[redacted]

By Hand

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Dear Melea and Dick:

In my recent discussions with the Premerger Notification [redacted] evident that the Office has not yet developed a comprehensive set of interpretations concerning the various Hart-Scott issues that these entities may present. I thought writing a letter would be [redacted] questions I have raised.

It is important to emphasize that I have asked about proper [redacted] company not limited liability companies in general. Under the [redacted] partnerships nor corporations, although they may closely resemble one or the other depending upon the terms of the particular company's limited liability company agreement. As stated in the Act, "It is the policy of this [Act] to give maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements." Id. at § 18-1101(b).

My questions thus relate to the following specific fact situation. A, B, and C intend to form X, a limited liability company, pursuant to the Delaware Limited Liability Company Act. Assume any applicable size tests are satisfied. The limited liability company agreement establishing X will provide for the following:

(a) X will have a manager or board of managers who will exercise functions similar to those exercised by a corporation's board of directors;

(b) X will issue voting interests to A, B, [redacted] vote for the manager or members of the board of managers;

(c) X will issue nonvoting interests to D, analogous to nonvoting, nonconvertible preferred stock in a corporation. These interests will, thus, not entitle D to vote for the manager or board of managers.

(d) A, B, C, and D will each contribute [redacted]

Pursuant to 16 C.F.R. § 803.30(a), I request an informal [redacted]

1. **Is the above formation transaction, in which [redacted] voting interests, subject to a reporting obligation?**

Under the Commission's rules, the answer should be "no," because a Delaware limited liability company is not a [redacted]

reportable, by virtue of § 801.40. The Statement of Basis and

> . . . [O]nly the formation of corporations the voting securities of which will be held [redacted]

applies only to the formation of [redacted]

than corporations is by virtue of this rule, not brought within the coverage of the act

43 Fed. Reg. 33450, 33485 (July 31, 1978).

The Statement of Basis and Purpose, the HSR Act, and the regulations all recognize that entities other than corporations can, in fact, issue voting securities. Id. at 33487. Clayton

have been adopted):

> There is evidence that Congress intended
>
> noncorporate entities. Section 7A(b)(3)(A) states:
>
> > The term "voting securities" means any securities which * * * entitle the owner or holder thereof to vote for the election of directors of the issuer or, with respect to unincorporated issuers, persons exercising similar functions.
>
> However, the Commission has instructed its
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> whether the rules provide appropriate
>
> prior to the transaction should not, of course, be construed as a Commission statement that such transactions are free

43 Fed. Reg. at 33487 (emphasis added).

Based upon these clear statements of the Commission's official position, it appears that the transaction in which X is formed should not be reportable under Hart-Scott.

2. **Are the interests to be held by A, B, C, and D "voting securities"?**

It seems plain under the rules that the interests to be held

Section 7A(b)(3)(A) of the Act and § 801.1(f)(1) of the regulations define "voting securities" identically, as follows:

> securities which at present or upon conversion entitle the owner or holder thereof to vote for the election of directors of the issuer, or of an entity included within the same person as the issuer, or, with respect to unincorporated entities, individuals exercising similar functions.

(Emphasis added.)

Applying this definition here is straightforward. X will be an unincorporated entity managed by a manager or board of managers who will exercise functions similar to those of a corporation's board of directors. The interests held by A, B, and C will be securities entitling the holder to vote for the

therefore should qualify as "voting securities."

On the other hand, the interests to be held by D will not entitle D to vote for the election of any managers, and D's interests will not be convertible into any such voting interests. Therefore, D's interests should not qualify as "voting

3. **How is "control" of X, the limited liability company, to be determined?**

It seems plain under the rules that control of X should be governed by §§ 801.12(b) and 801.1(b)(1)(i). Section 801.12(b)

sets forth the generally applicable rules for determining the percentage of an issuer's voting securities that a person holds. Section 801.1(b)(1)(i) provides that the term "control" means:

> Holding 50% or more of the outstanding voting securities of an issuer . . . .

As discussed above, the interests to be held by A, B, and C constitute voting securities. Since X is plainly the "issuer" of these securities, the § 801.1(b)(1)(i) test is clearly applicable.

The rules do not provide that an "issuer" must be a corporation. Indeed, given that an unincorporated entity may have voting securities, as recognized in § 7A(b)(3)(A) and § 801.1(f)(1), it seems axiomatic that an unincorporated entity may therefore be an "issuer." X would therefore be controlled by a person with 50% or more of X's voting securities. A person such as D, who would hold only nonvoting securities, could not control [redacted]

The alternative control test in § 801.1(b)(1)(i), applicable to partnerships, is based upon right to profits and right to [redacted] the case of an entity that has no outstanding voting securities." Because X will be an entity that has outstanding voting securities, this alternative test would be inapplicable.

4. Assuming arguendo that § 801.40 applies to the formation transaction, how should the transaction be analyzed?

If the Premerger Office determines that § 801.40 applies to the formation transaction of this noncorporate entity, despite the Commission's official position that formation of noncorporate entities is not reportable, it would seem that the normal § 801.40 rules applicable to corporations should be used. Thus, X [redacted] were met and no exemption applied. D would have no reporting obligation because D would be acquiring only nonvoting securities.

[redacted]

[redacted]
July 6, 1993

[redacted]

Very truly yours,

[redacted]

cc: John M. Sipple, Jr., Esquire