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All possible efforts made for simplification but still if any mistake found then also bring into my notice by just smsing *DO NOT CALL*

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☸BUY BACK OF EQUITY SHARES (Sec.77)☸

Learning Objectives :::::::::::::: *After studying this unit, you will be able to:*

- know meaning, objective of buy back;
- conditions of buy back;
- source of buy back;
- various effect of buy back; and
- different types of buy back.

HISTORY

Prior to the amendment of the 1999 of the companies act there was no way for a company so that it could buy its shares back from the shareholders without a prior sanction of the court (except for the preferential shares). The laws as to the buying of its share by the companies were very stringent. Some of the ways by which a company could buy its shares back were as follows:-

(i) Reduction of share capital as given in sections 100 to 104.

(ii) Redemption of redeemable preferential shares under section 80.

(iii) Purchase of shares under an order of the court for scheme of arrangement under section 391 in compliance with the provisions of sections 100 to 104.

(iv) Purchase of shares of minority shareholders under the order of the company law board under section 402(b).

Though there were ways by which a company could buy its shares back from the shareholders but it could not be done without the sanction of the court. This was done to protect the rights of the creditors as

well as the shareholders. But the need of less complex ways of buying its shares back by the company was always felt. The much needed change in the companies act was brought about by the companies' amendment act 1999.Sections 77A, 77AA and 77B were inserted in the companies act by this amendment.

Share capital is a very essential part of a company, listed or unlisted. Share capital can be of two types i.e. equity share capital or preferential share capital. The share capital of a company has to be subscribed by one or more persons. After the share of a company has been allotted to the subscribing members, the subscribers have no right over the money gone as proceeds of the shares subscribed. All / selective shareholder has the right to vote at the general meetings of the company or the right to receive dividends or right to such other benefits which may have been **prescribed**. The only option left with the shareholder in order to realise the price of the share is to transfer the share to some other person.
But there are certain provisions in the companies act which allow the shareholders to sell their shares directly to the company and such provisions are termed as buy back of shares. Buy back of shares can be understood as the process by which a company buys its share back from its shareholder or a resort a shareholder can take in order to sell the share back to the company.

As an alternative mode of buy-back but without requiring approval of the Court/NCLT, a Company can carry out buyback of shares and other specified securities (section 77A and related provisions). The conditions and requirements for carrying out buy-back of securities are as follows:

INTRODUCTION :

RESTRICTION ON PURCHASE OF ITS OWN SHARES BY A COMPANY:

- *Section 77 of the Companies Act does not allow a company to buy its own shares until the winding up of companies. But the subsequent Section 77A permits buyback subject to certain conditions. What is the rationale behind?*
  Most of the sections in the Companies Act tries to protect the interest of the outsiders who had lent money in the form of debentures or loans or deposits by restricting company not to pay unless outsiders (loan vendors) are paid fully.
  Shareholders are paid last and have taken maximum risk in the company.

Section 77(1) of the Company's Act provides that a company limited by shares or a company limited by guarantee having a share capital cannot buy its own shares.

As we were aware Indian Companies were not allowed to purchase its own securities prior to coming into come into force of companies Amendment Act 1999. The said amendment inserted new section 77A, 77AA, 77B into the Companies Act so as to enable Indian Companies to repurchase its own securities.
The repurchase of outstanding shares by a company in order to reduce the number of shares on the market. Companies will buy back shares either to increase the value of shares still available, or to eliminate any threats by shareholders who may be looking for a controlling stake.

The purpose of insertion of these provisions into companies act was to enable companies to get rid of their unwanted surplus share capital through a process of repurchase for cancellation/ extinguishment without having to resort to lengthy process of reduction of share capital of the company through high court approval. Apart from these, Listed Companies desirous of buyback of shares are required to comply with SEBI buy back regulations.

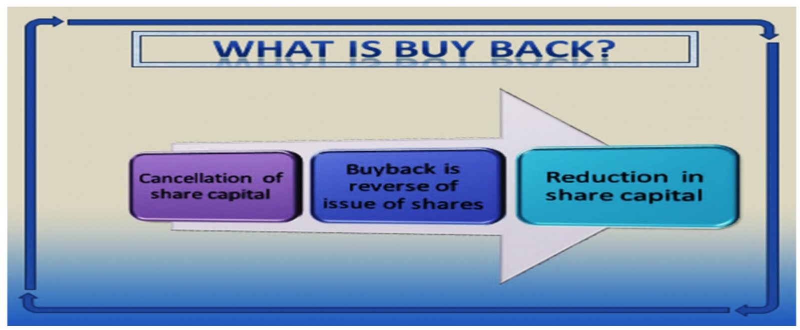
Example:- **Increase In The Value Of Shares.**

Mr. Anil Ambani (Reliance Energy)
Bought 6,50,000 Eq.Shares of the Company on Tuesday at Rs.1279.23/share, Aggregating Rs. 831.5 million [Amounting Company's 10% of Equity and Free Reserves].
Result:- At Noon Friday, Shares of the Company were trading at Rs. 1310 i.e. UP By 28.20 from its Previous close at BSE.

Meaning of Buy Back of Shares
There is no definition given by the Company Act, 1956 about the buy back of shares. But in simple words, we can say that buy back of shares means repurchase of its own shares by the company. In other words, buy back of shares means a company buying its own shares.
Buyback is reverse of issue of shares by a company where it offers to take back its shares owned by the investors at a specified price; this offer can be binding or optional to the investors
It is opted by company if there was an addition funds with company and there is no profitable application where these funds can be invested.

MEANING OF BUYBACK OF SHARES

- Cancellation of share capital
- Buyback is reverse of issue of shares
- Reduction in share capital
- company buy its own shares from public,
- at a specified price,
- which can be binding or optional to the investors.



What is Buyback?

- Simply put buyback of shares is processes where a company seeks to repurchase to its own securities from its existing shareholders directly through tender offer or from open market, i.e. through stock exchange. In other words is akin to a company investing in itself. In other word it is a Process by which a company to bring their shares back from the shareholders and shareholders sell their shares directly to the company.

Reasons for buyback / Why do companies buy back its own securities ?

Briefly a company resorting to the buyback may have surplus cash, and it may not have found the right avenue to invest such surplus cash, during such period of dilemma the company may decide to return the surplus cash by buying back its shares, with a hope that at a later time when the company brings on an expansion the investors do not lose their faith in the company. Secondly the company might as well think of buying its shares with a view to increase the value of the shares which after the process of buy back still remain in the market. For after the shares are bought back the number of marketable shares become less and thus the prices increase. Thirdly, at times there is a slump in the share market due to no fault of the company. Though the slouch may be temporary but may have continued far too long .The management then may decide to give value to the shareholders and buy back their shares at a price higher than the market price. This is generally done to install faith in the minds of the shareholders. Saving a company from hostile take-over has always been seen as a major force behind bringing about this amendment, the company may use the surplus cash available in buying back its shares and bringing the number of floating shares down, resulting in the suitor not finding it a worthy investment or a profitable acquisition. These could be certain reasons why a company may resort to buy back of its shares.

In detail below:
Buyback of securities offers several benefits to the company, particularly on financial fronts.

1. Buyback enables a company to get rid of their surplus unwanted share capital without recourse to reduction of share capital through High Court route under section 100 to 104 of the companies Act.
2. Buyback entails repurchase of its own shares by a company which are subsequently extinguished, the resulting in decrease in the number of outstanding shares. Consequently, Earning per shares improves which turns leads to higher market value in the stock market since EPS closely influences market price of shares quoted on stock exchange.

3. Quite often buyback may resorted to as a tool to pop up the stock prices whenever company feels that its shares are undervalued in the stock market.
4. If a company cannot deploy the surplus cash in a growth process from which it would be able to maintain average return on capital employed and earning per shares, Board of Directors is the custodian of shareholders money, if it cannot add better value or even maintain the current rate of value addition, it should refund the money to the shareholders. The management may like to return surplus cash to shareholder in the form of buyback when there are no proper investment opportunities to maintain the rate of return.
5. Likewise, buyback would lower the P/E ratio in the wake of improvement in EPS. Lower P/E ratio is viewed positively to stock market. Thus improved EPS coupled with lower P/E ratio and higher ROA would have an overall positive impact on the stock prices.
6. Buyback offer provide an easy exit route for the shareholders through which they can sell their share to the company itself at a premium, This is an attractive option for them particularly when shares of the company are undervalued.

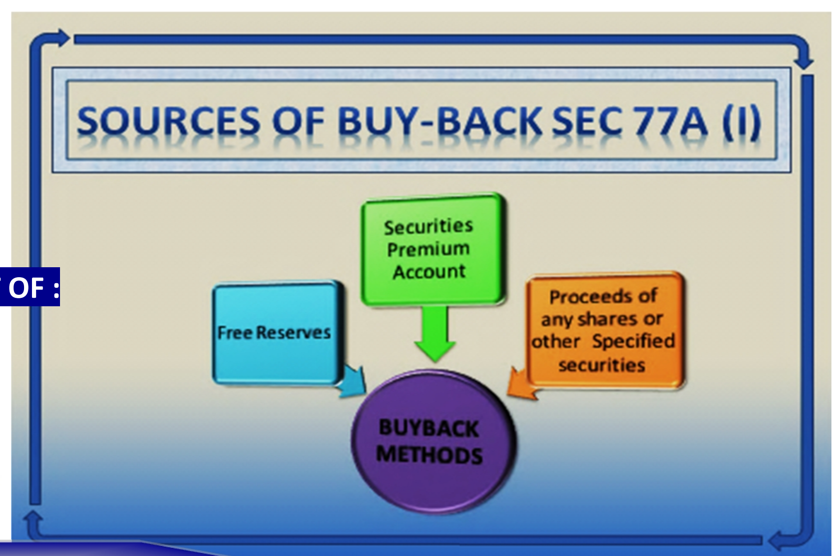
Reasons for buyback / objective of buy back of shares :

in simple:

In the words of the working group which recommended the introduction of buy back in the companies act:
"It is an erroneous belief that the sole reason for buy back is to block hostile take-overs. In this connection it is pertinent to list five reasons why the bank of England favoured the making of law to allow companies to repurchase their shares of which blocking take-over was only one:

Shares may be bought back by the company on account of one or more of the following reasons

- To facilitate reduction of share capital,
- To increase promoters holding.
- Increase earnings per share i.e. to increase the underlying share value/To generate higher return on the left over equity shareholders;
- To achieve or maintain a target capital structure or Rationalize the capital structure by writing off capital not represented by available assets.
- **Tax Gains**: Since dividends are taxed at higher rate than capital gains, companies prefer buyback to reward their Investors instead of distributing cash dividends, as capital gains tax is generally lower. At present, short-term capital gains are taxed at 10% and long-term capital gains are not taxed while DDT is 15%
- Support share value i.e. to support the share prices during temporary weakness/To maintain shareholder's value in the situation of poor secondary market;
- To shrink equity base/Smaller equity base
- To prevent takeover i.e. to prevent or inhibit unwelcome take-over bids / To prevent hostile takeover bids;
- To return/pay surplus cash not required by business i.e. Effective utilization of surplus cash/to return surplus cash to shareholders.
- To arrest downward trend in the value of shares.
- In fact the best strategy to maintain the share price in a bear run is to buy back the shares from the open market at a premium over the prevailing market price.



WHAT IS THE SOURCES OF BUY BACK? / BUY BACK OUT OF :

1. Free Reserves
2. Securities Premium Account
3. Proceeds of any shares or other specified securities.

[Under section 77A (1)]

A Company can purchase its own shares out of

- Free Reserves
- Securities Premium Account
- Proceeds of an earlier issue of shares but not as the same kind of shares that are buying back or
- other specified securities (Sec 77 A(1))

  Other specified securities include employees stock option or the securities as mentioned by central government from time to time.

  Buyback of any kind of shares is not allowed out of the proceeds of any earlier issue of same kind of shares of same kind of securities.

- **Free reserves:** Where a company purchases its own shares out of free reserves, then a sum equal to the nominal value of the share so purchased shall be transferred to the capital redemption reserve and details of such transfer shall be disclosed in the balance-sheet
- **Proceeds of any shares or other specified securities:** A company cannot buy back its shares or other specified securities out of the proceeds of an earlier issue of the same kind of shares or specified securities.

Meaning of Free Reserves :

For the purpose of section 372A the term ‘free reserves’ has being defined as those reserves which as per latest audited balance sheet are free for distribution as dividend and it includes balance of securities premium account. The term free reserves means the balance in the share premium account, capital and debenture redemption reserves shown or published in the balance sheet of the company and created by appropriation out of the profits of company, but does not include the balance in any reserves created:

i. For repayment of any future liability or for depreciation in assets or for bad debts;

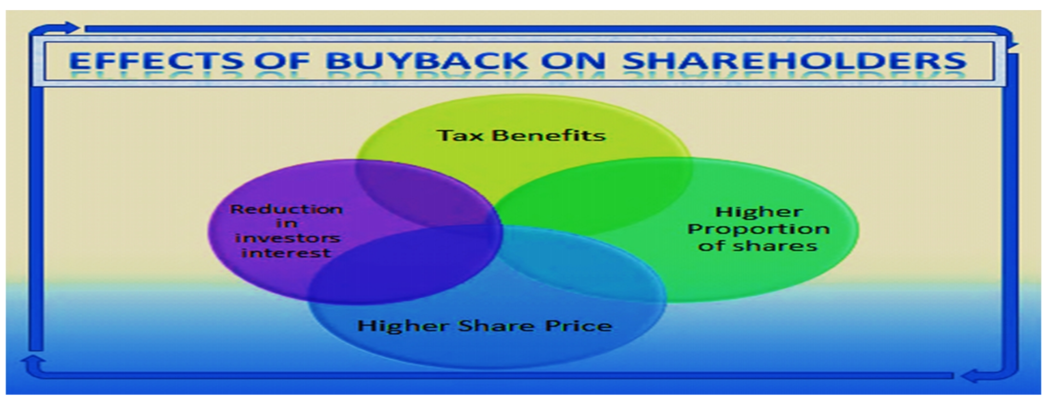
ii. By the revaluation of any assets of the company.

While determining the aggregate of paid up capital and free reserves the following items should be deducted:

i. Amount of accumulated losses

ii. Balance of deferred revenue expenditure

iii. Intangible assets



<u>EFFECTS OF BUYBACK OF SHARES</u>

Effects on Shareholders:

- Tax Benefits
- Higher Proportion of shares
- Higher share price
- Reduction in investors interest

<u>EFFECT OF BUY BACK ON STOCK EXCHANGES</u>

- In most of the cases the stock exchange won’t positively reply to the Buy back
- Buyback may leads to abnormal increase of prices
- Lead to reduction in interest of investor in the market particularly with de-listing of good share Eg: PHILIPS, P&G India etc.
- Posing heavy risk

Eg: It was feared in 2001-03 that de-listing by many MNC’s may drop the money flow to stock exchanges.

<u>Buy back positive impact</u>

- It could enable a company to achieve its desired capital structure more quickly or facilitate a major restructuring.
- Market generally interprets buy-back as a positive aspect.
- It could avert a hostile takeover bid by reducing the number of shares in circulation.

- Shareholders have a choice of deciding whether or not to receive the payout by selling or holding their shares, unlike a dividend payout.
- Returning excess cash by way of a share buy-back gives a company greater flexibility with regard to it's dividend policy.

Buy back negative impact

- Re-purchase of it's own shares may conversely have a negative signaling effect.
- Management may not seek to utilize any existing excess cash effectively
- Possible mismanagements may arise -
    - if too high a price is paid for the re-purchased shares or
    - if Cash resources are eroded to the level that could give rise to a risk of insolvency.
- A return of funds by way of a share buy-back is less certain than an annual dividend stream**.**

Checklist for investors before accepting the company's buyback offer

- Take a look at the share price movement immediately before the buyback. If there was a significant rise, the prima facie assumption is that the promoters have been up to tricks.
- Debt-equity ratio: The companies are hugely under debts are unlikely to have free cash.
- Companies that have just come to the capital markets to raise money are unlikely to be good candidates for buyback.
- Share price does not flare up due to speculators.
- Passing the resolution with lot of publicity, Empowering the board to buyback whenever allowed , there is enough scope for suspecting.

BUY BACK CONDITION AND LIMITS [Section 77A] :

Company shall not buy back its shares unless the following conditions are satisfied

Section 77A of the Company act, 1956 has allowed the company to buy back its shares subject to certain conditions which are as follow

Section 77 A (2) of the Companies Act, 1956 requires that buyback should be carried out if—

- ✓ Authorised by its articles of association of the Company;

- ✓ A special resolution have to be passed in the general meeting of the company authorising the buyback, in other word a **special resolution** has to be passed in the general meeting of the company authorising the buy-back if it was not authorised by Articles of association of the Company

Exception:

If the buy back is 10 % or less than 10 percent of the total paid up equity share capital, a resolution at the general meeting is not needed to be passed rather a simple board resolution is enough.

Provided that no offer of buy back shall be made within three sixty five (365) days reckoned from the date of proceeding offer of buy back or Similar Buyback i.e. by passing Board Resolution shall not be made in the next 365 days.

- ✓ The buy back does not exceeds 25 % (twenty five percent) of the paid up capital and free reserves of the company;

Also a company cannot buy back more than 25% (twenty five percent) of its paid up equity capital in any financial year.

In other word the buy-back should be up to 25% of the total paid-up capital and free reserves and in any case the buy-back of equity shares should not exceed 25% of the paid-up equity share capital in a financial year.

- ✓ The ratio of the debt owed by the company is not more than twice the capital and its free reserves after such buy back **(Debts include all amounts of unsecured and secured debts)**;

In other word debt equity ratio should not be more than 2:1 after buy back.

In simple the debt equity ratio post buy back should not exceed 2:1. For this purpose, the term "debt" includes all secured as well as unsecured debt.
However central government may prescribe a higher ratio.

- ✓ There has been no default in any of the following

Prohibition of buy back: Section 77B requires a company cannot buy back its shares or other securities in case any of the following defaults is subsisting:

- in repayment of deposit or interest payable thereon,
- redemption of debentures, or preference shares or
- payment of dividend, if declared, to all shareholders within the stipulated time of 30 days from the date of declaration of dividend or
- Repayment of any term loan or interest payable thereon to any financial institution or bank;

- ✓ All the shares and/or other specified securities should be fully paid up i.e. partly paid-up shares not allowed (It is same like redemption of preference shares);

- ✓ The buy-back has to be out of free reserves/securities premium account or out of proceeds of issue of shares or other specified securities other than the type of the same kind of securities. Where the buy-back is from **free reserves,** the Company is required to transfer an amount equal to the face value of the shares bought back to Capital Redemption Reserve.

For listed shares as per guidelines issued by SEBI

- ✓ Buy back of shares and/or other securities listed on any recognised stock exchange should be carried out in accordance with the Regulation made by the Securities and Exchange Board of India in this behalf. In other word buy back should be i accordance with SEBI guidelines for listed companies.

- ✓ The buy back in respect of shares and other specified securities other than those specified in the aforesaid clause is in accordance with the guidelines specified.

Time limit for completion of buy-back:

- ✓ Buyback shall be completed **within 12 months** from passing of Special Resolution or Board Resolution, as the case may be.

- ✓ There has been no default in complying with the provisions of filing of Annual Return, Payment of Dividend, and form and contents of Annual Accounts;

- ✓ A notice of meeting to authorise buy back should be given with explanatory statement.

- ✓ Before making purchases under buy back, a declaration of solvency in the prescribed form has to be filed with the ROC.

- ✓ Affidavit has to be submitted.

- ✓ Where buy back is for 10% or less than of the total paid-up equity capital and free reserves, the buy-back can be authorized by the Board without approval by special resolution. In such case, further, there should be gap of 365 days between two such buy-backs; and

- ✓ The authority by way of special resolution of Board will be valid for twelve months.

- ✓ **Prohibition on further Issue of similar shares for the period of 6 months.**

Prohibition on buy back / prohibition of buyback in few circumstance (section 77b) :

Section 77B puts the restrictions on companies to buy back its shares. Company shall not directly or indirectly purchase its own shares or other specified securities : -

- Through any subsidiary company including its own subsidiary companies or
- Through any investment companies or group of investment companies or
- If the company has not complied with the provisions of-
  * sec.159 (filing of annual return)
  *sec.207 (Payment of dividend within 30 days)
  *sec.211 (Annual accounts to present true and fair view)
- If There has been default in any of the following / If any of the following defaults are subsisting:
  - In repayment of deposit or interest payable thereon,
  - Redemption of debentures, or preference shares or
  - Payment of dividend, if declared, to all shareholders within the stipulated time of 30 days from the date of declaration of dividend.
  - Repayment of any term loan or interest payable thereon to any financial institution or bank;

In case a Company that has not complied with section 159, 207 or 211.

Penal provisions in case of default – Two years' imprisonment **or** a fine of Rs. 50,000/- **or** both to every person connected with the default.

NOTICE OF THE MEETING - Sec 77A (3) / BUY BACK RESOLUTION / DISCLOSURES IN THE EXPLANATORY STATEMENT :

Buy back resolution can be passed in the Annual General Meeting called under section 166 of the Companies Act, 1956 or in any other general meeting called under section 171. If the buy back agenda is brought before a general meeting convened under section 171, it's become a special business under section 173. In addition to the general requirement under section 173, it is necessary to enclose an explanatory statement with the notice of the meeting. Section 77 A (3) requires that a buy back notice should accompany the notice of the meeting and that explanatory statement should include the following information:

The notice of the meeting at which special resolution is proposed to be passed shall be accompanied by an explanatory statement stating:

- The date of the meeting at which the proposal for buy-back was approved by the Board of Directors of the company.
- A full and complete disclosure of all material facts;
- The necessity of buy back;
- The maximum amount required under the Buyback and the sources of funds from which the buy-back would be financed;
- The class of securities intended to be purchased under the buy back;
- The amount to be invested under the buy back;
- The time limit for completion of the buy back;
- The basis of arriving at the buy-back price;
- The number of securities that the company proposes to buy-back;

Time limit and mode of buy back / buy back within 1 year - sec 77a (4) :

As per section 77 A(4) of the companies Act 1956 the buy back should be completed **within twelve months** from the date of passing special resolution.

Four modes of buy back have been specified in Section 77 A (5) :

- From the existing security holders on a proportionate basis;
- From the open market;

- From odd lots
- By purchasing the securities issued to employees pursuant to a scheme of stock option or sweat equity

Declaration of Solvency:

A company intending to buy back is required to furnish a declaration of solvency after passing buy back resolution. This declaration of solvency should be filed before making purchase to the SEBI and the Registrar of Companies. It should be in the prescribed form and verified by affidavit. The declaration of solvency is to the effect that the Board has made a full inquiry into the affairs of the company as a result of which it is capable of meeting its liabilities and will not rendered insolvent within a period of one year of the date of declaration adopted by the Board.

Declaration of solvency – sec 77a (6), in simple

Declaration of solvency to be filed with the -

a. Registrar of company ; and
b. SEBI (for listed company only)

That it is capable of meeting its liabilities and will not be rendered insolvent within one year of the date of declaration adopted by the board.

Note : This declaration is to be signed by at least two directors of the co. one of whom shall be M.D., If any.

FILING OF DECLARATION WITH THE REGISTRAR OF COMPANIES AND SEBI :

As soon as a company has passed the Board/Special resolution for buy-back but before making the buy-back, the company shall file declaration of solvency in form 4A with the Registrar of Companies in the prescribed Form **4A** attached with the e-Form 62 a declaration of solvency duly verified by an affidavit to the effect that the Board of directors has made a full enquiry 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 one year of the date of declaration adopted by the Board. The declaration of solvency shall be accompanied with an affidavit. The declaration must be approved by the Board and signed by at least **two directors** one of whom shall be the managing director of the company, if any.

In case of listed companies, a copy of declaration of solvency is also required to be filed with SEBI also.

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 recognized stock exchange.

Format for declaration of solvency

Name of the Company : ABC (INDIA) LTD.
Address (Regd. Office) : 45, M.G. Road, Delhi
Presented by : Shri Ramesh, Managing Director

We, Shri Ramesh, the Managing Director and Shri Kishore, Jt. Managing Director, being all the directors of M/s ABC (INDIA) LTD. do:

Solemnly affirm and declare that we have formed the opinion that the Company is capable of meeting its total liabilities and that the Company will not be rendered insolvent within a period of one year from the date of making this declaration.

We append a statement of Company's assets and liabilities as at …….. being the latest date before making of this declaration.

We further declare that the Company's audited annual accounts including the Balance Sheet have been filed upto date with the Registrar of Companies, Maharashtra.

Ramesh	Kishore
Managing Director	Jt. Managing Director

Verification

And we make this solemn declaration believing the same to be true and we solemnly declare that we have made a full enquiry into the affairs of the Company including assets and liabilities of this Company and that having done so and having noted that the shareholders by a special resolution have approved the buy-back of 10,00,000 (Ten Lakhs) number of equity shares as per the provisions of the section 77A of the Companies Act, 1956.

Verified this day the .... day of 20

Ramesh	Kishore
Managing Director	Jt. Managing Director

Solemnly affirmed and declared at .... the .... day of .... 2005 .... before me.
Commissioner of Oaths and Notary
Public or Justice of the Peace

Regulatory Framework :

- **Passing of Special Resolution in General Meeting of the Company**
- **Methods of Buy Back**
- **Appointment of Merchant Banker to the offer**
- **Make the Public Announcement**
- **Draft the Letter of offer**
- **Dispatch the Letter of offer to the shareholders**
- **Pay full and final consideration to shareholders who have accepted the offer**
- **File final report with SEBI & Public announcement**
- **Extinguishment of Share Certificate**

REQUIERMENTS AFTER BUY BACK :

- **Extinguishing bought back shares/destruction of the securities, sec 77a(7):**

Section 77 A(7) requires that where a company buys back its own shares, it shall extinguish and physically destroy the securities so bought back **within seven days** of the last date of completion of buy back.
Bought back shares are called treasury stock. This treasury stock is utilised in the developed market for conversion of preference shares or debentures/bond into equity. This can be used for discharge of warrant. Treasury stock is also used for discharge of purchase consideration in merger and acquisition.

- **Restriction on further issue of shares Sec 77A(8):**

Every buy-back shall be completed within **twelve months** from the date of passing the special resolution or Board resolution as the case may be.
Section 77A (8) requires that where a company complete a buy back of its securities, it shall not make further issue of same kind of securities in any manner whether by way of public issue, rights issue **up to six months from the date of completion of buy back under section 81(1)(a) of the companies act 1956,** It may however issue bonus shares or discharge its subsisting obligations such as conversion of warrants, stock options scheme, sweat equity/other specified securities into equity shares or conversion of preference shares or debentures into equity.
OR company can make issue of same class of shares of Buy Backed Shares after a period of 24 Months.

- **Maintenance of Registrar relating to Buy back, Sec 77A(9):**
  After completion of buyback, a company shall maintain a register of the securities/shares so bought back and enter therein the following particulars :

i) Securities so bought,
ii) The consideration paid for the securities bought back.

ii) The date of cancellation of securities
iii) The date of extinguishing and physically destroying of securities.
iv) Other particulars as may be prescribed.

Section 77A(9) requires that where a company buys back its securities it shall maintain a register of the securities stating securities so bought, the consideration paid for the securities bought back, the date of cancellation of securities, date of extinguishment and physical destruction of securities and such other particulars as may be prescribed. The shares or the securities so bought back shall be physically destroyed within seven days from the last date of completion of such buy back.

- **Return of Buy back/filing a completion return – sec 77a(10):**

Section 77A (10) requires A Company shall after the completion of the buy-back file return with ROC and a SEBI return in form 4 C on completion of buy back. The return should contain the prescribed details relating to the buy-back. The return shall be submitted **within thirty days** from the date of completion of the buy back for listed company.
No return shall be filed with the Securities and Exchange Board of India by an unlisted company.

- **Stamp duty on Buy back:**

Buy back is transfer transaction under section 2(47) of the Income tax 1961. Under section 2(47) of the Income tax 1961. Under section 3 of the Indian Stamp Act, 1899 read with Item No. 62 of Schedule I transfer of shares is chargeable to stamp duty. Unless specifically exempt tendering shares under buy back requires an execution which is chargeable to stamp duty. And there is no special reason to exempt stamp duty chargeable on buy back. Stamp duty is payable by a person who executes transfer. However, share buy back through depository system is not subjected to stamp duty.

- **Tender offer for buy back:**

Buy back through tender offer is a method of buy back by which a company can buy back shares from its existing shareholders on proportionate basis. For buy back through tender offer it is necessary to make public announcement of buy back in atleast one English national daily,one Hindi national daily and one Regional language daily wide circulation at the place where the registered office of the company is situated.
A specified date should be announced in the public announcement which would be the date of reference for buy back offer. The shareholders whose name appear in the shareholder Register on the specified date should be given tender offer by the company.

Forms:

a. Form 4A – Form of Declaration of Solvency
b. Form 4B – Form of Register of Buy-back
c. Form 4C – Form of Return to be filed with ROC/SEBI within 30 days of buy-back

REQUIERMENTS AFTER BUY BACK : in simple

1. SECURITIES BOUGHT BACK SHOULD BE EXTINGUISHED AND PHYSICALLY DESTROYED WITHIN 7 DAYS AFTER THE COMPLETION OF BUYBACK;
2. COMPANY CANNOT ISSUE SAME KIND OF SHAES BOUGHT BACK WITHIN 24 MONTHS;
HOWEVER THE FOLLOWING ARE PERMISSIBLE:
a) ISSUE OF SHARE OF A DIFFERENT CLASS
b) BONUS ISSUE
c) CONVERTION OF WARRANTS
d) SWEAT EQUITY SHARE
e) EMPLOYEES STOCK OPTOIN
f) CONVERSION OF DEBENTURE OR PREFERANCE SHAES
3. MAINTAIN REGISTER OF SECURITIES BOUGHT BACK, CONSIDARATION PAID, DATE OF CANCALLATION OF SECURITIES, DATE OF EXTINGUISHMENT AND PHYSICAL DESTRUCTION OF SECURITIES;
4. RETURN OF BUY BACK TO BE FILED WITH ROC IN 30 DAYS;
5. IF BUY BACK IS FROM FREE RESERVES, SUM EQUAL TO NOMINAL VALUE OF SHARES BOUGHT BACK SHOULD BE TRANSFERRED TO CAPITAL REDEMPTION RESERVE AND TO BE DISCLOSED IN BALANCE SHEET.

Checklist for Buyback of Shares/Securities for Unlisted Companies

Particulars	Yes/No	Details	Comments
AOA should authorise buyback	No		➢ AOA must be amended as per procedure laid down u/s 31 of Companies Act, 1956 ➢ Form 23 to be filed within 30 days of passing special resolution.
Authorisation by special Resolution		A special resolution to be passed in AGM, authorising BOD to buy back. **Particulars of Explanatory statement.** ➢ Complete disclosure of material facts ➢ Necessity for Buy-back ➢ Classes of securities to be purchased under buy-back ➢ Amount to be invested under buyback ➢ Time limit for buyback	➢ Provisions of sec. 171,172 and 173 of Companies Act, 1956 are applicable. ➢ Above provisions are not applicable to Private Co, unless it is in the article of the Co. ➢ Even the private Co has to annex explanatory statement stating the particulars of Buyback. ➢ Form 23 to be filed within 30 days of passing special resolution.
RESOLUTIONS **a) Board Resolution** **b) Special Resolution**		 Upto 10% of total paid up equity capital & free reserves. Exceeds 10% of total paid up equity capital & free reserves.	➢ An offer for buyback shall not be made within a period of 365 days from date of the preceding offer of buyback, if any. ➢ Special Resolution to be passed with 3/4th majority. ➢ To file Form 23 within 30 days of passing special resolution.
Quantum of Buyback		➢ Buyback should be less than or equal to 25% of total paid up equity capital & free reserves. ➢ In any FY, buyback of **Equity Shares** shall not exceed 25% of total paid up equity capital in that FY.	➢ The quantum of shares to be bought back must be within both of aforesaid limits. ➢ All securities to be bought back are fully paid up.
Sources of Buyback		A company has statutory reserve, which has to be transferred to general reserve in consultation with the Auditor.	➢ Out of free reserves, ➢ Securities Premium a/c, ➢ Proceeds of any shares or securities.
Amount to be transferred to Capital Redemption Reserves		Where buyback is effected by free reserves, sum equal to nominal value of share purchased to be transferred to CRR & such transfer to be disclosed in B/S.	
Securities not allowed to be bought back		➢ Partly paid up ➢ Securities which are lock-in-period or non-transferable.	
Time Limit for completion of buyback		➢ Every buy back should be completed within a period of 12 months from date of passing special resolution or board resolution as the case may be.	
Debt-equity ratio			Ratio of Debt (secured & unsecured) should not be twice the paid up capital & free reserves after such buyback
Modes of Buy back		➢ From existing shareholders on proportionate basis ➢ From open market ➢ From odd lots holders ➢ From employees of the Co, to whom securities are issued under ESOP or sweat equity.	**Prohibited modes of Buyback** Company cannot buy back its own shares through; ➢ Subsidiary Companies ➢ Investment Companies ➢ Co. has also not defaulted in a) repayment of deposit or interest payable thereon

			b) redemption of Debentures or Preference shares c) payment of Dividend d) repayment of any term loan or interest payable thereon. e) Filing of annual return thereon u/s 159 f) Penalty for failure to distribute dividend within 30 days u/s 207 g) Forms & content of B/s & P/L A/c u/s 211.
Filing with ROC		Following documents to be filed with ROC. ➢ **Draft letter of offer** to be filed with ROC after passing special resolution but before buyback. ➢ Declaration of solvency by the Directors in form 4A. ➢ Report on the state of affairs of the Co. by the auditors of the Co.	
Dispatch letter of offer		Letter of offer to be dispatched within 21 days of filing with ROC	
Offer open		Offer to be open for 15 to 30 days from date of dispatch of letter of offer.	➢ If securities for buyback are more than the total no of securities, buyback to be made on proportionate basis. ➢ Shares deemed to be accepted unless communication is made within 21 days from the closure of the offer. ➢ To open special A/c after date of closure of the offer& deposit such sum payable as consideration for buy back. ➢ Make payment within 7 days from 15 days from date of closure of the offer.
After Buyback		➢ Share certificates to be physically destroyed within 7 days from completion of buyback ➢ Certificate verified by 2 directors including MD and certified by PCS for compliance of rules filed with ROC within 7 days of certificates destroyed ➢ Maintain a record of share which has been cancelled & destroyed within 7 days of buyback. ➢ Maintain a register of securities which are bought back. ➢ Return of buy back to be filed with ROC within 30 days of completion as is given in Form 4C.	

PROCEDURE FOR THE BUY BACK OF SHARES UNDER TENDER OFFER METHOD :

- Where a company proposes to buy back its shares, it shall, after passing of the special/Board resolution make a public announcement at least one in English National Daily **and** one in Hindi National daily **and** one in Regional Language Daily/Vernacular Newspaper at the place where the registered office of the company is situated.
- The public announcement shall specify a date, which shall be "specified date" for the purpose of determining the names of shareholders to whom the letter of offer has to be sent.
- A public notice shall be given containing disclosures as specified in Schedule I of the SEBI regulations.

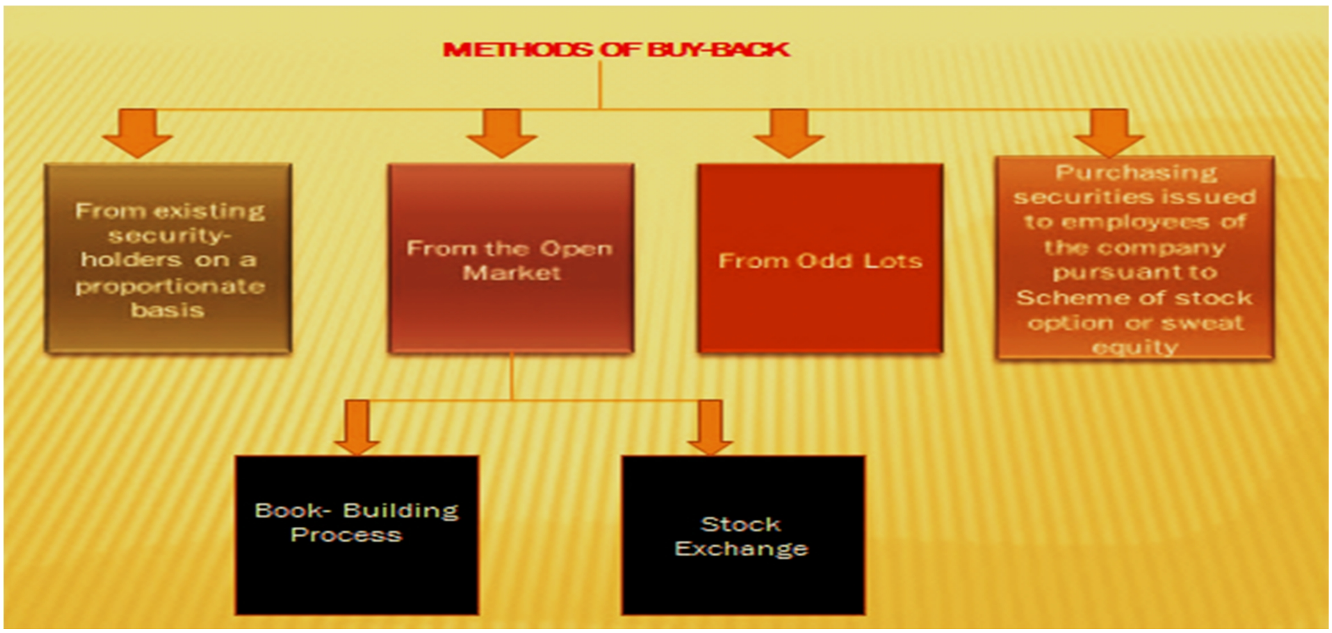
- A draft letter of offer shall be filed with SEBI through a merchant Banker. The letter of offer shall then be dispatched to the members of the company.
- A copy of the Board resolution authorising the buy back shall be filed with the SEBI and stock exchanges.
- The date of opening of the offer shall not be earlier than seven days or later than 30 days after the specified date i.e. the date which shall be given in public announcement.
- The buy back offer shall remain open for a period of not less than 15 days and not more than 30 days.
- A company opting for buy back through the public offer or tender offer shall open an escrow Account.

SEBI GUIDELINES

- **Company is required to make Public announcement in,**
- One NATIONAL English Daily
- One Hindi National Daily
- One Regional Language Daily
- **Public announcement should specify**
- Specified Date
- Company should inform SEBI within 7 days
- Offer shall remain open at least for 15 days
- Company shall complete verification within 15 days from the date of closure

Sr. No.	Particular	Time Limit
1.	Change article allowing buy back through special resolution in the general meeting	21 days notice is required for convening a general meeting.
2.	Register resolution with the ROC	Within thirty days from the date of passing the resolution
3.	Convene BM to approve buy back amount and method	
4.	Get the buyback approved in the general meeting through Special Resolution	21 days notice is required for convening a general meeting.
5.	Register resolution with the ROC	Within thirty days from the date of passing the resolution
6.	File the resolution to the SEBI and Stock Exchanges in case of listed companies	Within seven days from the date of passing the resolution
7.	Appointment of merchant banker	
7.	Public announcement in newspaper	Seven days prior to commencement of buy back
9.	Filling public announcement with the SEBI	Within two days from the date of public announcements
8.	Fixing up specified date	Not earlier than thirty days and not later than forty two days from the date of public announcement
9.	Letter offer should be filed with the SEBI through Merchant Banker	Within seven days from the date of public announcement
10.	Dispatch of letter of offer to the shareholder	It shall not dispatch earlier than 21 days from it submission to the SEBI.
11.	In case the SEBI proposes any changes in the draft offer letter , the company and merchant banker may consider to incorporate the same without any obligation	
12.	Along with the draft letter, a declaration of solvency verified by the affidavit should also be submitted to the SEBI	Form no 4A
13.	Date of opening of offer	Not earlier than 7 days or not later than 30 days after the date of specified date
14.	Date of Closing of offer	Buy back offer remains open for not less than 15 days and not more than 30 days.
15.	Opening of escrow account in the form of bank guarantee or deposit of securities	Within 30 days from the date of closure of offer.
16.	Verification of shares offer to the shareholder	Within 15 days from the date of closure of offer.
17.	Communication rejection	

18.	Immediately after the date of closure of buy back, the company has to open a special account to meet the payment obligation under buy back.	On the next day of closure of offer
19.	Payment to the shareholder	Within 7 days from the date of verification
20.	Extinguishment of Certificates in the presence of Registrar or Merchant Banker and the statutory auditor	Within 7 date from the date of acceptance of offer from the shareholder
21.	The company has to furnish a certificate to the SEBI regarding the extinguishment of share certificate	Within 7 days of extinguishment of shares
22.	Statutory auditor has to five compliance certificate as regards extinguishment of the bought back shares	
23.	The company has to furnish the particulars of extinguishment of shares to the stock exchanges in which the shares are listed	within seven days from the date of extinguishment and destruction of the certificates
24.	Register should maintain regarding the share certificate so canceled and destroyed	
25.	Filling of Return under sec 77 A (9) to the Registrar in **E form** 4 c and also to the SEBI.	Within 30 days from the date of completion of buy back.



MODES/METHODS OF BUY BACK OF SHARES

- PURCHASE FROM OPEN MARKET
- FIXED PRICE TENDER OFFER
- DUTCH AUCTION BUY BACK
- SELECTIVE BUY BACK
- EMPLOYEES STOCK OPTION

Buy back of shares or other specified *securities can be done through various sources which have been illustrated* under sub section 5 of section 77A, they are as follows:-

BUY BACK THROUGH OPEN MARKET/STOCK EXCHANGE:
There are two alternatives methods available for buy back through open market operations

a) Through Stock market/stock exchange operations;
b) Through book building operations.

Through Stock market/stock exchange operations in the USA

1. More than 95% of the purchase is done through this method.
2. Daily re-purchase of shares from market is limited.
3. Company may not openly announce that it repurchases its shares from open market.

Buy back through book building process
Buy back of shares in the book building process is an important method of price fixation.
The special resolution passed for buy back should specify the maximum price at which the buy back would be carried.
It is then necessary to appoint merchant banker and make a public announcement for buy back.
Buy back should commence after seven days from the date of public announcement.
A copy of the public announcement should be filed with the SEBI within two days from the date of public announcement.

SPECIFICATION OF MAXIMUM PRICE AND PUBLIC ANNOUNCEMENT
In the special resolution passed for buy back maximum price to be offered should be specified. There is an upper ceiling of specification of maximum price. Specification of such and upper limit helps to prevent fixing buy back price at a very high level to the loss of the company's resources.
Promoter and persons in control of the company are not allowed to participate in the stock exchange operation meant for buy back.
A merchant banker should be appointed for buy back through stock exchange operation also. A public announcement is to be made at least seven days prior to the commencement of the buy back.
Buy back shall be carried in the stock exchanges having electronics trading facilities. **Buy back shall be carried only through order matching mechanism except all or none other mechanism.** The company and the merchant banker shall give information to the stock exchange on daily basis regarding the shares purchased for buyback and the same shall be published in a national daily. The identity of the company as purchaser shall be disclosed on the electronic screen when the order is placed.
Since the maximum price for buy back is specified in the public announcement, it is likely that price in the stock exchange will be stable around that price during the tenure of buy back. Thus it can influence the market price.

FIXED PRICE TENDER OFFER/FROM THE EXISTING SECURITY HOLDERS ON A PROPORTIONATE BASIS :

a) Buyback of shares may be made by a tender offer through a letter of offer from the holders of shares of the company
b) Single purchase price and number of shares are to be sought are mentioned.
c) Person who likes to sell the shares will come up with offer price and number of shares that he offers to sell to company.
d) If offer from public exceed the number of shares sought then it may buy on pro-data basis. It means The buy-back can be on proportionate basis

SELECTIVE BUY BACK :

- **In broad terms, a selective buy-back is one in which identical offers are not made to every shareholder, for example, if offers are made to only some of the shareholders in the company. The scheme must first be approved by all shareholders, or by a special resolution (requiring a 75% majority) of the members in which no vote is cast by selling shareholders or their associates. Selling shareholders may not vote in favour of a special resolution to approve a selective buy-back**

a) A selective buy back is the buy back in which identical was not made to every shareholder.
b) Scheme must be approved by at least 75% of the shareholders i.e. Special Resolution.
c) Selling shareholder has no right to vote in the favour of the special resolution.

EMPLOYEES STOCK OPTION

- **A company may also buy back shares held by employees or salaried directors of the company or a related company. This type of buy-back, referred to as an employee share scheme buy-back, requires an ordinary resolution.**

By purchasing the securities issued to employees of the company under a scheme/pursuant to a scheme of stock option or sweat equity:

a) In this method, company has made buy back of shares from his employees or directors or related company.
b) Scheme must be approved by ordinary resolution.

- **Odd Lots**, that is to say, where the lot of securities of a public company, whose shares are listed on a recognized stock exchange , is smaller than such marketable lot, as may be specified by the stock exchange.

4.Equal access buy-backs

- All share holders have given equal opportunity to sell shares to the company.

PRICE FIXATION THROUGH DUTCH AUCTION METHOD:

dutch auction buy back

- Range of Price at which the company would like to repurchase mentioned in the offer.
- Share Holder can indicate their price with in the range prescribe by the company.
- Lowest bidder to highest price bidder are chosen.
- Company has the right to cancel the entire offer if few holders make the offer.

Under Dutch Auction method shareholders are asked to bid within the price range offered by the company. A Company may offer Rs. 100 to Rs. 130 for buy back . The lowest price may indicate the latest market price and the highest price may be the 52 week high price or price determined by Profit Earning Capacity Value or any other suitable value. Now the shareholders are entitle to bid for sale of their shares. Let us illustrate the bidding and pricing fixation. Bidding by the shareholder are given in Table table below. The tendering shareholders may quote for shares looking at the post offer market price. Of course, they quote higher than the highest market price of the quoting date in expectation that other will quote close to the highest price offered by the company. However, the market price may not move up that much because of the fundamental factor or because of lower demand in the stock exchange resulting from wait and watch policy to be adopted by the potential investors

Name of the shareholder	No. Of shares offered	Market price (High) on the date of offer	Price Quoted (Rs.)
A	20000	105	110
B	34000	115	119
C	25000	120	118
D	50000	120	130
E	10000	120	125
F	60000	120	122
G	15000	115	121
H	12000	115	120
I	30000	120	130
Total	256000		
No. Of Shares to be buy back	100000		

For fixing up price it is necessary to arrange the offer in ascending order of quote. Then move from the lowest checking number of shares available against each quote. See table below offers are arranged in order of quote in ascending order. Third column is indicating cumulative position of buy back at different price level. No. of shares offered at Rs. 110 is 20000, if the price is fixed at Rs. 110 buy back target of Rs 100000 shares cannot be purchased. If the price is fixed ar Rs. 118, maximum number of shares available would be 45000 which is also below the level of buyback target. At a price of Rs. 121, it would be possible to acquire 106000 shares which is above the buy back target. So price should be fixed at Rs. 121. Each tendering shareholder who offered Rs. 121 or less should get a price of Rs. 121. They should be offered proportionately. For example A should be offered 11867[20000*(100000/106000)] The formula offering is-

No. Of shares offered * buyback target/ total shares offered at price fixed or less

Name of the shareholder	No. Of Shares offered	Market Price(high) on the date of offer	Price quoted (Rs.)	Cumulative shares offered	No. Of shares to be bought back
A	20000	105	110	20000	18867
C	25000	120	118	45000	23585
B	34000	115	119	79000	32076
H	12000	115	120	91000	11321
G	15000	115	121	**106000**	14151
F	60000	120	122	166000	
E	10000	120	125	176000	
D	50000	120	130	226000	
I	30000	120	120	256000	
Total	256000				
No. Of Shares to be bought back	100000				

on-market buy-backs and minimum holding buy-back

- **A listed company may also buy back its shares in on-market trading on the stock exchange, following the passing of an ordinary resolution. The stock exchange's rules apply to on-market buy-backs.**
- **A listed company may also buy unmarketable parcels of shares from shareholders (called a minimum holding buy-back). This does not require a resolution but the purchased shares must still be cancelled.**

PENALTY

If a company makes default in complying with the provisions the company or any officer of the company who is in default shall be punishable with imprisonment for a term which may extend to two years, or with fine which may extend to fifty thousand rupees, or with both. The offences are, of course compoundable under Section 621A of the Companies Act, 1956.

PENALTIES- Sec 77A(11)

For default:

a. Imprisonment upto 2 years; or

b. Fine upto Rs. 50,000; or

c. Both