

## SEC PROPOSES ISSUER STOCK REPURCHASE AMENDMENTS

On December 10, 2002, the Securities and Exchange Commission (the “Commission”) issued a Release seeking public comment on proposed amendments to Rule 10b-18 under the Securities Exchange Act of 1934 (the “Exchange Act”).<sup>1</sup> Rule 10b-18 establishes a non exclusive “safe harbor” for issuer repurchases of their own common stock. The proposed amendments are intended to simplify and update the safe harbor provisions in light of market developments since the Rule’s adoption. The Commission has asked that comments on the proposal be filed no later than February 18, 2003.

Exchange Act Rule 10b-18 was originally adopted in 1982. It provides issuers with a “safe harbor” from charges of manipulation under Section 9(a)(2) of the Exchange Act and Rule 10b-5 (but not from liability under Regulation M, which pertains to bids and purchases during a securities offering, and not from liability for insider trading) when the issuer purchases its own common stock in the market in accordance with the Rule’s manner, timing, price and volume conditions. Rule 10b-18 currently applies to bids for and purchases of an issuer’s common stock by or for such issuer or affiliated purchasers, excluding bids and purchases made during certain corporate events, such as mergers, tender offers and distributions that involve the issuer. To qualify for protection under the Rule’s safe harbor on a given day, the issuer must satisfy the following conditions:

1. Manner of Purchase: The issuer must use a single broker or dealer per day to bid for or purchase its common stock.
2. Timing: Purchases must not be made at the market opening or within one-half hour of the close.
3. Price: The price at which the issuer repurchases its securities must comply with a formula set forth in the Rule that is designed to prevent the purchases from leading the market upward.
4. Volume: An issuer may effect purchases only in an aggregate amount per day not exceeding 25% of the average daily trading volume (“ADTV”) of its shares,

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<sup>1</sup> Securities Exchange Act Release No. 46980 (December 10, 2002). The text of the Release is available at <http://www.sec.gov/rules/proposed/33-8160.htm>.

excluding block purchases, during the four calendar weeks preceding the Rule 10b-18 purchase or bid.

According to the Commission, the proposed amendments would simplify and update the safe harbor provisions to reflect market developments since the Rule's adoption. The proposals would allow issuers whose securities are less susceptible to manipulation to participate in repurchases of their securities with greater ease.

The proposed changes are as follows:

Eligible Securities:

- The definition of a "Rule 10b-18 purchase" would be amended to include any "bid or limit order that would effect such purchase."
- The amendment would codify the Commission staff's view that the safe harbor is available for repurchases of all common equity securities (i.e., an issuer's common stock or an equivalent interest, including a unit of beneficial interest in a trust or limited partnership or a depository share). The Rule 10b-18 safe harbor would continue not to apply, however, to any other type of security — even if related to the common stock (e.g., warrants, options, or security futures products that are physically settled).
- The definition of a "Rule 10b-18 purchase" would be further amended to clarify that the exclusion of purchases effected pursuant to a merger includes purchases effected "during the period from the time of public announcement of the merger, acquisition or similar transaction until the completion of such transaction."

Timing:

- The limitations on repurchases at the close of trading each day would vary on the basis of the ADTV value and public float of the security to reflect the relative liquidity of the security and, therefore, the ability of the issuer to affect the closing price.
- The timing limit would be relaxed for issuers of more liquid securities (the proposal suggests an ADTV value of \$1 million or more and a public float value of \$150 million or more) from the current 30-minute black out period before the

close to 10 minutes.<sup>2</sup> All other issuers would remain subject to the 30-minute black out.

Price:

- A uniform price condition would be applied by limiting issuers to purchasing their securities at a price that does not exceed the highest independent bid or the last independent transaction price, whichever is higher, quoted or reported in the consolidated system. For those securities not quoted or reported in the consolidated system, the proposed amendments would provide that an issuer's Rule 10b-18 purchases could be effected at a purchase price that did not exceed the highest independent bid or the last independent transaction price (regular way), whichever is higher, displayed and disseminated on any national securities exchange or in any inter-dealer quotation system that displays at least two priced quotations for the security. For all other securities, Rule 10b-18 purchases would have to be made at a price that did not exceed the highest independent bid received from three dealers. The Commission is still contemplating removing the "last independent transaction price" alternative from this proposal, leaving only the bid test.

Volume:

- The "block purchase exception" would be eliminated from the volume limitation. Issuers would have to include their block purchases in applying the Rule's 25% ADTV limitation. Issuers would be able, however, to include their block purchases in calculating a security's ADTV, which would increase the amount that some issuers could repurchase under the safe harbor.
- The definition of ADTV would be amended to include block purchases made by or on behalf of the issuer and reported for the security during the four calendar weeks preceding the week in which the Rule 10b-18 purchase is effected.
- As an alternative to the 25% volume limitation, issuers would be allowed to purchase up to a daily aggregate amount of 500 shares.

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<sup>2</sup> The proposed modifications to the timing condition would work as follows: to qualify for the safe harbor, issuers of more liquid securities (i.e., those having an ADTV value of \$1 million or more and a public float value of \$150 million or more), could not bid for or purchase their securities during any of the following periods: (i) in the 10 minutes before the scheduled close of the regular trading session in the principal market for the security; (ii) in the 10 minutes before the scheduled close of the regular trading session in the market where the purchase is made; or (iii) after the termination of the period in which last sale prices are reported in the consolidated system (i.e., after the consolidated tape stops running).

Rule 10b-18 Alternative Conditions:

- The 25% volume limitation condition in a trading session immediately following a market-wide suspension or circuit breaker would be increased to 100% of the ADTV of that security.

Disclosure:

- Regulations S-K and S-B and Forms 10-Q, 10-QSB, 10-K, 10-KSB and 20-F and proposed Form N-CSR would be amended to require periodic disclosure of all issuer repurchases of shares or other units of any class of the issuer's equity securities registered by the issuer pursuant to Section 12 of the Exchange Act, including those made in reliance on Rule 10b-18.
- Issuers would be required to disclose, among other things, the total number of shares repurchased during the past quarter, the average price paid per share, the identity of any broker-dealers used to effect the purchases, the number of shares purchased as part of a publicly announced repurchase plan or program, and the number of shares remaining to be purchased under the plan or program.

The Commission believes that these proposed amendments would continue to allow issuer repurchases under conditions that will not likely create manipulative effects on the price of the issuer's security or on market activity, without imposing undue restrictions on the operation of such repurchases or undermining the benefit that they provide for issuers, investors and the marketplace.

In addition to comments on the proposed amendments, the Commission is requesting comment on several other related issues under Rule 10b-18, including (i) expanding the scope of the definition of "affiliated purchaser"; (ii) whether the single broker-dealer condition should be amended to accommodate issuer repurchases through ATSS; (iii) whether riskless principal trades should be eligible for the safe harbor; (iv) the applicability of the safe harbor during after-hours trading sessions; (v) the petition for rulemaking filed by the NYSE on June 13, 2001; and (vi) whether closed-end funds should be subject to the additional disclosure requirements.

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If you wish to obtain additional information regarding these proposed amendments, please contact Roger D. Blanc (212-728-8206), William H. Gump (212-728-8285) or the corporate partner with whom you regularly work.

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