STOCK BUY-BACKS

***e*Research Corporation** is pleased to provide a commentary, courtesy of CNBC Markets, on restricting insiders from selling after a buy-back announcement.

Buybacks Are Under Attack Again As A Senator Pushes To Restrict Insider Sales After Announcements

- Corporate insiders would be barred from selling shares for an undetermined time after buyback announcements, under a plan floated by Sen. Chris Van Hollen.
- The Maryland Democrat is the latest legislator to take on share repurchases, following fellow Sens. Chuck Schumer, Bernie Sanders and Republican Marco Rubio.
- Van Hollen says he's prepared to push legislation that forces the SEC to revisit its buyback rules.

Corporate insiders could be barred from selling stock within a certain time period after share buybacks are announced, if one Democratic senator has his way.

Sen. Chris Van Hollen, of Maryland, pointed to evidence from a Securities and Exchange Commission study indicating that share repurchases are benefiting corporate insiders at the expense of long-term investors. As a result, he said he is preparing legislation that would direct the SEC to study the rule on buybacks, with hopes, ultimately, that a time-frame can be established delineating the period during which sales would be prohibited.

"It could be a long period of time like several years, or maybe analysis would show another period of time that might be appropriate," Van Hollen said during a media call.

The senator had asked the SEC to look into stock performance after buyback announcements to determine the impact on individual stocks. What the study found, as reported in a letter from Commissioner Robert L. Jackson Jr., was that "firms that let insiders sell on buyback announcements perform worse over the long run," Van Hollen said.

COMMENT: *This statement that insiders who sell on buyback announcements do worse in the long term does not make sense. Management instigates a buy-back program because they believe their stock is under-valued and buying the stock would be an attempt to prevent it from falling further. This "support" should limit further downside. If the stock subject to the buy-back does "perform worse over the long run", this has to be compared to how the general market also performed in the same time-frame. One would think the market performed worse.*

"In other words, the executives' gain is at the expense of the other stock-holders who are not insiders," he added. "It raises the concern that buybacks are used as a way to maximize executive pay."

The senator's comments come as share repurchases, announcements of which totaled more than $1 trillion in 2018, have come under bipartisan fire.

Earlier this year, Sens. Charles Schumer, a New York Democrat, and Bernie Sanders, a Vermont independent who is running for president on the Democratic ticket, unveiled a plan that would force companies engaging in repurchases to pay a living wage and provide health-care benefits.

Shortly after, Florida Republican Sen. Marco Rubio said he wanted to change tax laws that reward buybacks.

Jackson's letter indicates that momentum may be building within the SEC to revisit the buyback rules. In the missive, the commissioner said he found that studying buybacks from January 2017 through the end of 2018 showed that insiders sell more stock right after buyback announcements, indicating the repurchases are geared toward their enrichment rather than the benefit of the company.

"Whether insider sales cause the stock to fall or simply reflect insiders' view that the buyback won't add value in the long run, the opportunity to cash out stock-based pay gives executives reason to pursue buybacks that do not produce long-term value," Jackson wrote.

The SEC declined comment on the matter. Jackson did not return a request for further comment.

Van Hollen indicated the next step is to reach out to the commission to get it to conduct a roundtable and hearing on the buybacks rule, and to use legislation to force it do so if necessary.

"I don't know exactly what the appropriate period is, whether it is a year, more than a yea,r or less than a year" to restrict insider sales after buybacks, Van Hollen said.

COMMENT: *eResearch is against buy-backs as a matter of principle. Instead of using corporate money to repurchase shares – a program whereby corporate management believes its stock is under-valued and, therefore, buying back stock is designed to boost the company's share price, or at least support it from falling further – a more appropraite use of the money should be to return it directly to the shareholders, i.e., in the form of increased dividends or a dividend bonus. The hue and cry from institutional investors is that increased dividends is not tax efficient – to them! Stock buy-backs are great – in theory. But there are so many factors at play in the markets every day that supporting one's stock by buying shares in the open market is subject to the very whims and actual events that impact the market continually. What if a company bought a lot of its own stock at, say, $40 per share and a negative global-impacting event occurred, well, guess what, no amount of corporate buying will save that company's stock from plunging in the market like all others. So, the money spent at $40 is now in a significant loss position as the stock is now trading at $30. It is not good enough for corporate management to then say that their stock is even more under-valued and that they can buy their stock at even more attractive prices. Mr. CEO, your stock is now down $10 per share from where you bought it yesterday! That money could have been declared as a dividend and would be safely in your shareholders' pockets.*

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COMMENT: *If there is to be a period of insider restrictions on selling shares during a buy-back, it should commence the day that the buy-back is announced and end on the day that the buy-back terminates. Most buy-backs last for about one year, so that is a suitable time to restrict insider trading. In addition, since executive management compensation is often tied to stock performance, the price of executive options should be adjusted under buyback provisions.*

Bob Weir, CFA
Contributing Analyst