Webcast – Accounting for a purchase of own shares out of distributable reserves

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Introduction – how can we do a purchase of own shares?

- Small cash purchase (SI 2013/999)
- Purchase out of distributable reserves (CA06 s690-708)
- Purchase out of capital (CA06 s709-723)
Content of this webcast

- This webcast only deals with purchases out of distributable reserves and includes:
  - Legal requirements
  - Bookkeeping entries
  - FAQs
The legal requirements
**Legal requirements under CA06**

- **Articles must not prohibit purchase** (CA06 s690)
- **Cannot purchase by way of loan or installments** (CA06 s691)
- **Authorisation by ordinary resolution (OR)** (CA06 s694)
- **Contract or the memorandum available for 15 days prior to the ordinary resolution**
- **Consent from shareholders that have priority rights**
- **OR must be filed with Companies House within 15 days of OR**
- **Shares must be fully paid and cancelled immediately on acquisition, unless holding as treasury shares**
- **The contract must be kept for ten years**
- **Return must be delivered to the Co. House within 28 days of the shares being delivered to company (CA06 s707)**
Legal requirements

If the correct procedure is not followed then the purchase is VOID.
Bookkeeping entries
Example

Question:
A Ltd has 4 shareholders: Mr A, Ms B, Mr C and Mrs D. Each shareholder owns 25% of the share capital, originally sold at a premium of £350 per share. The company has 100 £1 nominal value shares and has a total share premium of £35,000.
Ms B would like to dispose of her investment in the company, and has agreed a price of £12,000.
The company are going to do a purchase of owns shares.
What are the accounting entries?
Example – required journal

Answer:
Dr: Share Capital - £25
Cr: Capital Redemption Reserve - £25
Dr: Distributable Reserves (eg P&L Reserve) - £12,000
Cr: Cash - £12,000
### Example – balance sheet extracts

<table>
<thead>
<tr>
<th></th>
<th>Before</th>
<th>Adjustments</th>
<th>After</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed assets</td>
<td>120,000</td>
<td></td>
<td>120,000</td>
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<tr>
<td>Current assets:</td>
<td></td>
<td></td>
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<tr>
<td>Debtors</td>
<td>12,000</td>
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<td>12,000</td>
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<tr>
<td>Cash at bank</td>
<td>32,000</td>
<td>(12,000)</td>
<td>20,000</td>
</tr>
<tr>
<td>Current liabilities:</td>
<td>(23,000)</td>
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<td>(23,000)</td>
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<tr>
<td>Net assets</td>
<td>141,000</td>
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<td>129,000</td>
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<tr>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Share capital</td>
<td>100</td>
<td>(25)</td>
<td>75</td>
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<tr>
<td>Share premium</td>
<td>35,000</td>
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<td>35,000</td>
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<tr>
<td>Capital redemption</td>
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<td>25</td>
<td>25</td>
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<tr>
<td>Capital redemption</td>
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<td></td>
<td></td>
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<tr>
<td>Retained earnings</td>
<td>105,900</td>
<td>(12,000)</td>
<td>93,900</td>
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FAQs

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FAQs

Question: What about the share premium attached to these shares? Why has this not been reduced?

Answer: The share premium remains
FAQs

Question: How do we “release” the share premium then?

Answer: There are a number of uses, including:

- **CA06 s610(2)** – when issuing shares at a premium, you can use the premium to write off
  - The expenses of the issue of those shares
  - Any commission paid on the issue of those shares
- **CA06 s610(3)** – to issue fully paid bonus shares (scrip issue)
- **CA06 s710** - payment of a permissible capital payment if doing a purchase of owns shares out of capital
- Via a reduction of capital (CA06 s641-657)
  (see the technical helpsheet entitled “Private company reduction of share capital” for more information)
FAQs

Question: Is the capital redemption reserve distributable?

Answer: No. It is treated like any other capital reserve.
FAQs

Question: What if we don’t have sufficient distributable reserves to do the purchase?

Answer: It could be possible to do a payment out of capital. If sufficient capital, this would require the following:

- a special resolution; and
- a directors’ statement supported by an auditor’s report to be available for inspection and a public notice of the proposed payment (CA 2006 s709-723).
- must utilise the distributable reserves first
Conclusion
Questions

If you have any questions on purchase of own shares, or any other technical, ethical or money laundering question, please do call the Advisory team on +44(0)1908 248250 (option 2)