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February 21, 2006

VIA E-MAIL: rule-comments@sec.gov

Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street N.W.
Washington, D.C. 20549-0609

Re: File No. S7-11-05
Release Nos. 34-52968; IC-27193
Amendments to the Tender Offer Best-Price Rule

Ladies and Gentlemen:

This letter is submitted on behalf of Shearman & Sterling LLP in response to the request by the Securities and Exchange Commission (the "Commission") for comments on its December 16, 2005 release entitled "Amendments to the Tender Offer Best-Price Rule" (the "Proposing Release").

Introduction

We believe that the proposed amendments to Rule 14d-10 (the "Proposed Rule") promulgated under the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"), successfully meets the purposes stated in the Commission's Proposing Release. While we respectfully submit the following requests for further clarification or changes, we believe that the Proposed Rule is a substantial step forward. By clarifying that legitimate payments to target employees and directors – which are often a commercial necessity – should not be recharacterized as tender offer consideration, the Proposed Rule should create certainty in the face of case law that has become difficult to predict and rife with negative public policy implications. We have found that, to the detriment of stockholders, this uncertainty has caused parties to structure transactions as mergers, rather than tender offers, if they believe it is important to implement employee arrangements.

Both sellers and buyers often find that appropriate employment arrangements are essential to a successful acquisition transaction. In particular, if a potential target announces that it is

exploring a sale (or "strategic alternatives", in the common parlance), its competitors often will seek to exploit the resulting period of uncertainty by attempting to hire the target's key personnel. To address this situation, companies often seek to implement retention programs that are designed to ensure that key personnel remain with the company through the closing of a transaction. Similarly, buyers often conclude that the retention of key personnel, either on a transition or long-term basis, is essential to a successful acquisition, and will seek to implement retention programs designed to achieve that result. No benefit is served by having U.S. securities laws imposing legal impediments to valid employment arrangements entered into in connection with a tender offer with the same arrangements could be put in place without legal risk in connection with a merger.

From a stockholder's perspective, a tender offer is often preferable to a merger because a tender offer can be closed more quickly, and, thus, with less completion risks than long-form mergers. Because the recent application of Rule 14d-10 has driven acquirers to use long-form mergers rather than tender offers, stockholders have been affirmatively harmed because they have received their consideration later, and they have been subjected to greater risk that the transaction will not close.

Obviously, there is always a risk that a public company will enter into employment arrangements that are not in the best interests of its stockholders. To the extent that this risk exists, however, it exists every day, not just in the context of a tender offer. We believe that existing state law remedies, rather than a court's post-hoc analysis of whether employment arrangements should be recharacterized as tender offer consideration, is the most appropriate means to protect stockholders from this risk.

The most important developments in the Proposing Release are the procedures for safe harbor protection created by proposed Rule 14d-10(c)(3) and the criteria for the exemption for employment arrangements provided by proposed Rule 14d-10(c)(2). Accordingly, our comments center on these areas in an attempt to clarify the Commission's stated intention and to maximize the benefit of the amendments in a manner that adequately protects stockholders' interests.

Comments

1. *Safe Harbor Protection*

We believe that the procedures set forth in proposed Rule 14d-10(c)(3) to qualify for safe harbor protection mirror those procedures already utilized by most well-advised domestic companies. Being responsible for ensuring that a proposed transaction is a *bona fide* employment

arrangement falls within the appropriate ambit of the compensation committee's[1] responsibility. We agree that stockholders are adequately protected when independent directors – who have a fiduciary duty to safeguard the stockholders' best interests – duly decide that the transaction is a *bona fide* employment arrangement. Nevertheless, we offer the following specific comments that we believe will clarify the proposed safe harbor and provide for more efficient and effective implementation of the exemption.

(a) Basis For Reliance On Safe Harbor

If employment arrangements have been adopted by a compensation committee that meets the requirements of the safe harbor provision in the ordinary course of its business, we believe it would be inefficient and unduly burdensome to require a company with such existing arrangements to have them re-approved following adoption of the Proposed Rule. Thus, there should be no need for compensation committees to ratify those employment arrangements that were previously adopted in a manner that complies with the safe harbor. Similarly, we feel that it should be unnecessary to require a company to adopt specific resolutions evidencing the basis for reliance on the safe harbor for every arrangement in contemplation of the hypothetical eventuality that the best price rule may become relevant to that company.

In contrast, to the extent employment arrangements were adopted by a compensation committee that did not meet the requirements of the safe harbor, companies should be afforded the opportunity to ratify those existing arrangements without the need to enter into new arrangements. We do not believe "transaction-specific" approval should be required; general approval that complies with the Proposed Rule should suffice. If the Proposed Rule is adopted, we expect that it will become standard practice for compensation committees to ensure that all employment arrangements involving senior management are adopted in a manner that would comply with the safe harbor requirements. Thus, we would expect transaction-specific ratification to diminish over time. It is important, however, to allow such ratification of employment arrangements that exist at the time the Proposed Rule is adopted.

(b) Applicability To Foreign Private Issuers

As a structural matter, many foreign private issuers do not have compensation committees of their boards of directors in form or function, nor would they be able to constitute such committees to be comprised solely of independent directors or in a manner that otherwise meet the requirements imposed by the Proposed Rule. For similar reasons, foreign private issuers

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[1] References herein to "compensation committee" are intended to include other committees performing similar functions, as contemplated in the Proposing Release.

have been removed from the ambit of many recent corporate governance reforms.[2] Indeed, due to non-U.S. law requirements, in certain jurisdictions, it may not be possible or appropriate for foreign private issuers to have compensatory decisions taken by disinterested board members.

By way of illustration, German stock corporations are governed by a Management Board (the "*Vorstand*") and a Supervisory Board (the "*Aufsichtsrat*"). The *Vorstand* is responsible for the management of the business of the company in accordance with German law and the company's articles of association. The *Vorstand* generally makes decisions with respect to all significant business matters and major policy decisions, including acquisitions and divestitures and capital expenditures. The *Vorstand* is only comprised of the most senior executives, thus, the members of the *Vorstand* would have a potential conflict of interest in approving their own compensation arrangements. Consequently, the *Vorstand* makes compensation decisions for only those other officers who are not its members.

In accordance with the German Codetermination Act, half of the members of the *Aufsichtsrat* of large German stock corporations with more than 2,000 employees are "labor" members, elected by the employees of the company who are either themselves employees or labor union representatives.[3] The remaining half of the *Aufsichtsrat* are elected by shareholders at the company's annual meeting and are often officers of other German stock corporations. The principal function of the *Aufsichtsrat* is to appoint and terminate members of the *Vorstand*, to negotiate the terms and conditions of (including the compensation under) and conclude (each on behalf of the respective German stock corporation) the service agreements with each member of the *Vorstand*, to supervise the *Vorstand*'s activities and consent to transactions as required. Because of the strong public policies behind having a significant rank-and-file employee/union representation on the *Aufsichtsrat*, executive compensation decisions affecting members of the *Vorstand* could in practice, although legally possible, not appropriately be made by only the non-employee members of the *Aufsichtsrat* without the cooperation of the employee representatives.

Accordingly, foreign private issuers may not be able to avail themselves of the safe harbor since there are no independent directors who would be authorized to make compensation-related decisions. In the case of Germany, the *Aufsichtsrat* (as constituted in accordance with the

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2 While there is no general exemption for foreign private issuers under the Sarbanes-Oxley Act of 2002, the SEC did make several accommodations for foreign private issuers that take into account conflicting corporate governance practices required by non-U.S. law or listing standards. For example, Exchange Act Rule 10A-3 provides an accommodation for foreign private issuers required to have non-executive employees or government representatives on their audit committees, to maintain a two-tiered board structure (management and supervisory) or to have a board of auditors.

3 If a German stock corporation has less than 2,000 but more than 500 employees, only one-third of the *Aufsichtsrat* are employee representatives.

German Codetermination Act), being the competent board for *Vorstand* compensation-related matters, is not comprised solely of independent directors and, thus, would not meet the requirements of the safe harbor provision. Its independent members could in practice not appropriately approve such arrangements and the full *Aufsichtsrat* could not appropriately act as to any compensatory arrangements with officers other than the *Vorstand* members. Having the members of the *Vorstand* approve their own arrangements (for purposes of Rule 14d-10 only) would result in a paradigm where the target's senior-most management approves their own payments. Requiring actions by both the *Vorstand* and the *Aufsichtsrat* to cover all officer arrangements makes the burden on foreign private issuers for satisfying the safe harbor more onerous than that imposed on domestic issuers.

The relief provided in the Proposed Rule should not be unavailable to a foreign private issuer based solely on formalistic reliance on governance structures that may be unique to domestic issuers. Accordingly, we believe that *bona fide* compensatory arrangements with employees, directors and consultants to foreign private issuers competently adopted in accordance with local law and governance practices should be excluded from the coverage of the best price rule of Rule 14d-10 without requiring any specific form of corporate approval.

(c) Retroactivity Of Safe Harbor Protection

Because the safe harbor provides adequate protection and in an effort to avoid needless, costly litigation, we believe that the Proposed Rule should have retroactive effect.

(d) Definition of Independence

We support the Commission's suggestion in the Proposing Release that the appropriate standard for independence is that articulated in Rule 16b-3(d) of the Exchange Act. Using this definition makes sense both because (i) Rule 14d-10 is promulgated under the Exchange Act and (ii) it is preferable, in our opinion, to harmonize the varying independence definitions used for different but similar purposes. We feel that this would be an important step in that direction.

2. *Exemption For Employment Arrangements*

(a) Requirements of Rule 14d-10(c)(2): "Solely to past services"

In order to qualify for the safe- harbor, clause (i) of Proposed Rule 14d-10(c)(2) requires that amounts paid pursuant to employee arrangements must relate "solely" to past services performed or future services to be performed or refrained from performing. In contrast, the narrative in Section II.B.1 at p.19 of the Proposing Release states that "part of the consideration" required for the exemption should be past or future services. We believe that the word "solely" in the

Proposed Rule is unnecessary and inconsistent with authorizing a compensation committee to approve compensatory arrangements in its discretion.

The sentence preceding clause (i) provides that the arrangement must be a *bona fide* employment arrangement approved by the compensation committee. Thus, it should be sufficient that the compensation committee approve the arrangements, and no other specific fact-finding should be required. Furthermore, if the intent of the provision is to provide a broad safe harbor for *bona fide*, duly approved employment arrangements, use of the word "solely" appears to unnecessarily circumscribe the availability of the exemption.

(b) Applicability To Independent Contractors And Consultants

The safe harbor and exemption currently are available only to arrangements with employees and directors. We believe it is consistent with the principles articulated in the Proposing Release that the Proposed Rule be available to compensatory arrangements with contractors and consultants who are individuals and who are providing *bona fide* services to the target. In this regard, we recommend that the Proposed Rule be expanded to cover arrangements with consultants and advisors, using a definition of such persons similar to that found in Rule 701(c)(1)(i) and (ii) of the Securities Act of 1933, as amended.

3. *Analogous Amendment In Self-Tender Context*

In our experience, similar concerns to those raised by Rule 14d-10 can be present in the context of issuer tender offers governed by Rule 13e-4. Accordingly, if one accepts that the compensation committee is the appropriate body to approve employment arrangements in the context of a tender offer because it is best positioned to protect stockholders' interests, we see no principled basis for excluding analogous revisions to the best price rule's counterpart in the context of issuer self-tenders. Stockholders are protected by state law fiduciary obligations imposed in going private transactions to the same degree they are in third party tender offers. To not enact a similar amendment with respect to Rule 13e-4 creates an opportunity for

misinterpretations and inconsistencies not grounded in any cogent public policy.

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Please fee to contact Peter D. Lyons (212 848 7666) or Doreen E. Lilienfeld (212 848 7171), if you have any questions or would like to discuss the comments contained herein.

Respectfully submitted,

Shearman & Sterling LLP