

Illustration 3 (Buy-Back from Free Reserves)

Following information is available from the books of Bharat Steel Ltd.:

1,20,000 Equity Shares of ₹10 each
 Securities Premium Account
 General Reserves

₹
 12,00,000
 70,000
 3,50,000

The company decides to buy-back 25% of the equity capital at ₹ 12 per share. Pass journal entries with full narration.

Solution

Bharat Steel Ltd. Journal Entries

S.No.	Particulars		Debit (₹)	Credit (₹)
(i)	Buy-Back Bank Account To Bank Account (Being the opening of buy-back bank account for buy-back of shares)	Dr.	3,60,000	3,60,000
(ii)	Securities Premium Account	Dr.	10,000	
	General Reserve Account To Capital Redemption Reserve Account (Being the amount payable on nominal value of equity shares for buy back transferred from free reserve to Capital Redemption Reserve Account)	Dr.	2,90,000	3,00,000
(iii)	Equity Share Capital Account	Dr.	3,00,000	
	Premium on Buy-Back of Shares Account To Equity Shareholders Account (Being the amount payable on buy-back of 30,000 equity shares of ₹ 10 each, at ₹ 12 each)	Dr.	60,000	3,60,000
(iv)	Equity Shareholders Account To Buy-Back Bank Account (Being payment to equity shareholders on buy-back of their shares)	Dr.	3,60,000	3,60,000
(v)	Securities Premium Account To Premium on Buy-Back of Shares (Being premium on Buy-back of shares adjusted through securities premium account)	Dr.	60,000	60,000

LEGAL NOTES

- (i) Only 25% of ₹ 12,00,000 equity share capital has been bought back.
- (ii) Securities Premium is a free reserves *vide* Explanation II to Section 68 of the Companies Act, 2013
- (iii) A sum equivalent to nominal value of equity shares bought back has been transferred from free reserves to Capital Redemption Reserve Account.

Illustration 7 (Buy-Back At Premium; Source: Free Profits and Issue of Preference Shares)

The following is the Balance Sheet of Super Active Ltd. as on 31st March, 2017:

Particulars	Note No.	(₹)
I EQUITY AND LIABILITIES		
1. Shareholder's Funds		
(a) Share Capital		
40,000 Equity shares of ₹ 15 each		6,00,000
3,000, 8% Preference shares of ₹ 100 each		3,00,000
(b) Reserve and Surplus		
Securities Premium Reserve		25,000
Surplus Account		30,000
2. Current Liabilities		
(a) Trade Payables (Creditor)		95,000
Total		10,50,000
II ASSETS		
1. Non-Current Assets		
(a) Fixed Assets (Tangible)		4,00,000
(b) Non-Current Investments		1,00,000
2. Current Assets		
(a) Trade Receivables (Debtors)		3,00,000
(b) Cash and Cash Equivalents (Bank)		2,50,000
Total		10,50,000

The company decides to buy-back 25% of its equity capital at 10% premium. For this purpose the company issues 1,000 8% preference shares of ₹ 100 each at a premium of 10% payable fully on application. These shares were fully subscribed and the company purchased the equity shares as per section 68.

Pass the necessary journal entries to record the above transactions.

Solution

Super Active Ltd.
Journal Entries

S.No.	Particulars	Debit (₹)	Credit (₹)
(i)	Buy-Back Bank Account To Bank Account (Being the opening of buy-back bank account for buy-back of shares)	Dr. 1,65,000	1,65,000
(ii)	Bank Account To Share Application and Allotment Account (Being application money received @ ₹ 110 on 1,000 8% Preference Shares)	Dr. 1,10,000	1,10,000
(iii)	Share Application And Allotment Account To 8% Preference Share Capital Account To Securities Premium Account (Being the allotment of preference shares)	Dr. 1,10,000	1,00,000 10,000

(iv)	Securities Premium Account	Dr.	35,000	
	Surplus Account	Dr.	15,000	
	To Capital Redemption Reserve Account			50,000
	(Being transfer from free reserves equivalent to the nominal value of equity shares bought back)			
(v)	Equity Share Capital Account	Dr.	1,50,000	
	Premium on Buy-back of Shares Account	Dr.	15,000	
	To Equity Shareholders Account			1,65,000
	(Being amount payable to equity shareholders on buyback of shares)			
(vi)	Surplus Account	Dr.	15,000	
	To Premium on Buy-back of Shares Account			15,000
	(Being the provision for premium on buy back of shares from free reserves)			
(vii)	Equity Shareholders Account	Dr.	1,65,000	
	To Buy-Back Bank Account			1,65,000
	(Being payment to equity shareholders on buy-back of their shares)			

Super Activa Ltd.
Balance Sheet As On 1 April 2017

Particulars		Note	₹	₹
I.	EQUITY AND LIABILITIES			
	1 Shareholders' Funds			
	(a) Share Capital	1	8,50,000	
	(b) Reserves and Surplus	2	50,000	
				9,00,000
	2. Current Liabilities			
	Trades Payables (Creditors)			50,000
	Total Equity and Liabilities			9,50,000
II.	ASSETS			
	1. Non-current Assets			
	(a) Fixed Assets (Tangible)		4,00,000	
	(i) Tangible Assets		1,00,000	5,00,000
	2. Current Assets			
	(a) Inventories, Debtors etc.		3,00,000	
	(b) Cash and Cash equivalents	3	1,95,000	4,95,000
	Total Assets			9,95,000

Notes to Accounts

1.	Share Capital	₹	₹
	Authorised		
	Equity Share Capital		
	Issued, subscribed and fully paid		
	30,000 equity shares of ₹ 15 each		4,50,000
	(After Buy-back of 10,000 Equity Shares)		
	8% Preference Share Capital		
	Issued, subscribed and fully paid		

5.22

Opening Balance: 3,000 shares of ₹ 100 each	3,00,000	
Add: Issued for buy-back 1,000 8% Preference Shares of ₹ 100 each.	1,00,000	4,00,000
Total 4,000 shares of ₹ 10 each		8,50,000
2. Reserve and Surplus		
(i) Capital Redemption Reserve	35,000	
From securities premium	15,000	50,000
From Surplus		
(ii) Securities Premium	25,000	
Reserve b/d		
Add: From Issue of 8% Preference shares	10,000	
	35,000	
	35,000	
Less: Premium on Buy-back		
(iii) Surplus :	30,000	
Opening Balance		
Transferred to Capital Redemption Reserve	(15,000)	
Premium on Buy-back	(15,000)	
		50,000
3. Cash and Cash Equivalents		
Cash at Bank b/d		2,50,000
Issue of Preference Shares (including premium of ₹ 10,000)		1,10,000
Payment on Buy-back of Equity Shares (including premium of ₹ 15,000)		3,60,000
		(1,65,000)
		1,95,000

LEGAL NOTES

- (i) No buy-back of equity shares is allowed from the proceeds of the recently issued equity shares. Hence company has rightly issued preference shares for the purpose of buy-back of equity shares.
- (ii) Premium on buy-back of shares could be directly paid from free reserves
- (iii) Capital structure has been kept intact:
- | | |
|--|----------|
| Nominal value of buy-back of equity shares (10,000 shares of ₹ 15) | 1,50,000 |
| Less: Proceeds from fresh issue of 8% preference shares | 1,00,000 |
| | 50,000 |
| Less: Capital Redemption Reserve | 50,000 |
| | x |
- (iv) The situation is very precarious as the balance in the Surplus Account (after transfer to Capital Redemption Reserve) is just sufficient to pay premium on buy-back of equity shares.