"Company Buybacks: Best Practices"

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Audio Archive

Stock repurchases continue to be on a tear - and they continue to be controversial at times. This webcast will provide practical guidance about how to conduct a stock repurchase program, including analysis of whether it's the best use of funds. Join:

- **Scott Kimpel**, Partner, Hunton Andrews Kurth LLP
- **Josh LaGrange**, Counsel, Skadden, Arps, Slate, Meagher & Flom LLP
- **Lee Meyerson**, Partner, Simpson Thacher & Bartlett LLP
- **Pat Quick**, Partner, Foley & Lardner LLP

Liz Dunshee, *Editor, TheCorporateCounsel.net*: This is Liz Dunshee, Editor at TheCorporateCounsel.net. Welcome to our webcast on "Company Buybacks: Best Practices."

Our panel today consists of Scott Kimpel, who is a Partner at Hunton Andrews Kurth; Josh LaGrange, Counsel at Skadden, Arps; Lee Meyerson, a Partner with Simpson Thacher; and Pat Quick, a Partner at Foley & Lardner.

Scott's going to kick us off by covering the debate about whether buybacks are the best use of a company's funds.

Debate About Whether Buybacks Are Best Use of Company Funds

Scott Kimpel, *Partner, Hunton Andrews Kurth*: Thank you, Liz. Good afternoon, everyone. As long as there have been corporations, corporate managers have wrestled with the best way to deploy their excess cash. Should we open new stores? Should we buy more advertising? Should we acquire a competitor? Do we increase wages?

Eventually, management has to ask if the company is best served by returning some of its capital to shareholders. There are several techniques for doing so. The two most straightforward are to declare a cash dividend and offer to buyback shares on the open market.

With a dividend, of course, each shareholder receives the same amount per share. On the other hand, buybacks give shareholders more optionality to participate. If an investor wants cash immediately, it can sell into the market. If an investor would prefer to stay long in the stock, it need not participate.

Buybacks do return cash to investors and have the potential to boost the value of the company's shares by reducing the total number of shares outstanding. If earnings are flat but the number of outstanding shares decreases, a company experiences an immediate increase in earnings per share.

In many cases, a buyback program can affect supply and demand of the stock, such that it causes a stock price to increase. Buybacks can also be more tax efficient to investors than dividends. If an investor receives dividends, it may have to pay taxes on them immediately. If shares are rising in value due to a buyback, the investor pays no tax until it sells the shares for a profit.

Another consideration for companies carrying excess cash on their balance sheets is the rise of shareholder activism. Companies with under-deployed free cash make easy targets for economic shareholder activists. Such activists frequently demand that companies return some of that cash to their investors. In these situations, many companies determine that commencing a buyback program is a far better alternative to defending against an acrimonious activist campaign.

One criticism of buybacks is that they can distort or conceal a decline in fundamentals at a given company. There is also a growing body of academic literature suggesting that companies that heavily engage in buybacks underperform companies that do not.

Perhaps coincidentally, some of the recent economic data suggest that the aggregate value of share buybacks has decreased over calendar year 2019 relative to past years. While buybacks can be a good strategy if management thinks the company's shares are undervalued, it does reduce the amount of capital available to fund other possibly more productive expenditures.

Some investors believe buybacks sacrifice long-term organic growth. I recently heard a company CEO say that buybacks are a sign that management has no good entrepreneurial ideas left. As we will get to later in the program, some politicians are also making these kinds of arguments.

What is the SEC's position on buybacks? Well, there are two SEC rules that usually come into play when a company is considering a share repurchase program, each of which was adopted under the SEC's antifraud authority. Rule 10b-18 provides a safe harbor against the claim of market manipulation so long as the company follows a series of restrictions on the timing, price, volume and manner of purchase. Rule 10b5-1 provides an affirmative defense to an allegation of insider trading.

It's important to note that both rules are agnostic as to the merits of a share repurchase program. Our panel will discuss each of them further in the remainder of our time today.

On a parting note, before we move on, at a U.S. Chamber of Commerce panel discussion last week, SEC Chairman Jay Clayton and Corpfin Director Bill Hinman touched on several topics related to corporate governance - including buybacks. They mentioned that the SEC is not looking to regulate the use of buybacks further.

However, the agency is considering whether companies should disclose more information around buybacks, such as how the compensation committee is taking into account repurchase programs, or why a stock buyback was chosen over other distributions of capital.

Cash Dividends as an Alternative to Stock Repurchases

Lee Meyerson, *Partner, Simpson Thacher*: Thanks, Scott. It's Lee Meyerson. Moving on from what Scott was talking about, one of the great ironies of some of the current political debate over share buybacks is that cash dividends seem to not be on anybody's hit list politically although share buybacks are, and economically they're really the same thing.

They're both capital management tools for a board and management to use in distributing excess capital to the shareholders. Each has advantages and disadvantages. For most companies, they're complementary, and you can do both and toggle at least one of them on and off as needed.

The cash dividends have significant advantages. One, it's a steady stream of income to investors regardless of market movements. Even if the stock price goes up, the dividend and income remain the same. That is important to many retail investors, for whom the steady stream of dividends is an important source of income.

Certain classes of investors are not permitted to hold shares unless they have a dividend on them. It increases your universe of potential investors. Also, it provides cash to investors without requiring them to sell their shares and reduce their ownership interest in the company.

There's generally no tax rate difference between dividends and buybacks for U.S. investors, although on a net basis a share buyback is better because you only pay tax on the difference between the basis and the sale price of the shares. In contrast, the dividend is fully taxable. In addition, many investors are not taxpayers anyway. So, they wouldn't typically prefer one over the other for tax reasons.

What makes some companies prefer buybacks is that they're more flexible compared to cash dividends. Dividends typically only go one way, which is up, and cutting a dividend is usually viewed as a damaging admission by the company that there are problems. Even if you decide you need the capital for some other use like an acquisition, with the dividend, you are locked into the current rate. With the stock buyback, you can toggle it on and off as needed.

Dividends also don't do anything to increase earnings per share, because the number of shares outstanding remains the same. They also don't do anything to provide liquidity to the market for your shares - although one of the key principles of the Rule 10b-18 safe harbor for buybacks is that it's not supposed to and can't be done to prop up a stock price. If done properly, a buyback shouldn't prop up the stock price. It does provide a source of liquidity in the market, and that's particularly important for smaller cap companies where there may not be that much other regular trading in the stock.

The conclusion is that both should be viewed as equally useful tools in every company's toolkit. There are some companies like the FAANG companies that seem to disfavor dividends as a matter of policy. For everybody else, it's a useful tool that should be used as appropriate.

Debate Over Restricting Buybacks When Insiders Are Selling (& Vice Versa)

Kimpel: You know another argument in the debate over buybacks is the idea that insiders sell more stock after a company announces a buyback than on any other trading day. SEC Commissioner Robert Jackson has written and spoken extensively on this point.

Regular readers of TheCorporateCounsel.net blog know that the AFL-CIO recently ubmitted a rulemaking petition urging the SEC to replace Rule 10b-18. The central premise of that petition is that, I'm quoting, "executives retain a strong financial incentive to use repurchases to artificially inflate stock prices and boost their own compensation without real firm improvement."

The petition argues that in today's market, the majority of executive compensation is performance-based and tied to stock price or earnings per share, which presents executives with a financial incentive to increase short-term stock price or decrease the volume of outstanding shares to meet performance goals. Echoing Commissioner Jackson, it also alleges that executives time the sale of their personal holdings to take advantage of the price increase created at the time company repurchases are announced.

Building on these general sentiments, there are several bills winding their way through Congress that involve stock buybacks. I think it's important to touch on a few of them to give our listeners a flavor.

For example, Senators Bernie Sanders and Chuck Schumer penned an op-ed in *The New York Times* in February announcing their plan to introduce legislation aimed at limiting corporate stock buybacks. In the op-ed, the senators assert their belief that corporations have increased stock buybacks in order to maximize shareholder earnings - to the detriment of workers and the long-term strength of the business.

Their bill would prohibit a corporation from buying back its own stock unless it first invests in workers and communities, including things like paying all workers $15 an hour, providing seven days of paid sick leave and offering approved health benefits and more generous pensions.

Another bill under consideration by the House of Representatives directs the SEC to study buyback practices and adopt rules based on its findings. In particular, the bill instructs the SEC to determine whether Rule 10b-18 should be amended - and in doing so, says the SEC should give consideration to changes such as limiting the ability of a company to announce the stock repurchase if it has previously announced one in the preceding year and has not completed it, requiring a company that announces a stock repurchase plan to make disclosures regarding any minimum number of dollar amount or shares that the company intends to repurchase and the expiration date of the repurchase plan and requiring the company to make timely disclosures about each transaction conducted under the announced repurchase plan.

This proposed bill also contains provisions aimed at limiting the ability of officers and directors to trade in their company stock. The relevant provision would establish a period after a stock repurchase plan is announced, during which an officer or director of the company may not sell any common stock of the company or exercise any option on common stock of that company.

Going even further, a group of progressive senators introduced the "Reward Work Act" on March 27th. A parallel version of the bill has also been introduced in the House. That bill provides an outright bar against company buybacks. It's clear that no company may repurchase its own equity security on a national securities exchange.

The bill would explicitly repeal Rule 10b-18 and prohibit any national securities exchange from listing a company unless at least one-third of the company's directors are chosen by the company's employees, in a one-employee-one-vote election process. Under the Reward Work Act, companies could still, however, conduct a traditional stock repurchase through a formal tender offer.

Curtailing stock buybacks is an issue that seems to be gaining momentum on both sides of aisle. Senator Marco Rubio, who's generally viewed as a moderate pro-business senator, has also expressed support for limiting buybacks in interviews with the press.

He has even suggested introducing a bill on the subject that would tax stock buybacks more aggressively, while extending a provision in the 2017 tax law that allows companies to immediately and fully deduct the cost of new investments. It thereby makes it more attractive for companies to make those kinds of investments in lieu of buying back their own stock.

Other bills under consideration in the House would impose blackout periods on insiders, preventing them from trading in the company securities, or would require the SEC to carry out a study on whether Rule 10b5-1 itself should be amended.

Of course, passage of any of these bills is far from certain. Each underscores the growing dissatisfaction with the current legal regime and a perception that some executives had been exploiting it for personal gain.

Dunshee: If no one has anything to add to that, thank you, Scott. Pat, perhaps you could discuss some of the best practices for a buyback program.

Best Practices For Company Repurchase Programs

Pat Quick, *Partner, Foley & Lardner*: I'll do that. Thank you, and good day, all. I will put politics mostly aside in addressing five topics: planning, housekeeping, board approval, disclosure and then execution of a buyback plan.

Best practices start with planning. What are the company's objectives? As we've discussed, has the company considered alternative uses for funds? Has it considered the impact of buybacks on the float? Someone noted that buybacks can create liquidity, but it can cut both ways, because you decrease the float of the stock as well.

Also, in planning what method or methods to buy back shares, are you considering open market purchases, privately negotiated transactions, perhaps an issuer tender offer or an accelerated stock repurchase program? An ASR has a more immediate EPS impact by reducing the number of shares outstanding immediately. That involves a complicated arrangement with the broker that's outside the scope of the session. Does the company understand tax and accounting implications of the buyback?

Second, from a topical perspective, you ought to consider housekeeping and technical implications, watch restrictions in loan documents on dividends, and ensure that there is nothing in your charter or bylaws that comes into play. That would be relatively unusual, but it has happened.

Also, buybacks increase a percentage of stock that other shareholders hold at the end of the day. You should consider the potential impact under rights, plans or a business combination or similar statutes and see if there is a way to address that impact.

Be mindful of industry-specific rules like insurance, regulations, banks and other capital requirements. Consider stock exchange implications. There are no limitations to consider, but there can be reporting consequences.

Lastly, consider the impacts on compensation. This goes hand in hand with some prior comments. Make sure there are no unintended consequences from buying back stock, decreasing shares outstanding and positively impacting EPS.

The third step is getting board approval. Buying back stock can be a big investment, perhaps the biggest single investment a company might make in a year. Also remember that a buyback is tantamount to a dividend for state law purposes. The board should get complete information just like any other large decision - including information about the debate regarding alternative investment opportunities.

The board should act to approve any buyback in good faith and for appropriate purposes. It should also consider compensation implications, as I alluded to before. It may vary by company, but I wonder these days if the board pays enough attention to the various things that go into a buyback decision and whether the board gets enough materials to help guide that decision.

Again, in this context, it's necessary to consider state statutes about dividends, including a solvency test. You need to keep in mind that this is tantamount to a dividend, the payment is not just on approval but with each individual repurchase.

When the board acts, the board's approval terms should be carefully considered. The board decides about discretion that management has and who can exercise it.

If the company needs to borrow to effect buybacks, consider what that might entail. Consider how to express the authority and limitations of the board approval. Is there express authority as to a number of shares or a dollar amount or both? Might there be limits on the share price that management can pay to buy back stock?

Management will want the greatest flexibility, and what will the board want? Can you as board advisors anticipate what the board might want as you prepare materials and resolutions in advance? Also, in light of the dividend implications, the board should get regular updates and monitor the process along the way, because, again, company actions down the road can result in potential liability to directors.

My fourth topic is disclosure and there are several things to mention on that subject. When buying back its own stock, a company must be fully disclosed under Rule 10b-5. Subject to having a Rule 10b5-1 plan in place, which we'll discuss, the company can't buy back stock unless it has disclosed fully all material information to the marketplace.

Does that mean that a company should adhere to a trading window when it's buying back stock? I would first start with an insider trading policy. It may or may not apply to the company, strictly speaking. Even if its terms don't expressly apply to the company, the starting point is still the company - and typically it should try to comply with it. In some situations, under the right circumstances, a company may make a judgment that it's okay for the company to buy even at a time when insiders are precluded from trading.

That said, keep in mind that there will be Form 10-Q disclosures on a month by month basis. The world will know if the company was in a market during the last months of the quarter.

On a related point, if a material development arises that is undisclosed, you need to ensure that you put the brakes on buybacks immediately. As a result, the right people must be in the loop on both sides of that equation. That is, knowing material developments and being able to put the brakes on the program.

Your process should involve a disclosure test. I will remind you of that later. The company's intentions regarding buybacks are itself generally considered material information. A company needs to disclose buyback authority before exercising that authority.

Then you might ask, "How much disclosure should a company make about its buyback plans?" It is relatively common for a company to disclose that a board has authorized buybacks and the general limitations, without disclosing its specific intentions as to timing whether near or longer term.

My view is that more disclosure is better if you can make the disclosure. A company's circumstances may argue for more details - for example, if a company is responding to activist pressures and therefore wants to make its intentions clear to stave off that pressure.

A company should say something about how it might buy back stock, and that should be, in my view, be as broad as possible. By that I mean that you would reference privately negotiated transactions, 10b5-1 plans, and maybe even related party purchases as possibilities.

Of course, there is ongoing disclosure in your Form 10-Q or 10-K about buyback activity in the quarter that just ended and the remaining buyback authority. As I noted, that's on a month-to-month basis. Even if you haven't repurchased in the quarter, I recommend keeping current your disclosure about the remaining authority that you have. Ideally, you should give a hint as to when you might be exercising that authority.

A company should also consider the possibility of buybacks when it's giving guidance, particularly guidance focusing on EPS, because buybacks can then impact that guidance. I suggest giving share assumptions rather than estimates of share buybacks because the latter is a little more fluid. Earnings disclosure then down the road should include some mention of the favorable impact of buybacks at a minimum, by noting the weighted average number of shares outstanding in the current quarter compared to the prior year quarter.

There can also be compensation implications, and that has received more attention of late. A company, in my view, should be transparent about those potential implications in its public disclosures.

There can be disclosure associated with repurchases from a related party if that's a possibility. Again, go back to your initial disclosure and see if you contemplated that as a possibility. Also, you might have a policy in place that may require disclosure. While you're looking at the policy, consider whether there is a need for special approval of related party repurchases. Then there may be Item 404 disclosure in your proxy statement. There are also potential director independence implications if you're buying from a related party.

Also, from a disclosure perspective, be wary of Rule 13e-3 and 13e-4. Rule 13e-3 under the Exchange Act imposes requirements on going-private transactions, which can include repurchases that either had a reasonable likelihood or have a purpose of causing a class of your common stock to be held of record by fewer than 300 persons or be delisted. Rule 13e-4 applies to repurchases affected in the form of an issuer tender offer.

You should be careful about avoiding accidental tender offers. That's not often a problem, but it can be helpful to use a broker and avoid tight deadlines and pressures that can lead you to an accidental tender offer. There is also an exception to 13e-4 for so called odd-lot tender offers, which are offers to buy from holders who own less than 100 shares.

Fifth and finally on my execution topics is executing the buyback plan. You need to have decisionmakers at the company and an agreement on strategy and authority. Again, you need to cover the "fully disclosed" question as part of the process.

Also, watch trading by insiders. There is an affiliated purchaser concern and potential for aggregation. In addition, you don't want people involved in the buyback decisions and mechanics selling their stock at the exact time the company is buying. We alluded earlier to a debate about insiders selling in the wake of buyback announcements. This concern is more specific - it applies down the road when a buyback plan is being carried out, and what implications are there to those involved in the buyback mechanics? In fact, you might think of limiting insider sales in some way following a buyback announcement or in the wake of buyback purchases.

You need a broker to assist in the buybacks. Pick one or two that you can work with. There can be some issues along the way, and you'd like to have a friendly person helping you. Make sure you agree on financial and other terms. There will likely be some written engagement letters with the broker.

Consider whether to use a Rule 10b5-1 plan - Josh will address that in more detail shortly. Also, consider whether to use an accelerated repurchase plan, and then there is 10b-18 compliance, which was alluded to earlier. That provides a safe harbor from claims of market manipulation for a company in connection with buybacks through a broker or dealer. It does not protect the company from antifraud or nondisclosure allegations, so that is something to keep in mind.

The limits under 10b-18 are expressed as four conditions: (1) there is a manner of purchases, and you can only buyback through one broker or dealer on a single day; (2) there are limits on timing of purchases near the opening and the closing of the trading day; (3) there are price limitations; and (4) there are volume limitations.

So far, the SEC has emphasized that 10b-18 is neither mandatory nor exclusive. You can go outside the bounds of 10b-18, and that's not per se manipulative, at least under the current regime. No presumption will result from nonconformity, and there are companies that choose not to comply within 10b-18, although brokers get a little nervous when that happens.

Be wary of affiliated purchasers, which the 10b-18 test draws in. Also, 10b-18 does not apply to certain privately negotiated share repurchases. That's good and bad, but you have to be wary of it.

Accelerated share repurchase plans and forward contracts are off-market so they're not eligible for 10b-18. The 10b-18 safe harbor is not available for brokers covering transactions. Rule 10b-18 can be more complicated than you might think, and there are SEC FAQs on the subject.

Significant corporate events can raise issues in the context of 10b-18, as well. There's also Reg M that imposes limitations on a company while it's engaged in a distribution. In general, you're prohibited from buying your stock during a distribution, although it would be strange to buy when you're selling stock. Stranger things have happened, so you need to look at Reg M implications in your mechanics.

That is it as to best practices. If there are no questions or comments, Josh can address 10b5-1 plans.

Using Rule 10b5-1 Plans in Buybacks

Josh LaGrange, *Counsel, Skadden, Arps, Slate, Meagher & Flom*: Thanks Pat. As Pat mentioned when he was talking about disclosure, sometimes material developments do occur at the company while it's already engaged in a repurchase program, or maybe the company comes into some information that could be material, but it's not necessarily obvious.

Generally, when a company comes into material nonpublic information, it's going to need to suspend its repurchasing activity to avoid violating Rule 10b-5 or similar prohibitions. That brings us to the reason for considering using a Rule 10b5-1 plan as part of a buyback program.

I know most of the audience is familiar with Rule10b5-1, but, as a quick summary and to highlight the key points for this purpose, that rule creates an affirmative defense to claims that trading was based on MNPI.

A 10b5-1 plan is basically a trading decision made by the company at a time when it does not have material nonpublic information, to be implemented by someone else, usually a broker, without further influence by the company. A plan can specify individual transactions on certain dates, or it can operate by establishing a formulaic rule for trading based on external inputs like market price or volume.

Since trading under a Rule 10b5-1 plan can continue even when the company later comes into MNPI, it can be a useful tool for facilitating repurchasing even when the company may later be precluded from making discretionary repurchases. The big tension inherent in using a 10b5-1 plan as part of a buyback program, though, is that the company needs to cede control over that piece of its repurchase activity at the time it adopts the plan.

In order to get the protection of Rule 10b5-1, the plan needs to be entered into in good faith. So, it must be seen as a real commitment when a company adopts it. And that raises the question of what exactly the company is willing to commit to at the time it enters the plan, for example, how long should the plan last? How many shares should ultimately or potentially be covered by the plan?

It can be hard for a company to answer those questions and determine the specific repurchasing triggers that should be used under a Rule 10b5-1 plan, but it doesn't have to be an all-or-nothing approach. With some thought in advance, a company can operate a 10b5-1 plan that can continue to function even if the company has to cease its own volitional purchases. It can also make discretionary repurchases at the times that it doesn't have MNPI.

I should say that generally, when a company enters a repurchase plan with a broker, that one plan will be meant to comply with both Rule 10b5-1 and 10b-18. As Pat discussed, Rule 10b-18 creates some specific considerations for companies that might want to make discretionary repurchases while their repurchase plan is running. Most fundamentally, Rule 10b-18 says that the company can't use two brokers on any one day without compromising that safe harbor. In addition, the company needs to respect the daily volume limit across all of it repurchases.

There are a couple of other things to think about for a company that may want to both operate a plan and make discretionary repurchases. First, at a contractual level, the company obviously needs to make sure that the plan it enters with its broker permits the company to make additional repurchases outside of that plan.

Some form documents don't allow that, and they would need to be negotiated up front to avoid creating a later question of whether a plan has been modified after it's already adopted, which could create additional issues.

Second, to preserve the protection of Rule 10b5-1 for the transactions that happen under the plan, the discretionary transactions cannot influence the trading that occurs under the plan. For example, the volume of trading to be carried out under the Rule 10b5-1 and 10b-18 plan can't be contingent on the company's other repurchase activities.

Assuming the plan is meant to satisfy both of those rules, the volume limit that's available under the plan needs to be lower than the maximum volume limit that would be available under Rule 10b-18 itself. That needs to be true to provide some headroom for discretionary transactions to be carried out without impacting the plan transactions.

Really, if you want to do both Rule 10b5-1 repurchases and discretionary repurchases, then once the 10b5-1 plan is in place, the discretionary transactions need to accommodate the plan and its terms rather than the other way around. That must be considered when the terms of the plan are first being established.

When you have such an arrangement in place, where you have both operating, even when a company needs to pause its discretionary purchases, the Rule 10b5-1 plan buybacks can carry on. A 10b5-1 plan can be a helpful tool for achieving repurchase goals, especially for companies that often find themselves with material nonpublic information.

I want to circle back to one point that I touched on briefly earlier, to emphasize it. And that's that companies need to temper their enthusiasm for adopting a 10b5-1 plan with a realistic assessment of their ability to commit to the plan's terms, considering all the uncertainties that companies face at any given time.

That doesn't mean that subsequent events can never justify a company's decision to terminate or modify a plan. It means that a company shouldn't enter into a plan with the expectation that it's optional, or a soft commitment. I wouldn't expect many companies to look down the road and say, "Well, okay, we have so much certainty of our vision that we can adopt a plan right now that lasts two years. We know that these are going to be the right repurchasing triggers over that extended period."

Sometimes, when a company has a plan in place, there will be pressure to cancel it. I want to spend another minute on that topic. While it's true that potential purchases that never come to be, because the plan is cancelled, cannot themselves be Rule 10b5-1 violations, how a company treats a plan after it's first adopted can be a factor in any investigation whether the plan was initially entered in good faith.

The qualification that the plan was entered into in good faith is necessary to get the protection of the plan for all its transactions. A termination or a modification that suggests that the plan was not initially adopted in good faith can cost the company the protection of Rule 10b5-1 for the purchases that occurred under the plan before it was canceled. So, after the fact changes in how the plan operates can cost the company, or at least suggest a basis for costing the company, the benefit of the plan for the transactions that did in fact occur.

Switching gears briefly and emphasizing a point Scott made earlier, the House did pass a bill earlier this year, which is now in committee in the Senate, that would require the SEC to examine Rule 10b5-

1 practices and adjust the rule based on its findings. You need to be aware that all of what I said is subject to change and is the subject of current legislative attention. That change may be coming sooner rather than later.

Should a Rule 10b5-1 Plan Only Apply During Blackout Periods?

Quick: Josh, that was a good discussion about 10b5-1 plans. Now the question is, should that plan apply just during a blackout period or around the clock or calendar for a company?

I like to think that a company likes to have flexibility to make its own decision. That's the opposite of a 10b5-1 plan. To the extent it's possible, I recommend a company maintain buybacks outside the 10b5-1 plan while it can, because it gives it greater flexibility.

That said, I also suggest that a company should adopt the 10b5-1 plan early in a quarter, rather than waiting until the end of the quarter, so that it has its 10b5-1 plan in place to cover the blackout period while it can do that. The danger, of course, being that as a quarter moves along, if you haven't put your 10b5-1 plan in place, there could be some development as a result of which the company no longer is able to put the 10b5-1 plan in place.

That leads to the third question. If a company is making repurchases outside a 10b5-1 plan at the start of a quarter, should the 10b5-1 plan that it adopts apply during the open window or only during the blackout? There are two sides to that question.

My suggestion is that you try to structure a 10b5-1 plan that goes hand and glove with 10b-18 purchases during the open window to the greatest extent possible. At least you have a 10b5-1 plan in place that operates during what would ordinarily be an open window just in case the window closes to you.

Josh suggested that might be hard to do. But it is worth considering and exploring that possibility. I would then turn it back to Josh.

Use of Multiple Brokers & Plans

LaGrange: Thanks. The idea that you may have plans and discretionary transactions happening at different periods, or even potentially multiple plans in play, often raises the question of whether it's okay to have multiple 10b5-1/10b-18 plans in operation over the same period, whether truly contemporaneously or whether in some kind of alternating arrangement, and whether there are complications from doing that.

While it's certainly true that the simplest scenario is to work with one broker regarding one plan at a time, we do sometimes see overlapping plans. There's nothing inherently wrong with that under Rule 10b5-1. Of course, where the company is looking to Rule 10b-18 as well, it needs to consider that the requirements of that rule apply to all the company's transactions.

Specifically, the company needs to keep in mind that requirement that it use only one broker per day to satisfy Rule 10b-18 and that the rule creates a single daily volume limit that would apply to any transaction, or in the alternative creates the possibility of using one block trade per week.

That last point of a single block trade per week may be a good reason to say, "Well, at a minimum, we don't want two plans in operation in the same week," unless the company intends to hamstring one of the brokers or specifically allocate the possibility of a block trade with one of the brokers or otherwise get in a really micromanaging how the brokers implement the trading under multiple plans.

That said, if there are specific goals that a company is trying to achieve that really require using two brokers in the same week, even that's possible to do depending on the goals. Not all that long ago, I worked on overlapping plans where one traded one day per week and the other traded in the remainder of the week. In that case, we did have to address the block trades specifically.

Generally speaking, when I hear companies say that they have some interest in using multiple plans, it seems that a lot of the motive is either business or relationship reasons for one of the multiple brokers - say, to avoid being taken for granted as a captive client by a broker.

If that's the primary driver, then the company can probably achieve its goals by switching brokers when the company adopts a new plan every three or six months, or at least make the brokers reaudition for the business, rather than letting them treat it as a foregone conclusion that they'll always be selected for any subsequent plan.

How to Conduct Buybacks When Engaging in M&A

Meyerson: We're a little behind schedule, so I will do the concise version of conducting buybacks in connection with an M&A transaction.

For more than 15 years, the SEC has made it clear that doing share buybacks during a stock merger is something that's very sensitive because among other things, the acquiror has a financial interest in getting its stock price up to facilitate the merger being approved.

There is heightened scrutiny. In 2003 and 2004, the SEC changed some of the principal buyback rules in order to make it clear this was an activity that certainly should be done very carefully. Nevertheless, there are some good reasons why companies doing stock acquisitions also may want to be repurchasing shares.

There are many legitimate business reasons why companies want to do buybacks during an M&A deal - addressing flow-back issues from a cross-border stock acquisition, for example, or for some of the larger banks that have a Fed-approved program and a narrow window to buy back shares, not missing that window. There are three major rules that you need to navigate around in order to accomplish this.

The first is that Rule 10b-18, the safe harbor for share repurchases, is not available once an M&A deal involving any stock consideration is announced. Neither party, on the buying nor the selling side, has the benefit of the 10b-18 safe harbor for purchases of its own shares or purchases of the other party's shares.

There's a limited three-month lookback exception that says the acquiror can buy back shares consistent with its activity over the prior three months. In practice, that tends not to be useful because the parties probably had suspended their own share repurchases in the months leading up to the merger while they did due diligence and negotiated the deal because of the 10b-5 concerns. So that typically is not a very useful exemption.

What companies often do when they do want to do share repurchases after announcing a deal is make sure that they are completely transparent about it so there is no possible claim of market manipulation.

It typically means either in the press release announcing the deal or in a press release following the deal announcement, state the intention to buy back shares and potentially even how many shares you're considering buying back. When the proxy statement is going to be mailed, which triggers another restricted period (under Regulation M, discussed below), disclose in the proxy statement how many shares were repurchased and at what average price (or some other metrics), so the market and investors understand what effect the buybacks had on the market between deal announcement and the proxy mailing.

The second restriction is Regulation M. Regulation M applies to purchases by the acquiror or by the target of the acquiror shares, and it's an absolute ban. From the moment the proxy statement is mailed until the shareholders meet to vote on the merger, neither party can buy back the shares in distribution, which are the acquiror shares.

If there is a subsequent measuring period, for example, if it's a floating exchange ratio deal where the market price near closing determines the exchange ratio, that's also a restricted period. During this restricted period, there is also a flat ban on share repurchases. That would even include share repurchases pursuant to a previously adopted 10b5-1 plan.

The10b5-1safe harbor is basically protection from a 10b-5 claim. It does not override Reg M. If you had an outstanding 10b5-1 plan, you would have to terminate it because you can't have the agent in the market buying shares on your behalf while you have a proxy statement in the shareholders' hands.

The final one is Rule 10b-5, which basically is the same rule that applies to all share repurchases. The sensitivity in connection with a merger is that when you announce the merger, there may not be full information in the market about the merger, parties and financial effects of the merger. It's a judgment call in each case at what point between deal announcement and the mailing of the proxy there is enough information in the market that the purchaser feels comfortable that the investors can make an informed choice on whether to sell their shares or wait for the merger agreement to be completed.

That depends on a number of factors, including the complexity of the deal, size and its materiality to the acquiror. Companies should consider whether releasing the press release and the investor deck is enough for parties to feel comfortable that the market has full information.

Sometimes, parties feel more comfortable waiting until there's pro forma information that could be filed early, perhaps with an 8-K. Sometimes parties feel the deal is so complicated and material that they don't want to be buying shares until the market has full information, which would be the filing of the proxy statement itself.

It's a facts and circumstances determination that varies from deal to deal. It's one of the most critical decisions navigating around those three rules, but while complicated, it can be done. It is often important to the party's business plan that it has been done. Properly structured, it can safely be done.

Dunshee: Thank you, Lee, and thank you to all of our panelists for their insights today. Also, thanks to everyone who joined us to listen. The audio archive for this program will be available shortly, and we'll post the transcript of the program in a few weeks. Thanks again and have a great day.