Question mark over buyback pipeline as fresh tax bites

Others likely to follow KPR Mill in withdrawing share repurchase

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The 20 per cent buyback distribution tax introduced in the Budget has put a question mark over share repurchase programmes worth nearly ₹15,000 crore, announced by 20 companies.

On Thursday, KPR Mill became the first to withdraw its share buyback, saying the increased tax burden has made it unviable for the firm to proceed with its ₹263-crore stock repurchase plan.

People in the know said more firms are seeking legal opinion on whether they could withdraw their plans. On Monday, the ₹460-crore proposed buyback of the BSE will be put to vote at its annual general meeting (AGM), where its shareholders will decide on going ahead with the buyback.

Several legal experts told Business Standard that companies have approached them seeking advice on the same.

According to data by PRIME Database, a primary market tracking firm, there are 20 companies including Wipro and Adani Ports & SEZ that have set the ball rolling on their buyback plans.

Although KPR Mill has withdrawn its buyback plan, legal experts believe it is not a straightforward decision, given it may clash with the Securities and Exchange Board of India's (Sebi's) Prohibition of Fraudulent and Unfair Trade Practices (FUTP) Regulation.

"There is a particular provision that allows for withdrawal of a buyback offer prior to the draft letter of offer being filed, or prior to the public announcement. However, it is not advisable to withdraw the same for reasons such as taxation or otherwise, since it exposes a listed company to allegations of FUTP violations," said a securities lawyer.

Not all are going back on the plan. Eris Lifesciences and SH Kelkar have filed their letter of offer for the buyback with the markets regulator and are likely to proceed.

Experts say withdrawing the buyback is unfair to shareholders, after a company has fixed the buyback price and the ex-date.

"A company could be vulnerable to complaints from shareholders who may have traded in its shares on or after the date of the board announcing the buyback to the bourses," said the lawyer quoted above.

However, smaller firms seem to be caught between a rock and a hard place.

"Withdrawal of a buyback may not be seen favourably by the market and Sebi. At the same time, the buyback outgo can't exceed 25 per cent of the capital and free reserves. After factoring in the new tax outgo, some companies may end up breaching this limit. Sebi may have to provide special dispensation given the unique situation," said another lawyer.

Given the tax advantage, buybacks had become a go-to tool for corporate India to return cash to shareholders in lieu of dividends, which are highly taxed. To end the tax arbitrage, the government has decided to levy a 20 per cent dividend distribution tax.

Given that this tax has come into effect from April 1, it has hit firms with ongoing buybacks and those that have made buyback proposals. Typically, the Budget takes place on February 1, and new taxes are applicable two months later, which allows companies to plan better.

However, the full Budget took place on July 5 since this was an election year, and changes were made applicable retrospectively from April 1 without any 'grandfathering' benefit, putting companies in a flux. Experts say factors other than taxation will drive the decision of opting between dividends and buybacks, hereon.

BUDGET IMPACT

"Now, as buybacks and dividends are tax-neutral, the consideration for companies will have to be different than tax. If a company thinks its share prices are undervalued, it can do a buyback to send a positive signal to the market," said Vikas Srivastava, partner at L&L Partners.

ILLUSTRATION: BINAY SINHA

TURNING THEIR BACKS

Companies that had set the ball rolling on their buyback programme before the change in tax structure

	Board approval date	Proposed amount (₹cr)
Wipro	Tuesday, April 16	10,500
Adani Ports	Saturday, April 6	1,960
BSE	Friday, July 5	459
Welspun Corp	Tuesday, May 14	390
KPR Mills*	Monday, April 29	263

*Now withdrawn

Source: PRIME Database