



Buy Back of Securities & Equity Shares

To Capital Redemption Reserve A/c (creation of capital redemption reserve to the extent of the equity shares bought back) 600

Section - 3 - Test of Buy - Back

3.1 - Test of Buy-Back

M-444 Ltd. has the following capital structure on 31st March 2018:

Particulars	Rs. in Crores
a. Equity Share capital (Shares of Rs. 10 each)	300
b. Reserves:	
General reserve	270
Security Premium	100
Profit and Loss A/c	50
Export Reserve (Statutory reserve)	80
c. Loan Funds	1800

The shareholders have on recommendation of Board of Directors approved vide special resolution at their meeting on 10th April 2018 a proposal to buy back maximum permissible equity shares considering the huge cash surplus following A/c of one of its divisions.

The market price was hovering in the range of Rs. 25 and in order to induce existing shareholders to offer their shares for buy back, it was decided to offer a price of 20% above market.

Advice the company of (maximum number of shares) that can be bought back and record journal entries for the same assuming the buyback has been completed in full within the next 3 months, if borrowed funds were Rs. 1200 crores, and Rs. 1500 crores respectively would your answer change?

Application of tests:

Note: Solution is based on the assumption that company is not having surplus funds

Test one:

Shares Outstanding test:

Max. No. of Shares that can be bought back = 25% of 30 = 7.5 crores of shares

In this case total funds requirement shall be Rs. 7.5 crores of shares x Buy Back price per share that is Rs. 30 = Rs. 225 crores

Test Two

Resources Test:

Max. No. of shares that can be bought back = 25% of Paid up capital + free reserves

Buy back Price

25% of 300 + 270 + 100 + 50

30

= 6 crores of shares

Funds requirement in this case shall be 6 x 30 = 180 crores

Test 3

Debt Equity Ratio Test

Particulars	Situation one	Situation Two	Situation Three
a. Loan funds Rs. In crores	800	1,200	1,800
b. Minimum Equity to be maintained to keep Debt equity ratio at 2:1 Rs. In crores	400	600	900
c. Present Equity	720	720	720

Step 1: a) No of shares to be bought back = 30 cr.

b) 25% of 30 x 25% = 7.5 cr.

Step 2: 25% of SHF (2)

Paid up Capital + free Reserve

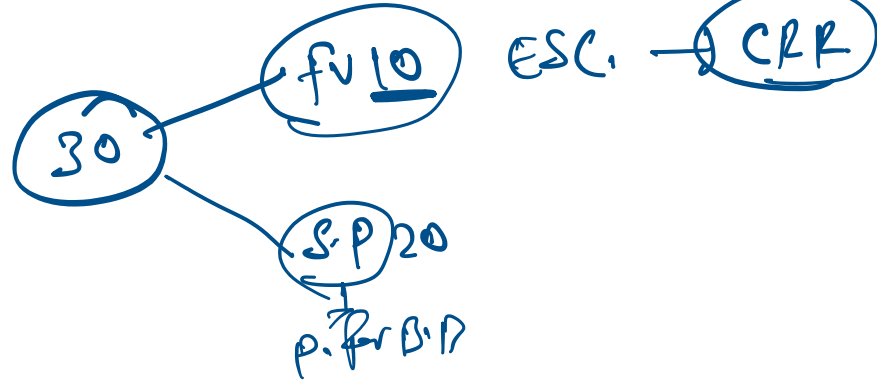
300 + 420 = 720 cr.

720 cr. x 25% = 180 cr.

B.B.P: 180 / 30 = 6

Debt - Equity Ratio: 2:1

	800	1200	1500
Debt	800	1200	1500
DE Ratio	2:1	2:1	2:1
Equity (SHF)	400	600	750
Present SHF	720	720	720
Maximum Amt for Equity (SHF)	320	120	N/A
÷ B.B.P + FV	40	40	
No of shares for B.B.	8 cr.	3 cr.	N/A



	800	1200	1500
Step 1	1	2	3
Step 2	2	2	2
Step 3	8	3	N/A
Lower	6	3	

7.5 = N.C.L.

2020 N.C.L. = 25

2024 = 27

C.L.

3.5 - Past Examination - 2016

Following is the summarized Balance Sheet of B-22 Limited as on 31st March, 2019:

Assets	Rs.	Assets	Rs.
Equity Shares of Rs. 10 each fully paid up	12,50,000	Fixed Assets	46,50,000
Revenue reserve	15,00,000	Current Assets	30,00,000
Securities Premium	2,50,000		
Profit & Loss Account	1,25,000		
Secured Loans:			
12% Debentures	18,75,000		
Unsecured Loans	10,00,000		
Current maturities of long term borrowings	16,50,000		
Total	76,50,000	Total	76,50,000

The company wants to buy back 25,000 equity shares of Rs. 10 each, on 1st April, 2019 at Rs. 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.

FV: 10

ESC: CRR

Buy Back of Securities & Equity Shares

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.

Complete 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	125,000
25% of the shares outstanding	31,250

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

Particulars	Rs.
Paid up capital (Rs.)	12,50,000
Free reserves (Rs.) (15,00,000 + 2,50,000 + 1,25,000)	18,75,000
Shareholders' funds (Rs.)	31,25,000
25% of Shareholders fund (Rs.)	7,81,250
Buy back price per share	Rs. 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	Rs.
(a) Loan funds (Rs.) (18,75,000 + 10,00,000 + 16,50,000)	45,25,000
(b) Minimum equity to be maintained after buy back in the ratio of 2:1 (Rs.) (a/2)	22,62,500
(c) Present equity/shareholders fund (Rs.)	31,25,000
(d) Maximum permitted buy back of Equity (Rs.) [(c) - (b)]	8,63,500
(f) Maximum number of shares that can be bought back @ Rs. 20 per share	43,175
(g) Actual Buy Back Proposed	25,000

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	43,175
Maximum number of shares that can be bought back [least of the above]	31,250

Company qualifies all tests for buy-back of shares and came to the conclusion that it can buy maximum 31,250 shares on 1st April, 2019.

Journal Entries for buy-back of 25,000 shares

Balance Sheet after Buy Back

Equity and Liabilities	Rs.
1. SHF	
a. SH Capital: Equity	10,00,000
2. Reserve & Surplus	1,25,000
3. Non-current Liability	
a) LTD	28,75,000
4. Current Liability	
a) STD:	1,50,000
Total	71,50,000

Assets	Rs.
1. NCA:	
a) PPE: (i) TA	4,50,000
(ii) IFA	-
2. Non-current Invest.	-
3. Current Asset	25,00,000
Total Asset	71,50,000

Step 1: a) No of share old: 125000

b) 25% of 125000 x 25% = 31250 shares

Step 2: SHF x 25% = 312500

125000 + 187500 = 312500

312500 x 25% = 78125

78125 / 20 = 3906.25 No of shares

Step 3: Debt-equity Ratio: 2:1

Debt (2) = 452500

Equity (1) = 226250

Present (SHF) = 312500

Maximum Gpvt = 862500

÷ B.B.P + FV

÷ 30

28750 No of shares

(Lowe is lower) 28750 maximum limit for B.B.

25000 S.R.

Journal Entries

- ESC Dr. 250000  
To B.B. Dr. 250000  
To ESTH 500000
- ESTH A/c Dr. 500000  
To Bank 500000
- Rev. Res. Dr. 250000  
To CRR 250000
- SP Dr. 250000  
To P.P. on B.B. 250000

Note: 1 RBS

Rev. Res.	1250000
PdL	1250000
CRR	250000
Total	1625000

Note: 2. N.C.L.: LTD

1) Deb	1875000
2) Unsec. loan	1000000
Total	2875000

Liab: Cr + Dr -

Asset: Dr + Cr -

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

Balance Sheet as on 31st March, 2019

Particulars	Note No	Amount
Equity and Liabilities		
Shareholders' funds		
(a) Share capital	1	10,00,000
(b) Reserves and Surplus	2	16,25,000
Non-current liabilities		
(a) Long-term borrowings	3	28,75,000
Current liabilities		
Total		71,50,000
Assets		
Non-current assets		
(a) Fixed assets		46,50,000
Current assets (30,00,000-5,00,000)		25,00,000
Total		71,50,000

Notes to accounts

	Rs.	Rs.
1. Share Capital		
Equity share capital		
1,00,000 Equity shares of Rs. 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: Utilisation for share buy-back (2,50,000)	-	
Capital Redemption Reserves	2,50,000	16,25,000
Long-term borrowings		