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BUY-BACK OF SHARES AND SECURITIES

Definitions:-

Buy-back is the process by which Company buy-back it's Shares from the existing Shareholders usually at a price higher than the market price. When the Company buy-back the Shares, the number of Shares outstanding in the market reduces/fall. It is the option available to Shareholder to exit from the Company business. It is governed by section 68 of the Companies Act, 2013.

Reasons of Buy-back:-

- To improve Earning per Share;
- To use ideal cash;
- To give confidence to the Shareholders at the time of falling price;
- To increase promoters shareholding to reduce the chances of takeover;
- To improve return on capital ,return on net-worth;
- To return surplus cash to the Shareholder.

Modes of Buy-back:-

A Company may buy-back its Shares or other specified Securities by any of the following method-

- From the existing shareholders or other specified holders on a proportionate basis through the tender offer;
- From the open market through-
    1. Book-Building process
    2. Stock Exchange

    Provided that no buy-back for fifteen percent or more of the paid up capital and reserves of the Company can be made through open market.
- From odd-lot holders.

Sources of Buy-back:-

A Company can purchase its own shares and other specified securities out of –

- its free reserve; or
- the securities premium account; or
- the proceeds of the issue of any shares or other specified securities.

However, Buy-back of any kind of shares or other specified securities cannot be made out of the proceeds of the earlier issue of same kind of shares or same kind of other specified securities.

Conditions of Buy-back:-

As per Section 68 of the Companies Act, 2013 the conditions for Buy-back of shares are-

- Articles must authorise otherwise Amend the Article by passing Special Resolution in General Meeting.
- For buy-back we need to pass Special Resolution in General Meeting, but if the buy-back is upto 10%, then a Resolution at Board Meeting need to be passed .

- Maximum number of Shares that can be brought back in a financial year is twenty-five percent of its paid up share capital.
- Maximum amount of Shares that can be brought back in a financial year is twenty-five percent of paid up share capital and free reserves (where paid up share capital includes equity share capital and preference share capital; & free reserves includes securities premium).
- Post buy-back debt-equity ratio cannot exceed 2:1.
- Only fully paid up shares can be brought back in a financial year.
- Company must declare its insolvency in Form SH-9 to Register of Companies, signed by Atleast 2 Directors out of which one must be a Managing Director, if any.
- The notice of the meeting for which the Special Resolution is proposed to be passed shall be accompanied by a explanatory statement stating-

    1. a full and complete disclosure of all the material facts;
    2. the necessity of buy-back;
    3. the class of shares intended to be bought back;
    4. the amount invested under the buyback;
    5. the time limit for completion of buyback;

- The Company must maintain a Register of buy-back in Form SH-10.
- Now, Submit Return of buy-back in Form SH-11 Annexed with Compliance Certificate in Form SH-15, Signed by 2 Directors out of which One must be a Managing Director, if any.
- A Company should extinguish and physically destroy shares bought back within 7 days of completion of the buy-back.
- Observe 6 months cooling period i.e. no fresh issue of share is allowed.
- No offer of buy-back should be made by a company within a period of one year from the date of the closure of the preceding offer of buy-back.
- The buy-back should be completed within a period of one year from the date of passing of Special Resolution or Board Resolution, as the case may be.

Transfer of certain sum to Capital Redemption Reserve Account (CRR)

According to section 69 of the Companies Act, 2013, where a Company brought back shares out of free reserves or out of the securities premium account, then an amount equal to the nominal value of the shares need to be

transferred to the Capital Redemption Reserve Account. Such transfer detailed to be disclosed in the Balance sheet.

The Capital Redemption Reserve account may be utilized for paying unissued shares of the company to the members as fully paid bonus shares.

Restrictions on Buy-back of Securities in certain circumstances

According to section 70 of the Companies Act, 2013, A Company should not buy-back its securities or other specified securities , directly or indirectly -

- Through any subsidiary including its own subsidiaries; or
- Through investment or group of investment Companies; or
- When Company has defaulted in repayment of deposits or interest payable thereon, or in redemption of debentures or preference shares or repayment of any term loan.
  The prohibition is lifted if the default has been remedied and a period of 3 years has elapsed after such default ceased to subsist.
- When Company has defaulted in filing of Annual Return, declaration of dividend & financial statement.

Conclusion

Thus, it can be concluded that Indian companies announce buyback in response to undervaluation position of their stocks in capital markets and they are well supported by availability of sufficient cash balance available for the same. Thus, on one hand, premium offered in terms of buyback prices announced offers an exit opportunity for shareholders and on the other hand, it offers an opportunity for the company to use its liquidity position to extinguish its shares today and issue them again in future.

It prevents takeovers and mergers thus preventing monopolization and aiding the survival of consumer sovereignty. On the other hand Buy back can help in manipulating the records in flatting share prices Price-Earning Ratio, Earning per share, thus misleading shareholders. Thus, knowledge of the impacts of

Buy-back becomes vital and every shareholder must reconsider all his views before purchasing the shares of companies involved in the process of Buy-back.

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