

GOODBYE BUYBACKS? WHY RECENT STOCK BUYBACK REFORM PROPOSALS GO BEYOND WHAT IS NECESSARY

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ABSTRACT

This note provides an overview of the intensifying debate around the impact that stock buybacks have on economic inequality and the proposals designed to reform the practice. With the advent of the Securities and Exchange Commission's (SEC) 1982 promulgation of Rule 10b-18, corporations began allocating vast portions of their profits to stock buybacks. In recent years, this practice has become increasingly more common and has surpassed previous historical benchmarks.

Critics of stock buybacks primarily view the practice as a misuse of excess corporate funds that could instead be allocated to improve employee working conditions, benefits, and future outcomes. Opponent's concerns surrounding buybacks and inequality have been fueled by recent corporate tax cuts under the Trump administration. In many instances, additional funds provided by these tax cuts have been used to conduct buybacks as workers' wages remain stagnant and executive compensation becomes more frequently tied to stock-based instruments. As a result of stock price increases associated with buyback announcements, issues around the incentive for executives to initiate such programs have come into question.

In an effort to curb buybacks, many prominent lawmakers and academics have undertaken efforts to reform current regulations governing corporations conducting repurchase programs. However,

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proponents of buybacks believe that concerns related to buybacks impact on economic inequality are misplaced and potentially jeopardize legitimate uses of such programs. This Note examines the arguments shaping this debate and presents a reform proposal which endeavors to provide a balanced approach to regulating buybacks by modifying existing disclosure frameworks.

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INTRODUCTION

A stock buyback, also known as a share repurchase, occurs when a company purchases its own equity securities in the open market.¹ In the

1. Caroline Banton, *Share Repurchase*, INVESTOPEDIA (Nov. 19, 2020), <https://www.investopedia.com/terms/s/sharerepurchase.asp> [https://perma.cc/2PSL-U9GJ].

aftermath of the 2008 financial crisis, stock buybacks became increasingly prevalent.² In the decade since, 465 S&P 500 companies have spent an estimated \$4.3 trillion on stock buybacks, equal to 52 percent of net income.³ With the rising frequency of companies deciding to repurchase their own shares, this practice has come under criticism by prominent politicians, academics, and economic experts.⁴ A growing debate has begun to form over the effects of stock buybacks on economic inequality and calls for regulatory reform have risen to the forefront of the conversation.

Stock buybacks are currently regulated by the Securities and Exchange Commission's (SEC) Rule 10b-18.⁵ Rule 10b-18 creates a legal "safe harbor" that shields companies from liability for market manipulation under the Securities Exchange Act of 1934 ("34 Act").⁶ Companies in compliance with the conditions laid out in Rule 10b-18 can conduct "virtually unlimited stock buybacks."⁷ For example, over the last decade, the five largest U.S. airlines have used 96 percent of their free cash flow to conduct share repurchases, with most occurring in the last three years.⁸ Despite these significant buybacks, the airline

2. William Lazonick et al., *Why Stock Buybacks Are Dangerous for the Economy*, HARV. BUS. REV. (Jan. 7, 2020), <https://hbr.org/2020/01/why-stock-buybacks-are-dangerous-for-the-economy> [<https://perma.cc/UX62-6LMW>].

3. *Id.*

4. See, e.g., Sheelah Kolhatkar, *The Economist Who Put Stock Buybacks in Washington's Crosshairs*, NEW YORKER (June 20, 2019), <https://www.newyorker.com/business/currency/the-economist-who-put-stock-buybacks-in-washingtons-crosshairs> [<https://perma.cc/8N7P-YRHX>] (discussing Professor William Lazonick's long-standing skepticism toward the shareholder-value model and criticism of stock buybacks). See also Chuck Schumer & Bernie Sanders, *Schumer and Sanders: Limit Corporate Stock Buybacks*, N.Y. TIMES (Feb. 3, 2019), <https://www.nytimes.com/2019/02/03/opinion/chuck-schumer-bernie-sanders.html> [<https://perma.cc/9ZRB-4X54>] (outlining a proposal for reform by setting certain mandatory preconditions for firms); Brown Unveils Major New Legislation to Create 'Worker Dividend,' *Curb Stock Buybacks*, BROWN SENATE (July 31, 2019), <https://www.brown.senate.gov/newsroom/press/release/brown-unveils-major-new-legislation-to-create-worker-dividend-curb-stock-buybacks> [<https://perma.cc/8EXD-7XQG>].

5. See 17 C.F.R. § 240.10b-18 (2005).

6. Lenore Palladino, *The \$1 Trillion Question: New Approaches to Regulating Stock Buybacks*, 36 YALE J. ON REGUL. BULL. 89, 89-90 (2018).

7. *Id.*

8. Theron Mohamed, *5 Reasons Warren Buffett Loves Stock Buybacks, Which US Lawmakers Plan to Suspend for Companies They Bail Out*, INSIDER (Mar. 25, 2020, 02:51 PM), <https://markets.businessinsider.com/news/stocks/warren-buffett-stock->

industry, along with many other publicly traded companies, have requested billions of dollars in relief since the start of the Coronavirus pandemic.⁹ The staggering number of buybacks has some critics calling on Congress to prevent publicly traded companies from conducting stock buybacks as part of any agreement to receive a bailout or significant funding.¹⁰

Although stock buybacks have recently received increasing public criticism, many prominent figures in business have pushed back on the negative reputation associated with repurchase programs. Warren Buffett, chairman and Chief Executive Officer (CEO) of Berkshire Hathaway and a longtime proponent of stock buybacks, has publicly stated that he believes stock buybacks are the best use of corporate cash.¹¹ In 2020, Berkshire Hathaway repurchased a record \$25 billion of its own shares.¹² Widely considered one of the most successful investors in the world, Buffet claims that “American CEOs have an embarrassing record of devoting more company funds to repurchases when prices have risen than when they have tanked.”¹³ In contrast, Buffett says contends that the decision to conduct a buyback for his firm largely depends on the market’s valuation of the company’s stock and whether

buybacks-reasons-loves-face-bailout-ban-coronavirus-2020-3-1029032498
[<https://perma.cc/4YZN-3BXM>].

9. *Id.*

10. Mark Cuban (@mcuban), TWITTER (Mar. 17, 2020, 2:24 PM), <https://twitter.com/mcuban/status/1239980848759349249> [<https://perma.cc/U5SZ-WNJY>] (advocating for Congress to prevent companies receiving bailouts from also conducting buybacks); Alexandria Ocasio-Cortez (@AOC), TWITTER (Mar. 17, 2020, 2:28 PM), <https://twitter.com/aoc/status/1239981917057015809?lang=en> [<https://perma.cc/4A3Q-LZDV>] (calling on Congress to ban stock buybacks for companies bailed out by the 2020 COVID-19 relief package).

11. Eric Rosenbaum, *Warren Buffett Explains the Enduring Power of Stock Buybacks for Long-term Investors*, CNBC (Sept. 1, 2018, 8:00 AM), <https://www.cnbc.com/2018/08/31/warren-buffett-explains-the-enduring-power-of-stock-buybacks.html> [<https://perma.cc/6YRT-M9T9>].

12. Theron Mohamed, *Warren Buffett’s Berkshire Hathaway has Likely Poured \$5 Billion into Stock Buybacks This Year*, INSIDER (Mar. 16, 2021, 11:33 AM), <https://markets.businessinsider.com/news/stocks/warren-buffett-berkshire-hathaway-5-billion-stock-buybacks-repurchases02021-3-1030216013> [<https://perma.cc/MWS8-LPS5>].

13. Pippa Stevens, *Buffett is Buying Back More Berkshire Stock This Year After Record \$25 Billion Repurchase in 2020*, CNBC (Feb. 27, 2021, 8:49 AM), <https://www.cnbc.com/2021/02/27/berkshire-hathaway-earnings-q4-2020.html> [<https://perma.cc/MT7G-E9EM>].

he believes it is undervalued.¹⁴ In fact, as former SEC Commissioner Robert Jackson Jr. stated, “[b]asic corporate-finance theory tells us that, when a company announces a stock buyback, it is announcing to the world that it thinks the stock is cheap.”¹⁵

Academics have pushed back on the idea that buybacks prevent companies from investing in their workforce and existing operations.¹⁶ New research conducted by Harvard Law Professor Jesse M. Fried and Harvard Business School Professor Charles C.Y. Wang indicates that research and development (R&D) spending by public firms has hit a record high.¹⁷ Even when using a broader measurement focusing on R&D plus capital expenditures (CAPEX), these record high results remain.¹⁸ Professor Fried contends that these findings are evidence that stock buybacks do not cause the lack of investment in areas like personnel development and compensation.¹⁹

Part I of this Note explores the intensifying debate over the impact of stock buybacks on economic inequality. Part II analyzes regulations currently in place and critically examines proposed reforms. Part III advocates for a reform proposal that more adequately addresses the flaws of the current regulations governing stock repurchase programs by suggesting modifications to the existing regulatory framework rather than the creation of new legislation.

I. THE GROWING DEBATE SURROUNDING BUYBACKS AND ECONOMIC INEQUALITY

With workers’ wages remaining stagnant and corporations receiving large tax cuts, critics have argued that stock buybacks worsen

14. *Id.*

15. Robert J. Jackson Jr., Comm’r, Sec. & Exch. Comm’n, Keynote Address at the Center for American Progress: Stock Buybacks and Corporate Cashouts (June 11, 2018) (addressing stock buybacks and calling for an open comment period to reexamine the SEC’s current rules concerning share repurchase plans with the aim to protect employees, investors, and communities in light of the recent trend towards record numbers of buybacks).

16. Julia Hanna, *What’s the Deal with Stock Buybacks?*, HARV. L. TODAY (Feb. 19, 2019), <https://today.law.harvard.edu/whats-the-deal-with-stock-buybacks/> [<https://perma.cc/5EGU-LQ85>].

17. *Id.*

18. *Id.*

19. *Id.*

economic inequality.²⁰ These detractors' appeals to curtail buybacks have become more urgent in recent years due to the increasing frequency and magnitude of buyback programs by publicly traded corporations. However, some commentators have pushed back on the correlation between buybacks and economic inequality.²¹ Many proponents of buybacks believe that overly broad reforms would interfere with legitimate uses of such programs.²² The following subsections distill several arguments that have shaped the debate between proponents and critics of buybacks.

A. JUSTIFICATIONS FOR STOCK BUYBACKS

Many commentators believe that the corporate law principle of "shareholder primacy" is a driving force of the decision to repurchase shares.²³ This concept, popularized by American economist Milton Friedman, centers around the notion that shareholders have a "priority interest in both economics and governance of the corporation."²⁴ Stemming from this "priority interest" is the motivation for corporate boards of directors to take actions that maximize shareholder wealth.²⁵ With the shareholder primacy motivation in mind, corporations will decide to conduct buybacks to "juice share prices as much as possible."²⁶ This practice has critics sounding the alarm about the resulting externalities, potential for market manipulation, and regulatory issues surrounding buybacks.²⁷ In addition to the influence of shareholder primacy, corporations have several other legitimate reasons for conducting buybacks.

First, corporate management will elect to conduct buybacks as an alternative way to distribute cash that would have otherwise been paid

20. Schumer & Sanders, *supra* note 4.

21. *See infra* Section I.C.

22. *Id.*

23. Palladino, *supra* note 6, at 91.

24. Robert Rhee, *A Legal Theory of Shareholder Primacy*, 122 MINN. L. REV. 1951, 1951 (2018).

25. *Id.* at 1952.

26. Lenore Palladino, *End Shareholder Primacy Once and For All*, BOS. REV. (Mar. 30, 2020), <https://bostonreview.net/class-inequality/lenore-palladino-end-shareholder-primacy-once-and-all> [<https://perma.cc/WE8Z-UM44>].

27. *Id.*

as dividends.²⁸ This approach is preferred to paying dividends because continuing shareholders will receive a tax advantage.²⁹ Under federal tax law, dividends are immediately taxed at ordinary income tax rates.³⁰ On the other hand, buybacks allow shareholders to defer taxes because they can choose to hold onto their shares and avoid capital gains rates.³¹ Moreover, because distributing dividends typically causes the stock price to decline, buybacks are thought to be more desirable because they effectively prevent the devaluation of employee stock options.³²

Second, a firm may decide to repurchase its shares to “reduce the amount of free cash flow at management’s disposal.”³³ This justification is based on the “free cash flow” hypothesis first advanced by economist Michael Jensen in 1988.³⁴ Jensen’s hypothesis states that “managers endowed with free cash will invest it in negative net present value (NPV) projects rather than pay it out to shareholders.”³⁵ As it relates to buybacks, this is thought to be an indicator that a company believes it has fewer growth opportunities and that repurchases will ultimately lead to a better return on investment.³⁶

B. CRITICS CLAIM ULTERIOR MOTIVES INFLUENCE CORPORATE DECISIONS TO CONDUCT BUYBACKS

A key component of the critics’ economic inequality argument focuses on those who stand to benefit from buyback programs: short-term investors and executive compensation recipients. Academics have suggested short-term shareholders benefit the most from stock

28. COMM. ON CAP. MKTS. REGUL., SHORT-TERMISM, SHAREHOLDER ACTIVISM AND STOCK BUYBACKS 31 (2020), <https://www.capmksreg.org/wp-content/uploads/2020/04/Short-termism-04.08.2020-1.pdf> [<https://perma.cc/38M8-7PGD>] [hereinafter SHORT-TERMISM REPORT].

29. *Id.*

30. *See* 26 U.S.C. § 1(h)(11).

31. SHORT-TERMISM REPORT, *supra* note 28.

32. *Id.*

33. Gustavo Grullon & Roni Michaely, *The Information Content of Share Repurchase Programs*, 59 J. FIN. 651, 652 (2004).

34. Larry H. P. Lang et al., *A Test of the Free Cash Flow Hypothesis: The Case of Bidder Returns*, 29 J. FIN. ECON. 315, 315 (1991).

35. *Id.*

36. Grullon & Michaely, *supra* note 33.

buybacks.³⁷ When a company repurchases its shares in the open market, the total number of outstanding shares shrinks and the value of the remaining shares rises.³⁸ Short-term shareholders are primarily concerned with receiving a return on their investment following a rise in share prices.³⁹ In contrast, long-term shareholders are primarily concerned with the company's future and prefer to see excess capital spent on investments that will provide sustained growth for the company.⁴⁰ Critics argue that buybacks reduce the amount of cash available for long-term growth investments in the company's operations and personnel.⁴¹ Without investment in long-term growth opportunities, they contend that economic inequality has worsened.⁴²

Rather than investing in innovation, employee compensation, or the development of company personnel, profits used for share repurchases benefit a small number of executives, insiders, and short-term investors, who often sell their shares after the buyback takes place and the stock price has risen.⁴³

The other area of concern is that executive compensation is increasingly tied to stock-based instruments.⁴⁴ By making the decision to dedicate massive amounts of corporate resources to buybacks, critics question whether the underlying motivations for increasing buybacks are purely self-serving.⁴⁵ In 2015, the 500 highest-paid U.S. executives

37. See, e.g., William Lazonick, *Profits Without Prosperity*, HARV. BUS. REV., (Sept. 2014), <https://hbr.org/2014/09/profits-without-prosperity?registration=success> [<https://perma.cc/8B2V-SFCC>].

38. *Id.* at 27; Banton, *supra* note 1.

39. SHORT-TERMISM REPORT, *supra* note 28, at 7.

40. See generally David A. Katz & Laura McIntosh, *The Long Term, The Short Term, and The Strategic Term*, HARV. L. SCH. F. ON CORP. GOVERNANCE (2019), <https://corpgov.law.harvard.edu/2019/09/27/the-long-term-the-short-term-and-the-strategic-term/> [<https://perma.cc/S7S8-PDM8>].

41. Palladino, *supra* note 6, at 92. Cf. SHORT-TERMISM REPORT, *supra* note 28 (citing data that “indicates stock buybacks have not depleted public companies of their resources available for investment in long-term growth, but rather public companies simply ‘have more capital than they need for the investment opportunities available’”).

42. See sources cited *supra* note 4.

43. See Jackson Jr., *supra* note 15.

44. WILLIAM T. ALLEN & REINIER KRAAKMAN, COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATION 348 (Erwin Chemerinsky et al. eds., 5th ed. 2016).

45. See Lazonick, *supra* note 37.

received, on average, \$32.6 million each.⁴⁶ The breakdown of executive compensation in the proxy statements revealed that on average 46 percent of their compensation was tied to stock options and 36 percent was from stock awards.⁴⁷ With more than 80 percent of total executive compensation linked to stock-based instruments, executives have a personal motivation to boost stock prices by conducting buybacks.⁴⁸

Ironically, the movement towards stock-based compensation emerged from public outrage over CEO pay in the 1990s.⁴⁹ In response, Congress passed § 162(m) of the Internal Revenue Code, which states that “compensation above \$1 million for the CEO and any of the other four top officers would not be deductible to the corporation for income tax purposes unless it was ‘performance-based compensation.’”⁵⁰

At the time, these changes were thought to better “align the interests of corporate management with shareholders.”⁵¹ However, studies have found that stock-based executive compensation has proven to be “a powerful incentive for senior management to manipulate their company’s stock price by allocating corporate resources to massive repurchases of the company’s own outstanding shares.”⁵²

When a firm’s stock price rises after a buyback, companies can hit earnings per share (EPS) targets, which can impact executive compensation.⁵³ Studies have shown “that the likelihood and magnitude of repurchases increase when the bonus of the [CEO] is directly tied to [EPS].”⁵⁴ This enhances the concern that “executives might have an incentive to buy back shares simply to trigger a bonus, which . . . enriches them at public investors’ expense.”⁵⁵

46. William Lazonick, *The Value-Extracting CEO: How Executive Stock Based Pay Undermines Investment in Productive Capabilities* 5 (Inst. for New Econ. Thinking, Working Paper No. 54 2016).

47. *Id.*

48. *Id.* at 23.

49. See ALLEN & KRAAKMAN, *supra* note 44, at 347-48.

50. *Id.*

51. Lenore Palladino, *Do Corporate Insiders Use Stock Buybacks for Personal Gain?* 11 (Roosevelt Inst., Working Paper, 2019).

52. Matt Hopkins & William Lazonick, *The Mismeasure of Mammon: Uses and Abuses of Executive Pay Data* 8-9 (Inst. for New Econ. Thinking, Working Paper No. 49, 2016).

53. See ALLEN & KRAAKMAN, *supra* note 44.

54. Heitor Almeida et al., *The Real Effects of Share Repurchases*, 119 J. FIN. ECON. 168, 178 (2016).

55. *Examining Corporate Priorities: The Impact of Stock Buybacks on Workers, Communities, and Investment: Hearing Before the Subcomm. on Inv. Prot.*,

C. PUSHBACK ON THE CONNECTION BETWEEN BUYBACKS AND ECONOMIC
INEQUALITY

In a 2018 study, Professors Fried and Wang found little evidence to suggest that buybacks deprive firms of capital that would “otherwise [be used] for investment and paying workers.”⁵⁶ In particular, the professors’ research addresses the ratio of dividends and stock repurchases to net income, which was 96 percent between 2007 and 2016.⁵⁷ The professors contend that this metric, which is often cited by critics, is a poor indicator of negative outcomes associated with stock buybacks because it fails to account for “two important factors.”⁵⁸

First, capital that is distributed by S&P 500 firms is eventually returned to the firms, directly or indirectly.⁵⁹ For example, the firm will repurchase stock from shareholders and then issue new stock to be sold directly to investors.⁶⁰ In addition, companies can grant equity to employees who can then sell those shares to other investors.⁶¹

Second, the professors argue that net income should not be used as a metric of income that is available for investment “because it measures what’s left after R&D investments and many other future-oriented expenditures have already been deducted.”⁶² Instead, to reflect the flow of capital more accurately, the professors believe a better measure would place the sum of R&D and net income in the denominator of the ratio.⁶³ When examining the same data above from 2007 to 2016 and using this R&D adjusted net income, the ratio yields only 41 percent of net shareholder payouts.⁶⁴

In addition, Professors Fried and Wang claim that the data from 2007-2016 demonstrates that shareholders receiving payouts from S&P

Entrepreneurship, & Cap. Mkts & H. Comm. on Fin. Servs., 116th Cong. 9 (2019) (statement of Jesse Fried, Professor, Harvard Law School).

56. Jesse M. Fried & Charles C.Y. Wang, *Are Buybacks Really Shortchanging Investment?*, HARV. BUS. REV. (Mar.-Apr. 2018), <https://hbr.org/2018/03/are-buybacks-really-shortchanging-investment> [<https://perma.cc/HVV3-BAN9>].

57. *Id.*

58. *Id.*

59. *Id.*

60. *Id.*

61. *Id.*

62. *Id.*

63. *Id.*

64. *Id.*

500 firms (e.g., buybacks and dividends) reinvest in productive uses.⁶⁵ Throughout each year of this period, Non-S&P 500 firms reported “net shareholder inflows (that is, negative net shareholder payouts).”⁶⁶ This data suggests that non-S&P 500 public firms “were absorbing some of the net shareholder payouts by S&P 500 firms, to fuel investment, innovation, and job creation.”⁶⁷

II. CURRENT REGULATORY FRAMEWORK AND PROPOSED REFORM

Over the years, a variety of reform proposals have been introduced to address concerns surrounding stock buybacks.⁶⁸ These proposals consider modifications to current disclosure regulations, repeals of current SEC Rules, and the introduction of new legislation.⁶⁹ This Part begins with an overview of the current regulatory framework. The Subsections that follow provide an overview of several recent proposals that represent a variety of approaches aimed at resolving the key concerns of stock buyback critics. When examining these reform efforts, it is important to assess whether the proposal can balance legitimate uses of buybacks with the need to curb abuses.

A. CURRENT REGULATORY FRAMEWORK

Current regulations governing stock buybacks involve three types of rules: “(i) disclosure requirements, (ii) prohibitions on market manipulation, coupled with SEC Rule 10b-18’s safe harbor for buybacks that meet certain conditions and (iii) SEC Rule 10b-5’s prohibition on insider trading.”⁷⁰

65. *Id.*

66. *Id.*

67. *Id.*

68. *See infra* Section II.B-D.

69. *Id.*

70. JAY B. SYKES, CONG. RSCH. SERV., STOCK BUYBACKS: BACKGROUND AND REFORM PROPOSALS 3 (2019), <https://fas.org/sgp/crs/misc/LSB10266.pdf> [<https://perma.cc/9BAN-E5BH>].

1. Disclosure Requirements

At the end of 2003, the SEC adopted amendments to Rule 10b-18 under the 34 Act.⁷¹ These amendments mandated periodic disclosure of:

the total number of shares repurchased during the past quarter, the average price paid per share, the number of shares that were purchased as part of a publicly announced repurchase plan, and the maximum number (or approximate dollar value) of shares that may yet be purchased under the plans or programs.⁷²

In adopting these amendments, the SEC intended to increase transparency of issuer repurchases.⁷³ However, as will be discussed later in this Note, these “retrospective” disclosures have placed investors at an informational disadvantage.⁷⁴ Firms that repurchase their “own shares on the open market [are] not subject to Section 16(a)’s two-day disclosure requirement; that requirement applies only to firm insiders, not the firm itself.”⁷⁵ As such, investors would only learn the specific details of buyback programs several months after its initiation.⁷⁶

2. Market Manipulation and Rule 10b-18

As discussed in Part I, the repurchasing of shares by a company can have the effect of raising the stock’s price.⁷⁷ Recognizing the difficulty of fitting stock buyback programs into the definition of market manipulation, the SEC decided to adopt Rule 10b-18.⁷⁸ This legal “safe harbor” gives companies conducting repurchase programs protection from market manipulation liability, provided that they meet certain conditions.⁷⁹

71. Regulation of Purchase of Certain Equity Securities by the Issuer and Others, Exchange Act Release No. 33-8335 (Nov. 10, 2003), https://www.sec.gov/rules/final/33-8335.htm#P239_85172 [<https://perma.cc/5H2S-TBY4>].

72. *Id.*

73. *Id.*

74. See SYKES, *supra* note 70.

75. Jesse M. Fried, *Insider Trading Via the Corporation*, 162 U. PA. L. REV. 801, 814 (2014). See also *infra* Part III.

76. *Id.* at 829.

77. See SHORT-TERMISM REPORT *supra* note 28.

78. See SYKES, *supra* note 70.

79. *Id.*

Rule 10b-18's stipulations mandate companies: (1) to purchase the shares from one broker or dealer on any single day; and to comply with (2) various timing requirements; (3) purchase price limitations; and (4) volume restrictions.⁸⁰ However, between Rule 10b-18 being a "voluntary safe harbor" and the difficulty associated with the data analysis necessary to investigate issuer stock repurchases, the SEC has rarely enforced Rule 10b-18.⁸¹

3. SEC Rule 10b-5: Insider Trading

Despite the safe harbor provided by Rule 10b-18, companies can still be held liable for insider trading when conducting stock buybacks.⁸² Rule 10b-5 of the 34 Act prohibits parties from trading securities using material non-public information.⁸³ However, in the context of stock buybacks, it is extremely difficult to detect and enforce trading that incorporates information that could meet "the courts' high materiality threshold."⁸⁴ As previously discussed, the Rule 10b-18 disclosure regulations adopted in 2003 do not require companies repurchasing shares to disclose details about individual transactions.⁸⁵ Post 2003, firms were only required to report the price of each share and total number of buybacks in its quarterly filed Form 10-K.⁸⁶ The inability to track details beyond these broad disclosures "makes it difficult to determine whether a particular trade was illegal because the firm possessed material inside information at the time of the transaction."⁸⁷

B. THE LEGISLATION REFORM PROPOSAL OF U.S. SENATORS BERNIE SANDERS AND CHARLES SCHUMER

In February 2019, U.S. Senators Bernie Sanders (D-VT) and Charles Schumer (D-NY) announced plans to reform stock buyback

80. 17 C.F.R. § 240.10b-18 (2021).

81. Palladino, *supra* note 6, at 101.

82. See Mark J. Loewenstein & William K.S. Wang, *The Corporation as Insider Trader*, 30 DEL. J. CORP. L. 45, 70-72 (2005).

83. 17 C.F.R. § 240.10b-5 (2000).

84. Fried, *supra* note 75, at 814.

85. See *supra* Section II.A.1.

86. Fried, *supra* note 75, at 815.

87. *Id.*

regulation in a New York Times opinion piece.⁸⁸ Although the proposed legislation (“S&S Proposal”) has not been officially released to date, the Senators outlined its objectives.⁸⁹ Importantly, the bill would prohibit a company from making open-market stock buybacks unless it “invests in workers and communities first, including things like paying all workers at least \$15 an hour, providing seven days of paid sick leave, and offering decent pensions and more reliable health benefits.”⁹⁰

These preconditions to conducting buybacks are designed to provide incentives for long-term growth investments that benefit both workers and the company.⁹¹ Opponents of the S&S Proposal claim that the Senators fail to understand the economic reasons for conducting buybacks and are attempting to use the issue to gain political points with supporters.⁹²

Moreover, critics of the S&S Proposal contend that buybacks represent an example of the “multiplier effect.”⁹³ This means that “every time there is an increase in spending, it produces an increase in national income and consumption greater than the initial amount spent.”⁹⁴ These objectors further claim that the money used to repurchase shares ultimately ends up benefiting Americans because investors reinvest the proceeds gained from the buyback into an array of investment opportunities which can benefit the country as a whole.⁹⁵ For example, these investors can use the proceeds from buybacks to invest in initial public offerings, purchase U.S. Treasury Bonds, corporate or municipal securities, or support homeownership in America by purchasing mortgage-backed securities.⁹⁶ Similar to the arguments posed by professors Fried and Wang in Part I of this Note, this reallocation of

88. See Schumer & Sanders, *supra* note 4.

89. *Id.*

90. *Id.*

91. *Id.*

92. Liz Moyer, *Chuck Schumer and Bernie Sanders Call for Restricting Corporate Share Buybacks*, CNBC (Feb. 4, 2019, 2:29 PM), <https://www.cnbc.com/2019/02/04/senate-democrats-call-for-restricting-corporate-share-buy-backs.html> [<https://perma.cc/73HD-7CC5>].

93. Richard E. Thornburgh, *Here's Why Sens. Schumer and Sanders are Wrong on Stock Buybacks*, CNBC (May 15, 2019, 3:57 PM), <https://www.cnbc.com/2019/05/14/heres-why-sens-schumer-and-sanders-are-wrong-on-stock-buybacks.html> [<https://perma.cc/KA4S-U9S7>].

94. *Id.*

95. *Id.* See also *supra* Section I.C.

96. *Id.*

capital provides opportunities for job creation, funding of essential government services, and innovation.⁹⁷ This criticism is further supported by the fact that a large majority of adults from ages 30 to 64 own shares of stock and are benefited by the increase in stock prices that result from buybacks.⁹⁸

Despite the pushback from opposition, Senators Sanders and Schumer present a new take on buyback reform by requiring the corporation to consider workers' interests in the decision to initiate a stock buyback. The S&S Proposal represents an effort to provide a balanced solution which aims to allow for the continued existence of buyback programs while also seeking to mitigate concerns related to economic inequality. However, the S&S Proposal will likely face significant obstacles to become enacted because the means (conditional requirements) employed to achieve its ends effectively usurps the decision-making power from the corporation acting on behalf of its shareholders' interests.⁹⁹ As will be discussed in Part III of this Note, there are existing regulations in place that could be modified to strike a balance between both interests without unreasonably encroaching into the discretion that publicly traded companies have in making business decisions.¹⁰⁰

C. THE REWARD WORK ACT

The Reward Work Act ("RW Act"), first introduced in March 2018 and reintroduced in March of 2019 by Senator Tammy Baldwin (D-WI) is prospective legislation that would "ban open market stock buybacks that overwhelmingly benefit executives and activist hedge funds at the expense of workers and retirement savers."¹⁰¹ Senator Baldwin has released a staff report ("RW Act Report") that outlines the economic benefits that the bill would aim to achieve, namely, "higher wages,

97. *Id.* See also *supra* Section I.C.

98. *Id.*

99. Thornburgh *supra* note 93 (emphasizing that investors often demand buybacks when investment opportunities are limited).

100. See *infra* Part III.

101. Press Release, Office of Senator Tammy Baldwin, U.S. Senator Tammy Baldwin Reintroduces Legislation to Rein in Stock Buybacks and Give Workers a Voice on Corporate Boards (Mar. 27, 2019), <https://www.baldwin.senate.gov/press-releases/reward-work-act-2019> [<https://perma.cc/YW6F-65BS>].

improved firm performance, increased investment, less offshoring, lower income inequality, and greater socioeconomic opportunity.”¹⁰²

The RW Act proposes three major policy reforms. First, the bill would mandate that workers be given a one-third representation on the board of directors.¹⁰³ The RW Act Report cites a 2006 research study of German corporate governance which concluded that greater levels of worker participation on corporate boards of directors improved firm performance and shareholder wealth.¹⁰⁴ Second, the bill would ban open-market stock buybacks.¹⁰⁵ The Senator claims that many companies conducting repurchase programs have been funding them by taking on significant amounts of debt in order to fund such programs.¹⁰⁶ This benefits investors with short term goals, but leaves long-term investors, typically workers saving for retirement, with all the risk should the company go bankrupt.¹⁰⁷ Third, the bill proposes a repeal of Rule 10b-18.¹⁰⁸ Senator Baldwin contends that the SEC’s steadfast refusal to study the buyback phenomenon, coupled with its reluctance to admit that Rule 10b-18 has caused an increase in buybacks, are indications that it is incumbent upon Congress to take action.¹⁰⁹

The RW Act promotes bold reforms to current regulations governing stock buybacks. Requirements for employee representation on corporate boards could add a layer of protection for worker interests when the decision to conduct a repurchase program is being debated. However, prohibitions on open-market repurchase programs forego considerations of legitimate uses of the practice, such as when all other

102. OFF. OF SENATOR TAMMY BALDWIN, REWARD WORK NOT WEALTH 29 (2018), <https://www.baldwin.senate.gov/imo/media/doc/Reward%20Work%20Not%20Wealth%20Baldwin%20Staff%20Report%203.26.19.pdf> [<https://perma.cc/85BJ-HJUD>].

103. *Id.*

104. *Id.*

105. *Id.*

106. *Id.*

107. *Id.*

108. *Id.*

109. *Id.* See also SEC, Purchases of Certain Equity Securities by the Issuer and Others, 45 Fed. Reg. 70890, 70892 (Oct. 27, 1980), <https://www.sec.gov/rules/petitions/2019/petn4-746.pdf> [<https://perma.cc/8XTB-JT4K>] (following the 2018 corporate tax cuts implemented by the Trump Administration, a group of petitioners called on the SEC to make changes to Rule 10b-18. The petition claims that Rule 10b-18 has failed in its intended purpose which was designed to limit the ability of a firm to “manipulate its stock price and volume”).

corporate investment opportunities have been exhausted or where the company decides that the market is undervaluing their stock price.¹¹⁰

Undeniably, Rule 10b-18 has fallen short of its intended purpose.¹¹¹ The SEC's original objective for Rule 10b-18 was to "prevent abusive purchases designed to support the price of the issuer's securities to assist insider[s] in disposing of their holdings at or above the pegged price."¹¹² Practically speaking, Rule 10b-18 has failed to achieve this goal.¹¹³

In reality, there have been a record number of stock buybacks, as well as an increasing amount of insiders selling company stock during buyback programs.¹¹⁴ Interestingly, a study conducted by SEC researchers found that in a 15-month period between 2017 and 2018, at least 500 insiders sold company stock at the same time that their own company was conducting repurchase programs.¹¹⁵ This study also discovered that insiders were "twice as likely to sell on the days following buyback announcements as they were in the days leading up to announcements."¹¹⁶ The insiders' "average sale was also five times larger than before the announcements, at about \$500,000."¹¹⁷

On its face, the SEC's research appears to have uncovered evidence of efforts to increase stock prices artificially, the type of behavior that Rule 10b-18 was designed to prevent. Companies that announce a board's approval of a decision to conduct stock buybacks are not actually required to follow through with that publicized plan.¹¹⁸ When a

110. Alex Edmans, *The Case for Stock Buybacks*, HARV. BUS. REV. (Sept. 15, 2017), <https://hbr.org/2017/09/the-case-for-stock-buybacks> [<https://perma.cc/L9FS-E9DC>].

111. Palladino, *supra* note 51, at 10.

112. *Id.*

113. See SHORT-TERMISM REPORT, *supra* note 28 (finding that executives are "twice as likely to sell shares in the eight days following a buyback program announcement compared to an ordinary trading day").

114. Palladino, *supra* note 51. See also Gary Putka, *Company Insiders Are Selling Stock During Buyback Program and Making Additional Profits When Stock Prices Jump. And it's Legal.*, WASH. POST (Nov. 6, 2019), https://www.washingtonpost.com/business/economy/company-insiders-are-selling-stock-during-buyback-programs-and-making-additional-profits-when-stock-prices-jump-and-its-legal/2019/11/06/fc592f58-e493-11e9-a331-2df12d56a80b_story.html [<https://perma.cc/VV2V-GLEM>].

115. Putka, *supra* note 114 (noting that 50 of the 500 insiders selling stock during that period were chief executives of their company); Jackson Jr., *supra* note 15.

116. Putka, *supra* note 114. See also Jackson Jr., *supra* note 15.

117. Putka, *supra* note 114.

118. *Examining Corporate Priorities: The Impact of Stock Buybacks on Workers, Communities, and Investment: Hearing Before the Subcomm. on Inv. Prot.*,

buyback announcement is made, a firm signals to the market that the firm believes its stock price is undervalued.¹¹⁹ The market then reacts to these “misleading repurchase announcements” as it would to actual buyback announcements.¹²⁰ The stock prices rise and insiders are essentially able to sell their stock at a price higher than its actual value.¹²¹

Misleading repurchase announcements appear to be a form of market manipulation and indirect insider trading. However, under current law, these actions are all legal, provided that insiders file prearranged trading plans before selling their shares.¹²² By creating a “trading plan,” insiders can shield themselves from liability for insider trading violations.¹²³

D. THE STOCK BUYBACK REFORM AND WORKER DIVIDEND ACT OF 2019

Another option is the stock buyback reform proposal by U.S. Senator Sherrod Brown (D-OH).¹²⁴ The key feature of The Stock Buyback Reform and Worker Dividend Act of 2019 (“Worker Dividend Act”) would “[r]equire public companies to issue a worker dividend to all non-executive workers based on the total amount spent on stock buybacks, dividend increase, and special dividends.”¹²⁵ Importantly, for this Note, the “worker dividend” would be “equal to \$1 for every \$1 million spent on stock buybacks.”¹²⁶ Firms that violate the worker dividend requirement would be subject to a five-year moratorium on stock buybacks, and employees would be given a private right of action.¹²⁷ Other provisions in the bill would seek to limit the amount of stock buybacks companies make, increase reporting requirements, and

Entrepreneurship, & Cap. Mkts & H. Comm. on Fin. Servs., 116th Cong. 6 (2019) (statement of Jesse Fried, Professor, Harvard Law School).

119. *Id.*

120. *Id.*

121. *Id.*

122. Putka, *supra* note 114. *See also* 17 C.F.R. § 240.10b5-1 (1951).

123. Putka, *supra* note 114.

124. *See* BROWN SENATE, *supra* note 4.

125. *Id.*

126. *Id.*

127. *Id.*

convert Rule 10b-18 into a mandatory prohibition on excessive stock buyback activities.¹²⁸

Unlike other proposals, the Worker Dividend Act aims to strengthen employee interests by linking them together with shareholder interests. However, similar to the S&S Proposal, the Worker Dividend Act takes the decision of capital allocation out of the corporation's hands by requiring dividends that may not be in the firm's best interests.¹²⁹ Part III will set forth a solution that will increase disclosure requirements to protect public investors but also allow companies to have the latitude to make legitimate business decisions concerning buybacks.

E. SHARE REPURCHASE DISCLOSURE MODERNIZATION

On December 15, 2021, the SEC proposed a new disclosure rule under the 34 Act as part of its Share Repurchase Disclosure Modernization ("SRDM") effort which aims to increase transparency for investors by requiring more timely filings when companies engage in stock buybacks. The proposed rule would require issuers to report "any purchase made by or on behalf of the issuer or any affiliated purchaser of shares or other units of any class of the issuer's equity securities that is registered by the issuer pursuant to Exchange Act Section 12."¹³⁰ Importantly, this Rule would require the issuer to file a Form SR before the end of the first business day following the day that the issuer executes a share repurchase.¹³¹

If the proposed Rule is adopted, it would require several disclosures for each class of securities purchased:

- (1) Identification of the class of securities purchased;
- (2) The total number of shares (or units) purchased, including all issuer repurchases whether or not made pursuant to publicly announced plans or programs;
- (3) The average price paid per share (or unit);
- (4) The aggregate total number of shares (or units) purchased on the open market;
- (5) The aggregate total number of shares (or units) purchase

128. *Id.*

129. Schumer & Sanders, *supra* note 4.

130. Share Repurchase Disclosure Modernization, (proposed Dec. 15, 2021) (to be codified at 17 C.F.R. pts. 229, 232, 240, 249, and 274).

131. *Id.*

pursuant to a plan that is intended to satisfy the affirmative defense conditions of Rule 10b5-1(c).¹³²

In addition, the proposed rule would revise and expand the current periodic disclosure requirements in Item 703 of Regulation S-K (including the quarterly Form 10-K and Form 10Q). This would require issuers to disclose the objective or rationale behind the share repurchases and the structure of an issuer's repurchase program.

Notably, under this new rule, the Commission would require an issuer to indicate whether any officer or director purchased or sold shares that are part of the repurchase plan within 10 business days before or after the announcement of the repurchase plan.¹³³ Coinciding with this, the SEC will require issuers to disclose "any policies and procedures relating to the purchase and sales of the issuer's securities by its officers and directors during a repurchase program."¹³⁴

This proposed rule, through its more detailed and timely filing requirements, has the potential to enhance transparency for investors without prescribing conditions by which companies may elect to engage in share repurchases.¹³⁵ In addition, the proposed rule's requirement for officers and directors to disclose within 10 business days any transactions of securities after a buyback's initiation aims disincentivize self-serving motivations for initiating buybacks.¹³⁶

III. MODIFICATIONS TO EXISTING REGULATORY FRAMEWORKS: A PATHWAY TOWARDS A BALANCED APPROACH TO REFORM

As previously discussed, critics of stock buybacks point to issues such as a lack of transparency, self-interested motivations, and short-termism to explain why workers are not receiving greater development opportunities and compensation.¹³⁷ However, many proposals designed to reform the regulations governing stock buybacks effectively strip corporations of the discretion typically afforded to boards of directors to

132. *Id.*

133. *Id.* at 33.

134. *Id.*

135. Press Release, Securities and Exchange Commission, SEC Proposes New Share Repurchase Disclosure Rules (Dec. 15, 2021) (on file with author).

136. *See supra* Part I.

137. *See supra* note 4. *See also* SEC Purchases of Certain Equity Securities by the Issuer and Others, 45 Fed. Reg. 70890, 70892 (Oct. 27, 1980).

make legitimate business decisions concerning share repurchase programs.¹³⁸ In order to succeed, a new approach must delicately balance the interests of all involved parties in order to garner enough support.

Thus, a primary consideration for future reform proposals must be the feasibility of obtaining support for its enactment in Congress. As it stands, the correlation between stock repurchase programs and economic inequality is tenuous and fraught with disagreement.¹³⁹ For example, critics argue that economic inequality is worsened when corporations spend surplus capital on buybacks instead of long-term investment opportunities that could be used for the benefit of workers.¹⁴⁰ This argument fails to account for the possibility that corporations have already undertaken all of the long-term investment opportunities available to the corporation.¹⁴¹ Overly broad regulation can hinder corporate boards in situations where it has determined that growth opportunities are not favorable.¹⁴² Some proponents of buybacks have argued that “[i]t is the exhaustion of a firm’s investment opportunities that lead [sic] to buybacks, rather than buybacks causing investment cuts.”¹⁴³ Proposals which lack mechanisms that account for such scenarios can be detrimental to shareholders’ interests.

The intensifying debate over the effects of stock buybacks on economic inequality heightens the need for reform of current regulations governing the practice. Reform must strike a balance by addressing key concerns of critics while also permitting corporate boards to make legitimate business decisions. Instead of tethering the need for reform to “economic inequality,” the impetus for reform should aim to counteract the informational asymmetries between investors and corporate insiders.¹⁴⁴ The debate concerning economic inequality and stock buybacks is rife with political disagreement due to the tenuous

138. See Edmans, *supra* note 110 (discussing how critics of stock buybacks overlook the larger point, which is that firms first allocate funds for long-term investment based on whether those opportunities are available and then “[i]f they have spare cash left over . . . they may use it for buybacks”; Importantly, surplus capital “is by definition, capital left over after all productive investments have been made”).

139. See generally Fried & Wang, *supra* note 56 (discussing the conclusion of a study which tends to weaken stock buybacks impact on economic inequality).

140. See Edmans, *supra* note 110.

141. *Id.*

142. *Id.*

143. *Id.*

144. See *supra* note 135.

connection between two and could ultimately jeopardize the success of any burgeoning proposal.¹⁴⁵

Rather than drastic legislative reforms, existing SEC disclosure requirements can be modified to better serve investors and stakeholders alike. In fact, the SEC has historically shown a willingness to make modifications to stock buyback rules on two separate occasions in the last two decades. In 2003, the commission changed retrospective disclosures that companies were required to file.¹⁴⁶ Those regulations required companies that engaged in repurchase programs to disclose in their quarterly public filings:

- (1) The total number of shares repurchased during the previous quarter;
- (2) The average price paid for those shares;
- (3) The number of shares repurchased during the previous quarter as part of a publicly announced repurchase plan, and;
- (4) The maximum number (or approximate dollar value) of shares that may yet be purchased under the plan.¹⁴⁷

Although these disclosure requirements were a step in the right direction, they are only retrospective and, therefore, do not require companies to disclose prospective details concerning the “volume or expiration date of buyback programs.”¹⁴⁸ Without these prospective disclosures, investors are typically unable to acquire the details of these repurchase programs until many months after a program has already begun, at which point, it is too late.¹⁴⁹ This flaw has not gone unnoticed, as the SEC’s December 2021 SRDM proposed rule change, which was discussed in Part II, aims to provide aims to provide more timely disclosure by instituting a “next business day” requirement following execution of a buyback and a 10 business day disclosure requirement for

145. Mark Kolakowski, *5 Reasons Goldman Says Banning Buybacks Is Bad For Stocks*, INVESTOPEDIA (Apr. 08, 2019), <https://www.investopedia.com/5-reasons-goldman-says-banning-buybacks-is-bad-for-stocks-4684101> [https://perma.cc/652P-6C5T].

146. SYKES, *supra* note 70.

147. *Id.* at 2-3.

148. *Id.*

149. *Id.*

director and officer transactions associated with the repurchase plan.¹⁵⁰ These changes are designed to close the informational gap between investors and insiders.¹⁵¹ However, the SEC's December 2021 proposed rule change still fails to remedy several key issues that place investors at an informational disadvantage.

In particular, the 2021 proposed rule fails to address the problems surrounding buyback announcements. Although companies that do not voluntarily announce a share repurchase program are required under Item 703 to disclose the date that each repurchase plan or program was announced, such announcements do not provide investors with sufficient details about the buybacks.¹⁵² Notably, these communications are not required to provide the "number or dollar amount of shares to be repurchased. Nor must the firm indicate the expiration date of its buyback program."¹⁵³ These details would provide investors with crucial information to make reasonable decisions about whether to invest in the stock and prevent the potential to be misled by self-interested insiders.

Currently, SEC regulations require companies to file Form 8-K when certain material corporate events occur.¹⁵⁴ The purpose of filing this report is to alert shareholders of the event so that they can make informed decisions on their investment going forward.¹⁵⁵ Importantly, Form 8-K does not require the disclosure of stock repurchases.¹⁵⁶

To improve upon existing disclosures requirements for buyback programs, Section 3.02 of Form 8-K should be modified in several ways. Currently, this Section requires companies to disclose the sales of unregistered shares sold.¹⁵⁷ Notably missing is any requirement to disclose whether the company repurchased shares. Section 3.02 of Form 8-K should be amended to require companies to promptly disclose the details of the shares that they purchased, and the total number of shares purchased. In addition, this amended disclosure should require

150. See *supra* Section II.E.

151. *Id.*

152. Fried, *supra* note 75, at 813. See also NASDAQ RULE 5250(b)(1) (2014) (requiring companies to disclose material information impacting the value of securities).

153. Fried, *supra* note 75, at 813.

154. Form 8-K, SEC, <https://www.sec.gov/files/form8-k.pdf> [<https://perma.cc/D642-D2VZ>].

155. Will Kenton, 8-K (Form 8K), INVESTOPEDIA (Sept. 28, 2020), <https://www.investopedia.com/terms/1/8-k.asp> [<https://perma.cc/6Z56-JPRL>].

156. SHORT-TERMISM REPORT, *supra* note 28.

157. See Form 8-K *supra* note 154.

companies to announce to the public, via press release, the plan to repurchase their shares both before and after the purchase. While many companies already proffer these types of public announcements when conducting repurchase programs, making it a uniform requirement will even the playing field.¹⁵⁸ These proposed modifications to Form 8-K would improve the timeliness of alerting investors to an activity that can impact a firm's stock price. It would also be an improvement from the quarterly disclosure requirements adopted in 2003 concerning repurchases in Forms 10Q and 10K.¹⁵⁹ Additionally, more detailed, prompt, and transparent disclosures of these programs could discourage corporate insiders from selling stock following the announcement of a buyback program. Moreover, requiring further disclosure may ultimately lead to fewer stock buybacks conducted with short-term goals in mind.

Aside from improvements to the requirements of Form 8-K, this Note argues that the SEC should adopt Professor Fried's "Two-Day Disclosure Rule."¹⁶⁰ Currently, Section 16(a) of the 34 Act "requires corporate insiders to provide detailed information about any trade in their firm's shares within two business days."¹⁶¹ However, unlike individual insiders, firms that conduct stock buybacks do not have to disclose their trading activity until many months later.¹⁶² Compounding the issue, these disclosures typically contain less detailed specifics about the trades than individual insiders are required to provide, which has given insiders a way to avoid detection by regulators.¹⁶³

Professor Fried contends that these "lax" trade reporting rules allow insiders to trade indirectly on insider information, resulting in harm to public shareholders.¹⁶⁴ As a result, regulators face difficult obstacles when attempting to detect insider use of buybacks to either boost stock

158. *See id.* (providing companies an opportunity to disclose the approval of repurchase programs, the size of the program, and duration).

159. *See* Purchases of Certain Equity Securities by the Issuer and Others, Release No. 33-8335, 68 FR 64952 (Nov. 10, 2003), 68 FR 64952 (Nov. 17, 2003).

160. *Examining Corporate Priorities: The Impact of Stock Buybacks on Workers, Communities, and Investment: Hearing Before the Subcomm. on Inv. Prot., Entrepreneurship, & Cap. Mkts & H. Comm. on Fin. Servs.*, 116th Cong. 9 (2019) (statement of Jesse Fried, Professor, Harvard Law School).

161. *Id.*

162. *Id.*

163. *Id.*

164. *Id.*

prices to sell their executive stock or to hit the EPS targets contained in their compensation agreements.¹⁶⁵ The SEC's December 2021 proposed rule change would require these insider trades to be disclosed within 10 business days. However, 10 business days may still not provide sufficient notice to investors of an insider transactions associated with a repurchase. To curb the abuse of repurchase programs, firms should be required under Rule 16 "to disclose each trade in its own shares within two business days of the transaction."¹⁶⁶ This proposal strikes a balance by providing public shareholders with greater timeliness, transparency, and accuracy in reporting trades, while also dampening the advantage that corporate insiders have when trading their own stock post-buyback.¹⁶⁷ After the implementation of this proposal, if a pattern of corporate insiders trading stock in close proximity to buybacks emerges, the disclosure requirements can be reduced to one day, same day, or even made to be preemptive.¹⁶⁸ If this were the case, the SEC would need to monitor this type of trading activity and decide if more timely disclosures would be appropriate.

CONCLUSION

The debate concerning stock buybacks and economic inequality has led to calls for reform, but this is not the proper way to frame this issue. Rather than dramatic reform proposals, the issue must be framed around protecting public investors from being misled or taken advantage of. Recent legislative reform proposals by a variety of politicians do not appropriately account for circumstances where corporations have legitimate business purposes for conducting buybacks.

Ultimately, when deciding whether to impose more restrictive regulatory frameworks, there needs to be a balancing of interests. Although broad, sweeping legislative reform proposals would effectively curb the use of stock buybacks, they would fail to cure the principal complaint of critics and hamper good faith corporate decision making.¹⁶⁹ Opponents primarily suggest that buybacks worsen economic

165. *Id.* See also ALLEN & KRAAKMAN, *supra* note 44 (discussing the increased use of stock-based compensation and EPS targets tied to executive compensation).

166. Fried, *supra* note 75, at 834.

167. *Id.*

168. *Id.*

169. See *supra* Part I.

inequalities throughout society.¹⁷⁰ As Professors Fried and Wang's research has shown, the connection between economic inequality and stock buybacks is questionable.¹⁷¹ In reality, the causes of economic inequality are complicated and require a host of legislative and cultural solutions. Issuing blanket prohibitions on buybacks may serve short-term interests by eliminating a mechanism that has been identified as part of the problem. However, because the degree to which buybacks impact economic inequality is unclear, an overcorrection of that perceived issue may cause investors to lose the substantial value that buybacks can provide.¹⁷²

Modifications to existing disclosure regimes, as proposed in this Note, can enhance transparency and eliminate a substantial portion of the informational advantages that corporate insiders have over public investors. Fundamentally, at the core of these approaches is prompt and detailed (1) disclosure of corporate insiders transactions associated with repurchase plans and; (2) information about buyback plans provided to public investors. These enhanced disclosures will disincentivize the abuses of buyback programs and encourage companies to conduct such programs only if they serve a legitimate corporate purpose.

170. *Id.*

171. Fried & Wang, *supra* note 56.

172. *Id.*