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Using Treasury "Repurchase" Shares to Stabilize Stock Markets

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ABSTRACT

This paper aims to examine one of the most important issues in the international corporate laws, which is the issue of share repurchases known as treasury shares. This paper investigated corporate laws, stock exchange regulations, research literatures and stock trading volume for repurchase activities. Covering a sample of thirty-five countries developed and emerging markets.

The study found that there is an increasing movement in the world stock market towards adopting or deregulating the share repurchase activities, More than half of the selected sample witnessed a change in the related laws (especially corporate laws) of share repurchases during the period 1995 to 2000. Moreover, there is a toleration to use the treasury share in enhancing the stock market during stock crises and extraordinary market price volatility. Based on upon findings, a modal has been suggested and articulated to be considered as a stabilization instrument for stock marketing.

JEL: *G14; G18; G35*

Keywords: *Share repurchasing; Corporate laws; Stock market stability*

I. INTRODUCTION

The share repurchases is considered as one of the most significant issues in the corporate laws, due to the significant differences that exist in the world corporate laws. Major changes have been taking place concerning the share repurchases in the world stock market during last decade. First: The size of repurchases trading volume as an alternative to dividends has increased significantly. Second: many countries introduced the concept of share repurchases by corporate firms in the last five years. Third: many countries that already legitimized the share repurchasing activities are deregulating, and relaxing conditions and rules to encourage corporations using repurchases as an alternative to dividends, as well as, to serve other purposes including improving of stock prices. Fourth: Other countries moving from share repurchases activities towards holding the repurchased shares in treasury. Fifth: some countries are introducing more liberal rules applying to treasury shares to enhance the stability of stock markets.

The main purpose of this study is to investigate the issue of share repurchases in the world stock market, in order to suggest a new model of using a treasury stock as a stabilizing instrument in the stock market. In various countries, corporations might repurchase part of their own common stocks, which are fully paid, legally issued, in order to be cancelled or to be held for reselling. While considered as illegal by many other countries, the general known methods of share repurchasing are: repurchase from open market, Dutch auction, fixed –price tender offer repurchases, repurchase from off market and equal access repurchases. Repurchasing of its own shares by a firm is known as share repurchases or shares buybacks. If the repurchased shares are held for limited or unlimited time for future uses or reselling, they are considered as treasury shares. Generally, corporations may repurchase their own shares for one or more of the following reasons: to use for pension and compensation plans for employees, to invest some of the surplus cash, to be used as a substitute for dividends which may have a positive effect on the stock market prices of the company, to establish a market and create additional demand for the company's shares, to adjust owners' equity and capital structure, to take over defensive steps by reducing the public floating shares, to gain tax advantages, to increase earning per share by reducing the outstanding shares of the firm, and to meet merger needs.

This paper suggests another purpose for a corporation to repurchase and hold its own shares. The suggestion is to use the repurchase activity as a new financial instrument, in order to sustain the stock market price in case of market crisis produced by adverse information and overreaction. The high volatile stock prices, which may lead to stock market crises, have continued to occur in both developed and emerging stock markets in the last fifteen years. Such as the stock market crisis in 1987, 1989 and 1997. This phenomenon is still considered as a major issue in the global stock market, the performance of the stock market was unstable in the last three years. For example, the performance of all world countries stock market index decreased by 25.3% during 1998, while it showed a positive growth in 1999 of about 66.4%, and it decreased again and witnessed a negative record of 9% in the first half of 2000 (IMF, 2000).

Table 1
The selected sample of the States

Stock Market	Region	Countries	Stock traded value In $ M (1999)*
Developed	North America	Canada	364625
		USA	18574100
		Bermuda	70
		Cayman Islands	160
	Asia	Japan	1849228
		Hong Kong	244886
		Singapore	97985
	Europe	Italy	536475
		France	769951
		Netherlands	941804
		UK	1377859
		Germany	1357841
		Sweden	238237
		Norway	54135
		Ireland	50531
		Spain	744315
		Finland	111585
		Belgium	59129
		Denmark	61297
		Switzerland	538955
	Oceanic	Australia	105999
		New Zealand	11980
Emerging	Asia	Jordan	548
		Saudi Arabia	14816
		Oman	529
		Lebanon	91
		Taiwan	910016
		Chine	377099
		Malaysia	48512
		Korea	733591
		India	122247
	Europe	Greece	188722
		Poland	11149
	Africa	Morocco	2530
		South Africa	72917

Source: IFC factbook, 2000

The mechanism, rational, conditions and methods of share repurchases are different from one country to another, based on different corporate laws, stock exchange stock laws, tax laws, and accounting practices applying to repurchases activities. Accordingly, the study will examine related laws, regulations of corporate and stock exchanges, tax, and accounting practices for a sample of thirty five states. The selected sample represents both developed and emerging markets. In addition, rules and regulations of regional institutions including European Council and International Accounting Standard Committee related to the share repurchases are examined. The investigation covers consulting papers issued by related bodies in various countries related to changing of share repurchase activities' regulations. Table 1 represents the selected sample of the countries for the study, the regions, and the stock traded value in 1999. The sample form about 98% of the total trading value of the world stock market as expressed by trading volume, and include the top 15 countries in the world stock market (IFC, 2000). It includes 22 developed countries, and 13 emerging countries. The developed countries cover of North America, Europe, Asia, and Oceanic (Australia and New Zealand). The emerging countries regions cover Asia, Africa, and Europe.

The remainder of this research is organized as follows: Section II presents a review of the related literature. Section III provides a review of trading in stock repurchases in the selected sample. Section IV is devoted to findings of the study. Section five represents a suggested model, to use the treasury stock as an instrument in stabilizing the stock market. Finally, last section is devoted to present summary and concluding remarks for the study.

II. LITERATURE REVIEW

The majority of the share repurchase literature is aimed to measure the market response to repurchases announcements, other purposes are examined including tax advantages, takeover defense, and corporate payout policies. This section will be divided into two parts: the first part is related to US, while the second part is devoted to the related research in other countries.

A. Research in USA Share Repurchases

The majority of researches in USA used date of repurchases announcements between 1980 and 1995, in order to compare between dividends and repurchases, or to measure the impact of different methods of share repurchases announcements on the stock prices. Generally, the literature about share repurchases related to US data may be classified into four groups:

The first group is related to measure the market response to open market share repurchase method. Findings of these researches are mixed, while the majority reported positive response. The open market repurchase is the most significant method of share repurchasing in US markets as well as other countries. Various studies examined the market response to this method. Badrinath (2000) examined 200 US firms that completed open market repurchase and concluded that dividend ratios were higher after buybacks activities. Ikenberry et. al., (1995) examined the long-run firm performance following open market share repurchase announcement and found that the average abnormal return for four year return after announcement was 12%. Barth and Kasznik

(1999) reported that firms with more intangible assets associated with research and development are more likely to announce share repurchases having more positive repurchase announcement returns, and thus conveying good information to the market. McNally (1999) found that market valuation increases with the amount of share repurchasing using open market method. Vafeas and Joy (1995) found evidence that abnormal stock market returns on announcements of open market share repurchases were related to the reduction of agency cost of free cash flows.

The second group examined the market response to other share repurchases methods. For example: Persons (1997) examined the repurchasing share method of tender offer and concluded that a repurchase tender offer is used to signal large information asymmetries, and thus causes larger stock price increase than dividends. DÆmello and Sharoff (2000) examined the repurchase tender offers in case of share undervaluation and found that managers have private information about their firm's favorable future prospects. Nohel and Tarhan (1998) examined tender offer share repurchases through announcement returns, and concluded that operating performance following repurchases improves only in low-growth firms.

Other studies compared between methods of share repurchases and concluded mixed findings. For example: McNally, (1998) compared between fixed price and Dutch auctions methods of share repurchases and concluded that non-tendering shareholders gain the same under both methods, while tendering do better using fixed-price auctions. Lie and McConnell (1998) examined whether earnings improvement following fixed-price self-tender offers is greater than the Dutch auction self-tender offers, and concluded that there was evidence of earnings improvement following both types of self-tender offers. Comment, and Jarrell (1991) suggested that firms announce open market repurchase programs when their shares price is more likely to be undervalued, and found that tender offer method is related to the largest volume of shares and has the largest price reaction. Stephens, and Weisbach (1998) compared the Dutch auction, fixed price tender offer, and open market repurchase program, and found that open market repurchase program is more flexible and may use timing with undervaluation of shares' prices. Best et. al,. (1998) found that share repurchases using fixed price offers signal positive information in short and long term earning revisions, while Dutch auctions have only short term effects.

The third group of related studies compared between dividends and repurchases alternatives and corporate payout policies in general. Feen and Liang, (2000) examined corporate payout policy and suggested that growth in stock options may help to explain the rise in repurchases at the expense of dividends. Guay and Harford (2000) found that repurchasing of shares as cash payout policy allowing managers to distribute transient cash flows with commitment to frequent dividends. Jagannathan et al., (2000) found that dividends are paid by firms with higher permanent operating cash flows following good performance, while repurchasing policy is used by firms with temporary non-operating cash flows following poor market performance. Ofer and Thaker (1987) reported that the market reacts favorably for a repurchase share program than for dividends announcements, and found that when a firm pays dividends it never uses external funds. Vermaelen (1981) reported that a share repurchase announcement creates a higher positive response than a dividend.

The fourth group of studies is related to other issues of share repurchases such as accounting disclosures, defensive takeover, employee stock option, and tax considerations. For example: Gelb (2000) and (1999) examined corporate repurchase and accounting disclosures, and concluded that firms use share buybacks to avoid releasing information, which may be costly. Weisbenner (2000) examined how the growth of stock option programs affects corporate payout policy and reported that option grants in general are associated with increased share repurchases. Liang and Sharpe (1999) estimated the effects of share repurchases and employee stock option exercises and concluded that, share repurchases have reduced outstanding shares by 2% annually; while holding employee stock options formed only 1% of these shares. Bagwell (1992) considered takeover defense as a reasons for shares repurchasing and found that the individual bid is larger for firms that have been targeted of takeover activity.

B. Research in Other States

Research on share repurchases outside the USA is still limited, due to the fact that there is not enough data to examine the different aspects of share repurchase activities, and to the short experience. However, there are few studies in some countries like Canada, UK, Australia, Norway, Germany, Korea, and Norway. The majority of these researches examine market response to repurchases announcements. The following section provides a summary of researches in share repurchase experiences in other countries as presented in Table 2.

Table 2
Summary of share repurchasing research in other countries

State	Topics	Authors
Canada	Market response to share repurchase	Li and McNally, 2000
		Ikenberry et la., 2000
Australia	Market response to share repurchases	Otchere and Roess, 2000
		Lamba and Ramsay, 2000
		Harris and Ramsay, 1995
Norway	Market response to share repurchases	Skjeltorp, 2000
Germany	Market response to share repurchases	Pellens, 2000
South Korea	Marker response to share repurchases	CGRK Report, 2000
UK	Market response to share repurchase	Rees, 1996
	Repurchases and tax regulations	Rau and Vermaelen, 2000
	A case study of Reuters' repurchases	Stonham, 1995

Canada: Li and McNally (2000) found that Canadian firms use the share repurchase as a mean for reducing financial slack and the agency costs. While Ikenberry et. al., (2000) reported that firms with high book value to market value ratios announced a purchase program that tends to experience higher abnormal return compared to low book value firms, and concluded that stock prices that perceived undervaluation by managers were an important consideration to buybacks their own shares.

Korea: A LG Securities Report (CGRK Report, 2000) indicated that about 75 firms which announced to buyback their own shares witnessed arise by 19.1% in the first 10 days of public announcements compared to 10% in the Korean stock market price index, small and medium capital firms showed higher rises than large capital firms did as reported by the economy reports.

UK: Rau and Vermaelen (2000) examined the share buybacks activity in UK between 1985 and 1998, including a sample of 246 UK firms. He concluded that the UK firms' activities in repurchasing their own shares are influenced by the tax consequences. Rees (1996) reported less positive abnormal performance as response to buyback announcements. Stonham (1995) examined a case of Reuters' Share repurchase activity occurred in 1993 and concluded that Reuters' share took several jumps following the share repurchases as the market reacted to events.

Australia: Otchere and Ross (2000) used the Australian stock data and found that share buy- back announcements signal positive information about the values of both announcers and rivals. Harris and Ramsay (1995) found insignificant results due to limited sample and restricted regulations, which had been relaxed in 1995. Lamba and Ramsay (2000) indicated that the strict regulations on repurchasing for Australian firms up to 1995 made them less effective as a signal mechanism, and the market reactive was most positive to on market buybacks compared to other methods of repurchasing.

Norway: Skjeltorp (2000) examined the short-term market impact of the repurchase event during the short period since the Norway permitted repurchasing in 1999. He found that there was a 3.15% market reaction to the repurchase, and there was a positive relationship between the short-term market impact and the price-to-book value.

Germany: Pellens (2000) examined the share repurchase announcements of German firms, which has been legalized in Germany only since April 1998. Since then, about sixty corporations have received an authorization resolution from their shareholders' meeting which included in the sample. The study concluded that management used the announcement of a repurchase to signal information about the firm future prospects. Concerning methods of repurchasing, 51.4 % of the corporations in the sample have not yet decided about a repurchase method, while 37.8 % considering an open market repurchase, and 5.4% of the sample selected a Dutch auction tender offer.

III. TRADING VOLUME OF SHARE REPURCHASES

As indicated in the previous sections, just recently the majority of the countries in the World legalized the concept of share repurchases. The number of firms repurchasing their own shares is still limited in the entire world, with exception of USA, Canada and UK. The share repurchases activity was merely existed before 1980 outside the US stock market. It has increased significantly in the last five years in most of the selected countries. This section will present the repurchased shares value and the number of firms involving in repurchasing activities in the selected sample of the study. Summary of the number of share buybacks firms in 15 of the select sample is presented in Table 3.

USA represented the highest trading volume of repurchased shares. As a matter of fact the number of firms engaged in repurchase activities are three folds of the rest of the world. The number of firms engaged in share repurchases increased from115 firms in 1985, to 547 in 1994 and became 755 firms in 1996, with a value of $ 471 billion between 1985 and 1996, the annual value of repurchase trading increased from $15 billion in 1985 to 113 billion in 1996 (Jagannathan et al., 2000). The percentage of share repurchases volume compared to dividends increased from 20% in 1982, to 53% in 1994, to 130% in 1998 which was about $ 145 billion, however, the repurchase share is still limited to about 2% of the total volume of stock market for a sample of the largest 144 firms (Liang and Sharpe, 1999). This significant increasing in repurchases activities by US corporations is extended in other economic sectors, such as in the financial institutions. For example out of 47 banks with assets of more than $ 10 billions, 39 have announced repurchase programs within the last three years 1996-1999 (Hutchison, 2000).

Table 3

Number of firms repurchased its own shares in 15 of the selected sample

Country	Number	Period	Sources
United States	4743	1985-1996	Jagannathan et al. 2000
Canada	1060	1989-1997	Ikenberry, et al. 2000
UK	293	1985-1998	Rau & Vermelem 2000
Japan	285	1995-1998	OECD, 2000
Australia	132	1991-1999	Otchere & Ross, 2000
Korea	75	Up to 1999	Korean Economy Report, 2000
Norway	43	1999-1999	Skjeltop, 2000
Italy	42	1985-1998	Rau & Vermelem 2000
Netherlands	22	1985-1998	Rau & Vermelem 2000
Switzerland	29	1996-1999	Country Finance (2000)
Spain	21	1985-1998	Rau & Vermelem 2000
Malaysia	16	1997-1999	ROC, 1999
Greece	9	1985-1998	Rau & Vermelem 2000
Germany	7	1998-1999	Pellens, 2000
India	2 (46)	(Announced)	Kamal & Maitra, 1998

In UK, the number of firms engaged in repurchases activities were 293 firms between 1985 and 1998, with annual average of 31 firms (Rau & Vermelen, 2000). It is estimated that the repurchased shares value was £ 25 billion between October 1996 and 1999 (Perrin, 2000). In Canada, the number of firms engaged in share repurchases increased from 106 in 1989 to 129 in 1996 to 172 firms in 1997, with a total value of $35.6 billion (Ikenberry et la, 2000). In Switzerland, the number of firms engaged in repurchases activities increased from 2 in 1996 to 13 firms in 1999, with a value of SF 10.2 billion (Country Finance 2000).

In Malaysia, which permitted share repurchases activities only at September 1997, the number of firms received approval for repurchases were 171 firms up to February 1999. Of the total 16 companies have implemented the targeted repurchased shares (ROC, 1999). In Japan the number of firms implemented repurchases programs increased from 5 in 1995 to 78 in 1997 to 186 in 1998, while the number of companies announced to repurchase shares increased from 5 firms in 1995 to 1179 firms in 1998, (OECD, 2000). In Australia, the number of firms repurchased their own shares increased from 2 firms in 1991 to 8 firms in 1995, to 25 in 1996, to 35 firms in 1998. The total Austrian firms repurchased their own shares were 132 firms from 1991 to July 1999 (Otchere and Ross, 2000). In Norway, 20% of the 215 firms registered on Oslo Stock exchanges used the opportunity to repurchase their own shares during the first year (1999) of legalized repurchasing activities (Skjeltorp, 2000).

IV. FINDINGS OF THE STUDY

This section includes four parts; the first part indicates the recent changes in stock repurchasing issues, the second is related to practices concerning the repurchasing shares as existed in 2000. The third part is related to tax practices regarding repurchases activities in the selected sample, while the last part is related to accounting practices dealing with accounting aspects for share repurchases.

A. Legal Changes Aspects of Repurchasing Shares

Based on investigations of the related corporate laws, it may be concluded that about half of the selected sample witnessed a change in one or more of the related laws of share repurchases during the period 1995 to 2000, as been presented in Table 4 and Table 5. Some of those changes are related to introducing the concept of share repurchase for the first time, after being illegal, by amending corporate and other related laws. Those countries are Finland in 1997, Germany in 1998, India in 1999, Japan in 1995, Norway in 1999, Malaysia in 1997, Singapore in 1998, Denmark in 2000, Sweden in 2000, South Africa in 1999, Taiwan in 2000, and France in 1998. Other countries witnessed changes in share repurchase laws and regulations. For example New Zealand in 1999, Singapore in 1999, Netherlands in 2001, who changed tax laws to encourage share purchase activities. UK issued two consultation papers suggesting the amendment of share repurchases laws; the first one is related to allowing investment companies to repurchase their own shares using capital profits (DTI, May, 1999). The other document is related to financial assistance offered by a company for the acquisition of its own share (DTI, 1996).

Table 4
Changes in laws occurred in the selected countries regarding share repurchase between 1995 to 2000

Country	Effective Year	Major changes
Australia	1995	Deregulate the share buybacks including removing the limit of the 10%
Denmark	2000	New Law related to share repurchases applied since March, 2000
Finland	1997	Permitting companies to buyback their own shares
	1998	Change in tax regulation in favor of buybacks shares
Germany	1998	Permitting companies to buyback their own shares
	1998	Modify the Security Act (STA, 1998) related to disclosures of firms buy its own share
India	1999	Permitting companies to buyback their own shares
Japan	1995	Permitting listed companies to buyback their own shares
Netherlands	2001	Changes in Tax laws to encourage buybacks of shares
Norway	1999	Permitting listed companies to buybacks their own share
Malaysia	1997	Permitting a listed public company to buy its own shares or to give financial assistance to other persons to buyback its own shares.
Singapore	1998	Permitting companies to buybacks their own share
	1999	Approving revision of share buybacks by Singapore Monterey Authority
	2000	Issue tax treatment of buyback shares
New Zealand	1999	The buybacks of own shares law was amended
Sweden	2000	To allow listed companies to buybacks their own share
South Africa	1999	To allow listed companies to buybacks their own share by changing the companies Act of 1973
Taiwan	2000	To allow listed companies to buybacks their own share
United Kingdom	1999	A consultation paper regard that Investment companies to be allowed to repurchase their own shares using capital profits
	1996	A consultation paper regard to financial assistance by a company for the acquisition its own share

Sources: Compiled by the author based on the related companies Laws, Regulations of stock exchanges and other related laws and consultations papers for the above states.

Other significant changes in share repurchases were related to moving from corporate share repurchase to the concept of holding those shares in treasury for limited or unlimited periods as presented in Table 4. Malaysia and US permitted the holding the repurchased shares in Treasury. UK issued a consultative document in 1998 aimed at changing the current law that imposes cancellation of repurchased shares, in order to adopt the concept of holding them as treasury shares (DTI, 1998). In 1999, the department of UK Trade and Industry accepted recommendation of consultation document and decided to deregulate company law in respect of the holding shares in Treasury (DTI, December, 1999).

In Hong Kong a consultation paper was issued to consider permitting treasury shares. It stated five arguments in favor of legalizing treasury shares, including: better managing of the balance between debt and equity, providing flexibility in fund raising, better managing of employee share schemes, disposing shares in the relevant time, and permitting investment in a company's own shares (SFCHG, 1998).

Table 5

Major changes in selected countries adopting the concept of treasury share between 1995 to 2000

Country	Effective Year	Major changes
Hong Kong	1998	The Securities Commission of Hong Kong issued Consultation paper to introduce treasury shares
Japan	1999	Studying the idea of introducing the treasury stocks
Malaysia	1998	A company is given the choice to hold its own share in treasury shares
United Kingdom	1999	The department of trade and industry agreed on the consultation paper to deregulate the companies law to allow companies to hold repurchased share as treasury shares
United States	1999	Deregulate the Rule 10b-18, by changing the timing rules of buying shares to be hold as a treasury to improve liquidity during sever market downturns
	1998	Amendment of circuit breakers to avoid systemic breakdown when a severe one day market drop occurred (Rule 80B)

Sources: Compiled by the author based on (UK: DTI, 1999) (USA: SEC, 1998) (Japan: JFEO, 1998) (Hong Kong: SFCHG, 1998) (Malaysia: ROC, 1999).

US adopted in 1999 (SEC, 1999) an amendment to Rule 10b-18 (Rule) under the Securities Exchange Act of 1934 in order to improve liquidity during severe market downturns, by modifying timing condition during the trading session immediately following a market-wide trading suspension, while it continued to comply with the Rule 10b-18 conditions governing the manner, price and volume of market repurchases. In addition, it modified the market wide trading halts due to extraordinary market price volatility (SEC, 1998). In Japan the concept of treasury share is under investigation (JFEO, 1998).

To examine the corporate share repurchases practices of the total sample; these may be classified as presented in Table 6 into five groups as follows:

The first group: A corporate may not repurchase its own shares under no conditions. Reduction of capital should be conducted for all shareholders equally. There are countries in which corporate laws do not permit the firm to buy its own share under any circumstances, including the reduction of its own capital. They stated in their corporate laws that a firm may not buy its own share under any condition, while specifying the way and condition the firm may reduce its own capital, such as reducing the par value of each outstanding share in equal basis, after getting the consent of several parties including the creditors and official corporate controllers. Moreover, in case of merging two firms, if one firm used to own shares of the other firm before merging, such shares should be dispatched, as stated for example by the Jordanian corporate law (HKJ, 1988). Examples of these countries include: Jordan, Oman, Lebanon, Morocco, Poland, Saudi Arabia, and Republic of China.

The second group: A corporate may repurchase its own shares under specific conditions for the purpose of capital reductions that limited to 10% of the outstanding shares as a maximum. The majority of this group permitted share repurchases only during the last five years. They still have limited experience in share repurchasing activities as expressed by a number of firms and trading volume. Countries of this group are: South Africa, Australia, Taiwan, Sweden, Singapore, Japan, Germany, Netherlands, Denmark, Taiwan, Belgium, France, New Zealand, France, Finland, Korea, Norway, Belgium, Italy, Spain, and Ireland. Some countries such as Canada limited the size of repurchased shares to 5% of outstanding shares or 10% of public offering shares (Ikenbury et. al., 2000).

Table 6
Repurchasing practices based on related laws as existed in the selected sample

Repurchasing practices based on related corporate laws	Example of countries
A corporate may not repurchase its own share under no conditions.	Jordan, Oman, Lebanon, Morocco, Poland, Saudi Arabia, Republic of China
A corporate may repurchase its own share under specific conditions for purpose of capital reductions limited to 10% of outstanding shares as a maximum.	South Africa, Australia, Taiwan, Sweden, Singapore, Japan, Germany, Netherlands, Denmark, Taiwan, Belgium, New Zealand, Canada, France, Finland, Korea, Norway, Italy, Spain, Ireland
A corporate may repurchase its own share under specific conditions for capital reductions, but it is permitted to exceed 10% of outstanding share	UK, Australia, Hong Kong, India Bermuda, Cayman Islands
A corporate may repurchase its own share for purpose of capital reductions and to be holding for limited period.	Switzerland, (6years) Greece (3years) EC directives (one to three year)
A corporate may repurchase its own share for various purposes and to be holding as treasury stocks and for employee option plans, and reissue or redemption without limited time.	USA Malaysia UK (In process) Hong Kong (In process)

Source: Compiled by the author based on the related laws of above countries.

The third groups: A corporate may repurchase its own shares under specific conditions for capital reductions, but it is permitted to exceed the 10% outstanding shares. Example of this group is UK which requires specific regulations when the purchased share, are more than 15%, Hong Kong requires to meet specific regulations, in case the volume is more than 10% of outstanding shares and to get an independent financial advisor (SFCHG, 2000). India states the limit on 25% of the total paid capital and frees reserves as indicated by the amendment of Companies Act of 1999 (Sections 77A and 77B).

The fourth group: A corporate may repurchase its own shares for the purpose of capital reductions and hold it for a limited period. EC directive stated that "were the laws of member states permitting a company to acquire its own share, it must be disposed them within three years of their acquisition (EEC, 1999). European countries, which their laws permit corporations to repurchase their own share, have to comply with the Second Directive.

The fifth group: A corporate may repurchase its own shares for various purposes and hold them as treasury stocks, and reissue or redeem them without a limited time. US and Malaysia have no limits on the volume of holding treasury shares other than the minimum requirements of float shares in stock exchange, while UK and Hong Kong suggesting 10% of outstanding shares as maximum.

B. Share Repurchasing Law Statue

This study found that the majority of the selected sample accepts the share repurchases activities at one degree or another. However, there are some similarities and differences among the related laws and regulation across the selected countries, as presented in Table 7. All countries require a decision from the majority vote of the firm's shareholders and announce a repurchase program. In addition, some states require the consent of stock exchange such as Canada before starting a repurchase program (Ikenbury et. al, 2000). Other countries require only notification to the stock exchange and filling specific forms such as USA. The majority of the states require financing repurchasing activities from the retained earning and free reserve and not from the paid capital. The majority of the related laws do not permit offering financial assistance by a company for the acquisition of its own shares to third party. The condition of stating the fair price for repurchases varies among different countries.

Other details of the selected samples may be found in the related rules beside what are presented in Table No.7. For example: UK regulations require additional rules to meet disclosures requirements regarding volume and price, and to meet requirements of chapter 15 of Stock Exchange rules and the guidelines of investment protection committee, and specific rules for repurchases from off market as stated by Company laws section 164 (DTI, 1998). USA sated more detailed rules related to the manner of purchase condition, which requires an issuer to use a single broker or dealer on any given day. The volume condition is stated to prevent dominating the market. The timing condition specifies that an issuer's purchase may not be the opening transaction (SEC, 1999).

Table 7

The Existing corporate laws and stock practices of repurchasing shares as applied by ten countries and EC in 2000

Country	Major changes
EEC directives	Authorization of general meeting and to be implemented in 18 months Limited to 10% of the outstanding shares Only fully paid may be repurchased and to be disposed within three years To be financed by distribution profit
Canada	Approval from the exchange to initiate a repurchase program Limited to 10% of outstanding shares and last one year To be executed through a single broker Repurchases over 30 days not exceed 2% of outstanding shares
Greece	Approval of General assembly and to be disclosed 10 days in advance Limited to 10% of outstanding shares and last one year To be disposed within three years
Hong Kong	To be implemented by a general offer, other methods are permitted under specific conditions. To be financed by distribution profit or a share issue Minimum public float should be maintain, In case of repurchased shares are more than 10% specific conditions applied To notified the stock exchange and consent of the exchange is required
India	A company may only buyback shares and not to exceed 25% of the paid capital and reserves to be completion within 12 months To be financed from its free reserves, share premium, To be cancelled within seven days of the buyback date Debt-Equity Ratio net less than 2:1
Netherlands	Limited to 10% of outstanding shares and to be cancelled To be financed by retained earning, and to be implemented in 18 month Approval of shareholders, including volume and repurchases terms
New Zealand	Limited to 10% of outstanding shares, and shall be deemed Based on the average end of day market price The repurchase price shall be the average daily price of the previous month Notification to the stock exchange and to be implemented in 12 months
Singapore	To be financed from distribution profits Within the period mandated by shareholders Companies may place up to 20% of capital to institutional investors, at price discounts of up to 10 percent of the weighted market prices
Taiwan	Buybacks not more than 10% of outstanding shares A daily buybacks limited to 20% of average turnover To announce its program and volume and reasons To carryout within one month of buyback announcement
United Kingdom	It should be authorized by its articles and majority vote resolution To repurchase fully paid –up shares and must be canceled To be financed by distributable profit or a fresh share issue

Table 7 (continued)

United States	Minimum public floating of outstanding shares To issue a press release after approval of board of director and to notify stock exchange within specific period and filling forms To voluntary apply of safe harbor rules (10b-18) of SEC (manner of purchase, timing, price, and volume conditions)

Source: Compiled by the author based on (UK: DTI, 1998) (USA: SEC, 1998) (Singapore: USSE , 1999) (Hong Kong: SFCHG, 1998) (EEC, 1999) (Taiwan: Chou, 2000) (India: Kamal and Maitra, 1998). (Netherlands: Shrimpton, and Millerchip 1998) (Greece: Athens Stock Exchange, 2000). (Canada: Ikenberry et al. 2000) and (NZSE, 2000).

New Zealand permitted financial assistance to specific purposes under stated conditions to be given for employees as stated by article No.7.6.5 (NZSE, 2000). Hong Kong prevented a company from the distribution of shares following announcement of share repurchase for specific period. (SFCHK, 2000). In Greece, the repurchases' procedures should be disclosed to the public at least 10 days in advance (Athens Factbook, 2000). THE EEC Second Company Law Directive (EEC, 1999) permits shares to be held in treasury, subject to certain provisions. It requires that the annual report of a company to state the reasons for acquisitions made during the financial year. In addition, a company may not make loans or provide security regarding the acquisition of its own shares by a third party.

C. Tax Regulations and Share Repurchase Activities

Adopting new laws by a state regarding share repurchase activities requires changes in tax regulations to cope with new situation. The implication of tax practices in regard to the share repurchases activities are varied among the selected sample of the states. Some of those states don't apply capital gains tax such as Singapore, South Korea, Taiwan, Germany and Hong Kong (Moore and Silvia, 1995). Other states impose double taxation on corporation dividends such as US, while others impose income tax on corporate only such as applied in most of the developing countries. Other states may impose capital gain tax but they exempt the share repurchases activities such as US. Thus, the tax implications of share repurchases among the states are different. In addition, the reaction of the state tax policy to the concept of share repurchase is different from one state to another. In some states, the tax regulations were relaxed to encourage share repurchases, such as Netherlands, UK and Finland, while it was the opposite in case of South Africa. The tax effect regarding corporate share repurchase has three-folds:

First, corporate income tax: There is a need to indicate whether the difference between market value and previously issued par value of the repurchased share is considered a capital gains or not, and whether it is subject to income tax or not.

Second, personnel (shareholders) income tax: There is a need to indicate whether share repurchase is equal to dividend paid by company to shareholder or not, thus it is subject to income taxes or not.

Third, Fees imposed on transfer of stock ownership: It should be stated whether share repurchase is considered as transfer of ownership or cancellation of it.

Based on the investigation of tax implications attached to share repurchases of the selected sample, the following examples may be reported, in order to present the differences which existed among states in tax treatment of corporate share repurchase:

UK: It witnessed four tax law changes affected share buybacks activities in the last decade (Rau and Vermaelen, 2000). Until April 1999 a share buybacks by its own company was treated as distribution of profits to the extent that the price paid for the shares exceeds the par value of the share and thus applicable to advance corporation tax. However, the UK government proposed a bill to abolish the advance corporation tax from the date included in the finance bill (DTI, 1998).

Australia: The supreme court of Victoria ruled that the share buyback arrangements by Australian companies does not involve a transfer of rights, but an extinguishment of the rights attached to the shares, thus buybacks are exempt from stamp duties (TNI, 1998).

South Africa: There is a proposed amendment bill related to the Income Tax Act which indicates that the buyback of shares will be subject to tax, to the extent that the price at which the shares are bought back exceeds the nominal value of such shares at a rate of 12,5% (Pricewaterhouce & Coopers, 1998).

Switzerland: For a company, it should hold tax on share buybacks of 35% rate for the difference between par value and repurchase price, but individuals may reclaim the hold tax to be deducted from their income tax. (Shrimpton and Millerchip, 1998)

USA: According to IRC section 1032, a US corporation generally recognizes no gain or loss on the initial issuance of its stock or on the purchase and sale of treasury stock. Therefore any related gain is tax-free and loss is nondeductible, but a corporation recognizes taxable gain if it buys back its own shares with appreciated non cash property (Oliver and Moffeit, 2000).

Singapore: For example, shareholders who sell their shares to a company for the company's share buyback exercise through a special trading counter set up on the Singapore Exchange, the amount received by shareholders from such share buybacks will be treated as a receipt of dividends (IRAS 2000).

Netherlands: The present income tax treats share buyback as dividend payment and it is taxable for Individuals at tax rate from 38% to 60%, and for the company a share buyback is considered to be dividends by the company to shareholder, thus a tax rate of 25% to be held from the payment to the shareholders. However, A new tax system is due on January 2001 will not consider a dividend in regards to individuals' tax income (Herreveld, 2000).

Finland: After the Finnish corporate act permitted a company to acquire its own shares in 1997, the Finnish administration of taxation stated in June 1998 that provisions regarding concealed profit distribution are not applicable to share buybacks (GC, 1998).

D. Accounting Practices of Share Repurchasing Activities

The accounting practices may be similar among the countries in case of corporate share repurchases for the purpose of capital reduction, which is the case in most of the selected states' sample. In this case the objective of accounting practices is to determine the amounts of capital instruments and their associated costs in a way that reflects the obligations of the issuers, as stated for example by the FRS No. 4: capital instrument, issued by the Accounting Standard Board of UK (ASB,1998). It stated that where shares are repurchased or redeemed, shareholders' funds should be reduced by the value of the consideration given (paragraph 39, No.4 ASB, 1998). The accounting treatment of corporate share repurchases raises some issues. In this regard, we find that the following related practices are existed:

- The US FASB Instructions (APB opinion No. 6, FASB Technical Bulletin No. 85-6. FASB, 1995) stated the accounting practices of share repurchases as follows: The cost of repurchased shares of its own capital should be shown as a deduction from capital. Dividends on hold treasury shares shall not to be credited to income. Gains and losses on sales of treasury shares to be accounted for as adjustment to the capital. An excess of purchase price over par value may be allocated to capital surplus or retained earnings. (APB No. 6, FASB No. 85-6 and FASB (1998)
- The International Accounting Standards Committee interpretations (IASC, 2000a and 2000b) took a close line to the FASB of USA, which may be summarized as follows: Treasury shares should be presented in the balance sheet as a deduction from equity (a change in equity) and should not be considered as financial assets. No gain or loss should be recognized in the income statement on sale, issuance or cancellation activities, but to be presented as change in equity. The acquisition cost of treasury shares may be shown as one-line adjustment of equity. The par value may be shown as a reduction from share capital with adjustments of premiums or discounts (IASC, 2000a).
- The accounting practices of the EEC Second Company Law Directive and the Fourth Company Law Directive and its amendments (EEC, 1999) may be summarized as follows: The own shares should be presented in the financial assets of the balance sheet among other investments. If the shares are included among the assets shown in the company's balance sheet, a reserve of the same amount. The reserve for owns shares to be presented under Capital and Reserves sub-title. The own shares present with indication of their nominal value or accounting par value (EEC, 1999).

A country that legalizes holding the repurchased corporate shares in a treasury form may select one of the above three choices or to develop their own accounting model. However, for most of the countries outside the EEC, they may adopt the IASC standards. For example in the consultation document issued in Hong Kong related to legalized treasury shares, it suggested to adopt the IASC standards in case of legalizing the treasury shares (SFCHG, 1998). For UK, it refers to the EEC Law directives regarding the reporting of share buybacks in the accounting practices (DTI, 1998).

V. THE SUGGESTED MODEL

A. Introduction to the Model

This study found that there has been major developments in the world stock market during the last decade concerning share repurchase activities: First: an increasing movement in the world stock market towards adopting the share repurchase activities. Second: many countries tend to deregulate the share repurchase in order to be more flexible and effective to serve purposes other than an alternative to dividends. Third: there is a continuous increasing of repurchase trading volume in most of the countries permit share repurchases activities. Forth: there is a movement from corporate share repurchases to the concept of treasury shares. Fifth: there is a toleration to use the treasury share to interfere in the stock market during stock crises and high market price volatility, under condition that interference is not leading to manipulate the stock prices.

Concerning the interference in the stock markets through repurchase activities, there is few experiences support this trend. In Malaysia when, the stock market crises occurred and share prices in Kuala Lumpur stock exchange fell sharply in June, 1997, the first step was to legalize the share repurchases in order to help in stabilizing the stock market and put it in force within three months. After one year in 1998, the corporate law was amended once again to permit the corporate to hold repurchased shares in treasury (ROC, 1999).

The SEC of USA adopted two rules to deregulate the safe harbor's timing conditions and circuit breakers (SEC, 1998). The rational for such adaptation may be found in the stated objective of the proposed rules. It stated that "The events following the market breaks in October 1987 and October 1997 have underscored the significant role of issuer repurchases during market downturns and the need for clarity as the applicability of Rule 10b-18 in periods of extreme downturns. On those occasions issuer repurchases provided an important source of liquidity that helped ease market stress and may facilitate market participants' ability to reestablish equilibrium between buying and selling interests" (SEC, 1999). The consultation papers of the UK and Hong Kong stated that the objective of adopting treasury shares is to enable companies to manage effectively the level of capital in the same way as they manage labor and land, and to give companies greater flexibility to adjust their share capital which might stimulate investment (DTI, UK, 1998) and (SFCHG1998).

B. Definition and Framework of the Model

Based on the above findings, this study suggests the concept of using the treasury stock for distinctive purpose as to stabilize stock market. To work under unique trading mechanism, legal, financial, and accounting aspects. The concept of the model is based on the firm's interference in the stock market to buy its' own shares if the share prices fall to a certain level, or if the performance index of the home stock exchange fall to a certain level. The repurchased shares may be held as long as the market situation requires. In order to be ready for reselling at a convenient time or when the share prices rise to stated level or the performance index of the home stock exchange improved to certain level. The stated level of interference may be when the market share value fall below the par value, or the book value or a point between them. Thus, timing and volume of reselling and repurchasing transactions is bounded by the stated ratios of market prices, or performance index of the home stock exchange were the company is listed. The balance of holding treasury share to be named as treasury shares for market stabilization.

The suggested model has to be authorized by the corporations' laws or by a resolution of the majority of stockholders as well as by the home stock exchange. The authorization is limited for one year and should be renewed annually after a careful audit of previous activities. The approval and announcement of share repurchase for this model should not apply to activities related share-repurchasing announcement substitute to dividends. Using this model should be exclusive for corporations listed in the stock exchange, in case of dual or cross listing in more than stock exchanges; this privilege should work only in the home stock exchanges. The daily stock repurchasing transactions should not exceed 50% of the trading volume for that day. In any situation the holding shares should not exceed 25% of the total share outstanding.

Table 8

Framework of the suggested model using treasury stocks to stabilize the stock market

Major elements	Measures and techniques
Protection of creditors and investors	Finance limits (minimum debit to equity ratio) Finance from free reserves and retained earning 25 % limit of outstanding shares
Protection of shareholders	To buy from open market in official stock exchange
Companies laws	Limited to public corporation Listed to listed companies in home stock exchanges Permitted to repurchasing its own shares Permitted to be hold as treasury shares
Stock exchange regulations	Notification and approval of stock exchange for one fiscal year transactions and to be renewed after auditing Disclosures requirements
Accounting standards	Treasury shares to be presented as investment assets in the balance sheet Considering profit or loss in selling and repurchasing Of Treasury is part of extraordinary income statement items. Disclosures notes attached to financial statements
Stock market	Establish a market and create a demand under specified conditions

trading	Reselling and repurchasing is due to pre stated market price or performance level of stock exchange

The stock repurchasing transactions may be regarded as stock transfers among shareholders rather than dividend distributions. The treasury shares should be presented as an asset under the caption of long-term investments in the assets side of the balance sheet statement. The net profit and losses from reselling shares transactions may be considered as period costs or revenues, thus they are to be recognized in income statements as other profits or losses accomplished from other portfolios. Disclosure notes should be attached to financial statements to indicate the balance, reselling and repurchasing of treasury shares by dates, numbers, and values. The free reserves are the only source of funds to be used for repurchasing transactions for holding treasury shares. A corporation should not interfere as a buyer for its own shares in the stock market based on this model to hinder a hostile takeover attempt or to serve other purposes such as employee option plans or for tax advantages. Table 8 summarized the framework and features of the suggested model.

C. Rational of the Model

Rational and methods of financing share repurchases are varied based on the stated purposes of the model, as presented in Table 9. It indicates that there are four models of share repurchases, with different rational, purposes and financing. Our concern is in the last model, which suppose to finance through special reserve fund, and to be part of the earned capital. The following is explanation of the rational of the suggested model, covering financing and marketing aspects as follows:

Rational for financing: The suggested model aimed to interfere in stock market trading at certain conditions using a special reserve to be part of the earned capital. The owner equity of a firm includes two parts: the issued paid capital shares, and the earned capital. The earned capital includes various items based on the corporate laws of the different countries. In the majority of the world countries, the earned capital includes various items, such as mandatory reserves, voluntary reserves, share premium, and retained earning. In many countries and due to the corporate law requirements, the earned capital value is about several times of the paid capital. Accordingly, part of the earned capital may be specified for financing repurchasing treasury shares for stabilization of stock market.

Rational for interfering in stock market**:** The major concern of market interference by a firm to repurchasing and reselling its own shares in all corporate legislators is to avoid manipulation of stock market, and prevent insider trading**.** For example, the major argument against holding treasury shares is related to market manipulation (SFCHG, 1998). Other arguments claim that a firm may be given an opportunity to create a false market or to manipulate the price of their shares, and may support the share price artificially (DTI, 1998). The Malaysian Legislation repealed the permission for firms to offer financial assistance to other persons to buyback its own shares because the provision was misused after one year of application (ROC, 1999). In addition, one may claim that falling of stock prices may reflect fundamentals data, and it is better for a company to invest its available cash to implement specific reforms rather than repurchase its own shares.

Table 9

Rational of share repurchase and treasury for different situations

Objective	Sources of funds	Rational
Amortization of capital Alternative to dividends	Excess in paid capital Excess in earned capital	Redemption Cancellation for capital reduction
To serve other purposes of repurchase	Excess in retained earning, new share issues, share premium	Treasury share for future cancellation
To stabilize stock market when market value is less than book value	Special reserved (earned capital)	Treasury share for reselling

Accordingly, this model suggesting that the interference time of stock market is bounded by certain levels of share prices or stock exchange performance index, and not by corporate management decisions, to the extend that there is a fund available in the special free reserve. The level of interference for repurchase may be set at the share book value, or at par value or at level in between. The market value of a share in stock market supposes to reflect the earned capital beside the par value, the present, and future expectation of the firm. Accordingly, there is justification for interference if market price falls below the book value assuming the fundamentals data of the firm is true. In some states and due to differences in corporate laws and reserve requirements, the level of interference may be set between share book value and share par value. Other levels of interference may be set based on stock exchange performance index, in order to react for falling of index due to adverse information, overreaction, and noise trading.

VI. SUMMARY AND CONCLUSION REMARKS

This study aimed to examine the issue of share repurchase in the global stock market context. It used a sample of 36 countries that form 90% of the world market trade value. It found that there is an increasing movement in the world stock market towards adopting or deregulating the share repurchase activities as well as there is a significant change related to moving to the concept of treasury shares. In addition, there is a new trend to accept the concept of treasury share to strengthen the stock market during stock crises and in case of exceptional high market price volatility.

The study found that there are some similarities as well as some differences between the selected sample of states, in regards to the corporate laws, stock exchanges regulations, and other related rules applied to the share repurchase and treasury activities. In addition, the tax practices are varied among the selected sample. This applies to income tax imposed on the corporate, or in the stockholder, or related to other fees. There are three accounting models for share repurchase and treasury activities, including the FASB of USA, the International Accounting Standards of IASC, and the EEC accounting directives.

This study may conclude that the world stock market is affiliated to one of the following levels in regards to share repurchases:

- First level: not permitting the firm to buy its own share under any circumstances
- Second level: permitting share repurchase as an instrument of capital reduction.
- Third level: permitting the concept of holding firms' own shares for limited time.
- Forth level: permitting trading (reselling and buybacks) of treasury share in open stock exchange based on specific regulations and within finance and volume limits for specific purposes such as employee option plans and tax advantages.
- Fifth level: permitting free trading (reselling and buybacks) of the holding treasury shares in stock exchange to interfere in market to improve or absorb liquidity in certain conditions of stock market crises and high volatility prices using the suggested model.

The sample of thirty-five countries is located at one level or another from the first to the fourth levels. In regard to the fifth level, the study found that some countries are close or moving slowly to this level such as US, but some restrictions still exist. The suggested model is dealing with the fifth level, and proposes that mechanism and regulations. In addition, this paper is an attempt to call corporate governance in all countries to investigate this issue which may enhance stock market prices in future stock market crises and noise trading. However, to examine the validity of the suggested model in an empirical way, may not be possible unless be adopted by some countries.

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