

Guidance

Shares Purchase Out of Capital (“Off Market Purchase”)

There are two ways in which a company can buy its own shares:

- Purchase of shares
- Redemption of shares.

Generally, a company may decide to purchase its own shares in order to prevent a shareholder from being locked into the company with no way to sell his shares.

Because of the importance of share capital, there are very strict rules that companies must follow when purchasing or redeeming shares.

This document provides guidance on the purchase; for redemption of redeemable shares please see “Redemption of Shares – Guidance Notes” and “Redemption of Shares – Guidance Notes”.

A purchase of shares by a company purchases shares in itself from an existing shareholder. Shares purchased are not redeemable shares.

A company

- out of capital
- out of capital
- (in lieu of) cash; or
- out of capital

This document provides guidance on share purchase out of capital. For purchase of own shares out of capital, please see “Own Share Purchase – Guidance Notes” and “Own Share Issue/Cash – Guidance Notes”.

It should be noted that a company must follow for the first three methods which are less strict, and the last method must be followed for the last.

Please note that public companies can purchase their own shares or redeem redeemable shares, but private companies can reduce their capital in order to do so.

This document provides guidance on procedures that must be followed by private limited companies to purchase shares, the so called “off market purchase”, and (market purchase).

In order for a company to purchase shares in itself out of capital a number of conditions must be met.

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Purchase of own shares out of capital

must not be restricted or prohibited by the Articles
Articles introduced by the Companies Act 2006

by the company must be fully paid; and
of its own shares the company must continue to
non-redeemable shares.

shares out of capital

ts (or the proceeds of a new issue of shares made
available to fund the purchase of own shares, the
issue must first be used to fund the buy back before
of capital required is the “permissible capital
before proceeding.

th The Companies Act 2006 (Amendment of Part
into force on 6th April 2015, a private company
make small buy backs out of capital in a financial
permissible capital payment provisions in Part 18
2006. This means that purchases of own shares out
of capital are *permissible* annual limits as own shares purchased
must not exceed the lower of £15,000 or 5% of the company’s
share capital. This new section 692(1ZA) CA 2006. This new section
states that the company’s share capital will be the nominal
share capital as at the beginning of the financial year.

at any date within 3 months up to the date of the
statement are required for the Directors to determine
these need not be audited but must be reliable for

the following steps must be taken:

Purchase of own shares.

for running the business of the company, so the
must initially be taken by the board. The document
– Board Resolutions” contains the necessary

of Capital – Board Resolution (ESS – Multiple
for multiple buybacks for the purposes of an

of Capital – Board Resolutions (ESS version of
to use capital where the buyback is for the
purpose.

Please note that a director must not be involved in a decision dependent on the purchase of shares from a director of the company, that

and may not be permitted to vote on the board resolution. The company's Articles of Association.

STEP 2 – Contract to Purchase Own shares

- The contract to purchase own shares must be made available to the members.

See the document "Contract to Purchase Own Shares" for the "Purchase out of Capital – Contract to Purchase". For a contract not connected with an employees' share scheme, see "Contract to Purchase (ESS)".

Subject to the contract to purchase shares must be approved by either (i) an ordinary resolution or (ii) entered into before the contract provides that no shares can be purchased unless approved by ordinary resolution.

The exception to the above rule is that the 2013 shareholders can, by ordinary resolution, approve the purchase of shares, rather than authorising each individual shareholder to purchase shares for the purposes of an employees' share scheme.

The shares purchased for the purposes of the employees' share scheme may be paid for in instalments.

If the "Own Shares" contract is being used, the contract to purchase must be made available to members. If there is only a verbal contract, the main contract terms must be made available to members.

If the ordinary resolution is proposed as a written resolution then a copy of the contract to purchase must be sent at or before the time that the resolution is proposed to members.

If the ordinary resolution is passed at a meeting then a copy of the contract to purchase must be available for inspection for at least 15 days before the meeting and at the meeting itself.

STEP 3A – Directors' Statement and Auditor's Report

- The directors must make a statement in the company's financial statements by an auditor's report.
- The company must ensure that the shares are bought back for the purposes of the company. In this case, Step 3B should be taken.

The Directors must make a statement of the solvency of the company. The document "Contract to Purchase Own Shares – Directors' Statement" contains the required wording. A copy of the statement made by each of the directors must be made available to members.

SAMPLE

- the amount of the capital payment; and
- a statement of the full enquiry into the affairs and prospects of the company and the opinion:

(a) a statement of opinion immediately following the date on which the payment is proposed to be made, that there will be no ground on which the company could then be found unable to pay its debts;

(b) a statement of opinion for the year immediately following that date, that the company will be able to pay its debts as they fall due;

(c) a statement of opinion as to the management of the Company's affairs for that year; and

(d) a statement of opinion as to the financial resources that will in their view be available to the Company during that year,

and a statement of opinion as to whether the company is able to continue to carry on business as a going concern (being able to pay its debts as they fall due).

An auditor's report must be made available to the Directors' Statement and addressed to the directors stating the auditor's opinion on the company's state of affairs,

- the amount of the capital payment; and
- the statement of the full enquiry into the affairs and prospects of the company and the opinion:
- he is of opinion that the opinion expressed by the directors is unreasonable in all the circumstances.

If the Directors' Statement is adopted by the directors without having reasonable grounds for the opinion, then every director who is in default will have committed an offence and, may face imprisonment of up to two years or a fine or both. If the company is a public company, it is advisable to seek expert advice.

A copy of the Directors' Statement and the auditor's report must be made available to the members.

If the special resolution is adopted as a written resolution then the copy of the Directors' Statement and the auditor's report must be sent at or before the time that the resolution is adopted to the members. The notes should also emphasise that the resolution must be adopted within seven days (see Step 4 below) or it will not be valid.

If the special resolution is adopted at a meeting then the copy of the Directors' Statement and the auditor's report must be available for inspection at the meeting.

STEP 3B – For employees' share scheme purchases only)

- When the company is making a payment out of Capital for the purposes of an employees' share scheme, the requirements are less stringent. Instead of a Directors' Solvency Statement, the directors need only make a Solvency Statement.

The document is known as a "Payment Out of Capital – Solvency Statement for ESS Purchase" or simply "Solvency Statement". A Solvency Statement is a statement that each of the directors must make.

- has regard to the company's situation at the date of the statement and the state of affairs of the company at that time, and the soundness of the company's financial position, and the company's ability to pay (or otherwise discharge) its debts; and
- has regard to the company's ability to pay (or otherwise discharge) all due during the year immediately following that date.

If the Solvency Statement is made by the directors without having reasonable grounds for the opinion that the company is able to pay (or otherwise discharge) its debts, then every director who is in default will have committed an offence and, may face imprisonment of up to two years or a fine or both. Therefore, in such circumstances, it is advisable to seek expert advice.

A copy of the Solvency Statement must be made available to members.

If the special resolution is passed as a written resolution then the copy of the Solvency Statement must be made available to members at or before the time that the written resolution is passed. The written resolution should also emphasise that the written resolution must be passed in accordance with the requirements of section 4 (below) or it will not be valid).

If the special resolution is passed at a meeting then the copy of the Solvency Statement must be made available to members at the meeting.

STEP 4 – Shareholders' Approval

- The purchase of the company's own shares must be approved by the shareholders by a special resolution.
- The purchase of the company's own shares must also be approved by the shareholders. A special resolution is required for this.
- The purchase of the company's own shares for the purposes of an employees' share scheme is slightly different. If the company is making a payment out of capital is slightly different. If the company is making a payment out of capital for the purposes of an employees' share scheme, the requirements are less stringent.

The contract for the purchase of the company's own shares must be approved by the shareholders of the company by a special resolution.

A special resolution is required to approve the use of capital as follows:

- if the payment out of capital is not connected with an employees' share scheme, the special resolution must be passed within seven days of the Directors' Solvency Statement.
- If the payment out of capital is for the purposes of an employees' share scheme, a special resolution must be passed within 15 days of the Solvency Statement.

S A M P L E

The approval of written resolutions (private companies only) or by written resolutions at a general meeting.

In either case, the resolutions must be passed by shareholders who represent not less than 75% of the total voting rights of those shareholders who, being so entitled, are present at the meeting on a show of hands or would be so entitled if the written resolutions are circulated.

If written resolutions are passed by a member holding shares which are to be purchased, the member will not receive a copy of the written resolutions.

If a meeting is held to pass written resolutions, the meeting will not be effective if any member holding shares which are to be purchased does not exercise the voting rights of those shares and the company does so.

See the document "Own Share Purchase out of Capital – Written Resolutions" which can be used by the company to pass the resolutions or "Own Share Purchase out of Capital – Minutes" which can be used to record minutes of a meeting of shareholders.

In relation to the use of capital for the purposes of an employees' share scheme, see the document "Own Share Purchase out of Capital – Written Resolutions (ESS version)" and "Own Share Purchase out of Capital – Minutes (ESS version)". These documents contain resolutions approving the use of capital for the purposes of an employees' share scheme.

The documents "Own Share Purchase out of Capital – Written Resolutions" and "Own Share Purchase out of Capital – Minutes" provide that both the ordinary resolution and the special resolution must be passed by the shareholders for approval simultaneously. Each resolution must be passed by a majority of 75% but the ordinary resolution to approve the purchase of shares could be made first to save the company the expense of preparing a Statement of Solvency Statement only for the contract to be rejected.

For an ordinary resolution to approve multiple buybacks of shares for the purposes of an employees' share scheme, see the documents "Own Share Purchase out of Capital – Written Resolutions (Multiple Buybacks)" or "Own Share Purchase out of Capital – Minutes (Multiple Buybacks)".

STEP 5 – Register the company's share capital with the Registrar for shareholder approval

- The company must send a copy of the resolution to the Registrar for registration a copy of the resolution and certain documents for the purposes of an employees' share scheme. (This is required in the case of an ordinary resolution to approve a single buyback contract.)
- The company must send a copy of the resolution and certain documents to the Registrar for registration a copy of the resolution and certain documents for the purposes of an employees' share scheme.
- The company must publish notices in the Gazette and a national newspaper for the purposes of an employee's share scheme.

SAMPLE

For a covering letter to Companies House together with an ordinary resolution and a copy of the proposed scheme, please see Form SH19 – Own Share Purchase out of Capital – Letter to Companies House (Multiple Class Shares)

A letter to be sent to Companies House together with a copy of a special resolution (and the documents in support) can be found at “Own Share Purchase out of Capital – 1st Letter to Companies House (Multiple Class Shares)”

Within the year of the passing of a special resolution regarding the use of capital (other than for the purposes of an employees’ share scheme), the company must publish the proposed payment in the Gazette and must either publish the notice in a national newspaper or give written notice to the company’s creditors. The wording for the notice can be found in Form SH19 – Public Notice”.

Copies of the special resolution and auditor’s report must be sent to the Registrar of Companies for the purposes of publication of the above notices. The “1st Letter to Companies House (Multiple Class Shares)”

In the case of a company proposing to purchase shares out of capital for the purposes of an employees’ share scheme, a copy of the Statement of Capital (see “Form SH19 – Statement of Capital”) must be delivered to the Registrar. The company must also deliver to the Registrar a copy of the resolution on which the resolution was passed, and was made in accordance with the relevant sections of the Companies Act. See “Statement of Capital – 1st Letter to Companies House (ESS)”

The Statement of Capital must state with respect to the company’s shares:

- the total number of shares;
- the aggregate nominal value of shares;
- for each class of shares:

- (a) the number of the rights attached to the shares;
- (b) the nominal value of shares of that class;
- (c) the aggregate nominal value of shares of that class; and

- the amount of any unpaid share (whether on account of the share or by way of premium).

The Registrar will not register the resolution, Solvency Statement and Statement of Capital on behalf of the company until those documents are registered.

Note that the Companies (Amendment of Part 18) Regulations 2015 have removed the requirement for a company to provide a statement of capital in relation to a buy back under an employees’ share scheme where the company is already replicating one already delivered under section 720B(5). The “1st Letter to Companies House (Multiple Class Shares)”

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(employees' share scheme).

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urchase of own shares out of capital

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15 Regulations amend and clarify the position so
no earlier than five weeks and no later than seven
on approving the payment out of capital is passed.

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A copy of the company's own shares must be kept available for inspection at the company's registered office for 5 years from the date of purchase of own shares.

Copies of the company's financial statements and auditor's report must be available for inspection for 5 weeks from the date of the special resolution regarding the use of capital. (There is no such requirement in relation to the Solvency Statement produced in connection with the purchase of own shares for the purposes of an employees' share scheme.)

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If the permitted amount is less than the nominal amount of the shares purchased, the balance must be transferred to the company's capital redemption reserve.

If the permitted amount is greater than the nominal amount of the shares purchased, the balance may be used for any capital redemption reserve, share premium account or for any other purpose of the company, and (ii) any amount representing unrealised gains or losses on revaluation of the company's assets may be reduced by the balance of the capital redemption reserve if the total payment exceeds the nominal amount of the shares.

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In either case, the company must make a payment out of capital the aggregate of that payment and those proceeds.

Please note that the procedures involved in a purchase of own shares are complex and must be followed carefully. Failure to follow the statutory procedures could result in the company being liable to the shareholders. The company and any shareholders considering such a purchase should seek specialist legal and tax advice.

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