BETTING ON ONESELF

ISSUER EQUITY DERIVATIVE TRANSACTIONS

IN RECENT YEARS, we have worked closely with our investment banking clients to structure and document various equity derivative transactions that public companies execute in relation to their own shares. Two such types of transactions are structured accelerated share repurchases and forward equity sales hedged with registered share borrow.

A structured accelerated share repurchase transaction typically involves the upfront acquisition by an issuer of a block of its shares borrowed by a dealer, followed by a period during which the dealer determines an average price for the issuer's shares. The average price is used to determine final settlement of the upfront share purchase. Highly structured variants of this transaction may provide for flexible pricing periods, discounted average pricing favorable to the issuer and embedded caps or collars limiting the range of the average settlement price. Issuers find this a cost-efficient means of implementing all or some portion of a share repurchase program.

A forward equity transaction permits the issuer to fix or collar a price for a specified number of its shares on an agreed forward date. These transactions may vary based on how the dealer establishes the fixed forward price or collar range, computes the final price at maturity and determines the final maturity date. Typically, the dealer will borrow shares that it sells short to hedge its exposure under the forward transaction. These sales will be made by the dealer pursuant to a prospectus relating specifically to the borrowed shares. Issuers have found these transactions enable them to establish firm equity financing costs for projected future growth or acquisition needs. We also have assisted our dealer clients in a similar use of registered borrow involving short sales intended to facilitate hedging activities associated with convertible bond issuances.

While serving different purposes, each transaction structure implicates a broad array of issues under U.S. securities laws. The fact that the issuer is itself a counterparty to these transactions makes the securities law analysis more challenging, requiring that particular attention be paid to any possibility that the issuer's status might be attributable to the dealer as a result of the economics of the transaction. We work closely with our dealer clients to structure transactions that achieve the desired results from a securities law perspective. The intense focus on securities law compliance is almost always accompanied by significant tax and accounting issues. Each transaction structure presents different potential tax and accounting outcomes for issuers and, accordingly, must be structured to optimize these results. We work to help our clients develop structures that resolve tensions between the tax and accounting regimes without compromising our client's ability to comply with applicable securities laws. Not surprisingly given the nature of the equity derivatives market, we often find ourselves providing this assistance under tight timeframes and on relatively short notice.