# BUYBACK OF SHARES AND ITS VARIOUS ASPECTS

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**ABSTRACT**

Buy back of shares i.e. purchase of companies own share in order to complete process of Capital Restructuring. Capital Restructuring is performed to control value of a share through various ways. This paper focuses on understanding the concept of buy- back of shares and various others aspects regarding buy back of shares i.e. conditions for buy back, reasons for buy back and helps in contrasting provisions of buy back in Companies Act of 1956 and Companies Act of 2013.

**Keywords**- Buy Back, Capital Restructuring, Companies Act 1956, Companies Act 2013.

**OBJECTIVE OF THE ARTICLE**

1) To understand concept of buy- back of shares
2) To understand various provisions related to buy back
3) To understand difference in provisions of buy back in Companies Act of 1956 and Companies Act 2013.

**STATEMENT OF PURPOSE**

Concept of buy back was first time introduced in India in year 1999 by bringing an act by parliament. This act in way allowed buying back of shares and over the time the concept of buy- back is developing therefore, it is needed to understand about what is buy back of shares? How it is controlled? What is the purpose of buy back? Who are the agencies controlling buy back? Also we would try to understand what the financial requirement for successful buy back are?

## SCOPE AND SIGNIFICANCE OF ARTICLE

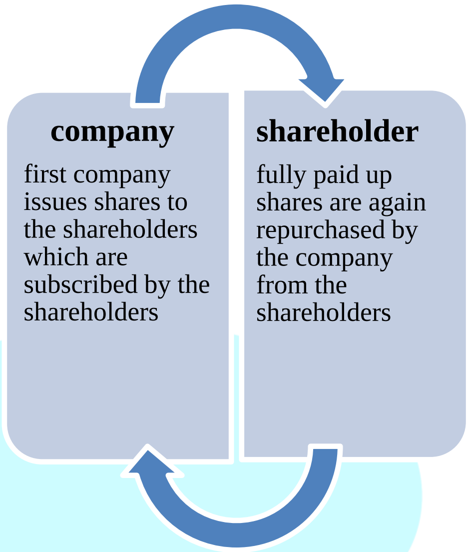
Buy back of shares in India gained popularity after year 1999.Companis and additionally capital market can be consequently revived by depending on this new device of money related re-building. The choices whether are for the most part that attractive to company and its investors rely on many components, which might be one of a kind to each case. Due thought has been given to each factor before a last choice is made. This research will help in seeing all variables. This research will help in understanding administrative prerequisite of the buyback choice the same number of a period company utilize buy back choice to control the cost.

## INTRODUCTION

Section 2(84) of companies act defines share as "*A share in the share capital of a company and includes stock*''. A share is the smaller part or fraction of share capital and also include interest of shareholder in the company. When shares are issued and subscribed by the shareholders it forms the share capital of the company each shareholder holding the part of the share capital in the form of shares of fixed value. Once the shares are subscribed by the shareholders they have no claim over money only option left to them it is to transfer their shares and realize money back.

But there are certain provisions in the company act of 2013 which allows the shareholders to sell their shares to the companies back and realize their price of shares. This process of selling back of shares back to the company is known as 'buying of shares'. Buying back provides shareholders with option to sell shares hold by them and exit from companies business therefrom. Further this buy-back should not be forced upon shareholder, in case of *National Consumer Disputes Redressal, Ritu Bhargava vs Godrej Industries Ltd & Ors.*[1] It was established that shareholders cannot be made to sell his shares without his consent and should follow appropriate steps.

[1] AIR 2008




Financial restructuring involves use of fund available in most appropriate way which is could put company at advantageous position, this sometimes involves pay out or use of excessive cash in a way of buy- back of shares. Thus buy-back can be consider as one of the best option for capital restructuring.

**HISTORY**

History of buying back of shares in India can be traced from year 1999. Before that buying of shares needs prior permission of court (except preference shares) and the rules where very stringent which discouraged buying back of shares. It was very time consuming and involved various complexities in a way curbing the rights of shareholders. Therefore in year 1999 this was amended and the process was made simpler and section 77A, 77AA, 77B was inserted which allowed the companies to explore new and easy way of buying back and to gain the confidence of its shareholders. However under Companies Act of 2013 amended Sections 77A, 77AA, 77B does not find place and the same provisions has been laid down under section 67 to 70 of Companies Act of 2013.

**PURCHASE/ BUY BACK OF SHARES**

Section 67(1) of the Companies Act, 2013 provides that a company limit by shares or a company limited by guarantee having a sharing capital is not allowed to buy back its shares and this restriction is applied to all companies having share capital whether private or public in nature.[2]

However section 68 of Companies Act, 2013 allows company to buy back its own shares but by putting some restrictions.

**SOURCES OF BUY- BACK OF SHARES**

1) **Free Reserves-** when a company buy back its shares out of free reserves then an amount equals to nominal value of shares (which are purchased) are to be transferred to Capital Redemption Reserve Account (CRRA) and this CRRA has to be shown in Balance Sheet of the company. This account is also used when fully paid bonus shares are issued.

2) **Proceeds of any shares or other Specified Securities-** A Company cannot buy back its shares or other Specified Securities of that kind or category which is already issued .For example, Preference shares can be issued to buy back of Equity shares but Equity shares cannot be issued for the purpose of buyback of Equity shares.

3) **The Securities Premium Account.**

**CONDITIONS FOR BUY- BACK OF SHARES**

1- Section 68(2) specifies conditions for buy back of shares which are

A. Buy back must be allowed by the articles of the company.
B. A special resolution must have been passed in the general meeting of the company regarding buy back of shares but if the buy -back is up to 10% of the total equity capital then it can be allowed by passing simple resolution in meeting.
C. The buy- back is 25% or less of paid up capital and the free reserve of the company.

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[2] KAPOOR G.K. & DHAMIJA SANJAY, COMPANY LAW 200-01 ( Taxman 20th Ed. 2016)

*D.* The total of secured and unsecured debt of company after buy- back should be less than twice the paid up capital and its reserves. It may be possible that government may by order fix higher ratio as decided in the case of *Securities & Exchange Board Of vs Sterlite Industries (India) Ltd*[3]

E. The shares and the other securities must be fully paid up for buy-back.

F. The buy- back of shares and the other securities listed on the recognized stock exchange must be in accordance with rules and regulations of SEBI.

2- The notice should contain explanatory statements with particulars which is to be proposed to pass at meeting with general resolution.

3- Once the resolution has been passed, buy- back shall be completed within one year.

4- Buy- back is permissible-

a) On a proportionate basis from existing shareholders.
b) From open market.
c) By purchasing securities issued to employees.

5- Before making buy-back of shares or other securities a declaration of solvency is to filled with Registrar or SEBI (in case shares are listed on recognized stock exchange) which need to be signed by at least 2 directors.

6- Offer of buy-back should remain open for minimum 15 days and maximum 30 days.

7- Once the buy-back has been completed, the company should not further issue same kind of share within period of 6 months except by the way of bonus issue.

8- A return containing particulars must be filled with registrar of office and SEBI within 30 days of competition of buy- back.

9- As it was laid down in case of *In Re: Shalibhadra InfoSec*[4] *Ltd* the buy-back should not be misleading, the company should have sufficient fund to meet the buy-back process.

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[3] 2003 113 Comp 273 Bombay, 2003 45 SCL 475 Bombay
[4] AIR 2008

In case the above mentioned conditions are not complied there may be penalty upon company, this penalty can be in the form of fine or imprisonment. In violation of such rules the company may be punishable with minimum amount of 1 lakh which may be increased up to 3 lakh further if any officer of company in default can also be fined with minimum amount of 1 lakh which can be increased up to 3 lakh or can be imprisoned with term which may be increased to 3 years or both.

**REASONS FOR BUY-BACK OF SHARES**

1) **Return of surplus cash to shareholders**- if the company has surplus cash and want to purchase their shares which might be profitable then they buy back shares from shareholders in consideration of cash.
2) **To increase the value of shares**- Sometimes company buys share from existing shareholders at premium which ameliorate their confidence which in a way allows the existing shareholder to quit company at premium amount and buy back of shares which signals undervaluation of shares helps in attracting new shareholders thus helps in controlling falling of share prices.
3) **To obtain correct capital structure**- company use the option of buy back when they have to maintain their capital structure which leads to reduction of share capital which further leads to increase in per share earnings and price earnings ratio, buy back also allows the company to substitute the buy-back share capital amount with cheaper debts.
4) **To enhance consolidation of stake in the company**[5]
5) **To support share price during periods of sluggish market conditions**[6]

**PROHIBITION OF BUY-BACK OF SHARES**

1) Section 70 of Companies Act, 2013 provides certain conditions which prohibits company from buying back their shares –

[5] https://www.quora.com/Why-companies-buy-back-shares
[6] Supra note no. 2

2) A company cannot buy-back its shares through subsidiary company.
3) A company cannot buy-back its shares through Investment Company.
4) Buy-back is only allowed after a period of 3 years, if company defaults repayment of any securities/dividend/loan/interest payable to shareholder or to any other person.
5) A company has to comply with the provisions of sections 92,123,127,129 in order to buy back its shares.

However a company can receive shares through bequest (by will) and gift and is allowed by companies act further a company may have transferred shares to a nominee in trust but that should be allowed by the articles of the company as laid down in the case of *In re, Indian iron & Steel Co. Ltd.*[7]

**FINANCIAL ASSISTANCE FOR PURCHASE OF ITS OWN SHARE**

Section 67(2) of the Companies Act, 2013 does not allow the company to provide loan or any other kind of financial assistance to any person who later directly or indirectly purchase or subscribe company's shares or shares of its holding company.

However this shall not affect-

*1)* Money lended by a banking company during ordinary course of business. In case of *Louis Steen vs. Charles Allen law*[8] it was held that a baking company cannot be exempted if it provide loans to finance the buy-back of its own shares.
2) A private company which is not the subsidiary of a public company may provide loans/financial assistance for purchase of its own shares although it is not allowed to purchase its own share.
3) A holding company purchasing the shares of own subsidiary company or providing financial assistance to any person to purchase the shares of its subsidiary company.
4) In *Batu Pahat vs. Official Assignee*[9] it was held that money cannot be lended even according to its memorandum and articles to shareholders on the security of company's shares.

[7] AIR 1957 Cal 234
[8] 1963] 3 All ER 770]
[9] [19330] AC 691

If the company does not follow the provisions stated in Section 67 of companies Act 2013, the punished of such contravention could be 1 lakh to 25 lakh and the officers of the company who are default shall also be punishable with fine from 1 lakh to 25 lakh and also can be imprisoned for maximum 3 years. It was held in the landmark case of *Unity Company (P.) Ltd. vs. Diamond Sugar Mills*[10]any financial assistance provided by the company should not in contravention of section 67(2) of companies act 2013.

**BUY- BACK OF SHARES: CONTRAST BETWEEN COMPANIES ACT 1956 AND 2013**

**COMPANIES ACT 1956**

Except few exceptions companies were not allowed to buy back but were later allowed after making amendment and inserting section 77A in companies act in year 1999.

Sub section (1) talks about the fund out of which buy back has to be financed i.e. reserves, security premium account. Further sub section (2) states that buy back is allowed only if articles of the company authorizes it and special resolution in the meeting of board of directors has to be passed in regarding issuance of buy-back of shares. Before passing of such resolution a certificate of solvency has to be submitted to registrar office and in case company is registered on recognized stock exchange then it has to be submitted before SEBI. This sections also states that except Bonus Share no securities can be issued within period of 6 months from the date buy back is done.

**COMPANIES ACT 2013**

This act states that the buy- back has to be completed within the period of 12 months. However this condition was not present in act of 1956. The new companies act had put the limit i.e. only up to 25% of the total paid up capital can be buy-backed and there should be at least gap of period of 1 year in successive buy-backs. Further this new act also talks about transferring of

[10] AIR 1971 Cal. 18

nominal value of amount of share to Capital Redemption Reserve (CRR). Rule 17 of company (capital and debenture) rules of 2014 also provides rules for buy back of shares of unlisted company.

**CONCLUSION**

Buy back which was introduced in year 1999 by an amendment in India has reached to its zenith position in year 2008 when 45 companies announced buy back of their shares in same year and this method is getting popular among corporate world for the last 7-8 years. If see on an average approximately 12% of shares of paid up capital are buy backed by the companies in India.

We can entail that main purpose or objective of buy back is to protect the interest of shareholders of the company and to get this thing done stringent rules and regulations are imposed and various conditions are imposed by the regulatory body such as SEBI which keeps vigilant eye on companies which intent to avoid any such rules.

With changing nature of environment for business in India different provisions related to buy-back also get changed, buy back of shares were first time introduced with an amendment. Provisions of buy back expanded with Companies Act of 2013 with allowed certain necessary conditions for buy back which Companies Act of 2013 didn't had.

Still buy back needs to comply with various rules and regulations which is very complex in nature which in a way delay the process of buy back of the shares which needs to be relaxed so that company announcing buy back function smoothly and does not create any trouble for shareholders.