SHARE BUY-BACKS:
LEGISLATIVE CHANGES

SHARE BUY-BACK SCHEMES

The share buy-back mechanism is looked upon favourably as a means by which a company can return surplus cash to shareholders. Obvious advantages are the immediate enhancement of earnings per share and the increased marketability of the company's shares. The use of share buy-backs is common in the U.S., and is fast gaining popularity across the globe. In Singapore, changes have been made to the Companies Act (Cap. 50) to allow both listed and non-listed companies to buy back their own shares.

A company can now buy back its shares in the market or off-market. Specifically, the three types of share buy-backs schemes are:

1. **Off-market acquisition under an equal access scheme**

   This arrangement applies to both listed and non-listed companies and allows a company to devise an “equal access scheme" to buy back its own shares. The scheme must be approved by the shareholders in advance and must satisfy the following requirements:-

   - dividend entitlements and different paid-up amounts of the shares; and
   - selective off-market acquisition

   This mechanism, which is not available to a listed company, allows a non-listed company to effect a share buy-back without an equal access scheme if the terms of the agreement for the share buy-back are approved by the shareholders.

   - an offer must be made to everyone holding shares;
   - the shareholders must have reasonable opportunity to accept the offer; and
   - the terms of the offer must be the same (with some exceptions, for example, differences in consideration attributable to different accrued dividend entitlements and different paid-up amounts of the shares).

2. **Selective off-market acquisition**

   This mechanism, which is not available to a listed company, allows a non-listed company to effect a share buy-back without an equal access scheme if the terms of the agreement for the share buy-back are approved by the shareholders.

   The notice of the shareholders' meeting must specify the date on which the authority approving the share buy-back expires (which, in any event, must not be later than the company's next annual general meeting) and detail the source of the funds for the proposed share buy-back and its impact on the financial position of the company.

3. **Market acquisition**

   A listed company may purchase its own shares if authorised by a general meeting of the company. In seeking authorisation, the company must specify the maximum number of shares or percentage of shares to be bought, the maximum price which may be paid, the date on which the authority approving the share buy back expires and the sources of funds to be used to purchase those shares.

   The Stock Exchange of Singapore Ltd (SES) has issued guidelines for share buy-backs by listed companies.

A listed company seeking to buy back its shares must provide certain minimum information to shareholders and must notify SES of all purchases of its shares for both market and off-market acquisitions within prescribed time frames. The purchase price of a share must not be more than 5% above the average closing market price of the share over the last 5 market days.

The company must also observe the SES Best Practices Guides on dealings in securities which, among other things, say that the company should not deal in its securities during the period commencing one month before the announcement of its annual or half-yearly results, and ending on the date of announcement of the results.

SOURCE OF FUNDING

Payment for shares purchased under the scheme must be from the company's "distributable profits" i.e. profits available for payment to shareholders as dividends but excluding any amount in the share premium account and the capital redemption reserve.

SAFEGUARDS

The amendments attempt to protect the interests of both shareholders and creditors. The main safeguard lies in the requirement of shareholders' approval for the scheme. Market and equal access schemes require ordinary resolutions of shareholders whereas selective off-market schemes require a special resolution, with the votes of interested parties and their associates not being taking into account.

The maximum number of shares that a company is permitted to buy back is 10% of its issued ordinary share capital. The company must be expressly authorised by its Articles of Association to conduct a share buy-back.

Creditors may take comfort that the amendments impose stringent duties on directors and managers, and provide that they shall be personally liable to creditors of the company for sums wrongfully utilised in the share buy back exercise. In addition, every director or manager who approves the purchase of the company's own shares knowing that the company is insolvent commits an offence and may be liable on conviction to a fine not exceeding $5,000 or to imprisonment not exceeding 12 months.

TAX IMPLICATIONS

In a Practice Note issued on 31 December 1998, the Inland Revenue Authority of Singapore (IRAS) stated that, for income tax purposes, a distribution to shareholders out of a company's distributable profits is a payment of dividends. As a company may only purchase or acquire its own shares using its distributable profits under the Companies Act, a company which purchases or acquires its own shares will therefore be regarded as having paid a dividend to the shareholders from whom such shares are purchased or acquired. The company would therefore have to provide for the franking of the share purchases at the prevailing corporate tax rate (currently 26%) in the same way as if it was paying a taxed dividend, the amount paid by the company for such share purchases being the net dividend. It was also stated in the Practice Note that the tax treatment of the receipt from a share purchase in the hands of the shareholders will depend on whether the disposal arises from a "market purchase" or an "off-market purchase".

Proceeds received by shareholders in an off-market purchase will be treated as receipt of a dividend. Unless the company has paid the amount out of exempt income so that the dividend is an exempt dividend, the shareholders will be assessed to tax on the gross amount of the notional dividend and be allowed a credit for the tax deducted at source (currently 26%) of the grossed up amount.

On 17 May 1999, SES issued another press release that stated that listed companies that have obtained shareholders' approval for share buy-backs can apply for a special trading terminal on their premises to enable them to key in buy orders for special trading counters that SES would establish for share buy-backs.

IRAS in its press statement of 14 May 1999 said that the proceeds received by shareholders from the sale of special trading counters through the share buy-back market will be treated, for

Singapore income tax purposes, as receipt of a dividend. Based on present tax rates, such shareholders will be assessed to tax on the amount received grossed up by a factor of 100/74 and allowed a credit for the tax deducted at source of 26% of the grossed up amount.

In other cases where there is a disposal of shares through a market purchase, this will be treated like any other disposal made on the Stock Exchange and the proceeds received by shareholders will be treated as proceeds from a disposal of shares and not a dividend. Whether or not such proceeds are taxable in the hands of such shareholders will depend on whether they are receipts of an income or of a capital nature.

FILING REQUIREMENTS

The shareholders' resolutions authorising the share buy back must be filed with the Singapore Registry of Companies and Businesses (RCB) within 30 days. A prescribed form will also have to be lodged with the RCB within 30 days of the acquisition or purchase of shares under any share buy-back scheme.