

# Share buy-backs

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## Introduction

A company may want to buy back its own shares for a number of reasons, including to return surplus cash to shareholders, to increase earnings per share, to adjust gearing ratios, to increase liquidity of shares (in the case of a listed fund) and to provide an exit route for shareholders.

## Share buy-backs as distributions

Share buy-backs, which are also referred to as 'share repurchases' or 'acquisitions of own shares', are treated under the Companies (Guernsey) Law, 2008 (the **Law**) as a form of 'distribution' made by a company to its shareholders.

The directors may only authorise a distribution such as a share buy-back if they are satisfied on reasonable grounds that the company will, immediately after the distribution, satisfy the 'solvency test' (as defined under the Law). The directors must also be satisfied that any other relevant requirements of the company's memorandum and articles (if any) are satisfied.

If, at any point after authorising a share buy-back but before the distribution has been made, the directors cease to be so satisfied, the distribution will be deemed to be unauthorised. A distribution that is made at a time when the company does not, immediately after the distribution, pass the solvency test is deemed unlawful and can, in certain circumstances, be recovered from shareholders. Moreover, the directors may, in certain circumstances, be personally liable to the company for any shortfall.

## Share buy-back programmes

If the directors propose to grant authority for an ongoing share buy-back programme, they must be satisfied that the company will pass the solvency test after **each and every** share buy-back, not just after the grant of the relevant authority.

The test essentially constitutes a cash flow test and a net assets test as well as the satisfaction of any regulatory solvency requirements. Logistically, it may be impracticable for the directors to consider the company's position immediately prior to each buy-back, particularly where they have granted authority to an investment manager or adviser to exercise the buy-back on the company's behalf. This issue may be overcome by instructing an appropriate person (usually the administrator and/or manager) to regularly monitor the financial status of the company and to notify the directors immediately upon the occurrence of any material change to the company's financial position that would or could cause it to fail the solvency test upon an exercise of the buy-back authority. If such a notification is made, the directors can revoke the authority prior to the relevant buy-back taking place.

## Shareholder authority

As long as a company is authorised to buy back its shares under the provisions of its memorandum or articles, a company may do so, subject to shareholder authority (in addition to the directors' authority

outlined above). The level of shareholder authority required for a share buy-back depends on whether it will be a 'market' or an 'off-market' repurchase of shares.

If the shares in question are not listed on a recognised investment exchange pursuant to a marketing arrangement, the buy-back is considered to be an 'off-market acquisition'. The Law requires that an off-market acquisition is made by contract, the proposed terms of which must be authorised in advance of the share buy-back by ordinary resolution of the company. The authority must specify a date on which it is to expire.

If the shares to be acquired are listed on a recognised investment exchange pursuant to a marketing arrangement, the company may undertake a 'market acquisition' (although it may still elect to undertake an off-market acquisition). For a market acquisition, the Law requires that the proposed terms of the transaction are either authorised by way of ordinary resolution or under the company's memorandum and articles. The authorisation may be general or limited to the buy-back of shares of any particular class or description, and it may also be unconditional or subject to conditions. In addition, the authority must specify the maximum number of shares authorised to be acquired, agree the maximum and minimum prices payable and specify the date on which the authority is to expire (which cannot be later than 18 months after the date on which the ordinary resolution is passed).

### **Treasury shares**

Shares repurchased by a company can be cancelled or, providing authorised by its memorandum or articles or by an ordinary resolution, held in treasury and re-issued at a later date. A company may hold up to 100 per cent of the total number of issued shares of any class or classes of shares as treasury shares, provided that at least one share is held by a person other than the company.

### **Contacts**

For further information, please get in touch with your usual Mourant contact or, alternatively, a list of contacts can be found [here](#).