

# Client Alert

A report  
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of the firm

October 2006

## SEC Adopts Best Price Rule Amendments

On October 18, 2006, the Securities and Exchange Commission approved changes to Rule 14d-10 of the Securities Exchange Act of 1934, known as the "best price rule." The changes will be effective thirty days after their publication in the Federal Register. The SEC will post the adopting release containing the final text of the amended best price rule on its website at [www.sec.gov](http://www.sec.gov), when the release becomes available.

The best price rule, which requires that all shareholders are paid the same price in a tender offer, has been the subject of differing interpretations among federal circuit courts. Some courts have applied the rule to compensatory arrangements entered into by employees or directors of the target company in contemplation of an acquisition.

On December 16, 2005, the SEC proposed amendments to the best price rule and invited comments from the general public to the proposed amendments. After receiving comments, the staff recommended that the SEC adopt the proposed amendments substantially as proposed. To address comments it received, the staff recommended the following modifications to the best price rule.

- *Revise the language to clarify that it applies to payments for securities.* Currently, the best price rule reads: "No bidder shall make a tender offer unless . . . the consideration paid to any security holder pursuant to the tender offer is the highest consideration paid to any other security holder during such tender offer." The staff recommended revising the rule to replace the phrases "pursuant to the tender offer" and "during such tender offer" with the phrase "for securities tendered in the tender offer."
- *Add an exemption for the negotiation, execution or amendment of employee benefit arrangements entered into with target company security holders.* The staff recommended that this exemption be adopted with the following three modifications to the version that was proposed:
 

First, the parties to compensatory arrangements that qualify for the exemption would be expanded to include all security holders of the target company rather than to only employees or directors of the target company.

Second, the exemption would be added to the issuer tender offer rules, not just the third-party tender offer rules.

Third, the two requirements that must be met in order to qualify for the exemption would be modified slightly. In the first requirement, rather than provide that the employee benefit arrangement must "relate solely to" services rendered or to be rendered, the phrase "relate solely to" would be replaced with the phrase "is being paid or granted for." As a result of this change, the exemption will be satisfied if the employee benefit arrangement "is being paid or granted as compensation for" services rendered or to be rendered. In the second requirement, the word "owned" would be replaced with the word "calculated" to make it clear that an arrangement will satisfy the exemption if it "is not *calculated* based on the number of securities tendered or to be tendered . . . ."
- *Adopt a safe harbor that would allow an independent compensation committee to approve an employee benefit arrangement.* The staff recommended that the safe harbor be adopted with the following five modifications to the version that was proposed:
 

First, the safe harbor would apply to both the issuer and the third-party best-price rule.

Second, the safe harbor would make clear that it is satisfied in all cases by approval of the target company directors and, where the bidder is a party to the transaction, by approval of the bidder company directors.

Third, the safe harbor would include arrangements approved by a special committee of the board of directors that is comprised solely of independent members and formed to approve the arrangement. This approval would be sufficient if the company does not have a compensation or similar committee or the company has such a committee, but none of its members are independent.

Fourth, for foreign private issuers, arrangements could be approved by any members of the board of directors or any board committee that is authorized to approve the arrangement under the laws or regulations of their home country. Members of the board or committee would need to be independent in accordance with the laws or regulations of their home country.

Fifth, an instruction to the safe harbor would be added to provide that a determination by the board of directors that its members approving an arrangement are independent in accordance with the provisions of the safe harbor, will satisfy the independence requirements of the safe harbor.

### **No exemption for commercial arrangements**

The staff acknowledged that it did not recommend changing the best price rule to create a general exemption for commercial arrangements in addition to the exemption for compensation arrangements, although the staff received comments requesting the SEC to adopt such a provision. The staff explained that it felt such an exemption would be too "open-ended" because it would allow any type of arrangement to come under such an exemption.

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**For more information contact:**

#### **Julie M. Allen**

212.969.3155 – [jallen@proskauer.com](mailto:jallen@proskauer.com)

#### **Allan R. Williams**

212.969.3220 – [awilliams@proskauer.com](mailto:awilliams@proskauer.com)

#### **Richard H. Rowe**

202.416.6820 – [rrowe@proskauer.com](mailto:rrowe@proskauer.com)

#### **Robyn Manos**

202.416.6816 – [rmanos@proskauer.com](mailto:rmanos@proskauer.com)

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