

## SEC Adopts Amendments to Tender Offer Best-Price Rule

New York  
November 6, 2006

The SEC has adopted the long anticipated amendments (originally proposed in December 2005) to the “best-price” rules for both issuer and third party tender offers. The amendments clarify that the rules apply only with respect to the consideration paid for securities tendered in a tender offer. In particular, the amendments provide that the rules will not be violated by the payment of consideration pursuant to employment compensation, severance, non-compete or other employment-related benefit arrangements entered into with any shareholder of a company whose shares are the subject of a tender offer if certain conditions are met. The new rules will become effective 30 days after publication in the Federal Register. The full text of SEC Release No. 34-54684 adopting the rules is available at <http://www.sec.gov/rules/final/2006/34-54684.pdf>.

The amendments modify the best-price rule found in Rule 14d-10 under the Securities Exchange Act of 1934 (and in Rule 13e-4(f)(8), which applies to issuer tender offers) to require that “[t]he consideration paid to any security holder for securities tendered in the tender offer is the highest consideration paid to any other security holder for securities tendered in the tender offer,” eliminating previous references in the rules to consideration paid “pursuant to the tender offer” and “during such tender offer.” In the adopting release the SEC explains that this change to the base language of the best-price rule is intended to “remove the potentially expansive concept of consideration paid ‘pursuant to’ a tender offer” and focus the rule on whether consideration was paid for securities tendered. The release helpfully makes explicit the SEC’s understanding that the best-price rules are not applicable to arrangements between a bidder (or the subject company) and subject company shareholders where the shareholders do not tender their shares in the tender offer.<sup>1</sup> (Adopting Release Section II.A.2 (p.12))

In addition to modifying the basic language of the rules for all purposes, the amendments create an explicit exemption from the best-price rules for the negotiation, execution or amendment of, or payments made under, any employment compensation, severance or other employee benefit arrangement with any shareholder of the subject of a tender offer, so long as two conditions are met. The amounts payable under the arrangement must be being paid or granted “as compensation for past services performed or future services to be performed or to be refrained from being performed”

<sup>1</sup> This understanding may be particularly helpful in facilitating the use of tender offers in leveraged acquisitions where management/shareholders wish to “roll” subject company equity.

and must not be calculated based on the number of securities tendered or to be tendered in the tender offer by the shareholder.

Finally, the amendments create a non-exclusive “safe harbor” making the exemption available for any arrangement that is approved “as an employment compensation, severance or other employee benefit arrangement solely by independent directors.” The independent directors approving the arrangement need not make any determination that it meets the two requirements of the exemption in order to take advantage of the safe harbor. Specifically, the availability of the safe harbor requires approval of an arrangement by the compensation committee (or a committee performing a similar function) of the target company’s board of directors, or in the alternative, the equivalent committee of the bidder’s board of directors, but only if the bidder is a party to the arrangement. All of the members of the body approving the arrangement must be independent directors, which for listed companies will be determined by reference to the independence requirements of the applicable listing standards.

The adopting release also contains an important clarification to the operation of the new “safe harbor” that is not explicit in the text of the amendments. The release makes clear that in order for the safe harbor to be available for a given compensation arrangement, it must have been approved by independent directors vested with fiduciary responsibilities for approving compensation arrangements who have “knowledge of the specific arrangements with security holders and the related tender offer when the approval is given.” Thus, although compensation arrangements put in place and approved by an issuer’s compensation committee prior to an acquisition will likely be eligible for the exemption, they will not be eligible for the safe harbor unless ratified specifically in connection with the tender offer.<sup>2</sup>

The amended “best-price” rules should provide greater certainty to bidders who desire to pursue business combination transactions via tender offers, which are generally quicker than statutory mergers. Accordingly, we expect there will be an increase in the use of tender offers except for acquisitions expected to involve a long regulatory or antitrust process.

If you have any questions regarding the newly-adopted rules please contact any of your regular contacts at the firm or Victor Lewkow, Daniel Sternberg, Christopher Austin, William Groll, Paul Shim, David Leinwand or Ethan Klingsberg at 212 225 2000.

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<sup>2</sup> Even under the prior Rule, it was the better view that honoring such “old and cold” employment arrangements did not raise a best-price issue. It remains to be seen whether bidders will rely on the “old and cold” concept for pre-existing contracts or will always seek to obtain re-approval of such contracts by an independent committee in the context of the proposed tender offer.

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