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B.Com Honours | Semester III | Calicut University

Corporate Accounting

Course Code: COM3CJ202 • Module 2 Notes

Module II: Accounting of Bonus and Rights Issue - Buyback of Shares - Redemption of Preference Shares

Corporate capital restructuring involves Section 55 (Redemption of Preference Shares), creation of Capital Redemption Reserve (CRR), Section 63 (Bonus Issue), Section 62 (Rights Issue), and Section 68 (Share Buyback).

Unit 4: Redemption of Preference Shares – Provisions of Companies Act

Section 55 of the Companies Act, 2013 governs preference share redemption: (1) Only fully paid preference shares can be redeemed. (2) Redemption must occur out of divisible profits available for dividend or out of proceeds of a fresh issue of shares made for redemption. (3) Premium on redemption must be met out of Securities Premium or divisible profits before redemption takes place.

Unit 5: Capital Redemption Reserve (CRR) & Minimum Fresh Issue

When preference shares are redeemed out of divisible profits, an amount equal to nominal value of shares redeemed must be transferred to Capital Redemption Reserve (CRR):

CRR = Nominal Value of Shares Redeemed - Nominal Value of Fresh Issue

Minimum Fresh Issue = Nominal Value of Shares Redeemed - Available Divisible Profits

Practical Problem 1 (Redemption of Preference Shares & Minimum Fresh Issue): DELTA Ltd. has 2,000 10% Redeemable Preference Shares of Rs. 100 each fully paid up. The company decides to redeem them at a premium of 5%. The General Reserve shows a balance of Rs. 1,20,000 and Securities Premium A/c shows Rs. 15,000. Calculate the minimum fresh issue of equity shares of Rs. 10 each required and pass journal entries.

Step-by-Step Solution:

- Nominal Value of Shares to be Redeemed = (2,000 imes 100 = ext{Rs. 2,00,000}). Premium on Redemption (5%) = Rs. 10,000.
- Premium on Redemption is met from Securities Premium A/c (Rs. 10,000 used out of Rs. 15,000).
- Available Divisible Profit (General Reserve) = Rs. 1,20,000. Therefore, CRR created from General Reserve = Rs. 1,20,000.
- **Minimum Fresh Issue Required:**

  Fresh Issue = Nominal Value (Rs. 2,00,000) - Divisible Profits Used (Rs. 1,20,000) = Rs. 80,000 (8,000 Equity Shares of Rs. 10)
- **Journal Entries:**
  1. *Bank A/c Dr. 80,000* to *Equity Share Capital A/c 80,000* (Fresh issue).
  2. *10% Preference Share Capital A/c Dr. 2,00,000* & *Premium on Redemption A/c Dr. 10,000* to

Preference Shareholders A/c 2,10,000.
3. *General Reserve A/c Dr. 1,20,000* to *Capital Redemption Reserve (CRR) A/c 1,20,000*.
4. *Securities Premium A/c Dr. 10,000* to *Premium on Redemption A/c 10,000*.
5. *Preference Shareholders A/c Dr. 2,10,000* to *Bank A/c 2,10,000* (Payment made).

Unit 6: Bonus Issue – Rights Issue – Buyback of Shares

1. Bonus Shares (Sec 63): Capitalization of CRR, Securities Premium, or Free Reserves into fully paid shares.
2. Rights Issue (Sec 62): Pre-emptive offer to existing shareholders.
3. Buyback of Shares (Sec 68): Max limit 25% of paid-up capital & free reserves. Debt-equity ratio (le 2:1).

Practical Problem 2 (Calculation of Value of Right): A company offers 1 right share of Rs. 100 for every 4 existing equity shares held at a rights price of Rs. 120 per share. The prevailing market price of an equity share is Rs. 150. Calculate the Value of Right.

Step-by-Step Calculation:

- Market value of 4 existing shares = (4 imes 150 = ext{Rs. 600}). Cost of 1 right share = Rs. 120. Total cost of 5 shares = Rs. 720.
- Average price per share = (↑rac{720}{5} = ext{Rs. 144}).
- **Value of Right:**
  > **Value of Right = Market Price (Rs. 150) - Average Price (Rs. 144) = Rs. 6 per right**

Practical Problem 3 (Share Buyback & CRR Entry): ECHO Ltd. buys back 10,000 Equity Shares of Rs. 10 each at Rs. 15 per share out of General Reserve. Pass journal entries.

Solution:

- 1. *Equity Share Buyback A/c Dr. 1,50,000* to *Bank A/c 1,50,000* (Shares bought back).
- 2. *Equity Share Capital A/c Dr. 1,00,000* & *General Reserve A/c Dr. 50,000* to *Equity Share Buyback A/c 1,50,000* (Cancellation).
- 3. *General Reserve A/c Dr. 1,00,000* to *Capital Redemption Reserve (CRR) A/c 1,00,000* (CRR created equal to nominal value).