

November 6, 2006

## SEC Publishes Best Price Amendments

The SEC has published final rules that modify the “all-holders, best-price” requirements of Exchange Act Rules 14d-10 and 13e-4 (together the “best price rules”) to exempt certain compensation, severance and other employee benefit arrangements and to create a safe harbor for these arrangements.

While the new rules modify the best price rules to clarify that the requirement applies only to consideration paid to shareholders for securities “tendered in a tender offer” as opposed to any consideration paid “during” and “pursuant to” a tender offer as in the old rules, the more significant of the changes are the creation of (i) a specific exemption from the application of the best price rules for certain compensation, severance and employee benefit arrangements and (ii) a related safe harbor for such arrangements that are approved by the compensation committee of the subject company or, where the acquirer (or, for self tenders, an affiliate of the issuer) is a party to the arrangement, by the compensation committee of the acquirer (or affiliate).

### New Exemption to the Best Price Rules

The new exemption provides that the issuer and third party tender offer best price rules will not prohibit the negotiation, execution or amendment of an employment compensation, severance or other employee benefit arrangement, or payments made or to be made or benefits granted or to be granted according to such an arrangement, with respect to any shareholder of the subject company (not just employee or director shareholders), if the amounts payable under the arrangement:

- Are paid or granted as compensation for past services performed, or future services to be performed or to be refrained from performing, by the shareholder; and
- Are not calculated based on the number of securities tendered or to be tendered by the shareholder.

The adopting release clarifies that conditioning an arrangement on a shareholder’s tendering into the tender offer would most likely violate at least one of the prongs of the exemption. However, conditioning an arrangement on the completion or consummation of the tender offer,

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without any requirement for the shareholder to tender into the offer, is acceptable. The adopting release further confirms the SEC's position that the best-price rule does not apply if a shareholder does not tender into an offer. So, for example, if management does not tender into the offer, then the acquirer can make any payments it wishes to management, subject to the tender offer rules' restrictions on purchasing shares outside of an offer.

### **New Safe Harbor**

The final rules also include a non-exclusive safe harbor for the negotiation, execution or amendment of employment-related arrangements if they are approved by the independent members of the compensation committee or a board committee performing similar functions of:

- The subject company, without regard to whether the subject company is a party to the arrangement or not, or
- The acquirer or, for self tenders, the affiliate of the issuer, if the acquirer or affiliate is a party to the arrangement.

The adopting release gave several practice pointers on the implementation of this safe harbor, including the following:

- While the committee must approve the arrangement as an employment compensation, severance or other employee benefit arrangement, the committee does not need specifically to determine that the arrangements meet the two conditions of the exemption in order to rely on the safe harbor.
- The committee must approve each specific arrangement, as opposed to approving plans or programs generally, but nothing prevents the committee from approving multiple specific arrangements or stock grants at the same time.
- A subcommittee of the compensation or other board committee may approve the arrangement so long as the subcommittee is fully independent. For instance, if a member of the compensation committee must recuse himself or herself from the approving vote because of a conflict of interest, the safe harbor is still available.
- Approval must be received before the consideration is paid in order to qualify for the safe harbor.

If the subject company or acquirer, as applicable, does not have a compensation committee or similar committee or if none of the members of the committee is independent, a special board committee may be formed to approve these arrangements. If the subject company or acquirer, as applicable, is a foreign private issuer, any or all of the members of the board or any board committee authorized to approve these types of arrangements under its home country laws or regulations may approve the arrangement.

For listed companies, the approving directors must qualify as independent under the company's definition of independence that it uses for stock exchange purposes. Those listed companies that have adopted standards of independence higher than that required by the particular exchange would, under a strict reading of the new rules, have to apply those higher standards for the independence determination for safe harbor purposes. Companies that are not subject to director independence standards may choose the independence definition that it wishes to use, but it must apply that definition consistently to all directors approving the arrangement. Foreign private issuers may either use the foregoing independence standards or the independence requirements of its home country. A determination by the board that the approving directors are independent satisfies the independence requirements of the safe harbor.

Finally, the safe harbor includes an instruction that the existence of the safe harbor for employment-related arrangements does not raise any inference that a payment under any other arrangement constitutes tender offer consideration.

### **Effectiveness**

These new rules will be effective 30 days after their publication in the Federal Register, which has yet to occur. For a copy of the final rules, see <http://sec.gov/rules/final/2006/34-54684.pdf>.

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning the issues addressed in this memorandum may be directed to any of the following:

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