

Checklist

Guide to buy-back shares of unlisted companies



Vinod Kothari & Company

nidhiladha@vinodkothari.com

aditi@vinodkothari.com

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Procedural Checklist for Buying Back shares of an unlisted company

INTRODUCTION:

Buy Back of securities simply implies purchase of its own securities by a Company. A company can buy back its shares under Section 77A of the Companies Act, 1956. A private or public unlisted company is further required to comply with Private Limited Company and Unlisted Public Company (Buy Back of Securities) Rules, 1999.

IN WHAT MANNER COMPANY CAN BUY-BACK ITS SHARES:

A Company may buy-back its shares by either of the following methods:

1. From the existing security holders on a proportionate basis through private offers;
or
2. By purchasing the securities issued to employees of the company pursuant to a scheme of a Stock Option or Sweat Equity.

CONTRIBUTION OF FUNDS TO FINANCE BUY-BACK:

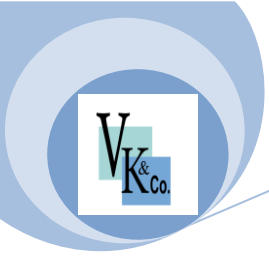
A Company may purchase its own shares or other specified securities out of:

1. Its free reserves; or
2. The securities premium account; or
3. The proceeds of any shares or other specified securities.

It is to be noted that the Company shall not utilise any money borrowed from Banks/Financial Institutions for the purpose of buying back its shares and that the buyback cannot be made out of proceeds of same kind of shares or same kind of securities.

CHECKLIST FOR BUYBACK:

1. 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.
2. Pass a Special Resolution in the General Meeting authorizing the buyback of shares.
3. Ensure that no buy back was made during a period of 365 days immediately preceding the current buy back.
4. 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.
5. Ensure that all the shares of the Company which are going to be purchased by the Company should be fully paid up.
6. Ensure that the Company does not issue same kind of securities within a period of 6 months from the completion of buy back



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7. Where a company buys-back its shares it should maintain the 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.

ACTIVITY SCHEDULE WITH CONSERVATIVE TIME FRAME

No. of days/time taken	Activity
	Obtaining Auditor's report stating the amount of the permissible capital payment for the securities in question is in their view properly determined and the Board of directors have formed the opinion on affairs of the company on reasonable grounds and that the company, having regard to its state of affairs, will not be rendered insolvent within a period of one year from that date
X days	Holding of Board Meeting for considering buy back proposal, approving buy back price and notice of EGM
X+2 days	Issue of Notice With Explanatory Statement (along with disclosures as mentioned below) to all the members
X+23 days	Holding EGM and passing Special Resolution
X+24 days	Obtaining Declaration of Solvency (verified by an affidavit) in Form 4C and filing of draft Letter of Offer with the RoC along with the declaration of solvency
X+24 days	Filing of Form 23 with the RoC
(X+24)+3 days	Dispatch of letter of offer to all members
Within 15 days from the closure of offer (Offer for buyback shall remain open to the members for a period not less than 15 days and not exceeding 30 days from the date of despatch of letter of offer)	Verification of offers to be completed
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



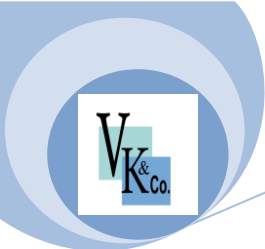
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Within 7 days from completion of verification	Making payment in cash or bank draft/pay order to those shareholders whose offer has been accepted or return the share certificates to the shareholders forthwith.
Within 7 days from completion of acceptance	Extinguish and physically destroy the shares bought back in the presence of the Company Secretary in whole time practice
Within 7 days of extinguishment of shares	Submit a certificate to RoC duly verified by (a) two whole-time directors including the Managing Director and (b) Company Secretary in whole time practice, certifying compliance of Private Limited Company and Unlisted Public Limited Company (Buy Back of Specified Securities) Rules, 1999
Within 30 days from completion of acceptance	File requisite form with the RoC

DISCLOSURES TO BE MADE IN EXPLANATORY STATEMENT

The notice of the meeting at which Special Resolution is proposed to be passed shall be accompanied by an explanatory statement stating all the details regarding buy back of shares viz:

1. The date of Board meeting at which the proposal for buyback was approved by the Board of Director of the Company;
2. Necessity for the Buy Back;
3. Class of security intended to be purchased under the buy back;
4. Method to be adopted for the buy-back;
5. The maximum required under the buy-back and the sources of funds from which the buy-back would finance;
6. The basis of arriving at the buy-back price;
7. The number of securities that the company proposed to buy-back;
8. The time limit for the completion of buy-back;
9. The aggregate of shareholding of promoter and the director as on the date of the notice convening the General Meeting;
 - a. Aggregate number of equity shares purchased or sold by persons including promoter and director during a period of 6 Months preceding the date of Board Meeting at which buy back was approved form the date of the notice convening the General Meeting;
 - b. The maximum and minimum price at which purchase and sales referred to above made along with the relevant date;
10. Intention of the promoter and person in control of the Company to tender shares for buy-back indicating the number of shares, detail of acquisition with date and price;



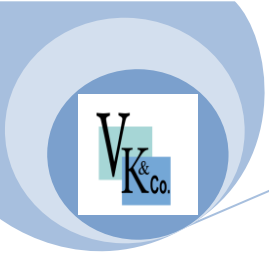
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11. A confirmation that there is no default subsisting in repayment of deposits, redemption of debenture or preference shares or repayment of term loan to any financial institution or banks;
12. A confirmation that the Board of Directors has made full enquiry into the affairs and prospects of the Company.
13. A report to the Board of Directors by the Company's auditors stating that they have inquired into the Company's state of affairs, the amount of permissible capital payment for the securities in question is in their view properly determine.
14. The price at which the buy-back of shares shall be made.
15. If promoters intend to offer their shares the quantum of shares proposed to be tendered and details of their transaction and their holding for the last six months prior to the passing of the Special Resolution.

DISCLOSURES TO BE MADE IN LETTER OF OFFER

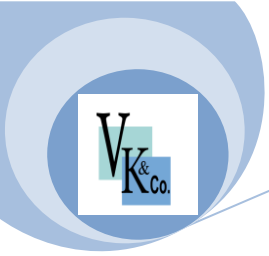
The Letter of Offer shall inter-alia include:

1. Details of the offer including the total number and percentage of the total paid up capital and free reserves proposed to be bought back and price;
2. Authority for the offer of buy-back
3. The proposed time table from opening of the offer till the extinguishment of the certificates;
4. A full and complete disclosure of all material facts including the contents of the explanatory statement annexed to the notice for the general meeting at which the special resolution approving the buy back was passed;
5. The necessity for the buy back;
6. The process to be adopted for the buy back;
7. The minimum and the maximum number of securities that the company proposes to buy-back, sources of funds from which the buy-back would be made and the cost of financing the buy-back;
8. Brief information about the company;
9. Audited Financial information for the last 3 years and ***the company and its Directors shall ensure that the particulars (audited statement and un-audited statement) contained therein shall not be more than 6 months old from the date of the offer document*** together with financial ratios as may be specified by the Board;



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10. Present capital structure (including the number of fully paid and partly paid securities) and shareholding pattern;
11. The capital structure including details of outstanding convertible instruments, if any, post buy-back;
12. The aggregate shareholding of the promoter group and of the directors of the promoters, where the promoter is a company and of persons who are in control of the company;
13. The aggregate number of equity shares purchased or sold by persons mentioned in clause (12) above during a period of twelve months preceding the date of the public announcement and from the date of public announcement to the date of the letter of offer; the maximum and minimum price at which purchases and sales referred to above were made alongwith the relevant date;
14. Management discussion and analysis on the likely impact of buy back on the company's earnings, public holdings, holdings of Non Resident Indians/Foreign Institutional Investors, etc., promoters holdings and any change in management structure;
15. The details of statutory approvals obtained;
16. A declaration to be signed
 - a. by at least two whole time directors that there are no defaults subsisting in repayment of deposit. Redemption of debentures or preference shares or repayment of a term loans to any financial institutions or banks;
 - b. by at least two whole time directors, one of whom shall be the managing director stating that the Board of Directors has made a full enquiry into the affairs and prospectus of the company and that they have formed the opinion –
 - i. as regards its prospects for the year immediately following the date of the letter of offer that, having regard to their intentions with respect to the management of the company's business during the year and to the amount and character of the financial resources which will in their view be available to the company during that year, the company will be able to meet its liabilities and will not be rendered insolvent within a period of one year from the date;
 - ii. in forming their opinion for the above purposes, the directors shall take into account the liabilities as if the company were being wound up under the



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provisions of the Companies Act, 1956 (including prospective and contingent liabilities)

17. The letter of offer must be accompanied by an Auditor's report obtained by the directors

TIMELIMIT FOR COMPLETION OF BUY-BACK PROCEDURE

Every buy-back shall be completed within 12 Months from the date of passing the Special Resolution or a resolution passed by the Board under clause (b) of sub-section 2.

BASIS OF VALUATION OF BUY-BACK PRICE

Private Limited Company and Unlisted Public Limited Company (Buy-Back of Securities) Rules, 1999 has not defined any basis of valuation of buy-back price. Company is free to make valuation of buy-back price on any relevant basis. Company can also make valuation on the basis of current book value of the shares or Net Asset Value (NAV). However company needs to give complete disclosure about basis of valuation in Explanatory Statement and also in the offer letter which needs to send to the Shareholders.

TAX TREATMENT FOR BUYBACK OF SHARES:

1. As per Indian Income Tax Act, 1961 any sum paid from accumulated profit to the shareholders of the company is treated as dividend under section 22(a). In case of buyback any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of Section 77A of the Companies Act, 1956 will not be treated as dividend hence Dividend Distribution Tax (DDT) under Section 115-O will not be applicable in this case.
2. Section 46A of the Income Tax Act, 1961 says that where a shareholder or a holder of other specified securities receives any consideration from any Company for purchase of its own shares or specified securities held by such shareholders or holder of other specified securities, then, subject to the provisions of section 48, the difference between the cost of acquisition and the value of consideration received by the shareholders or the holders of other specified securities, as the case may be, shall be deemed to be the capital gains arising to such shareholders or the holders of other specified securities, as the case may be, in the year in which such shares or other specified securities were purchased by the company.

To conclude, the company is not liable to pay any DDT but shareholders who are receiving consideration are liable to pay Capital Gain Tax as per Income Tax Act, 1961.

APPLICABILITY OF STAMP DUTY:



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No Stamp Duty is payable in case of buy back of shares as company is buying back its own shares and hence, the same does not result in any transfer.

For further assistance in relation to any of the above procedure, we can be reached at nidhiladha@vinodkothari.com or aditi@vinodkothari.com or vinod@vinodkothari.com.