revenue Reserve.

5) Later the company issue three fully paid up equity share of Rs. 20 each by way of bonus share for every 15 equity share held by the equity shareholder.

You are required to pass the necessary journal entries to record the above transactions and prepare Balance Sheet after buy back. **(15 Marks)**

Solution:

In the books of X Limited Journal Entries

Particulars	Dr. ₹	Cr. ₹
1. Bank A/c Dr.	3,60,000	
To 14 % Debenture A/c		3,00,000
To Securities Premium A/c		60,000
(Being 14 % debentures issued to finance buy back)		
2. Bank A/c Dr.	2,50,000	
To 10% preference share capital A/c		2,50,000
(Being 10% preference share issued to finance buy back)		
3. Bank A/c Dr.	1,50,000	
To Investment A/c		1,00,000
To Profit on sale of investment (Being investment sold on profit)		50,000
4. Equity Share Capital A/c (62,500 x ₹20) Dr.	12,50,000	
Securities premium A/c (62,500 x ₹16) Dr.	10,00,000	
To Equity shares buy back A/c (62,500 x ₹36)		22,50,000
(Being the amount due to equity shareholders on buy back)		
5. Equity shares buy back A/c Dr.	22,50,000	
To Bank A/c		22,50,000
(Being the payment made on account of buy back of 62,500 Equity Shares as per the Companies Act)		
6. Revenue reserve Dr.	3,00,000	
Securities premium Dr.	2,60,000	

Profit and Loss A/c Dr.	4,40,000	
To Capital redemption reserve A/c*		10,00,000
(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law) [12,50,000 less 2,50,000]		
7. Capital Redemption Reserve A/c Dr.	7,50,000	
To Bonus shares A/c (W.N.1)		7,50,000
(Being the utilization of capital redemption reserve to issue 37,500 bonus shares)		
8. Bonus shares A/c Dr.	7,50,000	
To Equity share capital A/c		7,50,000
(Being issue of 3 bonus equity share for every 15equity shares held)		

*Alternatively, entry for combination of different amounts (from Revenue reserve, Securities premium and profit and Loss account.) may be passed for transferring the required amount to CRR.

Note: It may be noted that as per the provisions of the Companies Act, no buy-back of any kind of shares or other **specified securities** shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other **specified securities.** Issue of debentures has been excluded for the purpose of "specified securities" and the entire amount of Rs; 10,00,000 (after deducting only pref. share capital) has been credited to CRR while solving the question.

Balance Sheet (After buy back and issue of bonus shares)

I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	57,50,000
(b) Reserves and Surplus	2	27,10,000
(2) Non-Current Liabilities	3	
(a) Long-term borrowings		15,50,000
(3) Current Liabilities		
(a) Trade payables –		
(b) current liabilities & Provisions		5,50,000
Total		**1,05,60,000**
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment		1,00,75,000
(2) Current assets		
(a) Investments		2,00,000
(b) Inventory		2,00,000
(c) Cash and cash equivalents (W.N. 2)		85,000
Total		**1,05,60,000**

Notes to Accounts

				₹
1	Share Capital			

	Equity share capital (Fully paid up shares of ₹ 20 each)			
	(2,50,000–62,500+37,500 shares)		45,00,000	
	10% preference shares @ ₹ 100 each (10,00,000 + 2,50,000)		12,50,000	57,50,000
2.	Reserves and Surplus			
	Capital Reserve		1,00,000	
	Revenue reserve		2,00,000	
	Securities premium	12,00,000		
	Add: Premium on debenture	60,000		
	Less: Adjustment for premium paid on buy back	(10,00,000)		
3	Less: Transfer to CRR	(2,60,000)	Nil	
	Capital Redemption Reserve			
	Transfer due to buy-back of shares from P&L			
		10,00,000		
	Less: Utilisation for issue of bonus shares	(7,50,000)	2,50,000	
	Profit & Loss A/c	20,00,000		
	Add: Profit on sale of investment	50,000		
	Less: Transfer to CRR	(4,40,000)	16,10,000	
	Dividend equalization reserve		5,50,000	27,10,000
3	Long-term borrowings – 12% Debentures	12,50,000		
	- 14% Debentures	3,00,000		15,50,000

Working Notes:

1. Amount of bonus shares = [(2,50,000 -25%)3/15] x 20 = 37,500 × 20=7,50,000
2. Cash at bank after issue of bonus shares

	Rs.
Cash balance as on 30.3.2018	15,75,000
Add: Issue of debenture	3,60,000
Add: issue of preference shares	2,50,000
Add: Sale of investments	1,50,000
	23,35,000
Less: Payment for buy back of shares (22,50,000)	85,000

Question 9 (PYQ Jan'21)

NB Pg. No.

The Directors of Umang Ltd. passed a resolution to buyback 5,00,000 of its fully paid equity shares of ₹ 10 each at ₹ 15 per share. This buyback is in compliance with the provisions of the Companies Act, 2013.

For this purpose, the company

(i) Sold its investments of ₹ 30,00,000 for ₹ 25,00,000.

(ii) Issued 20,000, 12% preference shares of ₹ 100 each at par, the entire amount being payable with application.

(iii) Used ₹ 15,00,000 of its Securities Premium Account apart from its adequate balance in General Reserve to fulfill the legal requirements regarding buy-back.

(iv) The company has necessary cash balance for the payment to shareholders.

You are required to pass necessary Journal Entries (including narration) regarding buy- back of shares in the books of Umang Ltd.

(5 Marks)

Solution:

Journal Entries in the books of Umang Ltd.

	Particulars	Dr.	Cr.
1.	Bank A/c Dr.	25,00,000	
	Profit and Loss A/c Dr.	5,00,000	
	To Investment A/c		30,00,000
	(Being investment sold for the purpose of buy-back of Equity Shares)		
2.	Bank A/c Dr.	20,00,000	
	To 12% Pref. Share capital A/c		20,00,000
	(Being 12% Pref. Shares issued for ₹ 20,00,000)		
3.	Equity share capital A/c Dr.	50,00,000	
	Premium payable on buy-back Dr.	25,00,000	
	To Equity shares buy-back A/c		75,00,000
	Equity shareholders A/c		
	(Being the amount due on buy-back of equity shares)		
4.	Equity shares buy-back A/c/ Equity shareholders A/c Dr.	75,00,000	
	To Bank A/c		75,00,000
	(Being payment made for buy-back of equity shares)		
5.	Securities Premium A/c General Dr.	15,00,000	
	Reserve A/c Dr.	10,00,000	
	To Premium payable on buy-back		25,00,000
	(Being premium payable on buy-back charged from Securities premium)		
6.	General Reserve A/c Dr.	30,00,000	
	To Capital Redemption Reserve A/c		30,00,000
	(Being creation of capital redemption reserve to the extent of the equity shares bought back after deducting fresh pref.shares issued)		

Question 10 (MTP Mar'23, Sep'23) (RTP Nov'20 MTP Sep'23) **NB Pg. No.**

Pratham Ltd. (a non-listed company) has the following Capital structure as on 31st March, 20X1:

Particulars	₹	₹
Equity Share Capital (shares of ₹ 10 each fully paid		30,00,000
Reserves & Surplus		

General Reserve	32,50,000	
Security Premium Account	6,00,000	
Profit & Loss Account	4,30,000	
Revaluation Reserve	6,20,000	49,00,000
Loan Funds		42,00,000

You are required to compute by Debt Equity Ratio Test, the maximum number of shares that can be bought back in the light of above information, when the offer price for buy-back is ₹ 30 per share.

(10 Marks)

Solution

Debt Equity Ratio Test

	Particulars	₹
(a)	Loan funds	42,00,000
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹ in crores)	21,00,000
(c)	Present equity shareholders fund (₹ in crores)	72,80,000
(d)	Future equity shareholder fund (₹ in crores) (See Note 2)	59,85,000
		(72,80,000–12,95,000)
(e)	Maximum permitted buy-back of Equity (₹ in crores) [(d) – (b)] (See Note 2)	38,85,000 (by simultaneous equation)
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share (shares in crores) (See Note 2)	1,29,500 (by simultaneous equation)

Working Note:

1. Shareholders' funds

Particulars	₹
Paid up capital	30,00,000
Free reserves (32,50,000 +6,00,000+4,30,000)	42,80,000
	72,80,000

2. As per section 68 of the Companies Act, 2013, amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

   Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

   Equation 1 : (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained = Maximum permissible buy-back of equity.

   $(72,80,000 - x) - 21,00,000 = y$ (1)

   Since $51,80,000 - x = y$

   Equation 2: $\left(\frac{\text{Maximum buy -back}}{\text{Offer price for buy -back}} \text{ X Nominal Value}\right)$

   = Nominal value of the shares bought -back to be transferred to CRR

   Equation 2: $\left(\frac{y}{30} \text{ X } 10\right) == x$

   $3x = y$ (2)

x = ₹ 12,95,000 crores and y

= ₹ 38,85,000 crores

Question 11 : (PYQ Sept.24) NB Pg. No.

Aerodots Ltd. has the following capital structure as on 31.03.2024 :

Particulars	Amount (Rs. in thousands)
Equity Share Capital (shares of Rs.10 each)	600
Reserves:	
General Reserve	540
Securities Premium	200
Profit & Loss	100
Revaluation Reserve	30
Investment Allowance Reserve (Statutory Reserve)	75
Infrastructure Development Reserve	25
Loan Funds	2000

On 1st April, 2024 the company wants to buy back 14,000 equity shares of Rs.10 each at Rs.30 per Equity share.

You are required to calculate maximum permissible number of equity shares that can be bought back.

Buy Back of shares is duly authorized by its articles and necessary resolution has been passed by the company. **(7 Marks)**

Solution :

Statement determining the maximum number of shares to be bought back

(in thousands)

Particulars	Number of shares
Shares Outstanding Test (W.N.1)	15
Resources Test (W.N.2)	12
Debt Equity Ratio Test (W.N.3)	11
Maximum number of shares that can be bought back [least of the above]	11

Thus, the lowest being 11,000 shares, the company cannot buy back 14,000 shares.

Working Notes:

1. **Shares Outstanding Test**

Particulars	(Shares in thousands)
Number of shares outstanding	60
25% of the shares outstanding	15

2. Resources Test

Particulars	Rs.(in thousands)
Paid up capital	600
Free reserves (540 + 200 +100)	840
Shareholders' funds	1,440
25% of Shareholders fund	360
Buy-back price per share	Rs.30
Number of shares that can be bought back	12,000 shares

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

Particulars	Rs. in thousands
(a) Loan funds	2,000
(b) Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs.) (a/2)	1,000
(c) Present equity shareholders fund (Rs.)	1,440
(d) Future equity shareholders fund (Rs.) (see W.N.4) (1,440–110)	1,330
(E) Maximum permitted buy-back of Equity (Rs.) [(d) – (b)]	330
(F) Maximum number of shares that can be bought back @ Rs.30 per share	11,000 shares

4. Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy-Back

$= (1,440 - x) - 1,000 = y$

$= 440 - x = y (1)$

Equation 2: Maximum Permitted Buy-Back X Nominal Value Per Share/Offer Price Per Share

$y/30 \times 10 = x$

Or

$3x = y$ (2)

by solving the above two equations we get

x = Rs.110 thousands

y = Rs.330 thousands

Alternatively, Maximum number of shares from debt equity ratio test may be worked out as follows:

Buy-back price + Face value of equity shares = Rs.30 + Rs.10 = Rs.40

Excess of equity fund over the minimum equity to be maintained 1440–1000 = 440 thousands

Number of Shares that can be bought back = 440/40 thousands = 11 thousands.

Question 12

NB Pg. No.

Following is the Balance Sheet of Competent Limited as at 31st March, 20X1:

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital		
	B	Reserves and Surplus	1	12,50,000
2		**Non-current liabilities**	2	18,75,000
		Long term borrowings		
3		**Current liabilities**	3	28,75,000
	A	Other Current Liabilities		
				16,50,000
		Assets	Total	76,50,000
1		**Non-current assets**		
	A	Property, plant and Equipment		
2		**Current assets**	4	46,50,000
	A	Other Current Assets		
				30,00,000
			Total	76,50,000

Notes to accounts

No.	Particulars		₹
1	**Share Capital**		
	Authorized, issued and subscribed capital:		
	Equity share capital (fully paid up shares of ₹ 10 each)		
2	**Reserves and Surplus**		12,50,000
	Securities premium		2,50,000
	Profit and loss account		1,25.000
	Revenue reserve		15,00,000
	Total		18,75,000
3	**Long term borrowings**		
	14% Debentures		18,75,000
	Unsecured Loans		10,00,000
	Total		28,75,000
4	**Property, plant and equipment**		
	Land and Building		19,30,000
	Plant and machinery		18,00,000
	Furniture and fitting		9,20,000
	Net carrying value		46,50,000

The company wants to buy-back 25,000 equity shares of ₹ 10 each, on 1st April, 20X1 at ₹ 20 per share. Buy-back of shares is duly authorized by its articles and necessary resolution has been passed by the company towards this. The payment for buy-back of shares will be made by the company out of sufficient bank balance available shown as part of Current Assets.

Comment with your calculations, whether buy-back of shares by company is within the provisions of the Companies Act, 2013. If yes, pass necessary journal entries towards buy-back of shares and prepare the Balance Sheet after buy-back of shares.

Solution:

Determination of Buy-back of maximum no. of shares as per the Companies Act, 2013

1. Shares Outstanding Test

Particulars	(Shares)
Number of shares outstanding	1,25,000
25% of the shares outstanding	31,250

2. Resources Test: Maximum permitted limit 25% of Equity paid up capital + Free Reserves

Particulars	
Paid up capital (₹)	12,50,000
Free reserves (₹) (15,00,000 + 2,50,000 + 1,25,000)	18,75,000
Shareholders' funds (₹)	31,25,000
25% of Shareholders fund (₹)	7,81,250
Buy-back price per share	₹ 20
Number of shares that can be bought back (shares)	39,062
Actual Number of shares for buy-back	25,000

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

Particulars	₹
(a) Loan funds (₹) (18,75,000 + 10,00,000 +16,50,000)	45,25,000
(b) Minimum equity to be maintained after buyback in the ratio of 2:1 (₹) (a/2)	22,62,500
(c) Present equity/shareholders fund (₹)	31,25,000
(d) Future equity/shareholders fund (₹) (see W.N.) (31,25,000 – 2,87,500)	28,37,500
(e) Maximum permitted buy-back of Equity (₹) [(d) – (b)]	5,75,000
(f) Maximum number of shares that can be bought back @ ₹ 20 per share	28,750 shares
(g) Actual Buy-Back Proposed	25,000 Shares

Summary statement determining the maximum number of shares to be bought back

Particulars	Number of shares
Shares Outstanding Test	31,250
Resources Test	39,062
Debt Equity Ratio Test	28,750
Maximum number of shares that can be bought back [least of the above]	28,750

Company qualifies all tests for buy-back of shares and came to the conclusion that it can buy maximum 28,750 shares on 1st April, 20X1.

However, company wants to buy-back only 25,000 equity shares @ ₹ 20. Therefore, buy-back of 25,000 shares, as desired by the company is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

Particulars		Debit (₹)	Credit (₹)
(a) Equity shares buy-back account	Dr.	5,00,000	
To Bank account			5,00,000
(Being buy-back of 25,000 equity shares of ₹ 10 each @ ₹ 20 per share)			
(b) Equity share capital account	Dr.	2,50,000	
Securities premium account	Dr.	2,50,000	
To Equity shares buy-back account			5,00,000
(Being cancellation of shares bought back)			
(c) Revenue reserve account	Dr.	2,50,000	
To Capital redemption reserve account			2,50,000
(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)			

Balance Sheet of M/s. Competent Ltd.

as at 31st March, 20X1

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	10,00,000
	B	Reserves and Surplus	2	16,25,000
2		**Non-current liabilities**		
		Long term borrowings	3	28,75,000
3		Current liabilities		
	A	Other Current Liabilities		16,50,000
		Total		**71,50,000**
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	4	46,50,000
2		**Current assets**		
	A	Other Current Assets (30,00,000 –5,00,000)		25,00,000
		Total		**71,50,000**

Notes to accounts

No.	Particulars		₹
1	**Share Capital**		
	Authorized, issued and subscribed capital:		
	Equity share capital (fully paid up shares of ₹ 10 each)		10,00,000
2	**Reserves and Surplus**		
	Profit and Loss A/c		1,25,000
	Revenue reserves	15,00,000	
	Less: Transfer to CRR	(2,50,000)	12,50,000

	Securities premium	2,50,000	
	Less: Utilization for share buy-back	(2,50,000)	-
	Capital Redemption Reserves		2,50,000
	Total		16,25,000
3	**Long term borrowings**		
	14% Debentures	18,75,000	
	Unsecured Loans	10,00,000	
	Total		28,75,000
4	**Property, plant and equipment**		
	Land and Building		19,30,000
	Plant and machinery		18,00,000
	Furniture and fitting		9,20,000
	Net carrying value		46,50,000

Working Note:

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Then

$(31,25,000 - x) - 22,62,500 = y$ (1)

$(y/20 \times 10) = x$ or $2x = y$ (2)

by solving the above equation, we get

$x = ₹2,87,500$

$y = ₹ 5,75,000$

Question 13 (PYQ Nov'23) NB Pg. No.

The following is the extract of Balance Sheet of Yellow Limited as on 31.03.2023:

	₹
4,00,000 Equity shares of ₹ 10 each	40,00,000
General Reserve	48,00,000
Profit & Loss Account	10,00,000
Securities Premium	18,00,000
Secured Loans	60,00,000
Unsecured Loans	32,00,000
Current Liabilities	28,00,000
	2,36,00,000
Property, Plant and Equipment	90,00,000
Investments	18,00,000
Current Assets	1,28,00,000
	2,36,00,000

The company intends to buy-back 80,000 equity shares of ₹ 10 each at a premium of 150%. You are required to state whether the company can buy back equity shares.

(5 Marks)

Solution:

Determination of Buy-back of maximum no. of shares as per the Companies Act, 2013

1. **Shares Outstanding Test**

Particulars	**(Shares)**
Number of shares outstanding	4,00,000
25% of the shares outstanding	1,00,000

2. **Resources Test: Maximum permitted limit 25% of Equity paid up capital + Free Reserves**

Particulars	
Paid up capital (₹)	40,00,000
Free reserves (₹) (48,00,000 + 18,00,000 + 10,00,000)	76,00,000
Shareholders' funds (₹)	1,16,00,000
25% of Shareholders fund (₹)	29,00,000
Buy-back price per share	₹ 25
Number of shares that can be bought back (shares)	1,16,000
Actual Number of shares for buy-back	80,000

3. **Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back**

Debt Equity ratio of the company should not exceed 2:1 after such buy-back. In this case, the debt is ₹ 92,00,000 (60,00,000 + 32,00,000)* and equity after such buy back will be ₹ 96,00,000 (1,16,00,000 – 20,00,000). Thus, the debt equity ratio is 0.96:1, which is less than 2:1.

Company qualifies all tests for buy-back of shares and came to the conclusion that it can buy 80,000 equity shares @ ₹ 25.

Question 14 NB Pg. No.

Perrotte Ltd. (a non-listed company) has the following Capital Structure as on 31.03.20X1:

	Particulars	(₹ in crores)	
(1)	Equity Share Capital (Shares of ₹ 10 each fully paid)	-	330
(2)	Reserves and Surplus		
	General Reserve	240	-
	Securities Premium Account	90	-
	Profit & Loss Account	90	-
	Infrastructure Development Reserve	180	600
(3)	Loan Funds	-	1,800

The Shareholders of Perrotte Ltd., on the recommendation of their Board of Directors, have approved on 12.09.20X1 a proposal to buy-back the maximum permissible number of Equity shares considering the large surplus funds available at the disposal of the company.

The prevailing market value of the company's shares is ₹ 25 per share and in order to induce the existing shareholders to offer their shares for buy-back, it was decided to offer a price of 20% over market.

You are also informed that the Infrastructure Development Reserve is created to satisfy Income-tax Act requirements.

You are required to compute the maximum number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either ₹ 1,200 crores or ₹ 1,500 crores.

Assuming that the entire buy-back is completed by 09.12.20X1, show the accounting entries in the company's books in each situation.

Solution

Statement determining the maximum number of shares to be bought back

Number of shares

Particulars	When loan fund is		
	₹ 1,800 crores	₹ 1,200 crores	₹ 1,500 crores
Shares Outstanding Test (W.N.1)	8.25	8.25	8.25
Resources Test (W.N.2)	6.25	6.25	6.25
Debt Equity Ratio Test (W.N.3)	Nil	3.75	Nil
Maximum number of shares that can be bought back [least of the above]	Nil	3.75	Nil

Journal Entries for the Buy-Back
(applicable only when loan fund is ₹ 1,200 crores)

₹ in crores

	Particulars	Debit	Credit
(a)	Equity share buy-back account Dr. To Bank account (Being buy-back of 3.75 crores equity shares of ₹ 10 each @ ₹ 30 per share)	112.5	112.5
(b)	Equity share capital account Dr. Securities premium account Dr. To Equity share buy-back account (Being cancellation of shares bought back)	37.5 75	112.5
(c)	General reserve account Dr. To Capital redemption reserve account (Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out of redeemed through free reserves)	37.5	37.5

Working Notes:

1. **Shares Outstanding Test**

Particulars	(Shares in crores)
Number of shares outstanding	33
25% of the shares outstanding	8.25

2. **Resources Test**

Particulars	
Paid up capital (₹ in crores)	330
Free reserves (₹ in crores)	420
Shareholders' funds (₹ in crores)	750

25% of Shareholders fund (₹ in crores)	₹ 187.5 crores
Buy-back price per share	₹ 30
Number of shares that can be bought back (shares in crores)	6.25 crores shares

3. **Debt Equity Ratio Test**

	Particulars	When loan fund is		
		₹ 1,800 crores	₹ 1,200 crores	₹ 1,500 crores
(a)	Loan funds (₹ in crores)	1,800	1,200	1,500
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹ in crores)	900	600	750
(c)	Present equity shareholders fund (₹ in crores)	750	750	750
(d)	Future equity shareholder fund (₹ in crores) (See Note 2)	N.A.	712.5 (750–37.5)	N.A.
(e)	Maximum permitted buy-back of Equity (₹ in crores) [(d) – (b)] (See Note 2)	Nil	112.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share (shares in crores) (See Note 2)	Nil	3.75 (by simultaneous equation)	Nil

Note:

1. Under Situations 1 & 3 the company does not qualify for buy-back of shares as per the provisions of the Companies Act, 2013.

2. As per section 68 of the Companies Act, 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserve after such buy-back. In the question, it is stated that the company has surplus funds to dispose of therefore, it is presumed that buy-back is out of free reserves or securities premium and hence a sum equal to the nominal value of the share bought back shall be transferred to Capital Redemption Reserve (CRR). Utilization of CRR is restricted to issuance of fully paid-up bonus shares only. It means CRR is not available for distribution as dividend. Hence, CRR is not a free reserve. Therefore, for calculation of future equity i.e. share capital and free reserves, amount transferred to CRR on buy-back has to be excluded from present equity.

   Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

   Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

   Then

   Equation 1: (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained= Maximum permissible buyback of equity

   $(750 - x) - 600 = y$ (1)

   Since $150 - x = y$

   Equation 2: $\left(\dfrac{\text{Maximum buy-back}}{\text{Offer price for buy-back}} \text{ X Nominal Value}\right)$

   = Nominal value of the shares bought -back to be transferred to CRR

   Equation 2: $\left(\dfrac{y}{30} \times 10\right) = x$

[here (30 = 25% x 120]

Or $3x = y$ (2)

by solving the above two equations we get

x = ₹ 37.5 crores

y = ₹ 112.5 crores

NB Pg. No.

Question 15 (PYQ May'22)

Quick Ltd. has the following capital structure as on 31st March,2021:

		₹ in Crores	
(1)	Share Capital:		462
	(Equity Shares of ₹ 10 each, fully paid)		
(2)	Reserves and Surplus:		
	General Reserve	336	
	Securities Premium Account	126	
	Profit and Loss Account	126	
	Statutory Reserve	180	
	Capital Redemption Reserve	87	
	Plant Revaluation Reserve	33	888
(3)	Loan Funds:		
	Secured	2,200	
	Unsecured	320	2,520

On the recommendations of the Board of Directors, on 16th September, 2021, the shareholders of the company have approved a proposal to buy-back of equity shares. The prevailing market value of the company's share is ₹ 20 per share and in order to induce the existing shareholders to offer their shares for buy-back, it was decided to offer a price of 50% over market value. The company had sufficient balance in its bank account for the buy-back of shares. You are required to compute the maximum number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either ₹ 1,680 Crores or ₹ 2,100 Crores; Assuming that the entire buy-back is completed by 31st December,2021, Pass the necessary accounting entries (narrations not required) in the books of the company in each situation.

(10 Marks)

Solution:

Statement determining the maximum number of shares to be bought back Number of shares

Particulars	When loan fund is		
	₹ 2,520 crores	₹ 1,680 crores	₹ 2,100 crores
Shares Outstanding Test (W.N.1)	11.55	11.55	11.55
Resources Test (W.N.2)	8.75	8.75	8.75
Debt Equity Ratio Test (W.N.3)	Nil	5.25	Nil
Maximum number of shares that can be bought back [least of the above]	Nil	5.25	Nil

Journal Entries for the Buy-Back (applicable only when loan fund is ₹ 1,680 crores)

₹ in crores

	Particulars	Debit	Credit
(a)	Equity share buy-back account Dr.	157.5	
	To Bank account		157.5
(b)	Equity share capital account (5;25 x ₹ 10) Dr.	52.5	
	Securities premium account (5;25 x ₹ 20) Dr.	105	
	To Equity share buy-back account		157.5
(c)	General reserve account Dr.	52.5	
	To Capital redemption reserve account		52.5

Working Notes:

1. **Shares Outstanding Test**

Particulars	(Shares in crores)
Number of shares outstanding	46.2
25% of the shares outstanding	11.55

2. **Resources Test**

Particulars	
Paid up capital (₹ in crores)	462
Free reserves (₹ in crores) (336+126+126)	588
Shareholders' funds (₹ in crores)	1,050
25% of Shareholders fund (₹ in crores)	₹ 262.5 crores
Buy-back price per share	₹ 30
Number of shares that can be bought back (shares in crores)	8.75 crores shares

3. **Debt Equity Ratio Test**

	Particulars	When loan fund is		
		₹ 2,520 crores	₹ 1,680 crores	₹ 2,100 crores
(a)	Loan funds (₹ in crores)	2,520	1,680	2,100
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (₹ in crores)	1,260	840	1,050
(c)	Present equity shareholders fund (₹ in crores)	1,050	1,050	1,050
(d)	Future equity shareholder fund (₹ in crores) (See Note 2)	N.A.	997.5 (1,050–52.5)	N.A.
(e)	Maximum permitted buy-back of Equity (₹ in crores) [(d) – (b)] (See Note 2)	Nil	157.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share (shares in crores) (See Note 2)	Nil	5.25 (by simultaneous equation)	Nil

Note:

1) Under Situations 1 & 3 the company does not qualify for buy-back of shares as per the provisions of the Companies Act, 2013.

2) As per section 68 of the Companies Act, 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserve after such buy-back. Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method. Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'; Then Equation 1: (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained= Maximum permissible buy-back of equity

(1,050 –x)-840 = y

Since 210 – x = y

$$\text{Equation 2} = \left[\frac{\text{Maximum buy -back}}{\text{Offer price for buy -back}} \text{ X Nominal Value}\right]$$

= Nominal value of the shares bought –back to be transferred to CRR

$$= \frac{y}{30} \text{ X } 10$$

Or   3x = y   (2)

by solving the above two equations we get

x = ₹ 52;5 crores y = ₹ 157;5 crores

3) Statutory reserves, capital redemption reserve and plant revaluation reserves are not free reserves.

4) For calculation of debt -equity ratio both secured and unsecured loans have been considered.

Question 16 (PYQ Dec'21)

NB Pg. No.

Mohan Ltd. furnishes the following summarised Balance Sheet on 31st March 2021. (₹ in Lakhs)

	Amount
Equity and Liabilities:	
Shareholders' fund	
Share Capital	
Equity Shares of ₹ 10 each fully paid up 6%	780
Redeemable Preference shares of ₹ 50 each fully Paid up	240
Reserves and Surplus	
Capital Reserves	58
General Reserve	625
Securities Premium	52
Profit & Loss	148
Revaluation Reserve	34
Infrastructure Development Reserve	16
Non-current liabilities	
7% Debentures	268
Unsecured Loans	36
Current Liabilities	395
	2652

Assets:	
Non-current Assets	
Plant and Equipment less depreciation	725
Investment at cost	720
Current Assets	1207
	2652

Other Information:

1) The company redeemed preference shares at a premium of 10% on 1st April,2021.
2) It also offered to buy back the maximum permissible number of equity shares of ₹ 10 each at ₹ 30 per share on 2nd April 2021.
3) The payment for the above was made out of available bank balance, which appeared as a part of the current assets.
4) The company had investment in own debentures costing ₹ 60 lakhs (face value ₹ 75 lakhs). These debentures were cancelled on 2nd April 2021.
5) On 4th April 2021 company issued one fully paid-up equity share of ₹ 10 each by way of bonus for every five equity shares held by the shareholders.

You are required to:

a) Calculate maximum possible number of equity shares that can be bought back as per the Companies Act, 2013 and
b) Record the Journal Entries for the above-mentioned information. **(10 Marks)**

Solution:

(a) (i) Statement determining the maximum number of shares to be bought back

Number of shares (in lakhs)

Particulars	When loan fund is ₹ 304 lakhs'
Shares Outstanding Test (W.N.1)	19.5
Resources Test (W.N.2)	11.175
Debt Equity Ratio Test (W.N.3)	29.725
Maximum number of shares that can be bought back [least of the above]	11.175

Thus, the company can buy 11,17,500 Equity shares at ₹ 30 each.

Working Notes:

1. Shares Outstanding Test

Particulars	(Shares in lakh)
Number of shares outstanding	78
25% of the shares outstanding	19.5

2. Resources Test

Particulars	
Paid up capital (₹ in lakh)	780
Free reserves (₹ in lakh) (625+52+148−24−240*)	561
Shareholders' funds (₹ in lakh)	1341
25% of Shareholders fund (₹ in lakh)	335.25

Buy-back price per share	30
Number of shares that can be bought back	11.175
*Amount transferred to CRR is excluded from free reserves.	
Premium on redemption also reduced.	

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	₹ In lakh
(a)	Loan funds (₹)	304
(b)	Minimum equity to be maintained after buyback in the ratio of 2:1 (₹) (a/2)	152
(c)	Present equity shareholders fund (₹)	1341
(d)	Future equity shareholders fund (₹) (see W.N.4)	1043.75 (1341–297.25)
(e)	Maximum permitted buy-back of Equity (₹) [(d) – (b)]	891.75
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share	29.725
	As per the provisions of the Companies Act, 2013, company	Qualifies

Alternatively, when current liabilities are considered as part of loan funds, in that case Debt Equity Ratio

Test will be done as follows:

Particulars	₹ in lakh
(a) Loan funds (₹)	699
(b) Minimum equity to be maintained after buyback in the ratio of 2:1 (₹) (a/2)	349.5
(c) Present equity shareholders fund (₹)	1341
(d) Future equity shareholders fund (₹) (see W.N.4)	1093.125 (1341-247.875)
(e) Maximum permitted buy-back of Equity (₹) [(d) – (b)]	743.625
(f) Maximum number of shares that can be bought back @ ₹ 30 per share	24.7875
As per the provisions of the Companies Act, 2013, company	Qualifies

4. Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method

Suppose amount transferred to CRR account is 'x' and maximum permitted buy- back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR) – Minimum Equity to be maintained = Maximum Permitted Buy-Back

$= (1341 - x) - 152 = y$

$= 1189 - x = y$ (1)

Equation 2: Maximum Permitted Buy-Back x Nominal Value Per Share/Offer Price Per Share

$y/30 \times 10 = x$ or $3x = y$ (2)

by solving the above two equations we get x = ₹ 297.25 and y = ₹ 891.75

Alternatively, when current liabilities are considered as part of loan funds, in that case

Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted

Buy-Back

$= (1341 - x) - 349.5 = y$

$= 991.5 - x = y$ (1)

Equation 2: Maximum Permitted Buy-Back X Nominal Value Per Share/Offer Price Per Share

$y/30 \times 10 = x$ or $3x = y$ (2)

by solving the above two equations we get $x = 247.875$ and $y = 743.625$

(ii) **Journal Entries for Buy Back (₹ in lakhs)**

Date	Particulars		Debit	Credit
2021 1st April	6% Redeemable preference share capital A/c	Dr.	240	
	Premium on redemption of preference shares A/c.	Dr	24	
	To Preference shareholders A/c			264
	6% Redeemable preference share capital A/c	Dr.	240	
	Premium on redemption of preference shares A/c.	Dr	24	
	To Preference shareholders A/c			264
	(Being premium on redemption of preference shares adjusted through securities premium)			
2nd April	Equity shares buy-back A/c	Dr.	335.25	
	To Bank A/c			335.25
	(Being 11.175 lakhs equity shares of ₹ 10 each bought back @ ₹ 30 per share)			
	Equity share capital A/c	Dr.	111.75	
	Securities Premium A/c.	Dr	52	
	General Reserve or P&L A/c	Dr.	171.50	
	To Equity Shares buy-back A/c			335.25
	(Being cancellation of shares bought back)			
	General reserve A/c.	Dr	351.75	
	To Capital redemption reserve A/c			351.75
	(Being creation of capital redemption reserve account to the extent of the face value of preference shares redeemed and equity shares bought back as per the law ie. 240+ 111.75 lakhs)			
2nd April	7% Debentures A/c.	Dr	75	
	To Investment (own debentures) A/c			60
	To Profit on cancellation of own debentures A/c			15

	(Being cancellation of own debentures costing ₹ 60 lakhs, face value being ₹ 75 lakhs and the balance being profit on cancellation of debentures)			
4th April	Capital Redemption Reserve	Dr.	133.65	
	To Bonus Shares A/c			133.65
	(Being issue of one bonus equity share for every five equity shares held)			
	Bonus shares A/c	Dr.	133.65	
	To Equity share capital A/c			133.65
	(Being bonus shares issued)			

Working Note: Bonus Share to be issued =66.825 (78 – 11.175) lakh shares divided by 5 = 13.365 lakh shares.

Note: *Securities premium has not been utilized for the purpose of premium payable on redemption of preference shares assuming that the company referred in the question is governed by Section 133 of the Companies Act, 2013 and complies with the Accounting Standards prescribed for them. Alternative entry considering otherwise is also possible by utilizing securities premium amount.

Question 17 (PYQ May'23) **NB Pg. No.**

What are the conditions to be fulfilled by a Joint Stock Company to buy-back its equity shares as per Companies Act, 2013? Explain in brief. **(5 Marks)**

Solution:

Section 68 to 70 of the Companies Act, 2013 lays down the provisions for a company to buy-back its own equity shares. For details, refer para 1.1 and 1.2 of the chapter