

involving a recapitalization" includes purchases effected during the period from the time of public announcement²⁷ of the merger, acquisition, or similar transaction involving a recapitalization, until the completion of such transaction.²⁸ Once a merger or acquisition is announced, an issuer has considerable incentive to support or raise the market price of its stock in order to facilitate the merger or acquisition. For example, in a recent contested takeover, several news articles suggested that the banks repurchased their respective securities in order to boost their stock price to enhance the value of their competing merger proposals.²⁹

Some of the commenters, however, argued that the proposed amendment would drastically expand the scope of the current exclusion and that Regulation M's restricted periods³⁰ and other federal and state laws adequately address any manipulative concerns.³¹ These commenters also argued that, because regulatory approvals for mergers may take several months, the proposed merger exclusion would keep issuers out of the market far longer than necessary.³² Other commenters argued that the proposed amendment should not apply to all cash mergers; after the shareholder vote in a merger; after the exchange ratio is fixed; or after the valuation period expires.³³

²⁷ "Public announcement" is any oral or written communication by any participant that is reasonably designed to, or has the effect of, informing the public or security holders in general about the business combination transaction. See 17 CFR 230.165(f).

²⁸ This includes any period where the market price of a security will be a factor in determining the consideration to be paid pursuant to a merger, acquisition, or similar transaction. See Proposing Release, *supra* note 1.

²⁹ See, e.g., Jeffrey N. Gordon, "Reviewing the New Merger Accounting Regime," *New York Law Journal*, at 1 (July 19, 2001) (stating that in the contest between First Union and SunTrust for Wachovia, all three banks have engaged in share buybacks in ways that affected the comparative deal prices). See also Liz Moyer, "SEC Rule May Hinder SunTrust: Buyback to Boost Stock Price Could be a Violation," *American Banker*, at 1 (June 28, 2001).

³⁰ See note 36, *infra*.

³¹ See, e.g., comment letters from Committee on Federal Regulation of Securities, Section of Business Law of the American Bar Association (Fed. Reg. Committee) and Merrill Lynch, Pierce, Fenner & Smith, Incorporated (Merrill).

³² See comment letters from Citigroup; Committee on Corporation Law of the Association of the Bar of the City of New York (Corp. Law Committee); Fed. Reg. Committee; Intel Corporation (Intel); Merrill; Sullivan & Cromwell, LLP (Sullivan); Valero Energy Corporation (Valero); Wachtell, Lipton, Rosen & Katz (Wachtell); Wal-Mart Stores, Incorporated (Wal-Mart); and Wells Fargo (Wells).

³³ See, e.g., comment letters from Cardinal Health; Dell Computer Corporation (Dell); Intel; Morgan Stanley; Sullivan; Valero; Wachtell; Wal-Mart; and Wells.

After considering the comments, and in view of the fact that we are limiting the amount that can be repurchased within the safe harbor (as discussed below and in Section III.B.6 of this Release), we have determined that it is not necessary to exclude from the safe harbor all issuer repurchase activity following the announcement of a merger, acquisition, or similar transaction involving a recapitalization. Instead, as adopted in 10b-18(a)(13)(iv), the merger exclusion applies to purchases that are effected during the period from the time of public announcement of a merger, acquisition, or similar transaction involving a recapitalization, until the earlier of the completion of such transaction or the completion of the vote by target shareholders (including during any period where the market price of a security will be a factor in determining the consideration to be paid pursuant to a merger, acquisition, or similar transaction),³⁴ with the following exceptions.

The exclusion does not extend to transactions in which the consideration is solely cash and there is no valuation period (*i.e.*, where the issuer has little or no incentive to manipulate the market price of its securities).³⁵ We also recognize that some issuers may desire to carry out ordinary repurchases (*i.e.*, purchases not made in connection with or relating to the merger or other covered transaction) during what could be an extended period of time until completion of the transaction. Thus, we are modifying the proposed merger exclusion to allow ordinary Rule 10b-18 purchases to be effected after the announcement of a merger or covered transaction (subject to Regulation M's restricted period³⁶ and any other

³⁴ This includes during the period following the vote by target security holders but before an election period. However, the safe harbor would be available after a shareholder vote is completed in instances where the only pending issue is regulatory approval or other action that could not influence the market price of the issuer's security.

³⁵ Amended Rule 10b-18 (a)(13)(iv)(A).

³⁶ In the case of a distribution involving a merger, acquisition, or exchange offer, Regulation M's restricted period begins on the day the proxy solicitation or offering materials are first disseminated to security holders, and ends upon the completion of the distribution (*i.e.*, the time of the shareholder vote or the expiration of the exchange offer), and includes any post-vote valuation or election period. 17 CFR 242.100. In addition, Rule 14e-5 under the Exchange Act prohibits purchases or arrangements to purchase securities that are the subject of an exchange offer, or a security immediately convertible into or exchangeable for those securities, from the time of public announcement until the expiration of the exchange offer. 17 CFR 240.14e-5.

While not making any substantive changes, we are shortening the language in subsection (a)(13)(i)

applicable restrictions) so long as the total amount of the issuer's Rule 10b-18 purchases effected on any single day does not exceed the lesser of 25% of the security's four-week ADTV or the issuer's average daily Rule 10b-18 purchases during the three full calendar months preceding the date of the announcement of the merger or other covered transaction.³⁷ Moreover, the issuer may effect block purchases pursuant to paragraph (b)(4) of the Rule (subject to Regulation M's restricted period and any other applicable restrictions) provided that the issuer does not exceed the average size and frequency of block purchases effected pursuant to paragraph (b)(4) of the Rule during the three full calendar months preceding the date of the announcement of such transaction.³⁸

We believe that limiting the amount an issuer may repurchase following the announcement of a merger or other covered transaction will safeguard against the heightened potential for manipulative abuse during this sensitive

(regarding purchases made during a Rule 102 of Regulation M restricted period) to read simply: "effected during the applicable restricted period of a distribution that is subject to Section 242.102 of this chapter."

³⁷ Amended Rule 10b-18 (a)(13)(iv)(B)(1). This latter calculation is different from ADTV, as defined in Amended Rule 10b-18 (a)(1).

³⁸ Amended Rule 10b-18 (a)(13)(iv)(B)(2). For example, if the daily average amount of the issuer's Rule 10b-18 purchases over the course of the three full calendar months prior to the merger announcement was 10,000 shares per day, and 25% of the security's four-week ADTV is 20,000 shares per day, then the issuer could purchase up to 10,000 shares per day during the post-announcement period. Accordingly, if the issuer did not make any Rule 10b-18 purchases during this three-month period, it would not be permitted to make any Rule 10b-18 purchases during the post-announcement period.

In addition, if the issuer made block purchases within the safe harbor (pursuant to paragraph (b)(4) of the amended Rule) over the course of the three full calendar months prior to the announcement of a merger or other covered transaction, then the issuer may make block purchases within the safe harbor with the same average size and frequency during the post-announcement period. For example, if a thinly traded issuer purchased three blocks over the course of the three full calendar months prior to a merger announcement (an average of one block per month) and the average block size was 7,800 shares, then the issuer could purchase a block no larger than 7,800 shares each month during the post-announcement period (subject to other applicable restrictions). If the issuer did not make any block purchases under the amended block exception during the three-month period, the issuer could not utilize the amended block exception during the post-announcement period.

Issuers are reminded that the safe harbor is not available for repurchases that, although made in technical compliance with the Rule, are fraudulent or manipulative, when viewed in the totality of the facts and circumstances surrounding the repurchases. See Adopted Preliminary Notes to Rule 10b-18. See also 1982 Adopting Release, *supra* note 4, and text accompanying *supra* notes 5 and 24.