

6 801.40 [LLC formation]

October 2, 1996

Via Facsimile 202 326-2624

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Federal Trade Commission
Premerger Notification Office
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PREMERGER NOTIFICATION OFFICE
FEDERAL TRADE COMMISSION

Re: HSR Reportability of Limited Liability Company Formation

Dear Dick:

I am writing to confirm the understanding I gained from our telephone conversation of the morning of Friday, September 13. The conversation concerned the circumstances under which the formation of a limited liability company ("LLC") is reportable under the Hart-Scott-Rodino Antitrust Improvements Act (the "HSR Act" or "the Act") and encompassed a number of letters addressed to you on that subject. I also want to present to you my understanding of another HSR letter which we did not discuss.

Our September 13 conversation included the following points:

1. When a contemplated transaction meets certain other threshold

Commission. The Act defines voting securities as "any securities which at present or upon conversion entitle the owner or holder thereof to vote for the

¹These other requirements are the Commerce Test of 16 C.F.R. §801.40(d), the Size of Person Test of 16 C.F.R. §801.40(b)(1)-(2), and the Size of Transaction Test found at 15 U.S.C. §18a(a)(3).

²15 U.S.C. § 18a(a). See also 16 C.F.R. § 801.40(b).

³15 U.S.C. § 18a(b)(3)(A).

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unincorporated. Thus, whether the formation of an LLC is a reportable event depends on whether the LLC members receive interests entitling the members to vote for or otherwise select a decision-making body that is functionally equivalent to a board of directors.

2. When a proposed transaction involves an LLC and the LLC contains a

a two-step analysis to determine reportability. The first step involves the identity of the persons who serve on that putative board equivalent. If all those persons will necessarily be:

- a. members of the LLC, or
- b. in the case of an LLC member that is an organization, directors, officers, or employees of the organization serving on the putative board equivalent as representatives of the organization.

3. That second step considers whether the putative board equivalent performs

and supervising overall operations. Running an LLC's day-to-day operations does not involve board-equivalent functions.

4. Voting securities are involved only if the putative board equivalent includes "outsiders" and performs board equivalent functions. As a result, and because your office looks first at the "outsider" issue, your office reaches the second step of the analysis only when a putative board equivalent exists and "outsiders" are to be present on the board equivalent.

5. A letter addressed to you dated November 20, 1995, involved an LLC with an

corporate LLC members. The advisory board also had the power to remove the LLC's CEO. The handwritten comments on the letter indicate that the advisory board was not deemed to be a board equivalent at least in part because it lacked the *exclusive* power to remove the CEO, a power a corporate board usually does hold exclusively. It is noted that, according to the letter, the advisory

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board had the power to resolve deadlocks between the two members and therefore in practice might hold ultimate management power. You explained that, he that as it may, the power to resolve deadlocks between shareholders is not

power to resolve deadlocks between the members was no reason to characterize the advisory board as a board equivalent. You also said that this

office and that we did not discuss in our October 19 telephone conversation. That

by a board of governors, with some of the governors appointed by each member. While the foundation member could appoint to the board only officers, directors, or employees of the foundation, the other organization was able to appoint outsiders. The handwritten comments on this letter indicate that the transaction was not reportable because only one of the parties involved would be receiving voting securities. Under

views as non-reportable the formation of an LLC in which only one member receives

Since



of AD I agreed with her conditions

Here, 801.40 required that two former persons of one stock. If only one does so (and voting stock which comes to be) then there is no reportable event under 801.40. Sec. 802.303 is not applicable to 801.40 by its specific language.

Richard B. Smith