

[Billing Code 675001-P]

FEDERAL TRADE COMMISSION

16 CFR Parts 801, 802 and 803

RIN 3084-AB46

Premerger Notification; Reporting and Waiting Period Requirements

AGENCY: Federal Trade Commission.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: The Federal Trade Commission (“FTC” or “Commission”) is issuing this advance notice of proposed rulemaking (“ANPRM”) to gather information, related to seven topics, that will help to determine the path for future amendments to the premerger notification rules (“the Rules”) under the Hart-Scott-Rodino Antitrust Improvements Act (“the Act” or “HSR”). This ANPRM relates to Parts 801, 802 and 803 of the Rules.

DATES: Comments must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]

ADDRESSES: Interested parties may file a comment online or on paper, by following the instructions in the Invitation to Comment part of the SUPPLEMENTARY

INFORMATION section below. Write “16 CFR Parts 801, 802, 803: Hart-Scott-Rodino

Rules ANPRM, Project No. P10014” on your comment. File your comment online at

<https://www.regulations.gov> by following the instructions on the web-based form. If you

prefer to file your comment on paper, mail your comment to the following address:

Federal Trade Commission, Office of the Secretary, 600 Pennsylvania Avenue NW, Suite

CC-5610, (Annex J) Washington, DC 20580, or deliver your comment to the following

the Secretary, 600 Pennsylvania Avenue NW, Suite CC-5610, (Annex J), Washington, DC 20580, or deliver your comment to the following address: Federal Trade Commission, Office of the Secretary, Constitution Center, 400 7th Street SW, 5th Floor, Suite 5610 (Annex J), Washington, DC 20024. If possible, please submit your paper comment to the Commission by courier or overnight service.

Because your comment will be placed on the publicly accessible website, <https://www.regulations.gov>, you are solely responsible for making sure your comment does not include any sensitive or confidential information. In particular, your comment should not include sensitive personal information, such as your or anyone else's Social Security number; date of birth; driver's license number or other state identification number, or foreign country equivalent; passport number; financial account number; or credit or debit card number. You are also solely responsible for making sure your comment does not include any sensitive health information, such as medical records or other individually identifiable health information. In addition, your comment should not include any "trade secret or any commercial or financial information which . . . is privileged or confidential," – as provided by Section 6(f) of the FTC Act, 15 U.S.C. 46(f), and FTC Rule 4.10(a)(2), 16 CFR 4.10(a)(2) – including in particular competitively sensitive information such as costs, sales statistics, inventories, formulas, patterns, devices, manufacturing processes, or customer names.

Comments containing material for which confidential treatment is requested must be filed in paper form, must be clearly labeled "Confidential," and must comply with FTC Rule 4.9(c). In particular, the written request for confidential treatment that

accompanies

may violate the antitrust laws if consummated and, when appropriate, to seek injunctions in federal court to prohibit anticompetitive transactions prior to consummation.

Section 7A(d)(1) of the Clayton Act, 15 U.S.C. 18a(d)(1), directs the Commission, with the concurrence of the Assistant Attorney General, in accordance with the Administrative Procedure Act, 5 U.S.C. 553, to require that

§ 801.1(i)(1) *Solely for the purpose of investment.*

§ 801.10(c)(2) *Acquisition price.*

§ 801.10(c)(3) *Fair market value.*

§ 801.90 *Transactions or devices for avoidance.*

PART 802 – EXEMPTION RULES

§ 802.2 *Certain acquisitions of real property assets.*

§ 802.5 *Acquisitions of investment rental property assets.*

§ 802.9 *Acquisition solely for the purpose of investment.*

§ 802.21 *Acquisitions of voting securities not meeting or exceeding greater notification threshold (as adjusted).*

§ 802.31 *Acquisitions of convertible voting securities.*

§ 802.64 *Acquisitions of voting securities by certain institutional investors.*

PART 803 – TRANSMITTAL RULES

Appendix A to Part 803 Notification and Report Form for Certain Mergers and Acquisitions

Appendix B to Part 803 Instructions to the Notification and Report Form for Certain Mergers and Acquisitions

Background

Although it regularly reviews the Rules and revises them on a rolling basis, the Commission is issuing this ANPRM to solicit information to support review of the Rules on a more unified basis as part of its systematic review of all FTC rules and guides. The Commission is aware that market and business practices are constantly evolving, and that these changes make it especially important to evaluate whether the Rules are still serving their intended purpose or if they need to be amended, eliminated, or supplemented.

To accomplish this, the Commission is publishing in this ANPRM a number of questions related to seven different topics about which questions frequently arise in discussions of the Rules: Size of Transaction, Real Estate Investment Trusts, Non-Corporate Entities, Acquisitions of Small Amounts of Voting Securities, Influence

outside the Scope of Voting Securities, Devices for Avoidance, and Filing Issues.

Answers to questions on these topics will provide information that may facilitate drafting of new or revised rules.

The Commission welcomes comments on all of these topics, or on any sub-topic within them. The Commission, however, does not expect that every commenter will address all seven topics, or even every question relating to each topic. The Commission notes that comments it receives in response to this ANPRM may also inform the Notice of Proposed Rulemaking regarding the proposed change in the § 801.1(a)(1) definition of “person” and

Under 16 CFR 801.10(c)(2), the Acquisition Price “shall include the value of all consideration for such voting securities, non-corporate interests, or assets to be acquired.”² The FTC’s Premerger Notification Office (“the PNO”) has long taken the position that, when a transaction has a determined Acquisition Price, debt may be excluded from the Acquisition Price in certain circumstances. For example, if a buyer pays off a target’s debt as part of the transaction, the buyer may deduct the amount of the retired debt from the Acquisition Price. This position dates from the earliest days of interpreting the HSR Rules in the late 1970s and early 1980s and is based, in part, on the analysis of a target’s balance sheet liabilities in the context of an acquisition of voting securities.

The PNO has also allowed the deduction of certain expenses when calculating the Acquisition Price. For example, where the purchase price in the parties’ transaction agreement includes funds earmarked to pay off the seller’s transaction expenses, the PNO has permitted the parties to deduct that amount when calculating the Acquisition Price based on the view that such payments do not reflect consideration for the target.

The Commission is aware that these informal PNO staff positions can have a significant impact on the calculation of the Acquisition Price and, in turn, on whether a transaction is reportable under the Act. Given the potential for these positions to affect the structure of a transaction, the Commission believes these informal PNO staff positions may need revision. As a result, the Commission aims to understand the

² 16 CFR 801.10(c)(2).

- f. Are there any limitations (legal or otherwise) on a buyer's ability to pay off or retire debt as part of the deal?

- e. Do sellers ever reject a buyer's offer to pay such expenses as part of the deal?
Under what circumstances? How have these circumstances evolved since the late 1970s/early 1980s? Have the competitive implications of the deal ever been a factor in this decision?
 - f. Are there any limitations (legal or otherwise) on a buyer's ability to pay such expenses as part of the deal? If so, what are they? Do these limitations differ from limitations in place in the late 1970s/early 1980s? If they differ, how do they differ?
 - g. Are buyers more or less likely to pay such expenses as part of the deal now than they were in the late 1970s/early 1980s? Why or why not?
3. How do parties currently calculate the Acquisition Price? How has the calculation changed since the late 1970s/early 1980s?
- a. Under what conditions is the Acquisition Price different from the purchase price or consideration identified in the transaction agreement? Have these conditions changed since the late 1970s/early 1980s? If they have changed, how have they changed?
 - b. Do transaction agreements ever lack a firm or certain purchase price? Under what conditions? Have these conditions changed since the late 1970s/early 1980s? If they have changed, how have they changed?
 - i. Why would parties negotiate a deal without a firm or certain purchase price? What factors have affected such a decision or deal structure? Have these factors evolved since the late 1970s/early 1980s? If they have

changed, how have they changed? Have the competitive implications of the deal ever been a factor in this negotiating a deal without a firm or certain purchase price?

ii. What are the limits on the scope of the undetermined payments or deductions? Have these limits changed since the late 1970s/early 1980s? If they have changed, how have they changed?

c. Can an Acquisition Price be subject to undeterminable deductions or deductions of undeterminable value? Under what conditions? Have these conditions evolved

since 1980 (1980s)?

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determination changed since the late 1970s/early 1980s? If it has changed, how has it changed?

- g. Does the form of employee compensation affect whether it is included in the Acquisition Price? Under what circumstances? Has this determination changed since the late 1970s/early 1980s? If it has changed, how has it changed?
- h. Is the value of employee compensation ever deducted from the Acquisition Price? Why or why not? Under what circumstances? Has this determination changed since the late 1970s/early 1980s? If it has changed, how has it changed?
- i. Is there a “control premium” associated with the acquisition of control? How does

an Acquisition Price determine that Control Premium is a Control Premium?

- d. Are any categories of payments excluded from the above definition of “consideration?” Why or why not? Has this changed since the late 1970s/early 1980s? If it has changed, how has it changed?
 - e. Is the ultimate recipient of the payment ever a factor in whether such payment is included as consideration? Why or why not? Has this changed since the late 1970s/early 1980s? If it has changed, how has it changed?
5. When calculating the Acquisition Price, how does debt affect the calculation? How has this approach changed since the late 1970s/early 1980s?
- a. Does the debt reported on the target’s balance sheet affect the calculation of the Acquisition Price? Why or why not? In what circumstances? Should it? Why or why not? Has this changed since the late 1970s/early 1980s? If it has changed, how has it changed?
 - b. Does the buyer’s pay off or retirement of debt affect the calculation of the Acquisition Price? Why or why not? In what circumstances? Should it? Why or why not? Has this changed since the late 1970s/early 1980s? If it has changed, how has it changed?
 - c. Does the treatment of debt (either reported on a balance sheet or being paid off or retired by the buyer) differ based on whether the acquisition is of (1) voting securities, (2) non-corporate interests, or (3) assets? Why or why not? Should it? Why or why not? Has this changed since the late 1970s/early 1980s? If it has changed, how has it changed?

- d. Should the calculation of Acquisition Price focus on the total amount paid by the Acquiring Person (including debt that is paid off or retired) or the net amount received by the Acquired Person (excluding debt that is paid off or retired)? Why? Has this changed since the late 1970s and early 1980s? If it has changed, how has it changed?
- 6. Where an acquisition is of voting and non-voting securities, how is the Acquisition Price allocated between the voting securities and the non-voting securities? How has this approach changed since the late 1970s/early 1980s?
 - a. Are the voting securities and non-voting securities separately valued? Why or why not? Has this changed since the late 1970s/early 1980s? If it has changed, how has it changed?
 - b. Are each of the voting securities and the non-voting securities valued? Why or why not? Has this changed since the late 1970s and early 1980s? If it has changed, how has it changed?

B. Fair Market Value (16 CFR 801.10(c)(3))

Sometimes a transaction does not have a determined Acquisition Price. This is often due to the fluctuation in stock prices or the inability to calculate the exact amount of contingent future payments. As a result, the Fair Market Value (“FMV”) of the transaction becomes critical to determining reportability under the Act.

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function by such board or officials.” Once the Acquiring Person, or its delegate, has determined the FMV, there is no requirement to share with the Agencies the details of how that FMV was determined. The Commission would like to understand better the determination of FMV through responses to the following questions:

1. When an Acquiring Person is evaluating the potential acquisition of voting securities, non-corporate interests, or assets, what methodologies does that Acquiring Person use to support valuation in the ordinary course of due diligence and negotiation of the acquisition? How have these methodologies changed since the late 1970s/early 1980s?
 - a. If an acquisition involves the acquisition of non-voting securities, what methodologies does the Acquiring Person use to value the non-voting securities? Have these methodologies changed since the late 1970s/early 1980s? If they have changed, how have they changed?
 - b. In an acquisition of both voting securities and non-voting securities, does the Acquiring Person ever use one methodology to value the voting securities and a different methodology to value the non-voting securities? Why or why not? Have these methodologies changed since the late 1970s/early 1980s? If they have changed, how have they changed?
 - c. Where the Acquiring Person receives board appointment or board designation rights (or their non-corporate equivalent) in conjunction with the acquisition of voting (or non-voting) securities, do those rights

non-voting) securities acquired? Has this changed since the late 1970s/early 1980s? If this has changed, how has it changed?

2. How does the determination of FMV under 16 CFR 801.10(c)(3) differ from the Acquiring Person's determination of value in the ordinary course of due diligence and negotiation of an acquisition? How has this determination changed since the late

1970s/early 1980s?

- a. What factors go into determining FMV? Do these factors vary by industry, type of acquisition (asset, non-corporate interest, intellectual property), size of the target, or for other reasons? Describe each of the ways these factors vary and how each one varies. How have these factors changed since the late 1970s/early 1980s? Are there difficulties involved in performing FMV analyses? If so, what are those difficulties? Have these difficulties changed since the late 1970s/early 1980s? If they have changed, how have they changed?

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what type of transactions should the Commission require independent FMV analysis? If the Commission requires an independent analysis, who should conduct the FMV analysis?

3. When calculating the FMV because the Acquisition Price is not determined as a result of future or uncertain payments, what financial or valuation concepts are used to determine the value of those future or uncertain payments? Have these concepts changed since the late 1970s/early 1980s? If they have changed, how have they changed?

4. How does an Acquiring Person determine the present FMV of assets that are not yet commercialized? For example, how does an Acquiring Person determine the present FMV of intellectual property surrounding a product that currently is under development? Has this determination changed since the late 1970s/early 1980s? If it has changed, how has it changed?

5. In determining the FMV, how does the Acquiring Person account for the value of any assumed liabilities (or liabilities of the Acquired Entity)? What impact do such liabilities have on the FMV? Has this determination changed since the late 1970s/early 1980s? If it has changed, how has it changed?

6. Should the Commission require the Acquiring Person to provide the basis for its FMV determination? If so, why? If not, why not?

be limited to “clearly passive income from real estate investments, as contrasted to income from the active operation of businesses involving real estate,” and those real estate trusts engaging in active business operations would not be afforded REIT tax status.³

As a result, the PNO has long taken the informal staff position that when a REIT acquires real property (and assets incidental to the real property), the acquisition is exempt from HSR reporting under section 7A(c)(1) of the Clayton Act, the statutory ordinary course of business exemption. This position is based on the presumption that REITs are solely buying, owning, leasing, and selling real property, and therefore any acquisition of real property is exempt because it is done in the ordinary course of the REIT’s business and is unlikely to violate the antitrust laws.

The Commission is aware that the Internal Revenue Service (“IRS”) subsequently made changes in tax law to remove restrictions on REITs and expand the beneficial tax treatment. As a result, many REITs are no longer solely buying, owning, leasing, and selling real property..

detail the current structure and operation of REITs through responses to the following questions:

1. Have REITs evolved from entities that own only real property to entities that can hold operating companies?
 - a. If so, what has led to the evolution of REITs becoming entities that can hold operating companies?
 - b. How have changes in tax laws or regulations influenced this evolution?
2. How does an operating company convert to a REIT?
 - a. Do REIT structures involve one Ultimate Parent Entity ("UPE")? Two UPEs? How often is each type used? Why?
 - b. If a REIT has more than one UPE, what is the relationship between those UPEs?
 - c. If a REIT has more than one UPE, is there an entity above the UPEs that makes decisions for both of them?
3. Is there a way to distinguish REITs that own only real property from those that hold operating companies? If yes, what are the ways to distinguish REITs that own only real property and those that hold operating companies? In what instances are there differences in how they are structured? How else are they different?
4. Assume the PNO's informal staff position exempting REITs did not exist and REITs had to rely solely on the real property exemptions, §§ 802.2 and 802.5.
 - a. Are there situations in which REIT transactions would no longer be exempt? If so, what kinds of situations?
 - b. How often would the §§ 802.2 and 802.5 exemptions come into play?

- c. **Would it be easy for REITs to apply § 802.2 and 802.5 to transactions? If so, why? If not, why not?**

III. Non Corporate Entities (16 CFR 801.1f(1)(ii))

The Act applies to acquisitions of voting securities or assets. The rise of non corporate entities, such as partnerships and limited liability companies, has presented challenges under the Act because the PNO had long taken the position that interests in unincorporated entities were neither voting securities nor assets. Thus, any acquisition of interests in such entities had not been a reportable event unless 100% of the interests was acquired, in which case the acquisition was deemed to be that of all of the underlying assets of the partnership or other unincorporated entity.”

- b. Have the distinctions between NCIs and voting securities evolved since 2005? If they have evolved, what significant changes have occurred to make NCIs and voting securities more or less distinct between 2005 and now?
 - c. Are NCIs currently the same as voting securities? If not, how are they different? Is this different from 2005? If so, how? What has changed between 2005 and now?
 - d. Does any category of NCI currently carry a right equivalent to the right to vote for the election of the board of directors of a corporate entity? Is this different from 2005? If so, how? What has changed between 2005 and now?
 - e. Should the reporting obligations for the acquisition of an interest in a corporate entity and noncorporate entity differ? Is this different from 2005? If so, how? What has changed between 2005 and now?
2. Have the benefits and drawbacks of becoming an NCE evolved since 2005? If so, what have they changed between 2005 and now? Have the incentives to become an NCE changed?

resulted in some investment entities holding small stakes in a large number of firms, including competitors. This has caused some to raise concerns about the competitive effects of common ownership – that is, the competitive effect of an investor holding small minority positions in issuers that operate competing lines of business.¹¹

In light of these developments, the Commission is using this ANPRM to take a fresh look at the rules that apply to acquisitions of voting securities by investment entities to determine whether updates may be necessary. The Commission seeks information on the following rules:

A. Definition of “solely for the purpose of investment” (16 CFR 801.1, 802.9)

Section (c)(9) of the HSR Act exempts from the requirements of the Act “acquisitions, solely for the purpose of investment, of voting securities, if, as a result of such acquisition, the securities acquired or held do not exceed 10 per centum of the outstanding voting securities of the issuer.” To implement this statutory limitation, 16 CFR 802.9 exempts from the requirements of the Act an acquisition of voting securities if made solely for the purpose of investment and if, as a result of the acquisition, the Acquiring Person would hold 10% or less of the outstanding voting securities of the issuer, regardless of the dollar value of the voting securities so acquired or held. Under 16

CFR 801.1(i)(1), “[v]oting securities are held or acquired solely for the purpose of investment if the person holding or acquiring such voting securities has no intention of participating in the formulation, determination, or direction of the basic business decisions of the issuer.”¹²

In light of changing investor engagement with issuers, the Commission is interested in knowing if it is appropriate to rethink the definition of “solely for the purpose of investment” in 16 CFR 801.1(i)(1) and the exemption in 16 CFR 802.9. To that end, the Commission seeks to understand the incentives involved in applying the exemption in 16 CFR 802.9 through responses to the following questions:

1. The ability to rely on 16 CFR 802.9 depends on whether a potential filing person “has no intention of participating in the formulation, determination, or direction of basic business decisions of the issuer.”¹³
 - a. Are there benefits to this approach? If so, what are the benefits?
 - b. Are there drawbacks to this approach? If so, what are the drawbacks?
 - c. How could this approach be changed? How would such a change impact investors and issuers?
 - d. What are the “basic business decisions” of the issuer?
 - i. Is it clear what decisions comprise the “basic business decisions” of the issuer?

¹² 16 CFR 801.1(i)(1).

¹³ 16 CFR 801.1(i)(1).

- ii. Are there activities that clearly do not relate to the basic business decisions?
 - iii. Are there activities that clearly do relate to the basic business decisions?
 - iv. Is there uncertainty about whether an activity relates to the basic business decisions? If so, why is there uncertainty? To what extent is there uncertainty about whether an activity relates to the basic business decisions?
- e. Should the Commission define the “basic business decisions of the issuer” as used in the existing Rule?
- i. What should the definition include?
 - ii. Should specific items be excluded from the definition? Which items?
 - iii. What are the benefits of providing a definition?
 - iv. What are the risks of providing a definition?
- f. Is it clear what is meant by “no intention of participating” in the formulation, determination, or direction of the basic business decisions?
- i. What type of activity related to determining whether to participate in business decisions currently takes one out of the exemption, or at what point in the process of deciding whether to participate in business decisions is one no longer within the exemption?
 - ii. What type of activity related to determining whether to participate in business decisions should result in the exemption no longer applying, or at

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3. How does the Commission's interpretation of "solely for the purpose of investment" compare to the Securities and Exchange Commission (SEC) approach to "passive" investors?¹⁴
- Assuming no change in the SEC approach, could the Commission adopt the SEC approach? If yes, why? If no, why not?
 - What would be the benefits of adopting the SEC approach? Why?
 - What would be the drawbacks of adopting the SEC approach? Why?
 - Does the different role of each agency justify different approaches for investors who hold positions solely for the purpose of investment? If yes, why? If no, why not?
4. How does the Commission's interpretation of "solely for the purpose of investment" compare to the elements that must be disclosed in Item 4 of Schedule filed with the SEC?¹⁵

¹⁴ Under SEC Rule 13d(c), certain beneficial owners may file a short form statement on Schedule 13G in lieu of a 13D statement if that person "has not acquired the securities with any purpose, or with the effect, of changing or influencing the control of the issuer, or in connection with or as a participant in any transaction having that purpose or effect,"

- a. Assuming no change to the SEC rule, could the Commission adopt the SEC elements? If yes, why? If no, why not?
 - b. What would be the benefits of adopting the SEC elements?
 - c. What would be the drawbacks of adopting the SEC elements?
 - d. Does the different role of each agency justify different approaches for investors who hold positions solely for the purpose of investment?
5. How do the activities of investment firms differ from those of operating companies?
- a. Should the Commission treat different types of acquirers differently for the purpose of the exemption? If yes, why? If no, why not?

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- (a) The acquisition by any person of additional securities of the issuer, or the ~~disposit~~ securities of the issuer;
 - (b) An extraordinary corporate transaction, such as a merger, reorganization or liquidation, involving the issuer or any of its subsidiaries;
 - (c) A sale or transfer of a material amount of assets of the issuer or ~~as~~ subsidiaries;
 - (d) Any change in the present board of directors or management of the issuer, including any plans or proposals to change the number or term of directors or to fill any existing vacancies on the board;
 - (e) Any material change in the present capitalization or dividend policy of the issuer;
 - (f) Any other material change in the issuer's business or corporate structure, including but not limited to, if the issuer is a registered closed

- c. Would such a conditioning of the loss of the exemption be consistent with the wording of the statute, including “solely” and the “purpose” of the acquisition? If yes, why? If no, why not?
- i. Is the acquisition solely for investment if the Acquiring Person is considering taking action inconsistent with the exemption, but has not yet taken the action?
 - ii. Is the acquisition for the purpose of investment if the Acquiring Person has determined to take action inconsistent with the exemption, but has not yet taken the action?
- d. Should the Commission require an HSR filing for past acquisitions once the specified actions have been taken? If yes, why? If no, why not?
- i. Would this be consistent with the HSR Act’s requirement to make the filing prior to the acquisition? If yes, why not?

generally uninterested in “affecting management of the companies whose stock they buy” (e.g., broker-dealers).¹⁶ The list identifying what type of entities considered an institutional investor, which has never been updated, includes:

(1) A bank; (2) Savings bank; (3) Savings and loan or building and loan company or association; (4) Trust company; (5) Insurance company; (6) Investment company registered with the SEC; (7) Finance company; (8) Broker-dealer within the meaning of the SEC; (9) Small Business Investment Company or Minority Enterprise Small Business Investment Company as defined by the SBA; (10) A stock bonus, pension, or profit-sharing trust as defined by the IRS; (11) Bank holding company as defined by statute; (12) An entity which is controlled directly or indirectly by an institutional investor and the activities of which are in the ordinary course of business of the institutional investor; (13) An entity which may supply incidental services to entities which it controls directly or indirectly but which performs no operating functions, and which is otherwise engaged only in holding controlling interests in institutional investors; or (14) A profit entity as defined by the IRS.

It is unclear to the Commission whether this exemption should be maintained and implemented in the same manner in which it was first promulgated in 1978. In light of changes in the investor landscape since that time, the Commission may need to update the list of institutional investors that are presumed to engage in acquisitions solely for the purpose of investment. Thus, the Commission aims to understand the current institutional investor landscape in order to make that determination through responses to the following questions:

1. Given that 16 CFR 802.64 has not changed since 1978, does it need to be updated?

¹⁶ 43 FR 33450, 33503 (July 31, 1978).

¹⁷ 16 CFR 802.64.

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- iv. Does the amount, degree, or type of issue discussed vary by issuer, or are there consistent themes of discussion and engagement? Has this changed since 1978? If so, how has this changed?
 - v. When do institutional investors participate in the formulation, determination, or direction of the basic business decisions of issuers? Has this changed since 1978? If so, how has it changed?
- b. How do index funds fit within the portfolios of institutional investors? Have index funds evolved since 1978? If so, how have they evolved?
- i. Why do institutional investors choose to create an index fund, exchange traded fund or the like? What are the benefits and drawbacks of creating such a fund?
 - ii. How does the acquisition of voting securities held by an index fund, exchange traded fund, or the like occur? Do acquirers use an algorithm or some other automated mechanism to facilitate acquisitions?
 - iii. Who oversees an index fund, exchange traded fund, or the like? Is there one person or entity within an investment organization tasked with overseeing such a fund? More than one? How often is it one versus more than one?
4. How do institutional investors manage holdings in the same issuer? Has this changed since 1978?

- a. Do institutional investors jointly manage holdings in the same issuer? Do they separately manage holdings in the same issuer? Has this changed since 1978? If so, how has it changed?
 - b. How do institutional investors make the decision to jointly or separately manage holdings in the same issuer? Has this changed since 1978? If so, how has this changed?
 - c. Do answers to any of the above questions depend on the type of issuer or the type of institutional investor or other factors? If so, what factors are relevant? How does each factor influence the actions of institutional investors? Have the factors changed since 1978? If so, how have they changed?
5. How do institutional investors apply the concept of solely for the purpose of investment? Has this changed since 1978? If so, how has it changed?
- a. Do the entities listed in 16 CFR 802.64 currently hold the voting securities of issuers solely for the purpose of investment? How does this differ from institutional investor behavior in 1978? What significant changes in institutional investor behavior have occurred between 1978 and 2020?
 - b. What kinds of entities not listed in 16 CFR 802.64 currently hold the voting securities of issuers solely for the purpose of investment? How does the current behavior of these entities differ from their behavior in 1978?
 - c. If institutional investors make certain acquisitions solely for the purpose of investment and other acquisitions not solely for the purpose of investment?

The acquisition of convertible debentures (convertible into common stock) options, warrants, preferred shares, even with no present right to vote for directors may result in the ability to influence the business of a company. The Rules capture these kinds of stakes in the concept of a convertible voting security. The term convertible voting security means a voting security which presently does not entitle its owner or holder to vote for directors of any entity.²² Section 802.31 exempts the acquisition of convertible voting securities.

The PNO has taken the informal position that the acquisition of convertible voting securities, when accompanied by the right to designate or appoint individuals to the board of directors of the issuer equal to the percentage of voting securities that would be held upon conversion, is reportable under the Act. The Commission is considering revising § 802.31 to explicitly require compliance with the HSR's reporting requirements when the acquisition of convertible voting securities is coincident with a Person having or obtaining the right to designate or appoint any individual to the board of the issuer. The Commission aims to understand the potential benefits and burdens of such a change through responses to the following questions

1. Is the acquisition of convertible voting securities, when accompanied with the right of appointment or designation of individuals to the issuer's board of directors, equivalent to the acquisition of voting securities with the present right to vote for election of the issuer's board of directors? In what ways are they the same and in what ways are

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- a. Would the burden fall most on an identifiable class of transactions? How would such a change affect how an identifiable class of transactions is structured?
- b. Would such a change introduce significant inefficiencies into the market for corporate control? What would be the effect of that change in the market?

B. Board Observers

Another potential way to gain influence over a company, beyond the scope of acquiring voting securities through board observer²³. The Commission understands that it is becoming increasingly common for issuers and NCEs to include board observers as part of their governance structure. Issuers and NCEs often grant rights and appoint board observers to investors with significant equity, in addition to or in lieu of providing investors with board seats. Even though board observers lack the ability to vote on matters that come before the issuer's board, they may nevertheless have significant influence over the outcome of matters submitted to the board for approval.²³ At the very least, board observers gain insight into an issuer's strategic decision-making, which is not only useful to the investor sponsoring the board observer, but may also be useful to competitors in the market, especially when those board observers also serve as officers or directors of a competitor.²⁴ Companies likely benefit from interacting with board observers because company management can obtain additional investor insight without having to alter the composition or voting balance on the board.

²³ *Obasi Investment Ltd. et al v. Tibet Pharmaceuticals, Inc.*, 931 F.3d 179, 183 (3d Cir. 2019).

²⁴ See Complaint, *In re Altria Group/JUUL Labs* Dkt. 9383, ¶ 9, at https://www.ftc.gov/system/files/documents/cases/d09393_administrative_part_iii_complaint_public_version.pdf

Given the opportunities that board observers have to interact with corporate officers, directors and other managers and to gain access to confidential information related to strategic and operational decisions, the Commission would like to better understand the role of board observers. In particular, the Commission would like to know how investors might use board observers' rights to influence competitive decision-making of issuers and NCEs to ascertain whether the acquisition of rights that provide opportunities to wield this kind of influence should be reportable under the Act. To that end, the Commission seeks responses to the following questions

1. What types of information are available to an issuer/NCE board observer?
 - a. With what frequency i

- e. Do issuers/NCEs draft formal guidance for their boards as to what topics should not be discussed in the presence of board observers? If so, with what frequency? Are outside counsel involved in monitoring compliance? If so, with what frequency?
2. What means does an issuer/NCE board observer have to influence board policies or the strategic or operational direction of the firm?
 - a. Does a board observer ever enjoy any special right of notice or consultation regarding major capital expenditures or strategic decisions?
 - b. Does a board observer have access, outside of board meetings, to managers in the corporation, to investment committee members in an NCE, or to persons with similar decisionmaking roles regarding the operations of the business, with what frequency?
 - c. Do board observers have the ability to request a meeting of the issuer/NCE's board? If so, with what frequency?
 - d. Do issuers/NCEs impose restrictions on a board observer's speaking role during board meetings? If so, with what frequency? How common are "silent" board observers?
 - e. How frequently do board observers move into senior executive roles at issuers/NCEs?
 3. What are the parameters of the board observer role?

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VI. Transactions or Devices for Avoidance (16 CFR 801.90)

16 CFR 801.90 (16)

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the target no longer meets the size of person test.²⁵ The PNO's informal staff position is based on the idea that if an extraordinary dividend reduces the target's cash on hand, it is unlikely to present a 16 CFR 801.90 issue.

But there are situations where the purpose of such a payout may be more complicated. For instance, if the payout involves more than the distribution of cash on hand, this could present an issue under 16 CFR 801.90. Each issuance of an extraordinary dividend or like payment must be carefully analyzed to make sure that it is not a device for avoidance under § 801.90.

d. Is the buyer ever

20 to continue to acquire voting securities of the same issuer up to the next threshold, in this case \$500 million (as adjusted), as long as it crosses the \$100 million threshold (as adjusted) within one year.

The time period in proposed § 802.21 was 180 days, but numerous comments persuaded the Commission this time period was too short.²⁶ In the final rules, the Commission chose a period of five years, both as a result of these comments and because it made sense to correlate the timing of the exemption with the timing of the Census and resulting updated data.²⁷ Given the changes in worldwide economic activity since 1978, Commission is now concerned that the § 802.21 five-year period may be too long. At the time of the initial filing, the transaction may not present competition concerns, but such concerns could develop as a result of changes in the lines of business of the Acquiring Person and Acquired Person during the five-year period, but those changes would not require a new filing. As a result, the Commission seeks to understand the impact of shortening the § 802.21 five-year period through responses to the following questions:

1. Have there been changes in economic activity significant enough to raise concerns that the Commission may miss important competitive effects if it does not shorten the five-year term?
2. If there are reasons to believe that the § 802.21 five-year period is too long, what period would address concerns that additional acquisitions of the Acquired Entity present

²⁶ 43 FR 33450, 33493 (July 31, 1978).

²⁷ *Id.*

competitive concerns because the lines of business of the Acquiring Person and/or Acquired Person have changed? Why would another period be more appropriate?

3. Is there is a class of Acquiring Persons for whom the decrease in the exemption period would cause significant burden? If not, why not? If so, how?

B. Prior Acquisitions

When the Acquiring Person and the Acquired Person report in the same or “overlapping” NAICS revenue code in Item 5 of the HSR Form, the Acquiring Person must report certain prior acquisitions in Item 8: (1) the acquisition of 50% or more of the voting securities of an issuer or 50% or more of non-

relationship

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By direction of the Commission.

April Tabor,

Acting Secretary.