

# BUY-BACK OF SECURITIES

(For Unlisted Companies)

- **Introduction:**

Buy-back is an excellent tool for financial re-engineering. Buy-back of shares relates to the company buying back its shares which it has issued earlier from the market. Buy-back of shares is nothing but reverse of issue of shares by a company. It means the purchase of its own shares or other specified securities by a company. In case of buy-back, a company offers to take back its shares owned by the investors at a specified price generally determined or arrived at on the basis of the average price of the shares in the past few months. This calculation is usually done at a premium on the market price so as to attract more number of investors, which may vary as per the financial prudence of the company. Thus, Buy-back is one of the prominent modes of capital restructuring.

- **Provisions under the Companies Act, 2013 ('the Act') for Buy-back of shares:**

**Section 68, 69 and 70** brought in by the Companies Act, 2013, has caused this structural change in the theme and philosophy of company law that, subject to the restrictions envisaged in the section, a company may Buy-back its own securities. Thus now it falls under the exceptions where no confirmation by the court is necessary. In line with this, SEBI also came out with SEBI (*Buy Back of Securities*) Regulations, 1998 applicable to listed Company. **Rule 17** of Companies (*Share Capital & Debenture*) Rules, 2014 contains the regulations regarding buy-back of securities for unlisted companies.

- **Sources of Buy-Back:**

Section 68 (1) of the Act provides that buy-back of shares can be financed only out of,—

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

*It is provided that no Buy-back of any kind of shares or other specified securities can be made out of the proceeds of an earlier issue of the same kind of shares or other specified securities as it will frustrate the purpose sought to be achieved by an issue and will make no sense. It can however be used for buy-back of another kind of security.*

- **Conditions for a Buy-Back:**

Section 68 (2) of the Companies Act provides that a company can buy-back its shares or other specified securities only when-

- The buy-back is **authorised by its articles**;
- A special resolution has been passed at a general meeting of the company authorising the buy-back:
- The buy-back is **10% or less** of the total **paid-up equity capital** and **free reserves** of the company and such buy-back has been authorised by the Board by means of a resolution passed at Board meeting;
- The overall limit of buy-back is **25% or less** of the aggregate of **paid-up capital** and **free reserves** of the company.

*In respect of the buy-back of **Equity shares** in any financial year, the reference to **25%** in this clause shall be construed with respect to its total paid-up **equity capital** in that financial year;*

- The buy-back **debt-equity ratio** is within the permissible **2:1** range.  
*The ratio of the aggregate of **secured and unsecured debts** owed by the company after buy-back is not more than twice the **paid-up capital and its free reserves**.*  
*The Central Government is empowered to relax the debt-equity ratio in respect of a class or classes of companies but not in respect of any particular company.*
- All the shares or other specified securities for buy-back are **fully paid-up**.
- The buy-back of the shares or other specified securities listed on any recognized stock exchange is in accordance with the regulations made by the Securities and Exchange Board in this behalf.
- Every buy-back is required to be completed **within 12 months** from the date of passing the **Special Resolution** or the **Board Resolution**, as the case may be.
- *No offer of buy-back under this sub-section 68 (2) shall be made within a period of **1 year** reckoned from the date of **the closure of the preceding offer of buy-back**.*

According to Section 68 (3) the **notice containing the special resolution** should be passed and should be accompanied by an explanatory statement stating:

- All material facts, fully and completely disclosed;
- The necessity for buy-back;

- The class of security intended to be purchased by the buy-back;
- The amount to be invested under buy-back;
- The time limit for completion of buy-back.

*The company is also required to pass a special resolution in its general meeting after following the procedure laid down in section 101& 102.*

- **Time Limit of completion of buy-back:**

Section 68 (4) provides that every buy-back is required to be completed within **1 year** from the date of passing the special resolution or the Board resolution, as the case may be.

- **Modes of Buy-Back:**

Section 68 (5) states that the securities can be bought back from:

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

- **Other Formalities for Buy-back:**

- The company which has been authorized by a **special resolution** shall, before the buy-back of shares, file with the Registrar of Companies a **letter of offer in Form No. SH-8**, along with the fee.

*Provided that such letter of offer shall be dated and signed on behalf of the Board of directors of the company by not less than two directors of the company, one of whom shall be the managing director, where there is one. [Rule 17 (2)]*

- Under Section 68 (6) provides a **Declaration of Solvency** is required to be filed by the company with the Registrar in the prescribed **Form SH-9** signed by at least two directors of the company, one of whom shall be the managing director, if any, and **verified by an affidavit** before the buy-back is implemented to guarantee its solvency for at least a year after the completion of buy-back.

- A company after the completion of buy-back is required to **extinguish and physically destroy its securities within 7 days** of the last day on which the buy-back process is completed. *[U/s 68(7)]*
- A company buying back its securities is **prohibited from making a further issue of securities within a period of 6 months**. It may however make a bonus issue and discharge its existing obligations such as conversion of warrants, stock option schemes, sweat equity or conversion of preference shares or debentures into equity shares. *[U/s 68(8)]*
- A company is also required to **maintain a register** in the prescriber **form SH-10** containing the particulars of the bought back securities, including the consideration paid for them, the date of cancellation, the date of physically extinguishing and physically destroying securities and such other particulars as may be prescribed. Section 68 (9) also states that such particulars are required to be entered in the register of buy-back of securities **within 7 days** of the date of completion of buy-back.
- On completion of the buy-back process, the company shall within a period of **30 days file with SEBI and the Registrar** a return in the **Form No. SH-11** along with fees. A private company and a public company whose shares are not listed on a recognized stock exchange should file the return of buy-back with the Registrar only. Non-compliance with the above mentioned requisites is a punishable offence under Section 68 (11) of the Companies Act. *[U/s 68(10)]*
- Section 69 deals with transfer of certain sums to **capital redemption reserve account (CRR)**. Where a Company purchases its own shares out of free reserves or securities premium account then a sum equal to nominal value of the shares purchased has to be transferred to the CRR A/c and details of such transfer are required to be disclosed in the balance sheet. *[U/s 69(1)]*
- The CRR A/c 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. *[U/s 69(2)]*

- **Restrictions on Buy-Back:**

Section 70 (1) of the Companies Act restricts modes of Buy-back. The companies are restricted to Buy-back its shares-

- through any subsidiary company including its own subsidiary companies.
- through any investment company or group of investment companies; or
- if a default, is made by the company, in respect to
  - ❖ Repayment of deposits or interest payment thereon, or
  - ❖ Redemption of debentures or preference shares or
  - ❖ Payment of dividend to any shareholder, or
  - ❖ Repayment of any term loan or
  - ❖ Interest payable thereon to any financial institution or banking company.
- In case it has not complied with the provisions of section 92, 123, 127 and 129 of the Act.

- **Explanation:**

- For the purposes of Section 68 and Section 70, “**specified securities**” includes employees’ stock option or other securities as may be notified by the Central Government from time to time.
- For the purposes of Section 68, “**free reserves**” includes **securities premium account**.
- Noteworthy aspect is that as per the definition of “**Free reserves**” under Companies Act, 2013 does not include the **Securities Premium Account** as disparity to the free reserve definition under Companies Act, 1956 which included the Securities Premium Account.

- **Time Line of Buy-Back:**

No. of days/ time taken	Activity	Date
X days	Holding of Board Meeting for considering buy back proposal, approving buy back price and notice of EOGM (if required)	
X + 2	Issue of Notice With Explanatory Statement (as mentioned) to all the members	
X+ 25	Holding EOGM and passing Special Resolution	
X+ 26	Obtaining Declaration of Solvency (Verified by an affidavit) in Form SH-9 and filing of draft Letter of Offer with the ROC along with the declaration of solvency in e-Form SH-8	
X+26	Filing of Form MGT-14 with the ROC (for Registering Special Resolution)	
X+26	Dispatch of letter of offer to all members after filing the same with ROC but not later than 20 days from its filing with the ROC	
X+41 (Minimum) X+56(Maximum)	The offer for buy-back shall remain open for a period of not less than 15 days and not exceeding 30 days from the date of dispatch of the letter of offer.	
Within 15 days from the date of the closure of the offer	Verification of offers to be completed within 15 days from the date of the closure of the offer and the shares or other securities lodged shall be deemed to be accepted unless a communication of rejection is made within 21days from the date of closure of the offer.	
Immediately on closure of offer	Open a special bank account and deposit therein such sum, as would make up the entire sum due and payable as consideration for the buy-back	
Within 7 days from completion of verification	Making payment in cash or bank draft/pay order to those shareholders whose offer has been accepted or return the share certificates to the shareholders forthwith.	
Immediately after completion of acceptance	The company shall maintain a register of shares or other securities which have been bought-back in Form No. SH.10	
Within 7 days from completion of acceptance	Extinguish and physically destroy the shares bought back in the presence of the Company Secretary in whole time practice	
Within 30 days from completion of acceptance	File requisite form SH-11 ( <i>Form SH-15 as attachment</i> ) with the ROC	

- **Checklist of Buy-Back:**

- Ensure that there is a specific provision in the Articles of Association authorizing the Company to buy back its own shares. If the Articles don't contain such provision, then the Company first needs to amend its Articles of Association by passing a Special Resolution.
- Pass a Special Resolution or Board Resolution as case may be, in the General Meeting or Board Meeting authorizing the buyback of shares.
- Ensure that no buy back was made during a period of 365 days immediately preceding the current buy back.
- Ensure that post buy back Debt Equity Ratio of the Company i.e. amount of debt should not be more than twice the paid up capital and free reserves.
- Ensure that all the shares of the Company which are going to be purchased by the Company should be fully paid up.
- Ensure that the Company does not issue same kind of securities within a period of 6 months from the completion of buy back.
- Where a company buys-back its shares it should maintain the register of thesecurities so bought, the consideration paid for the securities bought-back, thedate of cancellation of securities, the date of extinguishing and physicallydestroying of securities and such other particulars as may be prescribed.

- **Buyback under Foreign Direct Investments Guidelines**

**Buyback of securities from Non-resident Shareholders:**

As per *RBI/2005-06/149A. P. (DIR Series) Circular No. 10 dated 30<sup>th</sup> August, 2015* transfer of shares/convertible debentures through buy-back or capital reduction falls under Automatic route. Therefore, it is clarified that the FC-TRS require to file with RBI for Buy-back of securities from Non-resident Shareholder under FDI.

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