COMPANY ACCOUNTS: ISSUE, FORFEITURE AND RE-ISSUE OF SHARES

MEANING OF COMPANY

The never-ending human desire to grow and grow further has given rise to the expansion of business activities, which in turn has necessitated the need to increase the scale of operations so as to provide goods and services to the ever-increasing needs of the growing population of consumers. Large amount of money, modern technology, large human contribution etc. is required for it, which is not possible to arrange under partnership or proprietorship. To overcome this difficulty, the concept of 'Company' or 'Corporation' came into existence.

Company begs its origin in law. It is an organisation consisting of individuals, called shareholders by virtue of holding the shares of a company, who are authorised by law to elect a board of directors and, through it, to act as a separate legal entity as regards its activities.

According to Justice Marshal, "A corporation is an artificial being, invisible, intangible and existing only in the contemplation of law".

Distinction between Ownership and Management: Since the number of shareholders is very large and may be distributed at different geographical locations, it becomes difficult for them to carry on the operational management of the company on a day-to-day basis. This gives rise to the need of separation of the management and ownership.

SALIENT FEATURES OF A COMPANY

Following are the salient features of a company:

1. *Incorporated Association:* A company comes into existence through the operation of law. Therefore, incorporation of company under the Companies Act is must. Without such registration, no company can come into existence. Being created by law, it is regarded as an artificial legal person.
2. *Separate Legal Entity:* A company has a separate legal entity and is not affected by changes in its membership. Therefore, being a separate business entity, a company can contract, sue and be sued in its incorporated name and capacity.
3. *Perpetual Existence:* Since company has existence independent of its members, it continues to be in existence despite the death, insolvency or change of members.
4. *Common Seal:* Company is not a natural person; therefore, it cannot sign the documents in the manner as a natural person would do. In order to enable the company to sign its documents, it is provided with a legal tool called 'Common Seal'. The common seal is affixed on all documents by the person authorised to do so who in turn puts his signature

for and on behalf of the company. Companies Act, 2013 required common seal to be affixed on certain documents (such as bill of exchange, share certificates, etc.). Now, the use of common seal has been made optional. All such documents which required affixing the common seal may now instead be signed by two directors or one director and a company secretary of the company.

5. *Limited Liability:* The liability of every shareholder of a company is limited to the amount he has agreed to pay to the company on the shares allotted to him. If such shares are fully paid-up, he is subject to no further liability.
6. *Not a citizen:* A company is not a citizen in the same sense as a natural person is, though it is created by the process of law. It has a legal existence but does not enjoy the citizenship rights and duties as are enjoyed by the natural citizens.
7. *Transferability of Shares:* The capital is contributed by the shareholders through the subscription of shares. Such shares are transferable by its members except in case of a private limited company, which may have certain restrictions on such transferability.
8. *Maintenance of Books:* A limited company is required by law to keep a prescribed set of account books and any failure in this regard attracts penalties.
9. *Periodic Audit:* A company has to get its accounts periodically audited through the chartered accountants appointed for the purpose by the shareholders on the recommendation of board of directors.
10. *Right of Access to Information:* The right of the shareholders of a company to inspect its books of account, with the exception of books open for inspection under the Statute, is governed by the Articles of Association. The shareholders have a right to seek information from the directors by participating in the meetings of the company and through the periodic reports.

SHARE CAPITAL

Total capital of the company is divided into a number of small indivisible units of a fixed amount and each such unit is called a **share**. The fixed value of a share, printed on the share certificate, is called nominal/ par/face value of a share. However, a company can issue shares at a price different from the face value of a share. The liability of holder of shares (called shareholders) is limited to the **issue price of shares** acquired by them. However, the issue price need not be equal to market price of the share.

These days the shares are generally priced on the basis of **book building process**. Book building is a process through which company determines it's share prices. Under this method company determines a price band of its shares and on the basis of bids received from potential investors at various prices within the price band finally fixes its issue price.

Share capital of a company is divided into following categories:

i. *Authorised Share Capital or Nominal Capital:* A company estimates its maximum capital requirements. This amount of capital is mentioned in 'Capital Clause' of the 'Memorandum of Association' registered with the Registrar of Companies. It puts a limit on the amount of capital, which a company is authorised to raise during its lifetime and is called 'Authorised Capital'. It is shown in the balance sheet at face value.

ii. *Issued Share Capital:* A company need not issue total authorised capital. Whatever portion of the share capital is issued by the company, it is called 'Issued Capital'. Issued capital means and includes the nominal value of shares issued by the company for cash, and consideration other than cash. It is also shown in the balance sheet at nominal value. The remaining portion of the authorised capital which is not issued either in cash or consideration may be termed as 'Un-issued Capital'. It is not shown in the balance sheet.

iii. *Subscribed Share Capital:* It is that part of the issued share capital, which is subscribed by the public i.e., applied by the public and allotted by the company. It also includes the face value of shares issued by the company for consideration other than cash.

iv. *Called-up Share Capital:* Companies may receive the issue price of shares in installments. The portion of the issue price of shares which a company has demanded or called from shareholders is known as 'Called-up Capital' and the balance, which the company has decided to demand in future may be referred to as UncalledCapital.

v. *Paid-up Share Capital:* It is the portion of called up capital which is paid by the shareholders. Whenever a particular amount is called by the company and the shareholder(s) fails to pay the amount fully or partially, it is known as *'unpaid calls' or 'instalments (or Calls) in Arrears'.* Call-in-advance is that portion of capital which is yet to be called by the company but has already been paid by shareholder.

vi. *Reserve Share Capital:* As per Section 65 of the Companies Act, 2013, a Company may decide by passing a resolution that a certain portion of its subscribed uncalled capital shall not be called up except in the event of winding up of the company. Portion of the uncalled capital which a company has decided to call only in case of liquidation of the company is called Reserve Capital. Reserve Capital is different from Capital reserve. Capital reserves are part of 'Reserves and Surplus' and refer to those reserves which are not available for declaration of dividend.

TYPES OF SHARES

Share issued by a company can be divided into following categories:

1. **Preference Shares:** According to Section 43 of the Companies Act, 2013 persons holding preference shares, called preference shareholders, are assured of a preferential dividend at a fixed rate during the life of the company. They also carry a preferential right over other shareholders to be paid first in case of winding up of the company. Thus, they enjoy preferential rights in the matter of:

- Payment of dividend, and
- Repayment of capital

Generally, holders of these shares do not get voting rights. Companies use this mode of financing as it is cheaper than raising debt. Dividend is generally cumulative in nature and need not be paid every year in case of deficiency of profits.

Types of Preference Shares

Preference shares can be of various types, which are as follows:

a) **Cumulative Preference Shares:** A cumulative preference share is one that carries the right to a fixed amount of dividend or dividend at a fixed rate. Such a dividend is payable even out of future profit if current year's profits are insufficient for the purpose. This means that dividend on these shares accumulates unless it is paid in full and, therefore, the shares are called Cumulative Preference Shares. The arrears of dividend are then shown in the balance sheet as a contingent liability.

b) **Non-cumulative Preference Shares:** A non-cumulative preference share carries with it the right to a fixed amount of dividend. In case no dividend is declared in a year due to any reason, the right to receive such dividend for that year expires. It implies that holder of such a share is not entitled to arrears of dividend in future.

c) **Participating Preference Shares:** Notwithstanding the right to a fixed dividend, this category of preference share confers on the holder the right to participate in the surplus profits, if any, after the equity shareholders have been paid dividend at a stipulated rate. Similarly, in the event of winding up of the company, this type of share carries the right to receive a pre-determined proportion of surplus as well once the equity shareholders have been paid out.

d) **Non-participating Preference Shares:** A share on which only a fixed rate of dividend is paid every year, without any accompanying additional rights in profits and in the surplus on winding-up, is called 'Non-participating Preference Shares.' Unless otherwise specified, the preference shares are generally non-participating.

e) **Redeemable Preference Shares:** These are shares that a company may issue on the condition that the company will repay after the fixed period or even earlier at company's discretion. The repayment on these shares is called redemption and is governed by Section 55 of the Companies Act, 2013.

f) **Non-redeemable Preference Shares:** The preference shares, which do not carry with them the arrangement regarding redemption, are called Non-Redeemable Preference Shares. According to Section 55, no company limited by shares shall issue irredeemable preference shares or preference shares redeemable after the expiry of 20 years from the date of issue. However, a company may issue preference shares redeemable after 20 years for such infrastructure projects as may be specified, under the Companies Act, 2013.

g) **Convertible Preference Shares:** These shares give the right to the holder to get them

converted into equity shares at their option according to the terms and conditions of their issue.

h) **Non-convertible Preference Shares:** When the holder of a preference share has not been conferred the right to get his holding converted into equity share, it is called Non -convertible Preference Shares. Preference shares are non-convertible unless otherwise stated.

2. **Equity Shares:** Equity shares are those shares, which are not preference shares. It means that they do not enjoy any preferential rights in the matter of payment of dividend or repayment of capital. The rate of dividend on equity shares is recommended by the Board of Directors and may vary from year to year. Rate of dividend depends upon the dividend policy and the availability of profits after satisfying the rights of preference shareholders. These shares carry voting rights. Companies Act, 2013 permits issue of equity share capital with differential rights as to dividend, voting or otherwise in accordance with prescribed rules.

The shares can be issued by a company either

1. for cash or
2. for consideration other than cash.

ISSUE OF SHARES FOR CASH

To issue shares, private companies depend upon 'Private Placement' of shares. Public companies issue a 'Prospectus' and invite general public to subscribe for shares.

To discuss accounting treatment, we shall concentrate on public companies who invite general public to subscribe for equity shares. Similar accounting treatment is applicable in other cases. However, for journal entries in case of issue of preference shares, the word 'Equity' is replaced with the word 'Preference'.

Minimum Subscription: A public limited company cannot make any allotment of shares unless the amount of minimum subscription stated in the prospectus has been subscribed and the sum payable as application money for such shares has been paid to and received by the company.

As per guidelines of the Securities Exchange Board of India (SEBI), the minimum subscription to be received in an issue shall not be less than ninety per cent of the offer through offer document. If the Company does not receive the minimum subscription of 90% of the issue, all application moneys received shall be refunded to the applicants forthwith. In order to avoid that risk, the public companies enter into underwriting arrangements. Underwriting means guaranteeing to subscribe to an agreed number of shares which are not taken up by the public for a certain consideration. As such, the person or institution who underwrites the issue is called 'underwriters' and the commission so paid is

known as ‘Underwriting Commission’. In our country, underwriting is done by the Industrial Development Bank of India, Industrial Finance Corporation of India, Life Insurance Corporation of India, The Industrial Credit and Investment Corporation of India, Commercial Banks, Investment Trust, etc.

The company reserves the right to reject or accept an application fully or partially. Successful applicants become shareholders of the company and are required to pay the second instalment which is known as ‘Allotment Money’ and unsuccessful applicants get back their money. However, in case of delay in refunding the money, the Company becomes liable to pay interest on the amount of refund. Subsequent instalments, if any, to be called by the company are known as ‘Calls’.

Journal Entries for Issue of Shares for Cash

Upon the issue of share capital by a company, the undermentioned entries are made in the financial books:

1 *On receipt of the application money*

Bank Account	Dr	(With the actual amount received.)
To Share Application Account		(Being application money received)

2 *On allotment of share*

Share Allotment Account	Dr	(With the amount due on allotment.)
Share Application Account	Dr	(With the application amount received on allotted shares.)
To Share Capital Account		(With the amount due on allotment and application.)

(Being the sum due on allotment and application money transferred to capital account)

3 *On receipt of allotment money*

Bank Account	Dr	(With the amount actually received on allotment.)
To Share Allotment Account		(Being money received on allotment)

Sometimes separate Application and Allotment Accounts are not prepared and entries relating to application and allotment monies are passed through a combined Application and Allotment Account.

1 *On receipt of Application Money:*

Bank A/c Dr

To Share Application and Allotment A/c

2 *On allotment of shares:*

Share Application & Allotment A/c Dr (With total application and allotment amount)

To Share Capital A/c

3 *On Allotment money being received*

Bank A/c Dr

To Share Application & Allotment A/c

4 *On a call being made*

Share Call Account Dr (With the amount due on the call.)

To Share Capital Account

5 *On receipt of call money*

Bank Account Dr (With the due amount actually received on call)

To Share Call Account

SUBSCRIPTION OF SHARES

Accounting for issue of shares depends upon the type of subscription. Whenever a company decides to issue shares to public, it invites applications for subscription by issuing a prospectus. It is not necessary that company receives applications for the number of shares to be issued by it. There are three possibilities:

1) Full Subscription

Issue is fully subscribed if the number of shares offered for subscription and the number of shares actually subscribed by the public are same. To start discussion on accounting treatment for issue of shares, let us assume that the issue is fully subscribed.

2) **Under Subscription**

It means the number of shares offered for subscription is more than the number of shares subscribed by the public. In this case, the journal entries as discussed above are passed but with one change i.e., calculation of application, allotment and for that matter, the call money is based on number of shares actually applied and allotted. It must be remembered that shares can be allotted, in this case, only when the minimum subscription is received.

3) **Over Subscription**

In actual practice, issue of shares is either under or over-subscribed. If an issue is over-subscribed, some applications may be rejected and application money refunded and in respect of others, only a part of the shares applied for may be allotted and the excess amount received can be utilised towards allotment or call money which has fallen due or will soon fall due for payment.

The entries are:

1 *On refund of application money to applicants to whom shares have not been allotted*

Share Application A/c	Dr.	
To Bank Account		
(Being application money refunded)		

2 *When only a part of shares applied for are allotted*

Share Application A/c	Dr.	
To Share Allotment* A/c		(With the application money accepted for allotment)
To Share Calls-in-Advance* A/c		(With the amount received in advance)
To Bank A/c		(With any excess amount to be refunded)
(Being application money adjusted)		

*Credited to Share Capital A/c subsequently.

SHARES ISSUED AT DISCOUNT

Shares are regarded to be issued at a discount, if issue is at an amount less than the nominal or par value of shares. The excess of the nominal value over the issue price represents discount on the issue of shares. For example, when a share of the nominal value of 100 is issued at 98, it is said to have been issued at a discount of 2 per cent.

According to Section 53 of the Companies Act, 2013, a Company cannot issue shares at a discount except in the case of issue of sweat equity shares (issued to employees and directors). Thus, any issue of shares at discount shall be void.

SHARES ISSUED AT PREMIUM

When a company issues its securities at a price more than the face value, it is said to be an issue at a premium. Premium is the excess of issue price over face value of the security. Thus, where a share of the nominal value of 100 is issued at105, it is said to have been issued at a premium of 5 per cent.

When the issue is at a premium, the amount of premium may technically be called at any stage of share capital transactions. However, premium is generally called with the amount due on allotment, sometimes with the application of money and rarely with the call money.

Accounting Treatment

When shares are issued at a premium, the premium amount is credited to a separate account called *"Securities Premium Account"* because it is not a part of share capital. Rather, it represents a gain of a capital nature to the company.

Being a credit balance, Securities Premium Account is shown under the heading, "Reserves and Surplus". However, 'Reserves and Surplus' is shown as 'shareholders' funds in the Balance Sheet as per Schedule III. According to Section 52 of the Companies Act, 2013, Securities Premium Account may be used by the company:

a) Towards issue of unissued shares of the company to be issued to members of the company as fully paid bonus securities.

b) To write off preliminary expenses of the company.

c) To write off the expenses of, or commission paid, or discount allowed on any of the securities or debentures of the company.

d) To provide for premium on the redemption of redeemable preference shares or debentures of the company.

e) For the purchase of own shares or other securities.

Note : It may be noted that certain class of Companies as prescribed under Section 133 of the Companies Act, 2013, whose financial statements comply with the accounting standards prescribed for them, can't apply the securities premium account for the purposes (b) and (d) mentioned above.

When shares are issued at a premium, the journal entries are as follows:

a) Premium amount called with Application money

1	Bank A/c	Dr.	(Total Application money + Premium Amount)
	To Share Application A/c		(Amount received)
	(Money received on applications for Shares @ per share including premium)		
2	Share Application A/c	Dr.	(No. of Shares Applied for x Application Amount per share)
	To Securities Premium A/c		(No. of Shares allotted x Premium Amount per share)
	To Share Capital A/c		(No. of Shares allotted x Nominal value per share for capital)

(b) Premium Amount called with Allotment Money

1	Share Allotment A/c	Dr.	(No. of Shares Allotted x Allotment and Premium Money per share)
	To Share Capital A/c		(No. of Shares Allotted x Allotment Amount per share)
	To Securities Premium A/c		(No. of Share Allotted x Premium Amount per share)
	(Amount due on allotment of shares @ ` per share including premium)		
2	Bank A/c	Dr.	
	To Share Allotment A/c		
	(Money received including premium consequent upon allotment).		

OVER SUBSCRIPTION AND PRO-RATA ALLOTMENT

Over subscription is the application money received for more than the number of shares offered to the public by a company. When the shares are oversubscribed, a decision is to be made on how the shares are going to be allotted. Shares can be allotted to the applicants by a company in any manner it thinks proper. The company may reject some applicants in full, i.e., no shares are allotted to some applicants and application money is refunded. Usually, multiple applications by the same persons are not considered. Allotment may be given to the rest of the applicants in full, i.e., for the number of shares they have applied for. A third alternative is that a company may allot shares to the applicants on **pro-rata** basis. 'Pro-rata allotment' means allotment in proportion of shares applied for.

For example, a company offers to the public 10,000 shares for subscription. The company receives applications for 12,000 shares. If the shares are to be allotted on pro-rata basis, applicants for 12,000 shares are to be allotted 10,000 shares, i.e., on the 12,000 : 10,000 or 6:5 ratio. Any applicant who has applied for 6 shares will be allotted 5 shares.

Under pro-rata allotment, the excess application money received is adjusted against the amount due on allotment or calls. Surplus money after making adjustment against future calls is returned to the applicants. The applicants are informed about the allotment procedure through an advertisement in leading newspapers.

Accounting Entries

(a) *For rejected applications:*

Share Application Account Dr.

To Bank Account

(Being application money refunded for rejected applications as per Board's Resolution No….dated….)

(b) *For pro-rata allotment:*

Share Application Account Dr.

To Share Allotment Account

(Being excess application money adjusted against allotment money as per Board's Resolution No….dated….)

CALLS-IN-ARREARS AND CALLS-IN-ADVANCE

Calls-in-Arrears

Sometimes shareholders fail to pay the amount due on allotment or calls. The total unpaid amount on one or more instalments is known as *Calls-in-Arrears* or *Unpaid Calls*.

For recording 'Calls-in-Arrears', the following journal entry is recorded :

Calls-in-Arrears A/c	Dr.	(Amount of Unpaid Calls)
Bank A/c	Dr.	(Amount received)
To Share Allotment A/c		(Total allotment money due)
To Share Calls A/c		(Total Call money due)

(Being call money/ allotment money received on .... shares at Rs per share.)

Calls-in-Advance

Some shareholders may sometimes pay a part, or whole, of the amount not yet called up, such amount is known as Calls-in-advance. According to Table F, interest at a rate not exceeding 12 per cent p.a. is to be paid on such advance call money. This amount is credited in Calls-in-Advance Account. The following entry is recorded:

Bank A/c Dr. (Call amount received in advance)

To Call-in-Advance A/c

When calls become actually due, calls-in-advance account is adjusted at the time of the call. For this the following journal entry is recorded:

Calls-in-Advance A/c Dr. (Call amount received in advance)

Bank A/c Dr. (Remaining call money received, if any)

To Particular Call A/c (Call money due)

(Being call in advance adjusted and call money due received)

ISSUE OF SHARES FOR CONSIDERATION OTHER THAN CASH

Public limited companies, generally, issue their shares for cash and use such cash to buy the various types of assets needed in the business. Sometimes, however, a company may issue shares in a direct exchange for land, buildings or other assets. Shares may also be issued in payment for services rendered by promoters, lawyers in the formation of the company. These shares should be shown separately under the heading 'Share Capital'.

Within specified time of allotment, the company must produce before the Registrar a written contract of sale of service in respect of which shares have been allotted.

Accounting Entries

When assets are purchased in exchange of shares

Assets Account Dr.

To Share Capital Account

ACCOUNTING FOR RIGHT ISSUE

The accounting treatment of rights share is the same as that of issue of ordinary shares and the following journal entry will be made:

Bank A/c Dr.

To Equity shares capital A/c

In case rights shares are being offered at a premium, the premium amount is credited to the securities premium account. The accounting entry is usual and is

Bank A/c Dr.

To Equity Share Capital A/c

To Securities Premium A/c

ADVANTAGES AND DISADVANTAGES OF RIGHT ISSUE

Advantages of right Issue

1. Right issue enables the existing shareholders to maintain their proportional holding in the company and retain their financial and governance rights. It works as a deterrent to the management, which may like to issue shares to known persons with a view to have a better control over the company's affairs.
2. In well-functioning capital markets, the right issue necessarily leads to dilution in the value of share. However, the existing shareholders are not affected by it because getting new shares at a discounted value from their cum-right value will compensate decrease in the value of shares. The cum-right value is maintained otherwise also, if the existing shareholders renounce their right in favour of a third party.
3. Right issue is a natural hedge against the issue expenses normally incurred by the company in relation to public issue.
4. Right issue has an image enhancement effect, as public and shareholders view it positively.
5. The chance of success of a right issue is better than that of a general public issue and is logistically much easier to handle.

Disadvantages of right issue

1. The right issue invariably leads to dilution in the market value of the share of the company.
2. The attractive price of the right issue should be objectively assessed against its true worth to ensure that you get a bargained deal.

BUY BACK OF EQUITY SHARES

Buy back of shares 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 buy back results in decrease in share capital of the company. A company cannot buy its own shares for the purpose of investment. A company having sufficient cash may decide to buy back its own shares. The following may be the Objectives/Advantages of Buy-Back of shares:

1. to increase earnings per share if there is no dilution in company's earnings as the buy-back of shares reduces the outstanding number of shares.
2. to increase promoters holding as the shares which are bought back are cancelled.
3. to discourage others to make hostile bid to take over the company as the buyback will increase the promoters holding.
4. to support the share price on the stock exchanges when the share price, in the opinion of company management, is less than its worth, especially in the depressed market.
5. to pay surplus cash to shareholders when the company does not need it for business.

The Companies Act, 2013 under Section 68 (1) permits companies to buy back their own shares and other specified securities out of:

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

Note: 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. For example, if equity shares are to be bought-back, then, preference shares may be used for the purpose.

The other important provisions relating to the buyback are:

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

    (a) the buy-back is authorised by its articles;

    (b) a special resolution has been passed in general meeting of the company authorising the buy-back;

    However, the above provisions do not apply where the buy back is ten percent or less of the paid up equity capital + free reserves and is authorized by a board resolution passed at a duly convened meeting of the directors. Hence, 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 without the necessity of its being authorized by the articles of association of the company and by a special resolution of its members passed at a general meeting of

the company.

(c) the buy-back must be equal or less than twenty five per cent of the total paid-up capital and free reserves of the company: (Resource Test)

(d) Further, the buy-back of shares in any financial year must not exceed 25% of its total paid-up capital and free reserves: (Share Outstanding Test)

(e) the ratio of the debt owed by the company (both secured and unsecured) after such buy-back is not more than twice the total of its paid up capital and its free reserves: (Debt-Equity Ratio Test)

Note: Central Government may prescribe a higher ratio of the debt than that specified under this clause for a class or classes of companies. Debt here should include both long term debt as well as short term debt.

(f) all the shares or other specified securities for buy-back are fully paid-up;

(g) the buy-back of the shares or other specified securities listed on any recognised stock exchange is in accordance with the regulations made by the Securities and Exchange Board of India in this behalf;

(h) the buy-back in respect of shares or other specified securities other than those specified in clause (f) is in accordance with the guidelines as may be prescribed.

Provided that no offer of buy back under this sub section shall be made within a period of one year reckoned from the date of closure of a previous offer of buy back if any. This means that there cannot be more than one buy back in one year.

(2) The notice of meeting at which special resolution is supposed to be passed must be accompanied by an explanatory statement stating-

(a) a full and complete disclosure of all material facts;

(b) the necessity of the buy-back;

(c) the class of security intended to be purchased under the buy-back;

(d) the amount to be invested under the buy-back;

(e) the time limit for completion of the buy-back

(3) Every buy-back shall be completed within twelve months from the date of passing the special resolution, or the resolution passed by the board of directors.

(4) The buy-back may be—

(a) from the existing security holders on a proportionate basis; or

(b) from the open market; or

(c) by purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity.

(5) Where a company has passed a special resolution under clause (b) of Sub- section (2) to buy-back its own shares or other securities under this section, it shall, before making such buy-back, file with the Registrar and the Securities and Exchange Board of India a declaration of solvency in the form as may be prescribed and verified by an affidavit

to the effect that the Board of Directors has made a full inquiry into the affairs of the company as a result of which they have formed an opinion that it is capable of meeting its liabilities and will not be rendered insolvent within a period of one year of the date of declaration adopted by the Board of Directors. It must be signed by at least two directors of the company, one of whom shall be the managing director, if any :

Note: No declaration of solvency shall be filed with the Securities and Exchange Board of India by a company whose shares are not listed on any recognised stock exchange.

(6) Where a company buys-back its own securities, it shall extinguish and physically destroy the securities so bought-back within seven days of the last date of completion of buy-back.

(7) Where a company completes a buy-back of its shares or other specified securities under this section, it shall not make further issue of same kind of shares (including allotment of further shares under clause (a) of Sub-section (1) of Section (62)) or other specified securities within a period of six months except by way of bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option scheme, sweat equity or conversion of preference shares or debentures into equity shares.

(8) Where a company buy-back its securities under this section, it shall maintain a register of the securities so bought, the consideration paid for the securities bought-back, the date of cancellation of securities, the date of extinguishing and physically destroying of securities and such other particulars as may be prescribed.

(9) A company shall, after the completion of the buy-back under this section, file with the Registrar and the Securities and Exchange Board of India, a return containing such particulars relating to the buy-back within thirty days of such completion, as may be prescribed, provided that no return shall be filed with the Securities and Exchange Board of India by a company whose shares are not listed on any recognised stock exchange.

(10) If a company makes default in complying with the provisions of this section or any regulations made by SEBI in this regard, the company may be punishable with a fine which shall not be less than Rs One Lakh but which may extend to three lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for upto 3 years or with a fine of not less than one lakh rupees but which may extend to three lakh rupees or with both.

(11) Section 69 (1) states that where a company purchases its own shares out of the free reserves or securities premium account, a sum equal to the nominal value of shares so purchased shall be transferred to the Capital Redemption Reserve Account and details of such account shall be disclosed in the Balance Sheet.

(12) The shares or other specified securities which are proposed to be bought-back must be fully paid-up.

(13) The Capital Redemption Reserve Account may be applied by the company in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.

(14) Premium (excess of buy-back price over the par value) paid on buy-back should be adjusted against free reserves and/or securities premium account. Revaluation reserve represents unrealized profit and hence it cannot be used for buy-back of securities.

Some Important Terms

(a) "specified securities" includes employees' stock option or other securities as may be notified by the Central Government from time to time;

(b) "free reserves" means such reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend:

Provided that-

(i) any amount representing unrealised gains, notional gains or revaluation of assets, whether shown as a reserve or otherwise, or

(ii) any change in carrying amount of an asset or of a liability recognised in equity, including surplus in profit and loss account on measurement of the asset or the liability at fair value, shall not be treated as free reserves.

For the purposes of Section 68, "free reserves" includes securities premium account.