



CA INTERMEDIATE

MARATHON

Advanced Accounting

BuyBack of Securities

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BUYBACK OF SECURITIES

"You can't go back and change the beginning, but you can start where you are and change the ending."

Meaning:

Buyback means purchase of its own shares by a company. When shares are bought back by a company they have to be cancelled by the company. Thus, shares bought back results in decrease in share capital of the company. A company having sufficient cash may decide to buyback its own shares.

Objectives/Advantages of Buyback:

- To increase Earning per share if there is no dilution in company's earnings as the buyback of shares reduces the outstanding number of shares.
- To increase promoters holding as the shares bought back are cancelled & also discourage others to make hostile bid to takeover the company (i.e. to eliminate threats by shareholders who are looking for a controlling stake)
- To support the share price on the stock exchange when the share price in the opinion of company management is less than its worth, especially in depressed market (i.e. to take the advantage of undervaluation. For instance, if a company is undervalued due to any microeconomic & macroeconomic reason, it buys its shares back at the current market price & issues those later when the prices go up)
- To pay surplus cash to the shareholders when the company does not need it for the business.

Earnings = ↑↑
No. of shares ↓

Basic Conditions:

Section 68 (2) further states that no company shall purchase its own shares or other specified securities unless—

- the buy-back is authorised by its articles
 - a special resolution has been passed in general meeting of the company authorizing the buy-back
- Exception:** In case the buy back is upto 10% of paid up equity + free reserves, the same may be done with the authorization of the Board Resolution
- There shall be a minimum gap of 1 year in buyback offer from the date of closure of the previous buy back
 - All the shares or other specified securities for buy-back are fully paid-up
 - Every buy-back shall be completed within 12 months from the date of passing the special resolution, or the resolution passed by the board of directors.

FV = 100 MP = 200 → 500
300

The buy-back may be—

- from the existing security holders on a proportionate basis; or
- from the open market; or
- by purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity.

As per Section 68 (1) of the Companies Act 2013, buy back of shares can be made out of: its free reserves; or securities premium account; or proceeds of any shares or other specified securities.

Provided that no buyback 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 other specified securities

JOURNAL ENTRIES

No.	Particulars	Journal Entry
1.	To make <u>partly paid</u> equity shares <u>fully paid up</u>	Equity Share Final Call A/c Dr. To Equity Share Capital A/c Bank A/c Dr. To Equity Share Final Call A/c
2.	To realize investments to provide <u>cash</u> for buyback	Bank A/c Dr. 95000 110000 P&L A/c (Loss) Dr. 5000 To Investments A/c 100000 To P&L A/c (Profit) 10000
3.	To issue <u>Preference</u> shares	Bank A/c Dr. To Preference Share Capital A/c To Securities Premium A/c
4.	To cancel the shares bought back	Equity Share Capital A/c Dr. (FV) 10 Premium on Buyback A/c Dr. 25 To Equity Share Buyback A/c / ESH 35 Equity Share Buyback A/c Dr. 35 To Bank A/c 35
5.	For closing (write off) the <u>premium on buyback</u> account	Securities Premium A/c Dr. 25 General (Revenue) Reserve/ P&L A/c Dr. 25 To Premium on Buyback A/c 25
6.	Transfer to CRR (Capital Redemption Reserve)*	General (Revenue) Reserve A/c Dr. 25 P&L A/c Dr. 25 Free Reserve (any) A/c Dr. 25 To CRR A/c 25

If Ques. specifies

FV = 10
MP = 30
BB = 35
cancel due

compliance

Sec. Item ✓
↓
ICAI do not consider

***Note:** CRR can be utilized for issuing fully paid bonus shares to its members.

Face Value of Equity Shares bought back	XX
Less: Face Value of shares issued	(XX)
Amount to be transferred to CRR	XX

Free Reserves: Those reserves which are available for distribution of dividend.

Examples:

- Surplus/ P&L A/c
- General/Revenue Reserve
- Dividend Equalisation Reserve
- Any other free reserve

Note:

- ❖ Securities Premium, Revaluation Reserve, Capital Reserve, CRR, DRR etc. are not free reserves.
- ❖ For the purpose of Buyback, Free reserves includes Securities Premium

Question 1: Inter Jan 2025 (4 Marks)

Following information are available in respect of Z Limited as on 31st March, 2024:

→	4,00,000 Equity share capital of ₹10 each	₹ 40,00,000
	Capital Reserve	₹ 20,000
→	Revenue Reserve	₹ 50,00,000
	Securities Premium	₹ 6,00,000
→	Profit and Loss Account	₹ 19,00,000
	Investments	₹ 40,00,000

The company decides to buy back 20% of its Equity capital @ ₹15 per share on 1st April, 2024. Buy back is as per provisions of the Companies Act and company passed the necessary resolutions for it. For this purpose, it sold its investments of ₹ 40 lakhs for ₹ 32 lakhs. You are required to pass the necessary journal entries.

$$4L \times 20\% = 80000 \text{ shares}$$

Solution

In the books of Z Limited
Journal Entries

	Particulars		(₹)	(₹)
1)	Bank A/c	Dr.	32,00,000	
	Profit & Loss A/c (Loss on sale)	Dr.	8,00,000	
	To Investments			40,00,000
	(Being investment sold for the purpose of buy-back of Equity Shares)			
2)	Equity share capital A/c (80000 x 15)	Dr.	8,00,000	
	Premium payable on buy-back A/c (5)	Dr.	4,00,000	
	To Equity shares buy-back A/c (15)			12,00,000
	(Being the amount due on buy-back of equity shares)			
3)	Equity shares buy-back A/c	Dr.	12,00,000	
	To Bank A/c			12,00,000
	(Being payment made for buy-back of equity shares)			
4)	Securities Premium A/c	Dr.	4,00,000	
	To Premium payable on buy-back			4,00,000
	(Being premium payable on buy-back charged from Securities premium)			
5)	Revenue Reserve / Profit & Loss A/c	Dr.	8,00,000	
	To Capital Redemption Reserve A/c			8,00,000
	(Being creation of capital redemption reserve to the extent of the equity shares bought back)			

Question 2: Inter Nov 2019 (15 Marks) / RTP Nov 2021

X Ltd. furnishes the following summarized Balance Sheet as at 31-03-2021.

	Amount (in ₹)	
Equity & Liabilities		
Share Capital:		
Equity Shares of ₹ 20 each fully paid up (2.50L x 20)	50,00,000	
10,000, 10% Preference Shares of ₹ 100 each fully paid up	10,00,000	60,00,000
Reserves and surplus:		
Capital Reserve	1,00,000	
Securities premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and loss account	20,00,000	
Dividend Equalization Fund	5,50,000	43,50,000
Non-Current Liabilities		
12% Debentures		12,50,000
Current Liabilities and Provisions		5,50,000
		1,21,50,000
Assets		
Non Current Assets		
Property, Plant & Equipment & Intangible Assets		
Property, Plant & Equipment		1,00,75,000
Current assets		
Investment	3,00,000	
Inventory	2,00,000	
Cash & Bank	15,75,000	20,75,000
		1,21,50,000

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

- (1) Buy back 25% of the paid up capital and it was decided to offer a price of 20% over market price. The prevailing market value of the company's share is ₹ 30 per share.
- (2) To finance the buy-back of shares, company:
 - (a) Issues 3000, 14% debentures of ₹ 100 each at a premium of 20%.
 - (b) Issues 2500, 10% preference shares of ₹ 100 each.
- (3) Sell investment worth ₹ 1,00,000 for ₹ 1,50,000.
- (4) Maintain a balance of ₹ 2,00,000 in Revenue Reserve.
- (5) Later the company issue three fully paid up equity share of ₹ 20 each by way of bonus share for every 15 equity share held by the equity shareholders.

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

$$250000 - 62500 = 187500$$

$$\times \frac{3}{15}$$

$$\text{Bonus} = 37500$$

$$\times 20 = 750000$$

Solution

In the books of X Limited
Journal Entries

S.No.	Particulars	L.F.	Debit	Credit
1.	Bank A/c Dr.		3,60,000	
	To 14 % Debenture A/c	(3000 x 100)		3,00,000
	To Securities Premium A/c	(3000 x 20)		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	(2500 x 100)		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	(P&L)		50,000
	(Being investment sold on profit)			
4.	Equity share capital A/c (62,500 x 20) Dr.		12,50,000	
	Premium on BuyBack 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 amount due to equity shareholders on buy back)			
5.	Securities Premium A/c Dr.		10,00,000	
	To Premium on Buyback A/c			10,00,000
	(Being premium on buyback written off)			
6.	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)			
7.	Revenue Reserve Dr.	(5L-2L)	3,00,000	
	Profit and Loss A/c Dr.	(8.5L)	7,00,000	
	To Capital redemption reserve A/c*			10,00,000
	(Being CRR created) [12,50,000 less 2,50,000]			
8.	Capital redemption reserve A/c Dr.		7,50,000	
	To Bonus to shareholder A/c (W.N.1)			7,50,000
	(Being the utilization of capital redemption reserve to issue 37,500 bonus shares)			
9.	Bonus to shareholder A/c Dr.		7,50,000	
	To Equity share capital A/c			7,50,000
	(Being issue of 3 bonus share for every 15 shares held)			

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

Particulars	Notes	Amount
Equity and Liabilities		
1 Shareholders' funds		
Share capital	1	57,50,000
Reserves and Surplus	2	27,10,000
2 Non-Current liabilities		
Long-term borrowings	3	15,50,000
3 Current liabilities		
Trade Payables		-
Current Liabilities & Provisions		5,50,000
Total		1,05,60,000

Assets		
1	Non-current assets	
	Property, Plant and Equipment & Intangible Asset	
	Property, Plant & Equipment	1,00,75,000
2	Current assets	
	Investments	2,00,000
	Inventory	2,00,000
	Cash and cash equivalent	85,000
	Total	1,05,60,000

Notes to accounts

	Amount
1	Share Capital
	Equity share capital (2,25,000 Fully paid up shares of 20 Each) (2,50,000-62,500+37,500 shares) (62,500 equity shares bought back) (37,500 shares issued by way of bonus)
	10% preference shares @ 100 each(10,00,000 + 2,50,000)
	57,50,000
2	Reserves and Surplus
	Capital Reserve
	Revenue reserve
	Securities premium 12,00,000
	Add: Premium on debenture 60,000
	Less: Adjustment for premium paid on buy back (10,00,000)
	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)
	Profit & Loss A/c 20,00,000
	Add: Profit on sale of investment 50,000
	Less: Transfer to CRR (7,00,000)
	Dividend equalization reserve
	27,10,000
3	Long-term borrowings - 12% Debentures 12,50,000
	- 14% Debentures 3,00,000
	15,50,000

Working Notes:

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

Particulars	Amount
Cash balance as on 31.3.2021	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: Buyback of Equity Shares	(22,50,000)
	85,000

Three Test Conditions

Whether BB is permissible as per Co's Act or
Maximum BB

1. Shares Outstanding Test:

Maximum Limit of number of equity shares to be bought back = 25% of total Equity shares

2. Resource Test:

Maximum Limit of Amount of bought back = 25% of (Paid up capital & Free reserves)

No. of shares = Amount calculated above / Buyback Price

incl. Sec. Premium

3. Debt Equity Ratio Test:

Debt Equity ratio must not be > 2:1 after buyback

i.e. Debt : Equity <= 2 : 1 after buyback

Minimum Equity after buyback = Debt / 2

Present Equity = Paid up capital + Free Reserves (Refer Test 2)

Find no. of shares by making simultaneous equations **OR**

No. of Shares = (Present Equity - Minimum Equity) / (Buyback price + Face value)

$$\frac{\text{Debt}}{\text{Equity}} \leq \frac{2}{1} \text{ (After BB)}$$

$$\frac{\text{Debt}}{2} \leq \text{Equity}$$

$$\text{Equity} \geq \frac{\text{Debt}}{2}$$

where

Debt = Secured + Unsecured Debt (both long term & short term)

Equity = Paid up Capital + Free Reserves

↳ STB, OLL

Number of Shares to be bought back = Lower of above 3 tests

current liab. → Assumption
Can be included / excluded

Question 3: Inter Sep 2024 (7 Marks)

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

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

On 1st April, 2024 the company wants to buy back 14,000 equity shares of ₹ 10 each at ₹ 30 per Equity share. Buy Back of shares is duly authorized by its articles and necessary resolution has been passed by the company. You are required to calculate maximum permissible number of equity shares that can be bought back.

Solution

Statement determining the maximum number of shares to be bought back

Particulars	Number of shares (in thousands)
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	₹ (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	₹ 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	₹ in thousands
(a) Loan funds	2,000
(b) Minimum equity to be maintained after buy-back in ratio of 2:1 (a/2)	1,000
(c) Present equity shareholders fund (₹)	1,440
(d) Future equity shareholders fund (₹) (see W.N.4) (1,440-110)	1,330
(e) Maximum permitted buy-back of Equity (₹) [(d) - (b)]	330
(f) Maximum no. of shares that can be bought back @ ₹ 30 per share	11,000 shares

Minimum Equity after 30 = $\frac{2000}{2} = 1000$
 Present Equity = 1440

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

Suppose amount transferred to CRR 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

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

$$= 440 - x = y \quad (1)$$

$$1440 - x - y = 1000$$

$$x + y = 440$$

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

$$y/30 \times 10 = x \quad \text{or}$$

$$3x = y \quad (2)$$

$$3x = y$$

by solving the above two equations we get

$$x = ₹ 110 \text{ thousands} \qquad y = ₹ 330 \text{ thousands}$$

$$\text{No.} = \frac{110}{10} = 11$$

$$\text{or } \frac{330}{30} = 11$$

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

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

$$\frac{1440 - 1000}{30 + 10} = 11$$

↓ ↓
 BB FV

Question 4: Inter May 2023 (10 Marks)

VIJ Ltd. has the following capital structure as on 31st March, 2022:

Particulars	(₹ in Lakhs)
Equity share capital (Shares of ₹ 10 each, fully paid)	990 ✓
Reserve and Surplus:	
General Reserve	720 ✓
Securities Premium Account	270 ✓
Profit & Loss Account	270 ✓
Infrastructure development Reserve ×	540
Loan Funds	1,800
	5,400 ✓

On the recommendation of the Board of Directors, the shareholders of the company have approved on 2nd September 2022 a proposal to buyback the maximum permissible number of equity shares, considering the sufficient funds available at the disposal of the company.

The current 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 value. You are also informed that the Infrastructure Development Reserve is created to satisfy income tax requirements.

You are required to compute the maximum permissible number of equity 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 ₹ 3600 lakh or ₹ 4500 lakh.

The entire buy-back is completed by 09/12/2022, show the accounting entries with full narrations in the company's books in each situation.

Solution**Statement determining the maximum number of shares to be bought back**

Particulars	When loan fund is		
	₹ 5,400 lakhs	₹ 3,600 lakhs	₹ 4,500 lakhs
Shares Outstanding Test (W.N.1)	24.75 ✓	24.75 ✓	24.75 ✓
Resources Test (W.N.2)	18.75 ✓	18.75 ✓	18.75 ✓
Debt Equity Ratio Test (W.N.3)	Nil ✓	11.25 ✓	Nil ✓
Maximum number of shares that can be bought back [least of the above]	Nil ✓	11.25 ✓	Nil ✓

Working Notes:**1. Shares Outstanding Test**

Particulars	(Shares in lakhs)
Number of shares outstanding	99
25% of the shares outstanding	24.75 ✓

2. Resource Test

Particulars	₹
Paid up capital (₹ in lakhs)	990 ✓
Free reserves (₹ in lakhs) (720+270+270)	1260 ✓
Shareholders' funds (₹ in lakhs)	2250
25% of Shareholders fund (₹ in lakhs)	₹ 562.5 lakhs ✓
Buy-back price per share	₹ 30 ✓
Number of shares that can be bought back (shares in lakhs)	18.75 lakhs shares ✓

$$\frac{2250 - 1800}{30 + 10} = \frac{450}{40} = 11.25$$

3. Debt Equity Ratio Test

*Debt
2*

	Particulars	When loan fund is (all ₹ are in lakhs)		
		5,400	3,600	4,500
(a)	Loan funds	5400	3600	4500
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1	2700	1800	2250
(c)	Present equity shareholders fund	2250	2250	2250
(d)	Future equity shareholder fund	N.A.	2137.5(2250-112.5)	N.A.
(e)	Maximum permitted buy-back of Equity [(d) – (b)]	Nil	337.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ ₹ 30 per share (shares in lakhs) (See Working Note)	Nil	11.25 (by simultaneous equation)	Nil

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

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 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

$$(2250 - x) - 1800 = y \quad (1)$$

Since $450 - x = y$

Equation 2: (Maximum Buy-back/Offer Price for Buy-back x Nominal Value)

$$= \text{Nominal value of the shares bought back to be transferred to CRR}$$

$$= (y/30 \times 10) = x \quad \text{Or}$$

$$= 3x = y \quad (2)$$

By solving the above two equations we get

$$x = ₹ 112.5 \text{ lakhs} \quad y = ₹ 337.5 \text{ lakhs}$$

Journal Entries for the Buy-Back (applicable only when loan fund is ₹ 3,600 lakhs)

₹ in lakhs

	Particulars		Debit	Credit
(a)	Equity share capital account <i>11.25 x 10</i>	Dr.	112.50	
	Premium payable on buy-back <i>x 20</i>	Dr.	225.00	
	To Equity share buy-back account <i>30</i>			337.5
	(Being cancellation of shares bought back)			
(b)	Securities Premium A/c	Dr.	225.00	
	To Premium payable on buy-back			225.00
	(Being premium payable on buy-back written off)			
(c)	Equity share buy-back account	Dr.	337.50	
	To Bank account			337.50
	(Being buy-back of 11.25 lakhs shares @ ₹ 30 per share)			
(d)	General reserve account	Dr.	112.50	
	To Capital redemption reserve account			112.50
	(Being transfer of free reserves to CRR to the extent of nominal value of share capital bought back)			

$$\left. \begin{array}{l} \text{Cap.} = 990 - 112.50 = 877.5 \\ \text{GR} = 720 - 112.50 = 607.5 \\ \text{S.P.A.} = 270 - 225 = 45 \\ \text{P.L.} = 270 \end{array} \right\} \Rightarrow 1800$$

Question 5: Inter Dec 2021 (10 Marks)

Mohan Ltd. furnishes the following summarised Balance Sheet as on 31st March 2021,

	Amount (₹ in Lakhs)
Equity & Liabilities:	
Shareholder's Fund	
Share Capital	
Equity Shares of 10 each fully paid up →	780
6% Redeemable Preference shares of 50 each fully paid up	240
Reserve & Surplus	
Capital Reserve	58
General Reserve ✓ ✓	625
Security Premium ✓	52
Profit & Loss ✓ ✓	148
Revaluation Reserve	34
Infrastructure Development Reserve ↗	16
Non Current Liabilities	
7% Debentures]	268
Unsecured Loans]	36
Current Liabilities →	395
Total	2652
Assets :	
Non Current Assets	
Plant and Equipment less depreciation	725
Investment at cost ✓	720
Current Assets	1207
Total	2652

Fr = 75

(Inv. in own cost = 60
deb) FV = 75

Other Information :

- The Company redeemed Preference shares at a premium of 10% on 1st April, 2021.
- It is also offered buyback the maximum permissible number of Equity shares of ₹10 each at ₹30 per share on 2nd April, 2021.
- The payment for the above was made out of available account balance, which appeared as a part of the current assets.
- The company had investment in own Debentures costing ₹60 lakhs (face value ₹75 lakhs). These Debenture were cancelled on 2nd April, 2021.
- 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 :

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

$$\begin{aligned}
 \text{No.} &= 78 - 11.175 = 66.825 \text{ eq. sh.} \\
 &\times \frac{1}{5} = 13.365 \text{ lakh eq. sh.} \\
 &\quad \text{of 10 each} \\
 \text{Amt.} &= 133.65
 \end{aligned}$$

Solution

(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 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

v.v Imp.

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

Mem. on redemption w/o Jfr to CRR

*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 buy-back in ratio of 2:1 (a/2)	152
(c) Present equity shareholders fund (₹)	1341
(d) Future equity shareholders fund (₹) (see W.N.4) (1341-297.25)	1043.75
(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 (304+395)
(b) Minimum equity to be maintained after buy-back in ratio of 2:1 (a/2)	349.5
(c) Present equity shareholders fund (₹)	1341
(d) Future equity shareholders fund (₹) (see W.N.4) (1341-247.875)	1093.125
(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

Loan = 304 Min. Equity after BB = 304/2 = 152 Present Eq. = 1341

No. = (1341 - 152) / (30 + 10) = 1189 / 40 = 29.725

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

Suppose amount transferred to CRR 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

$$= (1341 - x) - 152 = y \qquad \qquad \qquad = 1189 - x = y(1)$$

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

$$y/30 \times 10 = x \qquad \text{or} \qquad 3x = y(2)$$

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 fund, in that case

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

$$= (1341 - x) - 349.5 = y \qquad \qquad \qquad = 991.5 - x = y \qquad (1)$$

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

$$y/30 \times 10 = x \qquad \text{or} \qquad 3x = y(2)$$

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
1) 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
	(Being preference share capital tfd to shareholders A/c)		
2) 1st April	Preference shareholders A/c Dr.	264	
	To Bank A/c		264
	(Being payment made to shareholders)		
3) 1st April	General Reserve or P&L A/c* Dr.	24	
	To Premium on redemption of preference shares A/c		24
	(Being premium on redemption of preference shares adjusted through securities premium)		
4) 1st April	General reserve A/c Dr.	240	
	To Capital redemption reserve A/c		240
	(Being creation of capital redemption reserve to the extent of the face value of preference shares redeemed)		
5) 2nd April	Equity share capital A/c Dr.	111.75	
	Premium on Buy Back A/c Dr.	223.50	
	To Equity Shares buy-back A/c		335.25
	(Being cancellation of shares bought back)		
6) 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)		
7) 2nd April	Securities Premium A/c Dr.	52	
	General Reserve or P&L A/c Dr.	171.50	
	To Premium on BuyBack A/c		223.50
	(Being premium on buyback written off)		
8) 2nd April	General reserve A/c Dr.	111.75	
	To Capital redemption reserve A/c		111.75
	(Being creation of capital redemption reserve to the extent of the face value of equity shares bought back)		

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)			
4th April	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.

EXTRA POINT

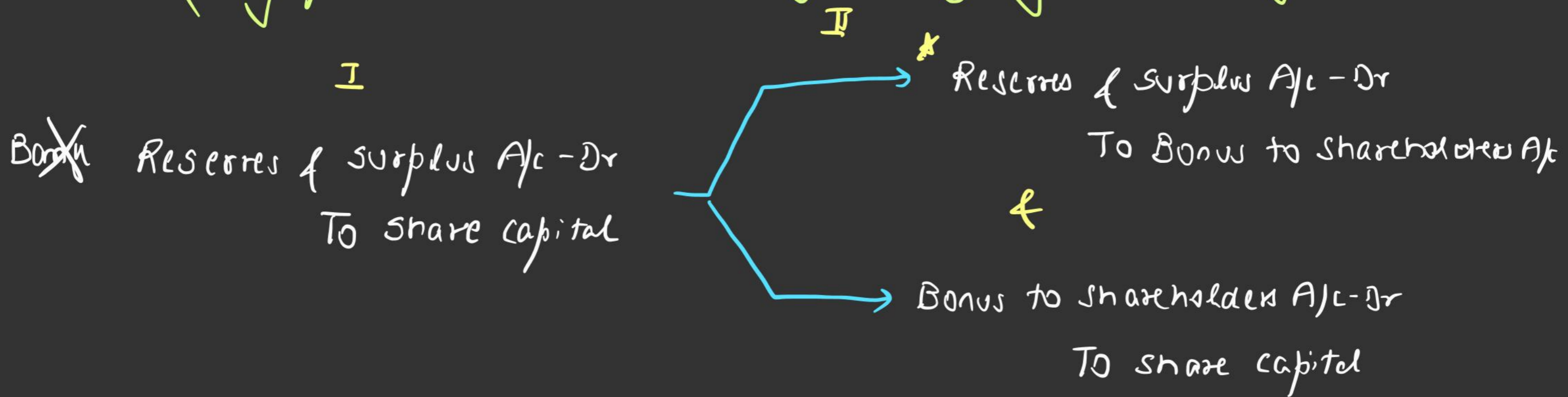
The company had 1,00,000 equity stock options outstanding on the above mentioned date, to the employees at ₹(20) when the market price was ₹(30) (This was included under current liabilities). On 1.04.2021 employees exercised their options for 50,000 shares. Face Value of Equity Share ₹ 10 each.

		(Lakhs)
Bank A/c - Dr	(50000 x 20)	10
Emp. Stock option a/c - Dr	(50000 x 10)	5
	To Eq. Share a/c (FV) (50000 x 10)	5
	To Sec. Premium A/c (Extra) (50000 x 20)	10

Bonus Issue (Sec 63)

(Issuing shares free of cost to existing shareholders)

(Fully paid Bonus shares to be given to fully paid existing shareholders)



* Reserves & surplus:

- ✓ 1) CRR
- ✓ 2) Securities Premium
- ✓ 3) Free Reserve (General Res. / PALA/c)

Redemption of Preference Shares (Sec 55)

Due

- 1) Preference Share Capital A/c - Dr
 Premium on Redemption A/c - Dr

To Preference Shareholders A/c

Payment

- 2) Preference Shareholders A/c - Dr
 To Bank A/c

Write off

- 3) * Securities Premium A/c - Dr
 PAL A/c / General Res. A/c - Dr

To Premium on Redemption A/c

Tr. to CRR

- 4) General Res. / PAL A/c - Dr
 To CRR A/c

} → Securities Premium cannot be used as per Law.

Face value of Pref. Shares redeemed	xx
- Face value of Shares issued	(xx)
	<u>xx</u>

* For Entry No-3: Write off of Premium on Redemption

Case 1: If Prescribed Co. of Financial Statements comply with AS 133.

Securities Premium cannot be used

Use General Res./ P/L A/c

Case 2: Other than Case 1

Securities Premium can be used.