

THE COMPANIES (ACQUISITION OF OWN SHARES) (TREASURY SHARES) REGULATIONS 2003 (SI 2003/1116)

THE COMPANIES (ACQUISITION OF OWN SHARES) (TREASURY SHARES) NO. 2 REGULATIONS 2003 (SI 2003/3031)

GUIDANCE NOTE FOR BUSINESS

The purpose of this note is to explain the principal changes that the Companies (Acquisition of Own Shares) (Treasury Shares) Regulations 2003 (SI 2003/1116) and the Companies (Acquisition of Own Shares) (Treasury Shares) No. 2 Regulations 2003 (SI 2003/3031) have made to the Companies Act 1985.

It is beyond the scope of this note to set out all the provisions of the regulations (the majority of which are consequential changes to various provisions of the Companies Act 1985 to take account of treasury shares) and any company intending to take advantage of the treasury shares regime is recommended to consider the regulations in detail with its legal advisers. The two sets of regulations - which are deregulatory and only need to be considered by companies if they want to take advantage of the treasury shares facility - came into effect in December 2003.

Background

2 Under the Companies Act 1985, companies may purchase their own shares but only in the circumstances and under the conditions laid down in the Act. The company must be authorised to purchase its own shares under its articles and the purchase must be approved by resolution of the shareholders. The shares must be fully paid up and, after the purchase, must be cancelled. In general, shares may only be purchased out of distributable profits or from the proceeds of a fresh share issue.

General effect

3 The regulations have relaxed the requirement that a company that purchases its own shares must subsequently cancel them. Companies that purchase their own shares out of distributable profits have the option of holding them "in treasury" for sale at a later date or of transferring them for the purposes of, or pursuant to, an employees' share scheme. Only "qualifying shares" may be held in treasury: "qualifying shares" are defined in the regulations as shares which:-

- i) are included in the official list (ie listed on the London Stock Exchange); or

- ii) are traded on the market known as the Alternative Investment Market; or
- iii) are officially listed in another EEA State; or
- iv) are traded on a market established in an EEA State which is a regulated market for the purposes of Article 16 of Council Directive 93/22/EEC on investment services in the securities field.

Private companies, and public companies with shares which are not listed or traded on one of the above markets, are required to cancel any of their own shares which they purchase.

Requirements which apply to companies that hold treasury shares

4 Companies are subject to the requirement that the aggregate nominal value of shares held in treasury must not at any time exceed 10% of the nominal value of the issued share capital of the company (or 10% of the nominal value of each class where a company holds more than one class of shares). If that limit is exceeded, the company must dispose of or cancel the excess shares within 12 months.

5 A company may not exercise any rights in respect of any treasury shares that it holds (including the right to vote at meetings) and any purported exercise of such a right is void. No dividend may be paid, and no other distribution of the company's assets may be made, to the company in respect of any treasury shares. However, these restrictions do not prevent the allotment of shares as fully paid bonus shares in respect of any treasury shares or the payment of any amount payable on the redemption of any treasury shares if they are redeemable shares.

6 If the treasury shares cease to be qualifying shares, eg if the shares cease to be listed, the company is required to cancel the shares forthwith. However, this does not apply in respect of shares which are only suspended from listing.

7 The holding of treasury shares by nominees is not permitted and the company is obliged to make the appropriate entries in the register of members in respect of the treasury shares. Accordingly, it will be apparent from an inspection of the register that the shares are held by the company and therefore constitute treasury shares.

8 Treasury shares may be sold; or transferred for the purposes of, or pursuant to, an employees' share scheme; or cancelled. However, they may

only be sold for cash (which includes the release of a liability for a liquidated sum or an undertaking to pay cash within 90 days).

9 The proceeds from a sale of treasury shares have to be dealt with as follows:-

i) where the proceeds of a sale are equal to or less than the purchase price paid by the company for the shares, the proceeds shall be treated as a realised profit of the company; and

ii) where the proceeds of a sale exceed the purchase price paid by the company for the shares, the part of the proceeds of the sale that is equal to the purchase price paid shall be treated as a realised profit of the company and a sum equal to the excess shall be transferred to the company's share premium account.

10 The pre-emption rights that apply to the allotment of new shares apply to the sale of treasury shares but may also be similarly disapplied with the agreement of shareholders. The requirements applying to the returns that a company makes to Companies House (section 169 notices) following a purchase of its own shares have been amended. Companies which purchase their own shares have to indicate any shares that are to be held in treasury and, subsequently, details of those treasury shares that are sold, transferred or cancelled. Investors making disclosures (under section 198 of the 1985 Act) of an interest in shares to a company need to exclude any treasury shares held by the company when calculating the percentage of the company's issued share capital that they hold. Such disclosures have to be made when investors hold 3% or more of a company's issued share capital.

11 Officers of a company are liable to a fine for any contravention of the regulations.

12 Copies of this note are available from the Department of Trade and Industry, Corporate Law and Governance Directorate, Room 507,1 Victoria Street, London SW1H 0ET.

Corporate Law and Governance Directorate
Department of Trade and Industry
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