



COME ON SEC, THINK OUTSIDE THE BOX!

Securities and Exchange Commission has willy-nilly established a new set of rules governing one of the latest buzz words: "Share Buy Backs". These rules (Rule 109B) in a nutshell have decreed that: it applies only to publicly quoted companies; permits a company to repurchase a maximum of 15% of its existing issued and paid up equity capital within each financial year; repurchases are only to be funded from the company's share premium account and/or accumulated profit of the company which would otherwise be available for dividends; shares may only be repurchased through the open market or via a self tender offer; the ultimate beneficiary of the buy back must be the company; the shares shall be cancelled in accordance with procedure in existing company law; all repurchases must be completed 12 months from date of shareholders resolutions; prices of the shares bought at open market shall be governed by the market rate, but if repurchase is by self tender, then the price set by the Directors shall not exceed 5% of the average market price in the last 5 days; and a host of others.

Several streams of thought alight in reviewing these restructurings aimed at acting as part of the government orchestrated life support machinery for the capital market.

Firstly, Sections 160-165 of the companies Act that deals with the "Acquisition by a company of its own shares" would of necessity need legislative amendment. In doing so, care needs to be taken to create a clear dichotomy between what would obtain with private and public companies. Since Rule 109B applies only to public companies there is a risk that the companies Act may be amended from a public company perspective. I have also read in some newspapers that the Attorney General of the Federation has been requested to approve some "waivers" or "fiats" or whatever, to the company laws permitting the regulators to begin operating these new rules. I must have read upside down! For the avoidance of doubt, the Federal Attorney General has no such powers and any such amendment has to be by the National Assembly – whenever they find time to legislate instead of acting in their oversight functions.

Secondly, it is noteworthy that SEC'S Rule 109B is a single lane road in terms of what happens to the repurchased shares. The rule is that all the shares that are repurchased by the company must be cancelled. So a company repurchases a fair amount of shares and simply destroys them as though they never existed. The usual aim would be to reduce the number of shareholders and increase the "take-home" of the few shareholders left to service.

The flipside with this inflexibility and insistence on shares being cancelled is that in many ways it may lead to a value loss for the company who could have for example have pursued an option of reissuing the shares at a later date - to build up capital in its share premium account. In this regard, it should be noted that SEC also insists that the repurchase should be funded from either the share premium account (a fund which is usually treated as capital and not paid out as dividend or otherwise depleted) or from its accumulated profits account. Clearly taking funds from the share premium account only to fund a mop-up for purposes of cancellation of shares gives no guarantees that value lost via a depletion of capital in funding the repurchase will be regained. Even if it is regained, would the trouble be worth it considering the intricacies and attendant costs of the entire buy back procedure?

In the same vein a company funding a repurchase from "accumulated profits" instead of simply declaring a dividend to existing shareholders may not exactly be a cut and dry mechanism for growing shareholder value. In fact, it may be viewed in some sense as a depletion of value particularly when the re-purchase price is 5% above market value - as the case may be with a purchase by self tender offers. It should be noted that share buy backs in

many jurisdictions give the company's the latitude to decide how they intend to deal with the shares repurchased. Besides, the current insistence on the repurchased shares being cancelled is not in consonance with the spirit of a free market economy or a stock market regulated by market dictates and financial prudence.

Thirdly, SEC'S rule 109 B (XIII) states that: "The buy-back shall not be made if the company is illiquid (i.e a Company defaulting in payments of its obligations including dividend payment)".

This rule if you ask me probably disqualifies a fair proportion (over 50% in my rough estimation of publicly quoted companies) from partaking in a share buy back – simply think about the number of moribund "PLC'S" quoted on the Nigerian Stock Exchange. My guess is that SEC assumes that an illiquid company would not have funds in its share premium account talk less of accumulated profits to fund a buy back. How true! However if the essence is to keep the market afloat, then it should be noted that this share buy back presents a brilliant bail-out opportunity for many companies. SEC may have (and may still explore the possibility) a mechanism that allows investors take over an illiquid company via a scheme whereby the company achieves three things: procure needed investment, pay of its debts and procure ample shares for the investor via a share buy back. This would only work if the company is allowed to purchase its on shares from funds obtained from such legitimate third party sources - other than the specified "share premium accounts" and/or "accumulated profits".

The other related restriction from Rule 109B is that the ultimate beneficiary of any buy back must be the company. Why must it be so? Could a company not arrange a share buy back simply to introduce a new investor and from funds provided by the investor? By the way, just think of how many shareholders in Nigeria would be glad to have an illiquid company make them some offer – whatever it may be – after many years of just holding sheets of paper (Share Certificates) that never translates to dividends or value.

Shall we think outside of the box for a moment?

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