



## Client Alert

# Financial Markets Developments

### Open market repurchases of debt securities—some regulatory issues to consider

#### Overview

In contemplating open market repurchases of debt securities, issuers will need to consider a number of questions, including:

- Do the terms of the debt instruments allow repurchases?
- Does the issuer have inside information?
- Is an announcement required prior to, or after making a repurchase?

This Insight aims to provide answers to some of these questions and provides a brief overview of the potential application of the European market abuse rules in the context of open market repurchases of debt securities outside an announced debt buy-back programme or tender offer process. The Market Abuse Directive (“MAD”) is the primary EU measure relevant to repurchases of securities, although individual EU member states may have additional legislation covering the issues mentioned in this note. Under MAD the relevant legislation will be that of the EEA country where the regulated market on which the debt securities are listed is situated or operating and also the legislation of the EEA country where any behaviour occurs (e.g., potentially via a broker based in another country).

#### MAD

MAD applies to behaviour concerning financial instruments admitted to trading on a regulated market in at least one member state of the EEA or for which a request for admission to trading on such a market has been made irrespective of whether or not the transaction itself actually takes place on that market. Behaviour in relation to “related instruments” such as certain derivatives is also covered by the regime.

MAD identifies three broad categories of prohibited behaviour:

- insider dealing,
- market manipulation, and
- the dissemination of false or misleading information.



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The legislation also requires that an issuer announces inside information directly concerning it without delay, and introduces a specific safe harbour regime for share buy-backs conducted within certain specified price parameters (but this safe harbour does not specifically cover buy-backs of debt securities).

### Does the Issuer have inside information?

Dealings based on inside information are prohibited. “Inside information” is, broadly speaking, non-public information of a “precise nature” relating directly or indirectly to a company or to its securities that would, if public, be likely to have a “significant effect” on the price of the security. For illustrative purposes, the following information is likely to amount to non-public price sensitive information in the context of a buy-back: information or events that may lead to a change in the issuer’s credit rating, information about potential M&A transactions by the issuer, the publication of pending financial accounts and trading announcements.

In the case of a tender offer or debt buy-back programme, prior announcement of the proposed repurchases will, effectively, have been made. For open market repurchases, there may be an argument as to whether an issuer’s intention to repurchase its own securities would, in itself, amount to inside information and thus, effectively, prevent a repurchase from happening in the absence of an announcement being made. However, in considering this issue, MAD provides that the carrying out of a person’s decision to deal should not be deemed, of itself, to constitute the use of inside information.

### Announcements

The legislation requires that issuers announce inside information directly concerning themselves without delay. Issuers can delay the announcement of inside information in certain circumstances—principally to protect the legitimate interests of the issuer in circumstances where the failure to announce would not mislead the public and where the confidentiality of the information can be maintained.

Once open market repurchases have been made, issuers must also consider whether, the existence of such repurchases would amount to inside information which needs to be disclosed. In considering this, issuers would need to consider whether at the time of the repurchase and after each purchase, if the information regarding the buy-back was made public, it would have a significant effect on the price of the securities. Failure to make an announcement when required could restrict the issuer’s ability to make further repurchases.

MAD prohibits transactions or orders to trade which give false or misleading impressions as to the supply, demand or price of investments or which secure the price at an abnormal or artificial level other than for legitimate reasons and in accordance with accepted market practices. In this context, the Directive considers the effect of behaviour on the market, not just the intention (or lack of intention) to manipulate or distort and it will be important to consider what the impact on the price might be if the repurchase was disclosed. The effect on liquidity in the market may also be an important factor and may require an issuer to keep investors informed about repurchases that may affect the liquidity of the relevant securities.

Although MAD provides issuers with a safe harbour under which they may repurchase their shares under a buy-back programme within certain parameters without violating MAD’s market abuse provisions, the safe harbour is not applicable to debt buy-backs. However, it may be helpful for issuers to try to observe similar standards (e.g., relating to announcements of repurchases, price and limits on repurchase amounts) in relation to debt repurchases under a programme to the extent possible.

In the UK, rules existed prior to the implementation of MAD which required issuers to announce repurchases of 10% or more of an outstanding issue. However, these rules were revoked on the implementation of MAD. The specific percentage level test as to whether an announcement might be required has effectively been replaced with a more subjective test as to whether the impact on the price would be significant or could give a false or misleading impression if the information is not announced although we believe the “10% test” may remain of interest in this context.

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## Conclusions

Careful thought may need to be given to whether an announcement relating to any open market repurchase proposal is required and what further announcements may be needed as and when repurchases are made.

As for individually negotiated open market purchases outside a tender offer or buy-back programme, we do not consider that prior or subsequent announcements would necessarily be required. However, this needs to be considered on a case by case basis depending on the facts and circumstances concerned. Separately, it will be important to analyse what, if any, inside information an issuer holds before embarking on any repurchase operations as, depending on the nature and type of such information, this could restrict the issuer's ability to effect the repurchases. In this context, issuers may wish to consider adopting "blackout periods" during which repurchases will not be made, e.g., for a certain period prior to results announcements or whilst inside information may otherwise be held.

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