The Repurchase of Own Shares by Public Companies and Aktiengesellschaften

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I. Introduction

For the German observer the idea of a Company repurchasing its own shares seems to resemble the picture of a snake eating its own tail. It appears to be highly unnatural and one wonders how the tail can possibly be eatable for the snake.

Not in the United States. Although repurchases have once been subject to the most stubbornly fought conflict in US Company law[1] only some modest disclosure requirements and safeguards against overt market manipulation exist today. Large repurchases are an almost everyday event and there is an increasing tendency. The aggregate value of shares repurchased by NYSE listed companies has increased from $ 1 .1 billion in 1975 to $ 6.3 billion in 1982 to $ 37.1 billion in 1985[2]. Few examples may illustrate this practice further:

Within three years Ford Motor Corp. repurchased 30 million shares for $ 1.2 billion[3]. In 1985 Phillips Petroleum Corp. was faced with two hostile bids and took several defensive steps, one of which was to tender for 20 million of its own shares at a total cost of $ 1 billion. And by the end of 1988 Exxon Corp. retired 28 percent of its shares that had once been outstanding at an aggregate cost of $ 14.5 billion[4].

The Situation in Germany is completely different. As it will be shown under German law repurchases are severely restricted and do not take place at an appreciable amount at all.

In contrast to German law the United Kingdom does not prohibit repurchases but requires companies to comply with such complex rules that US companies would regard simply as limiting their economic freedom. Therefore UK companies very seldom repurchase their own shares, too[5].

This paper deals with repurchases by quoted companies, in particular the UK public Company and the more or less German equivalent, the Aktiengesellschaft (AG). It seeks to ascertain the reasons why companies might want to engage in those activities. Moreover, it tries to analyse the problems which may arise from repurchases and the safeguards which the UK and German legal Systems provide for these Problems.

II. Historical Development

There were no problems arising out of the repurchase by a Company of its own shares until the concept of capital as a permanent fund to be kept intact was developed. The notion of shares as financial units was non-existent, and therefore no provisions for reducing the number of shares existed in the early history of English Company law.
This changed with its further development. The fact that deeds of settlement of many companies in the eighteenth century made provisions for the repurchase of own shares[6] shows that that the practice prevailed long before it gave rise to any litigation. The first cases, however, inclined to the view that if the power to repurchase shares was included in the deed of settlement, it would be upheld and the retiring member would be free from responsibility for the company’s debts[7]. On the other hand, several cases denied the validity of such provisions[8]. But none of these cases seemed to realise the deeper implications of this matter, so that it is no wonder that there was no uniformity in the case law.
A change was brought about by the Companies Act 1867 which provided for the reduction of capital. The courts had to face the problem of repurchases under new legislation, but there was still no common opinion on this matter’. However, the decision in *Trevor* v. *Whitworth*[10] settled the law on this subject and established that a Company could not repurchase its own shares, even

though there was an express power to do so in its memorandum, since this would amount to a reduction of capital. The protection of creditors was by far the most decisive point in this decision[11]. In considering the decision in this case one has to bear in mind that the principle of limited liability was still a relatively new concept and the ghost of the so-called South Sea Bubble, a financial scandal in which the limited liability of a Company had been used for fraudulent purposes, was still prominent in English jurisprudence. With this background one can readily understand the consternation of their Lordships at such transactions.

However, it was later recognised that the rigid application of this principle might be unduly strict and thus over the years the common law has allowed certain exceptions[12]. With the growth of the common law exceptions, it was recognised that to a certain extent the Prohibition was too restrictive upon commercial activities. There have emerged statutory modifications which evidenced a gradual movement away from the strictness of the rules. This showed an increasing realization that the Company, like an individual, requires flexibility if it is to be able to compete as a viable entity in the world market. However, in the years immediately following the decision the rule laid down in *Trevor* v. *Whitworth* and its basic principle remained intact[13].

The Second Council Directive on Company Law permitted the UK to maintain the existing exceptions to the *Trevor v. Whitworth* rule but did not require to extend them[14]. The UK, however, encouraged by a study undertaken by *L.C.B.* Gower for the government (a so-called 'Green paper')[15], decided to widen the exceptions. This decision, although taking into account the Situation in which public companies were at that time, was mainly motivated by the wish to make private companies more attractive for outside investors. Under the CA 1985 public companies are generally able, subject to procedural requirements, to repurchase their own shares[16]. The conditions for such a repurchase include that the purchase monies may only be found out of distributable profits or the proceeds of a fresh issue of shares and that, once repurchased, the shares must be treated as cancelled and the issued share capital of the Company reduced by their nominal amount.

The early history of German Company law shows a changeable attitude towards the repurchase of own shares. Before 1870 the Allgemeines Deutsches Handelsgesetzbuch did not contain any provisions relating to the repurchase of own shares at all[17]. Until the late 1960s some German scholars even denied the theoretical possibility that a Company could become its own member[18]. However, the first amendment to the ADHGB of 1870 brought into force a Provision which forbade the repurchase of shares for companies[19] and a few years later the Reichsoberhandelsgericht invalidated sales to a Company of its own shares[20]. As a reaction to vehement criticism against this absolute Prohibition in the academic literature[21], in 1884 an amendment of the ADHGB provided that companies might not acquire their own shares in the ‘course of their business’[22]. An amendment of 1897 altered the language of the Provision to the effect that a Company must not acquire its own shares ‘in its regular course of business’. The object of this amendment was to make clear that irregular occurrences, such as acquisition by gift, should be exempt from the Prohibition. However, the new wording of the statute was weak and interpreted both by scholars and practitioners to mean that any repurchase which was not a regular business transaction, such as repurchases to support the market price, was allowed. Therefore, in practice, the Prohibition remained ineffective and was ignored[23].

In the years of severe business contraction in 1929 as earnings declined, many German companies attempted to sustain the market price of their shares by repurchases. They were able to do so because the deflationary process released funds which could be used for the repurchase of shares. Particularly banks were active in this movement, prompted by the fear that the market price of their shares might fall below par value - an idea considered fatal to a bank. By the beginning of 1931 the Bremer Bankverein had repurchased 64 percent of its own shares, the Darmstädter Nationalbank 58 percent and the Dresdner Bank 55 percent[24]. Solely by reason of financial necessity was the practice abandoned after the 1931 collapse of the stock market. Shortly afterwards an emergency decree prohibited the repurchase of own shares in principle[25]. Only very limited exceptions were allowed. Amendments in 1937, 1959 and 1965 tightened up the provisions even further.

Therefore, the implementation of the 2nd Directive by an amendment in 1978 brought only limited changes for German Company law[26]. The content of the provisions in its earlier forms was restructured and markedly tightened up. At present, in principle an AG may not repurchase its own shares. It may repurchase its own shares, however, where it is necessary to prevent serious and imminent harm to its interests, to offer the shares for sale to its employees and its retired employees or to pay compensation to minority shareholders in subsidiaries that are being wound up or integrated into the parent AG[27]. In these circumstances the repurchase may not exceed 10 percent of the capital stock and the amount paid must come out of surplus capital. Those shares held by an AG have no voting rights.

At this point, it is already possible to see that in some respect UK law goes a different way from German law. While in the UK a Company may acquire as many shares as it likes as long as it complies with certain requirements, a German Company has this power only within very restricted situations and then only within the 10 percent limit. Because of the fact that there is no limit on the repurchases UK legislation contains a strict requirement that repurchased shares have to be cancelled. More differences have to be considered later.

II. Incentives for Repurchases

A short definition of the term 'repurchase' can be given by saying that it means that a Company acquires its own shares from one or more shareholders by paying or agreeing to pay in cash or another consideration. The repurchase results from a specific agreement between the Company and the shareholder which is entered into after the shares have been alloted. This distinguishes those transactions from those where companies buy back their redeemable shares[28]. While the redemption of shares is well known under UK law[29] it is not possible under German law. However, both are a transaction which purports to reverse the process of creating shares by terminating the legal incidents connoted by the shares involved.
Although it has been submitted that companies rarely have good reasons for repurchasing their shares[30], there are several possible reasons why they wish to do so[31].

1. Repurchases as a Capital Reduction

Some companies reach a point in their development where, through lack of new investment opportunities, contraction of markets, or a decision to scale down operations, it is desirable to reduce the equity base.
In the case of companies with excess equity they might be interested in returning the surplus resources to the shareholders through a repurchase, rather than go through the procedural complexities of a capital reduction. A repurchase, therefore, allows the retirement of capital no longer needed by companies and it removes the pressure on such companies to employ those surplus resources in uneconomic ways[32]. While repurchases in these cases resemble the payment of dividends in that both are methods of distributing and

therefore reducing corporate assets, they can be used to fulfill dividend-type functions[33].

However, it should not be overlooked that there are significant differences between a payment of a dividend and the repurchase of own shares. Repurchases may have advantages both for the Company and its shareholders under certain circumstances but sometimes may also put the shareholder at a disadvantage.

In the case where the surplus cash arises not from a continuing source like long-term profits, such repurchases at a premium may be a means of making a once and only special distribution to particular vendor shareholders without raising the general dividend rate. This might satisfy shareholders' preferences much better[34] and might be able to ensure a better dividend continuity for the Company. The management is usually reluctant to declare reduced dividends for the next year after a high dividend has been payed in the last.

Furthermore, in a repurchase the shareholders are given the choice as to whether to accept the offer or not, whereas they do not have any option in the case of dividend distributions. Keeping this in mind, a repurchase offer made to all shareholders has the benefit of providing shareholders with the choice between an increased share of corporate ownership by retaining their shares or a cash return by accepting the offer. Repurchases can, from this point of view, be a more flexible and efficient financial technique for shareholders than a capital reduction which are in some jurisdictions a more cumbersome procedure. The self-selectivity of this process can be an advantage for the shareholders as a group as well. However, it should not be forgotten that a dividend payment leaves unaffected the recipient shareholder's position as a participant in the Company. A repurchase, however, results either in his elimination as participant in the Company or at least in a reduction of his interest in the Company.

Moreover, a disadvantage is that while in the case of dividends the principle of pro rata participation is characteristic and all shareholders are treated with transparent fairness, in the case of repurchases it might be different. There is always the danger of discrimination if the Company is not be bound to take up shares pro-rata[35].

Lastly, whereas a dividend payment is a unilateral act, a repurchase is a transaction. The fairness of the transaction depends upon an Optimum balance of information between the Company and its shareholders. Any change in this relationship is able to create informational asymmetries between shareholders and the management and will put the shareholder at an disadvantage.

2. Repurchases as a Self-Investment

A repurchase may be used as a commercial investment by the Company.

From the managerial perspective, such a repurchase is a minimum risk-investment as the risk characteristics of the Company are not substantially changed: the management might feel that if the Company buys another company's shares, the risk to the enterprise may be greater by the possibly unfamiliar risk characteristics of the latter Company. From this point of view a repurchase is preferable to acquiring substantial or controlling interests in other companies, especially where the management takes the view that the market price of the shares is lower than the true value and profit can be made upon their latter reissue[36]. This objective, however, requires that the Company is permitted to hold the repurchased shares as treasury shares and that it is not obliged to cancel them.

But even where treasury shares are permitted, one has to question whether repurchases constitute a self-investment by the Company. If one is not too doubtful about the management's ability to identify an undervalued Situation in an efficient market, one still has to deny the possibilty of repurchases as an investment. With normal investment, cash is converted into working assets. Profitable investments will increase the size of the Company. However, if a Company repurchases its own shares no cash is converted into working assets. Both the Company assets and the shareholders' equity decreases. A repurchase is rather a 'disinvestment' than an investment[37].

3. Repurchases to Influence the Share Price

Company controllers may seek to conduct the repurchase in such a way as to influence the share price. This can be for several reasons.
Where a large shareholder in a Company intends to sell his shares, the Company may wish to ensure that these shares are not dumped on the market, with a resulting decline in the price of its shares. In those cases it can be in the interests of the Company to repurchase these shares. A repurchase allows companies to directly enter the market and soak up such surplus shares by acquiring them, thereby increasing demand for the shares and supporting their market price.
Further repurchases may be used to give price support for undervalued shares where the management believes the current market price of the shares is below their long term value. This was the main reason behind about 650 repurchase announcements made by US companies after the 1987 market crash[38]. Here the repurchase is nothing else than an attempt to lessen or eliminate any discrepancy between the market price of the shares and their estimated long-term net asset backing. The management might try to put a 'floor' under the current market price so as to preserve for shareholders the value of their marketable securities.
This could also help where the Company needs to improve the market price for the purpose of attracting new investors, thereby increasing demand for the

shares and further raising the market price, thus creating a so-called 'snowball effect'[39]. Selective purchases, designed to maintain or increase the market price of the shares, may allow the Company to issue fewer shares, but at a considerable premium.

Empirical findings seem to support this view: during periods of stock market decline, the number of US companies repurchasing their own shares and the frequency of their repurchases generally increases[40]. And during the economic crisis in the early 1930s many German companies engaged in repurchase activities to support the market price of their own shares.

It has been suggested that this market behavior is unobjectionable where, in an effort to support the market price of the shares and protect against professional manipulation, a large block of shares overhanging the market and threatening to depress the price of the shares on the stock exchange is repurchased by the Company itself[41]. Otherwise for a Company the result could be fatal, since depressed prices on the stock exchange affect sales and credit standings. Moreover, repurchases could be the only availiable means of safeguarding a decent market appraisal for the bulk of shareholders.

This view, however, is open to criticism because it fails to notice two important points:

Firstly, from the point of view the efficient market-theory takes[42], it is unlikely that the market systematically and persistently undervalues companies. At any rate, even if the effficient market occasionally makes mistakes, the number of such mistakes is unlikely to be as high as the number of actual repurchase Programmes.

Secondly, a better corrective to support an undervalued share price in a case in which the company's share price falls in isolation might be the supply of adequate information to the market. Where the market trusts nonverbal signals more, the Company will still be able to respond by raising its regular dividends.

4. Repurchases to Supply Market Information

This leads us to the next incentive for a Company to repurchase its own shares. A Company may undertake a repurchase to supply the stock market with new information about a company's operating Performance and its future projects.
Here the announcement may act as a market signal that the Company considers its shares undervalued. In addition to this it may signal that the Company expects large cash flows in the future and that it can afford to return some funds to shareholders.
Therefore, it has been suggested that repurchases are to be preferred as they are, in contrast to dividend distributions, unlikely to provide misleading signals to the market[43].
However, this does not take into account that a repurchase might be interpreted as a negative signal that the Company is exhausting profitable investment opportunities[44]. From that point of view repurchases are open to the same misinterpretation as dividends. There are less costly ways to provide the market with information, if it is necessary to do this.

Nevertheless, this view is not supported by empirical findings. Repurchases by tender offer typically lead to an increase in share price that persists beyond the exspiration of the offer[45]. Most commentators interpret this as evidence that repurchase announcements lead stock market participants to infer that the share price is too low and that the repurchase Programme is a signal to the market of the management's more favorable information, so-called 'signalling hypothesis'[46]. As a result, market participants revise their forecasts of the company's prospects and this leads to a higher market price.

5. Repurchases in a Takeover Context

The power to repurchase own shares can be utilised as a defensive technique in the face of a threatened, pending or actual takeover bid or as a preventive means of reducing a company's vulnerability to unwelcome offers.

A possible pre-bid measure might be to undertake a repurchase in order to lessen the attractiveness of the target Company by altering the company's financial profile. Such a repurchase will be designed to reduce the company's cash reserves or to increase its debt[47].
Another pre-bid measure is to eliminate potentially dissident or wavering shareholders who might accept a takeover bid through repurchases and so remove the threat of the shares falling into the hands of a hostile bidder[48].
Furthermore, repurchases from shareholders who have the lowest reservation values force the bidder to buy shares from shareholders with higher reservation values. This raises the cost of such a bid and makes the Company a less attractive target[49]. Such a repurchase may also enhance the proportional holding of an existing control or management supporting group[50].

After a bid has been made repurchases still can be used as a post-bid defensive measure.
A Company may support the market price of the company's shares and thereby thwart or diminish the capacity of potential or actual bidders to obtain a share foothold at a reduced cost. Knowledge that the Company is prepared to pay a higher than the current market price could cause a re-evaluation by investors of the worth of their shares. With an increased market price the danger of such a takeover bid could be reduced[51].
This defence, however, is not free of dangers. Even when the repurchase may succeed in increasing the market price of the shares, this benefit to the target may be offset by the bidder having to acquire fewer shares in order to achieve

control. This is the case where companies are required either to cancel repurchased shares, or to hold them as non-voting treasury shares. Where the bidder is already a shareholder, the repurchase Programme would serve to increase the bidder's percentage of the shareholding of the Company.

A transaction common in the US and related to repurchases is 'greenmail'[52] There exist two types of 'greenmail'. The first is the purchase of a substantial block of the target company's shares by an unfriendly suitor with the primary purpose of coercing the target into repurchasing the block at a premium. The other is where a target undertakes a self-serving buy-out of a bidder who seriously contemplated a takeover[53].

Lastly, repurchases may play a role in defence tatics called 'poison pills'. These are measures adopted by the management in response to takeover attempts or in advance of possible takeover attempts that can cause severe economic repercussions in an acquirer or potential controlling person[54]. Two of the 'poison pills' measures involve repurchases: back-end provisions[55] and Convertible preferred stock provisions[56].

Having looked at some of these defensive tatics, it is now wotth examining in how far these measures can be effectively used in the UK and Germany.

In the UK the City Code on Take-overs and Mergers prohibits the board of the target Company from taking any action which would prejudice the bid once it has been announced or when it is believed to be imminent[57]. This makes most post-bid defences almost impossible. Furthermore, when a Company repurchases its own voting shares, the percentage of the total voting rights represented will be increased. Any resulting increase in shareholdings of directors and persons acting in concert with them will be treated as an acquisition for the purpose of Rule 9[58]. In some cases, therefore, an Obligation to make a mandatory offer will arise. Moreover, any repurchase of its securities by an offeree during an offer period is normally prohibited unless the offeree's shareholders specifically approve the proposed action[59]. These provisions are expressions of the general rule that the Panel of Take-overs and Mergers does not consider it appropriate for parties to a bid to buy their own shares during an offer period[60]

But also the statutory provisions require prior shareholder authorisation which makes it difficult if not impossible for a target management to use repurchases in takeovers[61]. The procedural requirements are too time consuming to provide UK companies with a quick and effective response to an anticipated or announced bid.

In Germany a Company may acquire its own shares up to a total value of 10 percent of its share capital[62], if this is neceassary in order to avert serious and imminent darnage to the Company[63]. Darnage means here mere loss of assets and indirect consequential darnage is accepted to be sufficient[64]. The application of this Provision in a hostile takeover context has not yet been tested in court and the academic literature is divided on this point.

An older view maintains that the acquisition of a controlling interest in a Company by external capital constitutes such indirect darnage. The advocates of this view argue that such an acquisition is to be viewed in Company law as a threat, if the new controller would be a competing concern or a foreign capital investor-, and this justifies the repurchase of own shares[65]. And it has been submitted that this Provision would be applicable in the Situation in which the management thinks that a better bid is in the offering, from the point of view of the majority of the shareholders, and they repurchase in order to prevent the success of the former bid[66]. This view, however, is too one-sided because it does not take into account that only darnage to the Company as a whole and not to some part of its members or the board of directors falls under the provisions of the AktG[67].

An alternative view is that the repurchase of own shares is permissible only when the potential purchaser threatens to wind up the Company or darnage it severely[68]. Such an exceptional case could arise in the case of raiders who seek to make the acquisition with such high loans that they are dependent on the liquidation of the acquired company's capital in order to pay off their loans. However, most legal experts are of the opinion that an impending hostile bid will not justify a repurchase. It is argued that the concrete Organisation of a Company is something not protected by the AktG[69]. A change in the controlling interest may cause harm to an individual member of the board of directors, but involves no darnage to the Company. If the risk of a Company passing into foreign control were sufficient to fulfil the exceptions laid down by the AktG, then the board of directors could decide who would become a member of the Company. This is a right which the AktG does not give. Therefore, a risk of passing into foreign control is in any case not sufficient to justify the Supposition of imminent darnage to the Company[70].

Another possible defensive measure is the repurchase of shares with a view to issuing them to the employees of the Company. In accordance with the AktG shares acquired by the Company in order to offer them to the employees must be issued within one year from acquisition[71]. Therefore, before the bid is imminent, the target Company can reduce the possibility of shareholding of the hostile bidder by the repurchase of own shares. But a supplementary restriction on the transferability of the shares will be necessary, so that the hostile bidder cannot obtain these shares through the employees. And it may be as easily turned into an instrument benefiting the raider if he gets the employee shareholders to vote in favour of his proposals.
Therefore, repurchases under German law are even less a fit means for warding off a raider than under UK legislation[72].

6. Repurchases in a Going Private Transaction

A going private transaction is a transaction designed to eliminate or substantially reduce the company's outstanding public equity[73]. It can involve a cash repurchase offer by the Company, followed by a transaction to 'mop up' the shares of non-tendering shareholders through certain possible mechanisms, a pattern found in US going private transactions in the 1970s[74].
Such a transaction can be useful because the smaller the group of shareholders, the easier it will be for the management to negotiate the necessary contracts. And the management may seek to reduce the cost of a public tender by means of a preliminary repurchase Programme aimed at contracting the number of outstanding shares. The reduced liquidity of the remaining shares will depress the market price and also place the shareholders under a coercion to sell[75].
Such a reduction of public equity has been seen in Germany by some as objectionable for policy reasons. Following the principle that legislation should encourage wide public equity participation in companies, it would prima facie be undesirable that legislation facilitates the elimination or even only the reduction of public ownership[76].

Besides, there is no evidence that repurchases played any role in UK going private transactions so far. In a Management Buy-Out (MBO) where the management helds only a small part of the company's shares or no shares at all, and this is likely to be the case in a quoted Company, almost all of the target's asset value will need to be paid out on the repurchase and consequently, the Company will need to be refinanced by external investors[77].
From the point of view UK Company law takes there are no advantages for using repurchases in MBOs[78].

Similarly, in Germany the strict rules concerning the maintenance of capital make repurchases not feasible in going private transactions and have prevented MBOs occuring in greater numbers so far[79].

7. Repurchases to Increase the Earnings Per Share

Repurchases have been suggested as a way to increase the earnings per share (EPS) by reducing the number of shares outstanding because the future earnings are going to be divided among a smaller number of shares[80]. It is quite common in the US and a recent example may be given by Conner Peripherals Corp. which bought back shares for $ 241 million to boost the company's EPS[81].

This view, however, is wrong because the expected EPS does not automatically increase with a repurchase. Unless financed by a new debt offering, repurchases also mean a reduction in the company's assets. To the extent that those assets are efficiently employed and thus contribute proportionately to earnings, a reduction in assets will mean a reduction in earnings[82]. Expected EPS will increase only if the reduction in shares outstanding is proportionately greater than the reduction in expected net income[83].

Furthermore, even if the repurchase does cause an increase in expected EPS, this increase will be achieved only by increasing the financial leverage of the Company and, thus, the financial risk of the shareholders. Any rise in the EPS, will be offset by higher return demanded by shareholders as compensation for bearing greater risk. The price of the outstanding shares will increase only if the increase in expected return dominates the increase in risk brought about by this financial leveraging of EPS.

Therefore the EPS effect of a repurchase has to be seen as being a financial illusion.

8. Repurchases to Increase the Capital Mobility

A repurchase may act as a device to increase capital mobility in the securities market. Repurchases permit the redistribution of risk-taking venture capital towards new and rapidly growing companies and away from non-growth companies. On this view, repurchases increase investment opportunities by releasing to shareholders unneeded funds for alternative investment and thereby promote the more efficient distribution and allocation of capital resources in the economy.

9. Miscellaneous

In addition to these reasons, other valid bases for such transactions exist. Some of the more widely known are the facilitation of mergers and acquisitions[84], the settlement of a shareholder's indebtness[85], the encouragement of employee share schemes[86], the reduction of shareholder servicing costs[87] and the possibility to accelerate the redemption of shares[88]. Last but not least, it is worth mentioning that there might be circumstances where a Company might want to provide a market for its shares [89]. However, this is a reason more likely for the private, closely-held Company.

IV. Drawbacks Arising from a Repurchase

It has been shown that repurchases involve most doctrinal institutions of Company law. This consequently includes all possibilities of abuse. Some forms of abuse have been mentioned already. However, there are five aspects which will have to be examined seperately.

1. Effects on Creditors

One of the most important functions of Company law is still the protection of creditors. Because of the limited liability of companies, Company law has to secure the raising and maintenance of equity capital as a sort of guarantee for creditors[90]. Of course, no Company law Provision can remove the risk that the Company will incur losses in the usual course of its business, which will use up its assets. But the principle of raising and maintenance of capital has a stricter meaning: it prevents the founders and shareholders of a Company from harming creditors by keeping the minimum capital from the Company or by taking it arbitrarily away.

If, at the time the repurchase is made, the Company does not have an actual surplus or if the amount paid exceeds the Surplus, in economic terms the repurchase is a return of the shareholder's contribution[91]. And in the case of partly paid shares the raising of capital will be imperilled because the Company only holds a claim against itself.

Therefore, a repurchase may impair the creditors' margin of safety against the business losses incurred by the Company. Nothing of value to creditors takes the place of the shares repurchased except what is in reality an unissued share, as there is no certainty that the shares can be reselled in the future[92]. This shrinkage of the company's capital base threatens particularly the unsecured creditors whose de facto security is the liquidation value of the company's net marketable assets.

In the UK the principle that the creditors of a Company have a right to rely on the maintenance of its paid up capital as a guarantee fund for the payment of their claims was the principle rationale of the English common law rule prohibiting such repurchases. However, a repurchase by a Company of its own shares does not lead to a reduction of capital if the repurchase is out of the company's profits and an amount equivalent to the nominal value of the shares purchased is placed in a seperate capital account.

The CA 1985 stipulates therefore that the reduction in share capital account caused by the cancellation of the share repurchased must be compensated either by new capital from a new issue of shares made for the purpose[93] or by transferring distributable profits from the profit and loss account to a capital redemption reserve[94] which is to be treated as paid-up share capital[95]. If the price at which a Company repurchases its shares is greater than their nominal value then the excess is treated in the same way as a redemption premium on the redemption of own shares[96]. And shares that are to be repurchased have to be fully paid up[97], otherwise the creditors would lose a valuable asset on liquidation, namely uncalled capital. These provisions, enforced by effective penalties[98], ensure that there is no erosion of the capital maintenance doctrine[99].

German law goes a somewhat different way. It contains similar restrictions on the funds to be used for repurchases but seeks to protect creditors also by restricting the circumstances in which a repurchase is permitted.

In principle a Company may not repurchase its own shares[100] and a repurchase is only permitted when necessary to avert serious and imminent darnage to the Company[101], to offer the repurchased shares to employees and retired employees of the Company or a related enterprise[102] or to indemnify shareholders[103]. In all three cases the aggregate nominal amount of the repurchased shares may not exceed 10 percent of the capital stock including the shares which the Company has already acquired and still possesses[104].

Furthermore, the reserve to be formed to offset the repurchase of shares[105] must constitute an amount equal to the acquisition value of the shares without reducing the share capital or the reserves, to be formed in accordance with the

AktG or the articles, which may not be used for payments to the shareholders[106]. Thus, there exists a capital limit for the repurchase of the company's own shares. These provisions which serve to sustain the share capital[107] are complemented by the requirement that the par value or higher amount for issue of the shares must be fully paid[108]. Penalty provisions[109] and provisions granting damages from the board of directors[110] and from the supervisory board[111] in cases where the repurchase is undertaken illegaly ensure the effectiveness of the requirements.

2. Effects on Shareholders

A repurchase can in principle be done through an invitation to tender, as a targeted repurchase or through a transaction on a stock exchange.
Where the repurchase is made as an invitation to tender, the shareholders voluntarily decide whether or not to sell and divide themselves accordingly. In contrast, where the Company makes a targeted repurchase, the division is involuntary: the Company selects the selling shareholders and places all others in a remaining group. Therefore, in the latter case a repurchase may result in an improper discrimination between shareholders, where favoured members are bought out at a substantial premium to the market price or true value of their shares. This leads to a dilution of the value of the remaining shares[112].
Another possible instance may be where a Company acquires shares at a discount to their true value, thereby increasing the equity value of the remaining shares at the expense of the vendor shareholders[113].
And it is possible that majority shareholders, in expectation of losses of the Company and a decline in the share price, sell their shares to the Company at what is in fact an overvaluation. When it becomes obvious that the liquidation will result in less than par repayments for the other shareholders, the

repurchase brings about something which has to be called a 'preferential liquidation'.

In fact, where the shares are not repurchased at a fair value such a transaction always shifts wealth from one group of shareholders at the expense of another. The fact that a shareholder is not obliged to sell his shares to the Company[114] does not alter this fact.

The potential for internal inequities can be minimised through mainly three requirements: disclosure of details of any share repurchase activity before and after the event, prior Permission by shareholders and the requirement to repurchase shares through a stock exchange.

Adequate disclosure is ensured in the UK first of all by the requirement that companies are permitted to repurchase their shares only if authorised by their articles[115]. This prevents shareholders from unexpected activities by the Company although this alone does not provide adequate Publicity. Consequently, the CA 1985 contains a number of detailed disclosure and notification requirements to ensure that the transaction is done openly[116].

A second method of safeguarding shareholders' rights is to lay down a general requirement that companies wishing to repurchase their shares must obtain prior Permission from the groups whose interests might be adversly affected. This can be effective against most forms of abuse, without limiting the potential benefits from the use of share repurchases. It is for this reason that the CA 1985 distinguishes between market purchases and off-market purchases[117] and requires that both forms of repurchase must be authorised by a resolution of the shareholders, which must stipulate the terms of the repurchase. The sanction required for an off-market purchase is greater than that required for a market purchase because here the Company will be the price maker and there is not equality of access for the selling shareholders as in a market purchase. Furthermore, the lower level of regulation of market purchases takes into account that fact that the market authorities impose their own regulatory

requirements which, coupled with the higher degree of Publicity, will be sufficient to deter the more blatant abuses of the procedure. For market purchases a prior authorisation by an ordinary resolution subject to certain conditions is required[118] and requirements which are not contained in the CA 1985 itself might have to be observed under certain circumstances[119]. In the case of off-market purchases there has to be an approval of the terms of the purchase contract, including the actual price, by a special resolution before the Company enters into the purchase contract[120]. In order to prevent discrimination between the shareholders the CA 1985 provides that, in relation to an off-market purchase, votes in respect of shares to which the resolution relates are to be ignored[121].
Another requirement imposed by the London Stock Exchange on listed companies which ensures equal treatment of shareholders is that repurchases within a period of twelve months of 15 percent or more of its equity shares must be made by way of either a tender or a partial offer to all shareholders[122]. Selective repurchases are therefore prohibited.
Further safeguards are provided by the general remedies concerning the protection of minorities[123]. These rules provide remedies if the directors use their power in a way which is unfairly prejudicial to some part of the members. The requirements relating to repurchases, together with these general remedies, are strong deterrents to inequitable practices.

The fact that German law allows repurchases only to a very limited extent reduces the opportunities for unequal treatment of shareholders. But even in the cases where repurchases are allowed the provisions of the AktG still require that no shareholder should arbitrarily be treated differently from other shareholders[124]. The wish to buy out members at a favoured price or to buy out insurgent shareholders at a price above the market price will clearly violate this principle of equal treatment[125]. Therefore, it is submitted by commentators that repurchases in principle have to be made through a stock exchange and, if this is not possible, at least through a tender offer. Selected repurchases shall only be allowed in the case where it is necessary, in order to avoid serious and imminent darnage to the Company, to acquire shares from specific shareholders[126]. However, disclosure requirements still provide full information to all shareholders and leave no room to use this exception for benefiting only some part of the company's members[127]. Furthermore, each shareholder has duties of loyalty both to the Company and to other shareholders (so-called *Treuepflichten*)[128], which make it not feasible for a group of shareholders to be bought out at the exepense of another. Further, in a recent ruling from the *Oberlandesgericht Oldenburg* it was shown that the principle of equal treatment works the other way round, too. In the case where the Company is about to resell its repurchased shares, it was held, the Company has to keep to strict neutrality and is bound to observe the principle of equal treatment. Thus a Company has to resell its shares through the stock market or if not possible through a Stockbroker[129].

3. Effects on Corporate Governance

It is the management which controls the timing and terms of repurchase and, except for market repurchases and tender offers to all shareholders, selects the selling and remaining shareholders.

If the management holds shares, it is interested in the transaction, whether it belongs to the selling or remaining group[130]. If it is not a shareholder, the reorganisational effect of the transaction will make it an interested party in a wider sense. Targeted repurchases can have as their objective the elimination of shareholders who pose an actual or potential threat to the management. Furthermore, management could insulate itself against shareholder action by buying off shareholder opponents without regard to whether this will be beneficial to the Company or not. Such managerial behavior may then be described as management entrenchment, a behavior common in the 1920s and the early 1930s when many German companies were creating shares to protect themselves (so-called *Schutzaktien*)[131].

From the management's point of view a repurchase may be desirable to prevent shares from falling into the hands of potential 'unfriendly' bidders which might want to dismiss the management[132]. Also repurchases can be used to protect incumbent management from exposure to shareholder discontent in general meeting that might otherwise follow from a substantial decline in the market price of the shares.

Therefore, generally speaking, repurchases can be used to enable an incompetent management to remain in control[133], which is the 'most serious threat to owner control'[134].

And it should not be forgotten that since repurchases change ownership participation, they alter the existing allocation of authority between the management and the members. Thus, the management could try to strengthen its influence in the general meeting by using the company's assets to repurchase shares in order to alter the voting control of the Company. This would be contrary to the compelling division of powers between the organs of a Company and could lead to a Stabilisation of an unsuccessfull management. Shareholders will be affected directly or indirectly by a change in the balance of voting power if the repurchase is not from all shareholders and proportional to their holdings. The voting control will be directly affected if the repurchased shares carry voting rights which the management is entitled to use in the general meeting. But even where the Company is not entitled to enjoy the voting rights of repurchased shares, an abuse is still possible. By removing the repurchased shares from the voting arena a minority of shareholders can be converted into a majority, which is now able to gain control in general meeting. And even where a majority cannot be achieved, the relative voting strengh of the management or any related group will be increased anyway.

For directors of UK companies it is not enough to comply with the procedures laid down in the CA 1985 because the procedures simply provide an exception to the general Prohibition on a Company to repurchase its shares. As with all powers, the power to repurchase the company's own shares is subject to the general requirement that directors must act honestly, in good faith and in the best interests of the Company. The rules concerning the directors' duties of care, skill and good faith provide remedies if the directors use their power for an improper purpose or to benefit themselves[135]. It is clear that a repurchase by the directors on behalf of the Company of the company's own shares would be a breach of duty by the directors if the main purpose was to enhance their position[136], although suing directors for breaches of duty is notoriously difficult in the UK[137].

By providing that the repurchased shares have to be cancelled and not to be reissued[138], the CA 1985 helps to protect the rights of the remaining shareholders.

In Germany, as in the UK, the repurchase of own shares is always a measure of management and therefore taken by the board of directors[139]. By providing that the Company shall enjoy no voting, dividend or preemptive rights from its own shares, whether the shares were legally or illegally acquired, German law prevents the board of directors from extending its influence in general meeting directly[140]. And shares repurchased in order to issue them to employees have to be disposed of within one year[141] so that they cannot be used by the management for an improper purpose.

4. Effects on the Stock Market

Among the abuses associated with repurchases, market price manipulation can be seen as one of the most insidious.

In an efficient market a substantial increase in buying, normally reflecting increased demand, without any corresponding increase in supply, will disturb the elibrium and affect the market price.

The market price may also be affected if companies are entitled to hold acquired shares as treasury shares rather than cancelling them. This would enable a Company to buy shares, hold them as an asset, and later resell them. The Company would then have the ability to advance the market price through large-scale anonymus repurchases, and likewise depress the market price by putting a large block of repurchased shares back onto the market.

The London Stock Exchange requires companies intending to undertake repurchases to notify such activities in detail prior to and after the event takes place[142]. By this means, the market, the company's shareholders and potential investors are made aware of the influence of the Company in the market, and thereby can make more reasoned investment decisions.

Repurchases designed to manipulate the stock market will certainly fall foul of the Financial Services Act 1 986[143].

Moreover trafficking in shares by companies is avoided if shares have to be cancelled after repurchased by the Company. Therefore, UK law prescribes that shares have to be treated as cancelled on the repurchase[144]. Speculation by companies against their own share price by buying and selling rights to repurchase them is also prohibited[145].

Stock market manipulation by German companies is not likely because of the very limited extent to which a repurchase is possible.

The need to avoid serious and imminent darnage to the Company allows up to a certain extend a repurchase[146]. Very recently, there has been a ruling by the *Bundesgerichtshof* in an *obiter dictum* which accepted the disturbance of the stock market and a Variation in the market price as beeing such a darnage to the Company[147]. However, it was neither said how serious the disturbance has to **be nor in how far the Company has to be affected by the disturbance.** And one has to oberserve that the Company concerned in this judgement was a bank. It is therefore unclear in how far the ruling could also apply to a non bank[148]. On the top of this is the fact that the academic literature takes the view that the mere Variation of share prices constitutes not such a darnage. Only in a rare and extreme case a Company would be allowed to repurchase its own shares in order to influence the market price. Therefore, a Company will normally be prohibited from intervening in the functioning of the market by repurchases and from pegging the market price of their own shares[149]. Furthermore, German law contains certains requirements to transfer or redeem repurchased shares which do not make it feasible for companies to deal in their own shares[150].

Further, when a Company repurchases its own shares, it invariably possesses knowledge of facts not availiable to all shareholders or the general trading public. Therefore, a repurchase can increase the possibility of insider trading both by the Company which acquires its shares and third persons[151]. A Company could acquire shares for a price which is too low in a case where its decisionmakers are in possession of confidential price sensitive information concerning those shares and where the seller, if he had had that information, would have not sold at that price. It will not be uncommon for a Company to have material information of this nature in its possession.

Third persons may also benefit improperly from repurchases. For instance, insiders who are aware that the Company proposes to repurchase its shares at a premium price to the market, may be tempted to acquire the company's shares in advance of a public announcement of the intended repurchase. Another possibility would arise where an influential insider withdraws his contribution in the Company in which he has, because of confidential information, lost trust.

In the UK the provisions of the Criminal Justice Act 1993 dealing with insider dealing have to be oberserved[152]. If the directors are in possession of unpublished price sensitive information, they are not permitted to procure any other person (including the Company) to deal in those securities on a stock exchange for the purpose of making a profit or avoiding loss.
Furthermore, accordingly to the Model Code for Securities Transactions by Directors by the London Stock Exchange a director must not deal in any securities of a listed Company at any time when he is in possession of unpublished price-sensitive information in relation to those securities[153]. The terms of the Model Code apply also to a Company repurchasing own shares so that both, the company's director and the Company itself, are prohibited to act as an insider[154].

Market manipulation by means of a repurchase of own shares on a German stock exchange is, again, because of the restrictiveness of German law, quite unlikely to occur. However, such an attempt will clearly violate the new insider trading rules[155]. Under these rules an insider must not use insider information for transactions in securities for his own benefit or a third party, nor must he pass any information to a party who is not an insider.

5. Effects on the Company's Business

A repurchase of own shares increases the financial risk of the Company. The Company acquires an asset which does not contribute to its diversification as the value of that asset will correlate with the company's profits[156]. In the sense that the share prices reflect the future earnings of the Company in the long run, the share price will decline in the same degree as the profit prospects of the Company[157]. Economic failure will Capture the Company now twice. Therefore, it would be a bad advice for a Company which is in financial difficulties to lock up its capital because such shares could be sold only with great economic losses if at all.

However, as it was shown above both UK and German law contain restrictions on the funds availiable for repurchases. This prevents that repurchases will lead to a greater risk of Company failure. And since UK law requires cancellation of repurchased shares there is no acquisition of an asset by the Company at all. In that sense it is a simple distribution of assets.

IV. Concluding Remarks

Recently a discussion has come up as to whether to alter the strict German rules concerning the maintenance of capital. It has been suggested that this should include a relaxation of the rules prohibiting repurchases[158]. It is mainly argued that the protection of creditors would simply not justify such an effort. And it has been submitted that the rules prohibiting the repurchase of own shares should at least be interpreted in a way which would allow companies to pursue their economic aims in a better way[159].

This view is to reject because the rationale behind the prohibtion on the repurchase of own shares is not the protection of creditors alone. It has been shown that there are more good reasons for controlling the methods and purposes of repurchases. The abuses connected with repurchases span the entire range of Company chicanery. These practices, although they are not necessary incidents of repurchases, demand restrictive provisions for those transactions.

The 2nd Directive left it open to Member States whether or not to allow repurchases. By imposing only minimum requirements with regard to shareholder's authorization, the extent to which a Company may hold its own shares and the funds availiable for repurchases, a considerable discretion was left to Member States. The UK, more generous than Germany by not limiting the situtations in which repurchases might be permissible or the value of the shares that may be repurchased, therefore had to impose much more detailed provisions in order to prevent possible abuses. On the other hand German law does not know any self-regulatory rules imposed by the stock exchange like the UK. This type of rule, typical for UK Company law, is seen as unnecessary in the light of the AktG. Therefore, UK and German law differ to some extent. Both legal systems strike the balance between the conflicting interests of ensuring corporate flexibility and yet providing protection for creditors, shareholders and the general investing public differently. Nevertheless, it is submitted, are both alternatives acceptable. The lack of relevant litigation in these transactions shows that both legal systems have dealt with these type of corporate transaction properly.

On the other hand it has to be seen that most of the aims pursued by companies when repurchasing their own shares can be achieved through other methods. Some of the reasons, e.g. to use it as a self-investment or to increase the EPS, are even just illusory. One of the few reasons which may be valid is the use of repurchases to distribute surplus cash resources to shareholders. Thus there is simply no necessity to relax those rules.

Both legislative proposals from the Commission of the European Community and from the German government seem to share this view. In the proposed *Societas Europaea* the provisions concerning the acquisition of own shares are somewhat more stringent than those of the 2nd Directive[160]. Furthermore, the proposed Directive on Takeovers includes a Provision to limit the ability of target companies to repurchase their shares during a takover bid without prior shareholder approval[161]. And a change in the German provisions concerning the repurchase of own shares was only done in respect to banks dealing with their own shares. However, it does not contain any relaxation of these strict rules but is only seeking to clarify the law in this area[162].

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4 Source: L. Lowenstein, Sense and Nonsense in Corporate Finance (Reading 1991) p. 146; more recently see 'Transamerica in share buy-back' F.T. May 10, 1994; 'Coca Cola to buy back shares' F.T. July 21, 1992; for extensive surveys see C.J. Loomis, 'Beating the Market by Buying Back Stock Fortune April 29, 1985, 42; M.R. Richards, D.R. Fraser & J.C. Groth, 'Why Firms Repurchase Common Stock' [Oct.-Nov.-Dec.1982] Business 33; J.W. Wansley & E. Fayez, 'Stock Repurchases and Security Holder Return: A Case Study of Teledyne' (1986) 9 J.Fin.Res. 179.

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7 *Grady's* Case (1863) 1 De GJ & Sm 488; Ex Parte *Bennett (1854) 18* Beav 339; *Re The Royal Bank of Australia* (1850) 4 De G & Sm 177.

8 Lawe's *Case (1852) 1* De GM & G *421; Stanhope's* Case (1850) *3* De Ge & Sm 198; *Morgan's Case* (1849) 1 Mac & *G 225.*

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10 *Trevor v. Whitworth* (1887) *12* App Cas 409.

11 E. Magner, 'The Power of a Company to Purchase its Own Shares: A Comparative Approach' [1984] C.&.S.L. J. 79 at 80; these rules had been extended to most Commonwealth jurisdictions, see N.J. Leblovic, 'Stock Purchase and Redemption Legislation in Ontario' (1968) 26 U.Toronto Fac.L.Rev. 59 at 60; for a positive reception in the US see H.W. Ballantine, 'Questions of Policy in Drafting a Modern Corporation Law' (1931) 19 Cal.L. Rev. 465 at 480; G. Glenn, 'Treasury Stock' (1924) 15 Va.L.Rev. 625 at 642; contra: C.E. Cassidy, 'Right to Purchase Own Stock' (1924/25) 10 Cornell L.Q. 371 at 374; J. Levy, 'Purchase by an English Company of its Own Stock' (1930/31) 79 U.Pa.L.Rev. 45 at 68; I.M. Wormser, 'The Power of a Corporation to Acquire its Own Stock' (1915) 24 Yale L.J. 177 at 179-180.

12 E.g. acquisition of shares in lieu of a debt, see Re *Denver Hotel* [1893] *1* Ch 498; as a gift or bequest, see *Kirby* v. *Wilkins* [1929] *2* Ch 444; Re *Castiglion's Will Trust* [1958] *1* All ER 480.

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14 Art. 19 of Council Directive 77/91/EEC of 13 December 1976 OJL 26 of 31 .01.1977, p. 1 [hereinafter 2nd Directive]; see F. Wooldridge, Company Law in The United Kingdom and the European Communities: Its Harmonization and Unification (London 1991) pp. 30-31; G. Morse 'The Second Directive: Raising and Maintenance of Capital' (1977) 2 E.L.Rev. 126 at 129-130; E. Werlauff, 'The Development of Community Company Law' (1992) 17 E.L.Rev. 207 at 212-214; the Directive has been amended by Council Directive 92/101/EEC of

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52 See J.R. Macey & F.S. McChesey, 'A Theoretical Analysis of Corporate Greenmail' (1985) 95 Yale L.J. 13; Note, 'Greenmail: Targeted Stock Repurchase and the Management-Entrenchment Hypotheses' (1985) 89 Harv.L.Rev. 1045; I. Udechuku & K.J. Smith, 'Greenmail: Approptiate Regulation' (1989) 7 C.&S.L.J. 313-336; for empirical studies see M. Bradley & L.M. Wakeman, 'The Wealth Effects of Targeted Share Repurchases' (1983) 11 J.Fin.Econ. 301; W.H. Mikkelson & R.S. Buback, 'Targeted Repurchases and Common Stock Return' (1991) 22 Rand J.Econ. 544; A. Schleifer & R. W. Vishny, 'Greenmail, White Knights, and Shareholders' Interest' (1986) 17 Rand J.Econ. 293.

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e.g. by H. Bierman & S. Smidt, Financial Management for Decision Making (New York 1986) p. 510: A Company has *D* dollar availiable for distribution either in the form of a cash dividend or share rpurchase. If *n* is the number of shares outstanding prior to the repurchase and the firm pays *p* dollar per share to repurchase the shares, the number of shares after the repurchase will be $(n - D/p)$ rather than *n* if a dividend is paid. Since *D* is going to be distributed in either case, the company's future earning stream is unaffected and consequent the EPS will be higher if a repurchase is done.

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91 M. Lutter, Kapital, Sicherung der Kapitalaufbringung und Kapitalerhaltung in den Aktien- und GmbH - Rechten der EWG (Karlsruhe 1964) p. 431; G. Hueck, Gesellschaftsrecht (München 1991) p. 256; K. Schmidt, Gesellschaftsrecht (1991) p. 748; E.H. Warren, 'Safeguarding the Creditors of Corporations' (1923) 36 Harv.L.Rev. 509 at 542; cf. RGZ 77, 71 at 73; under German law this follows *argumentum e contrario* from § 57(1)(2) AktG.

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Repurchased Shares Under Texas Business Corporation Act' (1972) 26 Sw.L.J. 725 at 728.

93 s.160(1)(a) applied by s.162(2) CA 1985.

94 s.160(1)(a) applied by s.162(2) CA 1985, s.170(1) CA 1985.

95 s.170(4) CA 1985.

96 s.160(1)(b) and (2) applied by s.162(2) CA 1985.

97 s.159(3) applied by s.162(2) CA 1985.

98 s.143(2) CA 1985.

99 Note also s.168 CA 1985 (payments apart from repurchase price) and s.178 CA 1985 (effect of company's failure to repurchase).

100 § 71(1) AktG.

101 § 71(1)(1) AktG.

102 § 71(1)(2) AktG.

103 § 71(1)(3) AktG; there are four more exceptions: § 71(1)(4) AktG (if acquisition is gratis or if a bank executes a purchase order); § 71(1)(5) AktG (universal succession); § 71(1)(6) AktG (for the purpose of redeeming shares in capital reduction) and § 71(1)(7) (banks dealing in their own shares).

104 § 71(2)(1) AktG.

105 Under § 272(4) Handelsgesetzbuch of 10 May 1897.

106 § 71(2)(2) AktG; for a critique see U. Hüffer, 'Harmonisierung des aktienrechtlichen Kapitalschutzes' (1979) 21 NJW 1063 at 1069.

107 LG Göttingen (1993) 38 AG 46 et seq.

108 § 71(2)(3) AktG.

109 § 405(1)(4) AktG.

110 § 93(3)(3) AktG.

111 § 93(3)(3) applied by § 116 AktG.

112 I. Weinbaum, 'The Dilution of Shareholders' Interests' (1984) 5 CoLaw 3 at 8.

113 C.L. Israels, 'Coporate Purchase of its Own Shares - Are There New Overtones' (1964/65) 50 Cornell L.Q. 620.

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115 s.162(1) CA 1985; art. 35 of Table A of CA 1985 is a typical provision.

116 ss.164(6), 166(7), 169(1), 169(4) CA 1985.

117 s.163 CA 1985; for details see S. Barc & N. Bowen, Tolley's Company Law (London 13th edn. 1993) P6012-P6018.

118 s.166 CA 1985; G. Morse, Company Law (London 14th edn. 1991) p. 212 and Palmer's Company Law, supra n. 59, 6.414 advocate a special resolution.

119 Listed companies have to observe ch. 15 of Yellow Book and the requests of the Investment Committee of the Association of British Insurers which impose in some parts more stringent requirements than the CA 1985 itself, see G. Stedman, Takeovers (London 1993) 2.3.5.1; Tolley's Company Law, supra n. 119, P6019-P6027.

120 ss.164, 165 CA 1985.

121 s.164(5) CA 1985.

122 para. 15.7 of Yellow Book.

123 Detailed R. Hollington, Minority Shareholders' Rights (London 1990) ch. 2-6.

124 Principle of equal treatment ('*Gleichbehandlungsgrundsatz*') under § 53a AktG.

125 M. Lutter, 'Die entgeltliche Ablösung von Anfechtungsrechten' (1978) 7 ZGR 348 at 356-361; cf. K.-P. Martens, 'Die Vergleichs- und Abfindungsbefugnis des Vorstandes gegenüber opponierenden Aktionären' (1988) 33 AG 118 at 120 et seq.

126 Bungeroth & Hefermehl, supra n. 66, § 71 n. 125; Lutter, supra n. 20, § 71 n. 9.

127 §§ 71(3)(1), 160(1)(2) AktG; cf. BGH (1987) 41 WM 1965 at 1069-1070; OLG Frankfurt (1986) 31 AG 233 at 234; LG Frankfurt (1984) 29 AG 296 at 298 et seq.

128 BGH (1988) 41 DB 593 et seq.; G. Wiesner, in: M. Hoffmann-Becking (ed.), Münchener Handbuch des Gesellschaftsrechts, Band 4 (München 1988) p. 117.

129 OLG Oldenburg (1994) 47 DB 929 at 930.

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131 Huber, supra n. 76, p. 138.

132 L.P. Friedman, 'Defensive Stock Repurchase Programs: Tender Offers in Need of Regulation' (1985/86) 38 Stan.L.Rev. 535 at 537; Note, 'Buying Out Insurgent Shareholders With Corporate Funds' (1960/61) 70 Yale L.J. 308; Note, 'Targeted Stock Repurchases and the Management Entrenchment Hypothesis' (1985) 89 Harv.L.Rev. 1045 at 1054.

133 K.J. Hopt, 'Aktionärskreis und Vorstandsneutralität' (1993) 22 ZGR 534 at 563-564; M.L. Zilber, 'Corporate Tender Offers for Their Own Stock: Some Legal and Financial Considerations' (1964) 33 U.Cin.L.Rev. 315 at 328; for empirical studies see L.Y. Dann & H. DeAngelo, 'Standstill Agreements, Privately Negotiated Stock Repurchases, and the Market for Corporate Control' (1983) 11 J.Fin.Econ. 275; A. Klein & J. Rosenfeld, 'Targeted Share Repurchases and Top Management Changes' (1988) 20 J.Fin.Econ. 493.

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135 See, e.g., *Punt v. Symons* [1903] 2 Ch 506; *Re Smith and Fawcett Ltd* [1942] 1 All ER 542; *Hogg v. Cramphorn Ltd.* [1967] Ch 254; cf. R.R. Pennington, Directors' Personal Liability (London 1987) p. 33 et seq.

136 Jones & Bellringer, supra n. 91, p. 59; see sch. 7, part II of CA 1985 which requires a director's report on the repurchase.

137 A.J. Boyle, Directors' Fiduciary Duties: The Continuing Problem of Effective Enforcement (Deventer 1988).

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139 § 76(1) AktG; cf. Bungeroth & Hefermehl, supra n. 66, § 71 n. 124.

140 § 71b AktG.

141 § 71(3)(2) AktG.

142 paras. 9.10(a), 15.1, 15.8 and 15.9 of Yellow Book.

143 s.47 Financial Services Act 1986 (misleading statements and practices).

144 s.160(4) CA 1985 applied by s.162(2) CA 1985.

145 s.167(1) CA 1985.

146 § 71(1)(1) AktG.

147 BGH NJW (1994) 47 NJW 1410 at 1411.

148 But see OLG Frankfurt (1992) 37 AG 194 at 196.

149 Raiser, supra n. 70, p. 220; Hüffer, supra n. 63, § 71 n. 9; Bungeroth & Hefermehl, supra n. 66, § 71 n. 52; § 15 Gesetz über den Wertpapierhandel und zur Änderung börsenrechtlicher und wertpapierrechtlicher Vorschriften from 26 July 1994 [hereinafter WpHG] would also have to be observed.

150 § 71c AktG.

151 For an emprical study see J.M. Netter & M.L. Mitchell, 'Stock Repurchase Announcements and Insider Transactions After the October 1987 Market Crash' (1989) 18 Fin.Mgt. 84.

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159 T. Heinsius, 'Die Ausführung einer Verkaufskommission in eigenen Aktien durch ein Kreditinstitut und das Verbot des Erwerbs eigener Aktien nach § 71 AktG' 33 (1988) AG 253 at 258.

160 Art. 49 of Proposal for a Council Regulation on the Statute for a European Company COM(89) 268 final - SYN 218; see J. Murray, 'New Concepts in Corporate Law', in: Corporate Law, The European Dimension (London 1991) pp. 47-48; K.-P. Martens, 'Kapital und Kapitalschutz in der SE', in: M. Lutter (ed.), Die europäische Aktiengesellschaft (Köln 2nd edn. 1978) p. 115; note that the original draft of the 2nd Directive contained an absolute prohibition on the repurchase of shares, cf. E. Wymeersch, 'Company Law', in: K. J. Hopt & E. Wymeersch, European Company and Financial Law (Berlin 1991) p. 58.

161 Art. 8(1)(c) of Proposal for a Thirteenth Council Directive on Company Law COM(88) 823 final - SYN 186; see P. Bently, Public Takeover Bids, in: Corporate Law, The European Dimension (London 1991), pp. 145-146; W. Pfister, Europäisches Gesellschaftsrecht (1993) p. 27.

162 A new § 71(1)(7) AktG was inserted by the 2nd Finanzmarktförderungsgesetz from 26. July 1994 (BGBl. I, 1749); see Nirk, supra note 70, n. 415 et seq.