Tucker Ellis LLP

SEC proposes disclosure rule amendments related to share buybacks

Lingua Negoti

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On December 15, 2021, the Securities and Exchange Commission ("SEC") proposed amendments that would strengthen its rules regarding disclosure about an issuer's repurchases of its own shares. Share buybacks have become a controversial matter in public markets in recent years (for example, see our 2018 *Lingua Negoti* blog post "Stock buybacks are not evil" here). A majority of the SEC commissioners has stated, by a partisan vote, concerns that there is asymmetry of information between issuers and investors and that there is potential for abuse.

The proposed new requirements would apply to issuers with equity securities registered under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and would apply to purchases of shares by the issuer or any "affiliated purchaser," meaning anyone acting in concert with the issuer or an affiliate who controls the issuer's purchases, whose purchases are controlled by the issuer or are under common control with the issuer.

According to the SEC, share repurchases in 2020 alone were approximately $670 billion, and according to at least one source, they are on track to exceed that number substantially in 2021. The SEC calculates that approximately 3,300 registrants made share repurchases in 2020. Such programs have outspoken supporters and critics. Many of the criticisms focus on the ability of management to affect incentive compensation by influencing stock price or earnings per share. The merits of those arguments are beyond the scope of this post.

The Case for Daily Disclosure

One reason the SEC is concerned about the asymmetry of information between the issuer engaged in repurchases (and its insiders) on one hand and investors on the other is that announcements of share repurchase plans and actual purchases under those plans may affect prices, but under current rules the information about actual purchases is not available until the next periodic report on Form 10-Q or Form 10-K, which may occur months after some of the purchases. The proposed amendments would increase the speed and the detail of disclosures in order to provide more transparency.

The proposed new disclosure rule would require an issuer to furnish a report on a newly adopted form, Form SR, no later than the end of the next business day following the execution of any repurchase of shares. Form SR, as proposed, would require disclosure of:

- the class of securities purchased;
- the total number of shares purchased;

- the average price paid per share;
- the aggregate total number of shares purchased on the open market;
- the aggregate total number of shares purchased in reliance on the safe harbor in Rule 10b-18; and
- the aggregate total number of shares purchased pursuant to a plan that is intended to satisfy Rule 10b5-1(c).

Because Form SR would be *furnished* instead of *filed*, it would not be subject to all of the potential liabilities that apply to false information in a filed document.

More Qualitative Disclosures in Periodic Reports

The proposing release states, "Although some issuers announce details of their repurchase programs on a voluntary basis, issuers are not required to do so, or to disclose reasons for their repurchases. Further, issuers are not required to disclose whether they allow insiders to trade during repurchases. Thus, it can be difficult for investors to determine whether the undertaken repurchases were efficient and aligned with shareholder value maximization, or were at least in part driven by self-interested behavior of corporate insiders rather than shareholder interest."

The requirements for quarterly reports on Form 10-Q and annual reports on Form 10-K currently include tabular disclosure, on a month-by-month basis, of: (1) the total number of shares purchased; (2) the average price paid per share; (3) the total number of shares purchased as part of publicly announced repurchase plans or programs; and (4) the maximum number (or approximate dollar value) of shares that may yet be purchased under the plans or programs. The issuer must also disclose, by footnote to the table: (a) the date each plan or program was announced; (b) the dollar amount (or share amount) approved; (c) the expiration date (if any) of each plan or program; (d) each plan or program that has expired during the period covered by the table; and (e) each plan or program the issuer has determined to terminate prior to expiration or under which the issuer does not intend to make further purchases.

The SEC now proposes to expand these disclosure requirements to include:

- the objective or rationale for the share repurchases and the process or criteria used to determine the amount of repurchases;
- any policies and procedures relating to purchases and sales of the issuer's securities by its officers and directors during a repurchase program, including any restriction on such transactions;
- whether the issuer made its repurchases pursuant to a plan that is intended to satisfy the affirmative defense conditions of Rule 10b5-1(c), and if so, the date that the plan was adopted or terminated; and
- whether purchases were made in reliance on the Rule 10b-18 non-exclusive safe harbor; and whether any of their officers or directors subject to the insider trading reporting requirements under Section 16(a) of the Exchange Act purchased or sold shares or other units of the class of the issuer's equity securities that is the subject of an issuer share

> repurchase plan or program within 10 business days before or after the announcement of an issuer purchase plan or program.

Differences of Views from Dissenting Commissioners

A majority of the SEC commissioners believes that this additional information, together with the additional daily-level detail that it is proposing to require on Form SR, would help investors to assess whether the issuer or its insiders are potentially engaged in self-interested or otherwise inefficient repurchases and thereby help mitigate some of the potential harms associated with issuer repurchases. Commissioners Roisman and Peirce questioned the analysis used to justify the additional burdensome disclosures.

In a dissenting view, Commissioner Elad L. Roisman has stated:

> The proposal we are considering today provides a few justifications for new regulation of buybacks. One, which I do not believe is well enough substantiated in our analysis yet seems to be the most heavily discussed, is the concern that company insiders are using buybacks to manipulate companies' stock prices as a way to increase the value of their own equity compensation.
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> Although today's proposal includes considerable discussion of this purported problem, it includes very little discussion of substantial contrary evidence.

In a dissenting view, Commissioner Hester M. Peirce has stated:

> Opposition to buybacks is often rooted in the idea that surplus corporate cash ought to be reinvested in the company—in the form of higher salaries for employees, more research and development, new property, plant, and equipment, and so forth—rather than being returned to shareholders. Such an argument assumes that the politician, regulator, or academic making it is in a better position than management to assess corporate opportunities and determine appropriate levels of cash in company coffers. History is replete with examples of central planners allocating resources poorly, and I expect this experiment will end no better.

The comment period on these proposals will expire 45 days after publication of the proposals in the *Federal Register*, which is expected shortly. The proposing release is available here.