

# Share Repurchases in India, U.S.A. and U.K. — A Comparative Study

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## **Abstract**

Share repurchase activity has experienced a remarkable increase in popularity worldwide in the 1980s and 1990s. But it was not until 1998 that the Indian companies have been permitted to repurchase own shares. Since the legislation for share repurchases has originated recently in India, a modest attempt has been made in this paper to discuss the existing provisions and practices of repurchases and its emergence in India. Moreover, as U.S.A. and U.K. have pioneered the legalisation of repurchase mechanism, an attempt has been made to discuss the provisions and practices prevailing therein to identify the lacunae, if any, in the Indian regulations.

**Key-Words :** Share repurchase ; Safe harbour ; Block trades ; Blackout dates ; Treasury operations ; Permissible capital payment.

## **1. Introduction**

Share repurchases, the technical name of share buyback, is a mechanism by which a company buys back its own shares from its existing shareholders primarily because it intends to correct any perceived undervaluation of the company's shares by the market in comparison to its true or intrinsic value. There are a number of other reasons as to why companies might buy back own shares like making small adjustments in capital structure, boosting earnings per share and operating profit, preventing an impending takeover bid, arresting downward trend in share prices, serving as the means of distributing excess cash of the company when there are no other profitable investment opportunities etc. In view of these benefits, the introduction of buyback in the corporate sector in India has found favour with both the regulatory authorities and the captains of industry. Accordingly, buyback provisions have been introduced in India in the year 1998.

Although the concept of a company buying back its own shares is relatively new in so far as the Indian capital market operations are concerned, the practice has prevailed in the developed markets of the West like the U.S.A. and the U.K. since long ago. However, U.S. companies began adopting share repurchase programs in large numbers only since early 1980s. In 1990s, the U.S. repurchase movement went global, spreading not only to other market-based economies like Canada and the U.K. but also to countries like Germany, Japan, Taiwan and Hong Kong where such transactions were prohibited until recently. Today, a host of countries including India, Australia, New Zealand, Austria, Belgium, Denmark, France, Italy, Spain and Sweden, to name a few, have adopted buyback provisions in their company legislation. This surge in buyback activity since the last two decades may

be attributed to a number of reasons. Emergence of the concept of 'globalisation' and 'liberalisation' during this period has witnessed a new chapter being written down in the history of the world securities market marked by increasing instances of takeovers, share-price manipulation, insider trading, undervaluation of a company's scrip, stock market scams and the like. In this situation, the share repurchase mechanism has appeared to most countries as a defence weapon against all these hazards.

Since "buyback" has become the new buzzword in Indian corporate environment, this paper aims at examining the legislative provisions governing buyback practices in India. Besides, the paper discusses the buyback provisions prevailing in the U.S.A. and the U.K. in order to make a comparison of the legal provisions in these countries vis-a-vis the Indian requirements and hence identify the strengths and the weaknesses (if any) in the Indian system. India owes a lot, because of her historical colonial link, to the U.K. systems and company legislation in India is modelled after the U.K. legislation. The regulatory framework of corporations and its implementation are exemplary in the U.S. and have a worldwide impact. Moreover, these two countries have pioneered the buyback legislation in the world. Thus, U.S.A. and U.K. have been selected for making a comparison of buyback provisions with that of India.

The remaining part of the paper has been organised as follows. *Section 2* discusses the Indian provisions on buyback, its emergence and the legal position after its introduction. *Section 3* examines the U.S. provisions on share repurchases and its emergence. The buyback provisions prevailing in the U.K. and its emergence are discussed in *Section 4*. A brief comparison of the buyback provisions in the U.S., U.K., and India is made in *Section 5*. Finally, conclusions are drawn in *Section 6*.

## **2. Buyback Environment in India**

This section has been compartmentalised into three parts. Part (a) discusses the emergence of buyback provisions in India. Part (b) deals with the legal provisions regulating share buyback in India and part (c) examines the legal position after introduction of buyback provisions.

### **(a) Emergence of buyback provisions in India**

Section 77(1) of the Companies Act, 1956 had long prohibited an Indian company limited by shares or limited by guarantee and having a share capital from buying its own shares unless a consequent reduction of capital is effected and sanctioned in accordance with Sections 100 to 104 (dealing with formal reduction of capital) or Section 402 (requiring a company to purchase its own shares under the instructions of Company Law Board to give relief in a petition of oppression / mismanagement) of the Act. The primary reason for such a prohibition was the apprehension that buyback, if allowed, might facilitate improper use of the company's assets by speculators in the management of the company with a view to increasing their percentage shareholding and hence obtaining control of the company for their own advantage. But with the Indian stock market in shambles towards

the end 1980s and early 1990s, this perception had changed and soon after a consensus emerged among the government, captains of industry and the stock market fraternity to introduce share buyback in India in order to help restore the confidence of the shareholders, shore up the sagging Sensex and make the corporates happy. Accordingly, three new Sections—77A, 77AA and 77B were inserted by the Companies (Amendment) Act, 1999 permitting Indian companies to buyback own shares on and from 31<sup>st</sup> October, 1998. However, buyback has become operational with effect from 14<sup>th</sup> November, 1998 in respect of listed companies and 16<sup>th</sup> July, 1999 in case of unlisted and private limited companies because Securities and Exchange Board of India (SEBI) guidelines and Central Government rules governing buyback of securities were prescribed on respective dates.

In spite of a general restriction on buyback of shares, there was a procedure for share buyback through capital reduction process requiring Court approval, hearing of creditors' objections etc. or a repurchase as ordered by the Company Law Board under the old provisions of the Companies Act, 1956. This naturally raises the question why then a separate provision is required for buyback? It is argued that the capital reduction process is so lengthy, troublesome and tiresome that few companies choose to go through it. On the other hand, buying back own shares with the permission of the Company Law Board is a course of action which no company voluntarily commences as it arises out of petitions to provide relief in cases of oppression of the minority by majority members of the company or in cases of mismanagement of the affairs of the company by the majority. Thus, the need has arisen to specifically provide for less time-consuming and simplified procedural requirements in respect of buyback in the Companies Act, 1956.

**(b) Legal provisions regulating share buyback**

All Indian companies desirous of effecting a buyback have to abide by the provisions of Sections 77A, 77AA and 77B of the Companies (Amendment) Act, 1999 as modified subsequently. Of these three Sections, Section 77A lays down the eligibility criteria for buyback and outlines the requirements to be fulfilled on buyback like :

- authorisation in the company's articles ;
- special resolution in general meeting where buyback is more than 10% of the total paid-up capital and free reserves or otherwise board resolution [such a clause inserted by the Companies (Amendment) Act, 2001 has amended the earlier provisions of 1999 Amendment Act which required the companies to pass a special resolution irrespective of the percentage of paid-up capital and free reserves bought back] ;
- buyback not being more than 25% of the total paid-up capital and free reserves provided that buyback of equity shares in any financial year does not exceed 25% of its total paid-up equity capital in that financial year ;
- financing of buyback out of the company's free reserves or securities premium account or proceeds of any shares or other specified securities not being an earlier issue of the same kind as those bought back ;

- securities for buyback are fully paid-up ;
  - filing of solvency declaration with the Registrar and the SEBI (in case of a listed company) by the Board of Directors certifying that their company will be capable of meeting its liabilities and will not be rendered insolvent within a period of one year of the date of such declaration ;
  - completion of buyback within 12 months from the date of passing the necessary resolution ;
  - debt / equity ratio is not more than 2:1 after buyback ;
- and
- restraining from making a fresh issue of the same kind of shares or other specified securities [including allotment of right shares under Section 81(1)(a)] within a period of 6 months where buyback is effected by a special resolution [i.e., when buyback >10% (paid-up capital + free reserves)] or 1 year where buyback is approved by a board resolution [i.e., when buyback  $\leq$  10% (paid-up capital + free reserves)] except by way of bonus issue or conversion of warrants, stock option schemes, sweat equity, preference shares or debentures into equity shares [prior to this amendment by the 2001 Act, Companies (Amendment) Act, 1999 restricted the cooling-off period to 2 years from buyback].

There are four methods by which a company might repurchase its own securities — tender offer, Dutch auction, open market and negotiated deals. In case of tender offer, the company invites offers from its shareholders to tender their shares at a specific price fixed by the company. In case of Dutch auction, the company announces a price band and accepts the lowest bid price within the range as the buyback price that allows it to buy the number of shares sought in the offer. In case of open market repurchase, the shares are bought back at the prices prevailing on the stock exchanges at the time of buyback not exceeding the maximum buyback price announced by the company before buyback. In negotiated trades, the company restricts the right of participation in the buyback operations to a shareholder or a specific group of shareholders and bargains for the buyback price. Section 77A permits Indian companies to repurchase shares by tender offer or Dutch auction or through open market or by repurchasing securities issued as sweat equity or under employees stock option plans. But the Section prevents the use of negotiated deals for buyback.

The securities repurchased by a company by any of the above methods may either be treated as “cancelled” and hence compulsorily extinguished and physically destroyed after completion of buyback or they may be held in “treasury” for reissue at a later date. However, Section 77A does not permit treasury operations on securities bought back and requires the Indian companies to cancel and physically destroy such securities within 7 days of the last date of completion of buyback.

In addition, the Section requires a listed Indian company to comply with SEBI (buyback) guidelines and an unlisted and a private limited Indian company to adhere to Central Government rules issued in respect of buyback. On failure to comply with any of

the provisions of Section 77A, the company or any officer of the company who is in default shall be punishable with imprisonment for a term which may extend to 2 years, or with fine which may extend to Rs. 50,000, or with both.

Section 77AA deals with the requirement to transfer nominal value of shares repurchased out of free reserves and securities premium account to capital redemption reserve account and disclose the details of such transfer in the balance-sheet.

Section 77B, however, still prohibits an Indian company from repurchasing its own securities—(a) through any subsidiary or investment companies ; or (b) when default is made in repayment of deposit or interest payable thereon, redemption of debentures or preference shares, payment of dividend to any shareholder or repayment of term loan and interest payable thereon to any financial institution or bank ; or (c) if the company fails to file its annual return or pay dividend within 42 days of declaration or prepare Profit and Loss Account and Balance Sheet in accordance with Section 211 (dealing with form and contents of financial statements and requiring compliance with Accounting Standards) of the Companies Act, 1956.

As regards accounting and reporting for buyback, there are no legal requirements excepting that the reasons for the failure, if any, on the part of the company to complete the buyback within the specified time period are required to be disclosed in the Board of Directors' Report as per Section 217(2B) of the Companies (Amendment) Act, 1999. Moreover, the Institute of Chartered Accountants of India (ICAI) is yet to issue a standard regarding accounting and disclosure norms of buyback operations. Due to this dearth of mandatory disclosure requirements, disclosures of share repurchase trades are mostly voluntary in India.

The legal provisions, discussed above, have a far reaching impact on some of the old provisions in the Companies Act, 1956. To what extent the buyback provisions have changed the enforceability of old provisions has been examined in the next segment.

### **(c) *Legal position after introduction of buyback provisions in the Companies Act***

Insertion of Sections 77A, 77AA and 77B in the Companies Act allowing share buyback has cast a shadow over the future of existing Sections 77, 100 and 402 of the Act. However, the *non-obstante* words — “Notwithstanding anything contained in this Act, but subject to the provisions of sub-section (2) of this section and section 77B” — with which Section 77A begins has clarified that the provisions of Sections 77A, 77AA and 77B would override all other provisions of the Companies Act, 1956 including Section 77 which prohibits buyback of shares, Sections 100 to 104 which regulate reduction of capital subject to the confirmation of the Court and Section 402 which authorises the Company Law Board to order repurchase of own shares by the company from the minority shareholders to give relief in a petition of oppression /mismanagement. But this does not mean that the existing provisions of Sections 77, 100 to 104 and 402 have been deleted or made ineffective. These Sections can still have effect and can be invoked where necessary. It is only the general

restriction on companies to voluntarily buyback their own shares as and when necessary (as contained in Section 77) that has been lifted by insertion of the three new Sections in the Act.

Since redemption of preference shares amounts to share buyback in effect and as Section 77A separately provides for buyback of preference shares, the *non-obstante* clause of Section 77A further implies that the provisions of existing Sections 80 and 80A dealing with issue and redemption of preference shares are subordinate to the provisions of Section 77A. This means that Sections 80 and 80A shall apply only to the extent that these are not in conflict with Section 77A. That is, where a company redeems the redeemable preference shares in accordance with the terms of issue, it will be prohibited from issuing preference shares again within the cooling-off period as per provisions of Section 77A, although there is no such requirement under Section 80. Again, a company may redeem the preference shares out of securities premium account in accordance with Section 77A though such a practice is not permitted by Section 80 of the Act.

Moreover, by including share repurchases as one of the uses of securities premium, the buyback provisions have also enlarged the scope of Section 78, which has otherwise restricted the use of securities premium account to only issuing fully paid bonus shares, writing off preliminary expenses, meeting issue expenses or commission payment or discount allowed on share or debenture issue and providing premium on redemption of shares or debentures.

Thus, it appears that the buyback provisions, as embodied in Sections 77A, 77AA and 77B, have overriding authority over other allied Sections in the Indian Companies Act.

### 3. Share Repurchase in the U.S.A.

It becomes imperative at this stage to examine the buyback provisions prevailing in the U.S.A. in order to make a comparison between India and U.S.A. as regards share repurchases in a subsequent section. For the said purpose, this section has been segmented into two parts — part (a) deals with the emergence of buyback provisions in the U.S. while the U.S. regulatory provisions on share repurchases are discussed in part (b).

#### (a) *Emergence of buyback provisions in the U.S.A.*

The history of repurchase activity in the U.S.A. dates back to 1942 when the first case of an American company buying its own stock was reported. Although familiar, the use of buyback mechanism was not that widespread until mid 1980s. The period after mid 1980s witnessed an accelerated pace of buyback activity among U.S. corporations fueled by an explosion in the use of open market repurchase programs. In the year 1998 — and for the first time in the history of buyback — U.S. corporations distributed more cash to investors through share repurchases than through cash dividends.

The primary factor responsible for this surge in buyback activity after mid 1980s is the major changes initiated in the regulatory environment in the U.S. Prior to 1982, the

regulatory environment relating to repurchase programs was ambiguous and structured only by ill-defined case laws. As there was no regulatory road map to guide buybacks, the firm's concerns over potential accusations of price manipulation undoubtedly kept many U.S. companies out of the buyback market. This regulatory ambiguity and the associated litigation risk were substantially reduced in late 1982 when the Securities and Exchange Commission (SEC) adopted *Rule 10b-18*, the first and only rule that provides any legal structure and protection to the buyback process in the U.S.A. even today. Although this rule is not statutory law, yet it sufficiently reduced litigation uncertainty to allow the growth in share repurchase activity in the U.S.A. in the late '80s and '90s.

**(b) Regulatory provisions on buyback**

A company can repurchase its shares either by — (i) fixed price tender offer, or (ii) Dutch auction repurchase or (iii) open market repurchase program in the U.S.A. Of the three mechanisms, Dutch auction is a relatively recent transaction in the U.S. Companies may also buyback their shares through private negotiation and finance the offer by cash or by debt.

Open market programs are not firm commitments to buyback stocks ; rather it gives the companies an option to repurchase stock whenever they feel that their stock price falls below fair value. Though there is no statutory limit on the program size or duration in the U.S., a typical open market program is found to be roughly for 5% of the share base and generally last two to three years on average.

Tender offer repurchase in the U.S. is guided by *Rule 13e-4* adopted by SEC in *September, 1979*. Item 1 of the said rule requires the firm to specify exactly at the time of the offer the number of shares to be repurchased. Thus, if the number tendered exceeds the number the company purchases, the company must, compulsorily, repurchase shares on a *pro rata* basis. If fewer shares are tendered during the initial offer period than targeted by the company, the offer period may be extended and the company may buy all shares tendered before the first expiration date and then repurchase shares *pro rata* during the extended period. Dutch auction repurchases are also permitted under *Rule 13e-4*.

No matter by whichever method a company buys back its own shares in the U.S., it must be ensured that the repurchase transaction does not violate the *anti-manipulative* and *anti-fraud* provisions (Section 9a2 and *Rule 10b-5*) of the Securities and Exchange Act, 1934. In this regard, SEC adopted *Rule 10b-18* — “Purchases of Certain Equity Securities by the Issuer and Others” — in *November, 1982* prescribing multiple broker, price, time and trading volume restrictions on buyback. The rule is a '*safe-harbour*' that would provide legal protection to the buyback transaction against accusations of price manipulation as long as the following four trading limits, as laid down in the rule, are observed :

- (i) buyback transactions on any given day are made through only one broker or dealer ;

- (ii) buybacks are not executed at the opening or during the last half hour of trading before the market's close on any given day ;
- (iii) buybacks are not done at a price that exceeds the highest current independent bid price or the last independent sale price, whichever is higher ; and
- (iv) if the total repurchase volume does not exceed one round lot (i.e., 100 shares) or the number of round lots that is closest to 25% of the company's stocks' average daily trading volume (excluding *block trades*) over the preceding four calendar weeks, whichever is greater. To qualify as a *block trade*, the stock repurchase must have *at least one* of the following characteristics :
  - (a) a price of \$ 200,000 or more ;
  - (b) at least 5000 shares and a price of \$ 50,000 or more ;
  - (c) at least 20,000 shares and 150% of the stock's average daily trading volume (excluding block trades) in the four previous calendar weeks.

Since such 'block purchases' generally arise out of 'off-market' privately negotiated trades and can increase a buyback program's flexibility significantly, they are allowed as exception in the volume restriction clause of the safe harbour.

It may be noted that the safe harbour rule applies to repurchase of securities other than common stock as well. However, it does not apply to trades executed for an employee stock ownership plan or self-tenders or negotiated trades done off-market. Moreover, the rule provides no mandatory limits as to what companies can and cannot do in share buyback. As a result, despite good intentions, U.S. companies either cannot or choose not to follow the Rules limits for each repurchase trade they execute because obeying the Rules is not mandatory and they bear *little or no penalty* for non-compliance.

Although not compulsorily required by statute, U.S. companies, usually, voluntarily impose the "blackout dates" limit on repurchase activity. Blackout period refers to the period during which all trades on company's stock are forbidden and this occurs especially around the time of material events such as earnings announcements. As regards the fate of the shares repurchased in the U.S., they must be held in 'treasury' by the company for reissue at a later date.

Apart from Rule 10b-18, there is a surprising lack of regulatory structure in the U.S. governing share buyback and the most troubling regulatory gap in Rule 10b-18 is that it fails to address the *accounting and disclosure* aspects of actual repurchase trades. There are no disclosure requirements in the U.S. other than the mandated initial disclosures to the market. In practice, mandatory disclosures about actual repurchases is limited to a few pieces of information scattered throughout the firm's annual and quarterly financial statements like line items in cash flow statements published in the 10-Q and 10-K reports may disclose actual repurchase trade or the management discussion and analysis section may provide information on the number of shares repurchased, repurchase price etc. Besides such compulsory minimal summary information, companies have no other obligation to disclose any aspect of their repurchase trades on a periodic basis and hence share repurchase disclosures are mostly voluntary in the U.S.



But, inspite of some regulatory inconsistencies, share repurchases have gained momentum in the U.S. corporate environment in recent times.

#### **4. Share Buyback in the U.K.**

It is worth examining the buyback environment prevailing in the U.K. because Indian Companies Act has derived a lot from the U.K. Companies Act. The discussion on U.K.'s buyback provisions spreads over two parts — part (a) discusses the emergence of such provisions in the U.K. while part (b) examines the provisions governing buyback.

##### **(a) Emergence of buyback provisions in the U.K.**

In 1887, the House of Lords in England cited in *Trevor V. Whitworth* case that infringement of the maintenance of capital principle was the primary reason for disallowing purchase of own shares by a British company as repurchase would most likely cause a reduction in undistributable reserves of the company. The Companies Act, 1928 first allowed the U.K. companies to issue redeemable preference shares subject to certain safeguards for preserving the amount of companies' share capital. The *Jenkins Committee*, reviewing the position in 1962, compared the limited power allowed to U.K. companies with the freedom enjoyed by U.S. corporations to repurchase shares and acknowledged the usefulness of buyback in the U.S. After a series of Parliamentary debates and deliberations on the issue of allowing buyback in the U.K., provisions permitting both public and private companies in the U.K. to issue redeemable equity shares and repurchase own shares were enacted in the Companies Act, 1981 in line with the recommendations of Professor Gower in the *Consultative Document* on "The Purchase by a Company of its Own Shares" published by the Department of Trade in the U.K. The buyback provisions, as amended subsequently, are now contained in Sections 159 to 178 of the U.K. Companies Act, 1985. Thus, the 1981 Act replaced the narrow power with a general power to issue redeemable shares of any type and gave the British companies the additional power for the first time to repurchase their own shares.

Although buyback provisions had existed since the last 20 years, the repurchase activity in the U.K. has actually gained momentum over the last decade.

##### **(b) Regulatory framework in the U.K.**

U.K. companies derive power from the Companies Act, 1985 to purchase their own shares. It is worth noting that the thrust of *Trevor V. Whitworth* is still embodied in *Section 143(1)* of the Companies Act, 1985 but with a few exceptions under *Section 143(3)* of the Act which provides that a limited company must not acquire its own shares except in accordance with the provisions of Sections 159 to 178 of the 1985 Act. The buyback rules outlined in the 1985 Act are the strictest in relation to public companies whereas private companies are allowed to operate under a slightly more relaxed regime.

After being authorised by its articles as per requirements of Section 162 of the U.K. Companies Act, 1985, a limited company can repurchase own shares either through an *off-market purchase* (Section 164) or under *contingent purchase contract* (Section 165) or by an *on-market purchase* (Section 166). An *off-market purchase* of own shares by a limited company (whether listed or not) requires to be authorised by a *special resolution* approving the specific terms of the contract by which shares are to be repurchased. *Private companies* can use the statutory written resolution requiring unanimous consent of all those members entitled to vote i.e., whose shares are not the subject matter of the resolution authorising an off-market purchase. *Contingent purchase contracts* are not the contracts to repurchase own shares but under which the company may become entitled or obliged to repurchase in specified circumstances subject to fulfilment of certain conditions, as for example, an option contract. Contingent purchase contracts are approved by a special resolution and are regulated in the same way as off-market purchase contracts. An *on-market purchase* of own shares, applicable to a listed company and the company admitted to dealings on the London Stock Exchange's junior market, must be authorised by an ordinary resolution specifying the limits with regard to the maximum number of shares authorised to be acquired and the maximum and minimum prices (i.e., a price band) which may be paid for the shares. Both ordinary and special resolutions, as mentioned above, shall remain valid for 18 months from the date of passing such resolutions and they can be varied, revoked or renewed by another similar resolution.

Share buyback by a listed company, whether on- or off-market, is further regulated by *Chapter 15 of The Listing Rules* prescribed by the London Stock Exchange. As per the Listing Rules, repurchases by a company within a period of 12 months of less than 15% of the existing shares may be made through the market if the price to be paid is not more than 5% above the average of the market values of those shares for the 10 business days preceding the purchase. Purchase of more than 15% must be made by way of a tender or a partial offer to all shareholders.

Besides, as per Section 162(3), a U.K. company must ensure that there will be atleast one shareholder who holds non-redeemable shares after buyback so that repurchase does not result in there being no member of the company because of buybacks. Further, according to Section 159(3), shares should not be bought back unless they are fully paid and the purchase price must be paid in cash *up front* at the time of purchase and not by way of deferred instalment payments.

According to Sections 160(1) and (2) of the U.K. Companies Act, 1985, the nominal value of the shares repurchased may be funded either out of the company's distributable profits (i.e., the funds available for payment of dividend) or out of the proceeds of a fresh issue of shares made specifically for that purpose. As per Section 170, an amount equal to that of distributable profits used to fund the nominal value of shares repurchased must be transferred to an undistributable reserve i.e., capital redemption reserve on the

company's balance sheet. Premium on buyback shall be funded out of distributable profits or out of proceeds of a fresh issue of shares only in cases when the shares repurchased were originally issued at a premium. The proceeds of fresh issue for payment of premium can be used up to the extent of the aggregate premium received by the company on the issue of shares repurchased or the current amount of the company's share premium account, whichever is less, and the share premium account shall be reduced by the amount so used. In addition to distributable profits and proceeds of fresh issue, private companies in the U.K. can repurchase shares out of capital (i.e., undistributable profits like revaluation reserve, capital redemption reserve etc.) under Sections 171 to 177 of the Act. However, a private company can repurchase out of capital only when the available profits together with proceeds of fresh issue made for buyback purposes fall short of the amount needed for repurchase and this shortfall is referred to as *permissible capital payment (PCP)*.

Section 160(4) requires a U.K. company to treat the shares as *cancelled* after repurchase and diminish its issued capital by the nominal value of the repurchased shares accordingly. Thus, the U.K. companies are not allowed to hold the repurchased shares in *treasury* although the matter is under consideration.

Unlike the U.S., Section 178 of the U.K. Companies Act, 1985 prescribes penal measures for failing to complete the bargain to purchase own shares by a British company. The shareholders, however, do not have the right to claim for damages in the event of breach of contract to repurchase shares by a company. They can, at best, seek specific performance of such a contract. If the company goes into liquidation after the obligation to repurchase has arisen, the vendor-shareholder shall rank as *deferred creditor* and shall be paid off their dues after ordinary creditors but before ordinary shareholders. A party other than the shareholder can claim damages from the company for failure to buyback shares.

In contrast to India and U.S.A., the U.K. Companies Act, 1985 provides for extensive disclosure requirements in respect of buyback. Section 234 of the said Act requires that the details of shares repurchased in any financial year must be given in the relevant directors' report. If the company is listed, additional information upto the date of the report must be included and details of any shareholders' authority for the purchase by the company of its own shares which is still valid at the end of the period under review must also be given as per Listing Rules. Such Rules further require that the Exchange must be given details of actual purchases as soon as possible but not later than 8-30 a.m. on the business day following the calendar day on which the dealings took place. Again, as per Section 169 of the 1985 Act, the company must notify the Registrar of Companies of any share repurchase and also of its cancellation within 28 days of completion of buyback.

Thus, it seems that the buyback environment in the U.K. is far more organized and regulated than that in India or the U.S.A.

## 5. Comparison of the Buyback Provisions in the U.S., U.K. and India

In the light of the above discussions, a brief comparison of the buyback provisions in the U.S., U.K., and India is made in Exhibit 1 below.

**Exhibit 1**  
**Comparison of Buyback Provisions in U.S., U.K. and India**

Particulars	U.S.A	U.K.	India
(1) Year of emergence of buyback legislation	1982	1981	1998
(2) Whether authority under Articles of Association of a company is required ?	Required	Required	Required
(3) Nature of resolution approving share buyback	Board Resolution passed at the meeting of the board of directors of the company	(a) Ordinary Resolution passed at the general meeting of the company for <i>on-market</i> purchases. (b) Special Resolution passed at the company's general meeting for <i>off-market</i> purchases.	Special Resolution passed at the general meeting of the company where buyback is more than 10% of the total of paid-up capital and free reserves or otherwise board resolution
(4) Buyback limit	No statutory requirement	The Listing Rules prescribed by the London Stock Exchange require a listed company to repurchase <i>not more than 15%</i> of its shares through the market in 12 months if the price paid is not more than 5% above the average market values of those shares in 10 preceding business days; purchases of <i>more than 15%</i> must be made by way of <i>tender or partial offer</i> to all shareholders	As per Section 77A(2)(c) of the Indian Companies Act, 1999, buyback of equity shares in any financial year cannot exceed 25% of its total paid-up equity capital in that financial year and the amount used for buyback must not exceed 25% of total paid-up capital and free reserves of the company
(5) Sources of funds for buyback	(i) Distributable profits (ii) Institutional finance (i.e., debt-financing)	(i) Distributable profits (ii) Proceeds of a fresh issue of shares made specifically for the purpose of buyback (iii) Capital in case of private companies only, provided the 260 conditions under Sections 171-177 are duly complied with	(i) Free reserves (i.e., distributable profits) (ii) Securities premium account (iii) Proceeds of any shares or other specified securities other than those bought back

Exhibit 1 (Contd.)

Particulars	U.S.A	U.K.	India
(6) Buyback methods	(i) Fixed price tender offer (ii) Dutch auction repurchase (iii) Open market repurchase (iv) Private negotiation	(i) Off-market purchase (ii) Contingent purchase contracts (iii) On-market purchase	(i) Tender offer method (ii) Dutch auction repurchase (iii) Open market purchase (iv) Purchase of employees' securities issued under stock option plans or sweat equity
(7) Whether treasury operations are allowed on shares bought back ?	Allowed	Not available as yet ; the matter is, however, under consideration	Disallowed ; the Act compulsorily requires extinguishment of shares bought back within 7 days of completion of buyback
(8) Solvency norms after buyback	No specific requirement	No specific requirement	Debt-equity ratio of 2 : 1 as per the Companies Act, 1999
(9) Accounting and Disclosure requirements	No specific regulation ; mandatory disclosure about actual repurchases is limited to a few pieces of information scattered throughout the company's financial statements	The U.K. Companies Act, 1985 minutely provides for the manner in which buyback should be accounted for ; the Act also provides for extensive disclosures in the directors' report ; the Listing Rules also prescribe disclosure norms	No statutory requirement ; disclosure is mostly voluntary
(10) Penalty — (a) on failing to implement a buyback program already announced  (b) for non-compliance with legal provisions while effecting share buyback	No penalty  Little penalty	Shareholders have the right to seek specific performance of the contract to repurchase shares ; meanwhile if the company is wound up, such shareholders shall rank as deferred creditors  Company's directors may be personally liable and may commit offence	No penalty  As per the Companies Act's provisions, the company or any officer of the company who is in default shall be punishable with imprisonment for a term extending upto 2 years or with a fine upto Rs. 50,000 or with both

Exhibit 1 clearly shows that there is dearth of provisions relating to accounting and reporting aspects of buyback and penal provisions on failing to complete buyback in the U.S.A. and India. On the other hand, treasury operations on shares repurchased is allowed in U.S.A. but not in India and U.K. The loopholes in Indian provisions on buyback, therefore, need to be plugged to make it compatible with that of U.S.A. and U.K. Again, the Indian regulatory provisions on buyback appear to be stringent in certain respects when compared with that of U.S.A. and U.K. and hence needs to be relaxed to promote a healthy growth of buyback in future.

## 6. Conclusions

The detailed discussion on buyback provisions in India, U.S.A. and U.K. in the preceding sections, therefore, suggests that share repurchases are likely to remain a dominant transaction worldwide even in the distant future, given the amendments and the kind of changes being brought about in the regulatory climate regarding buyback. Although only time will tell whether buyback operations can be sustained within the Indian corporate environment, it is atleast expected that repurchase activity will grow in India as it adopts more and more enabling regulations providing greater transparency, an organized framework and disclosure environment for the repurchase process.

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