

Client Alert

A report
for clients
and friends
of the firm May 2005

New HSR Rules

The Federal Trade Commission's Premerger Notification Office has published new rules under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended (the "HSR Act"). The primary aim of the new rules is to harmonize the treatment of corporations and unincorporated entities — partnerships, limited partnerships and limited liability companies — under the HSR Act. In addition, the new rules include certain other changes to further clarify proper application of the HSR Act. The rules became effective on April 7, 2004. This Client Alert outlines the most significant of these new changes.

Reporting of a Change of Control of an Unincorporated Entity

The most significant change to the HSR rules is the requirement of notification upon a change of control of an unincorporated entity. Previously, parties were required to file only for qualifying (*i.e.*, transactions meeting the jurisdictional requirements) acquisitions of 100% of the interests of a non-corporate entity, which was deemed to be the same as an acquisition of all the assets of such entity. Under the new rules, parties are required to file for qualifying acquisitions of "non-corporate interests" sufficient to result in "control" of an unincorporated entity.

Under the new rules a "non-corporate interest" is defined as an interest in any unincorporated entity which gives the holder the right to any profits of the entity or in the event of a dissolution of that entity the right to any of its assets after the payment of its debts.

"Control" of an unincorporated entity is newly defined as holding 50% of the non-corporate interests, i.e., having (i) the right to 50% or more of the profits of the entity; or (ii) the right to 50% or more of the assets of the entity in the event of a dissolution.

Notably, this new definition of "control" no longer recognizes the contractual power to designate 50% or more of individuals exercising functions similar to directors of a corporation as indicia of control.

Formation of Unincorporated Entities

Under the old rules, the formation of an unincorporated entity was not reportable under the HSR Act unless two or more pre-existing, separately controlled businesses were contributed to form the new entity meeting the jurisdictional thresholds and at least one of the members of the new entity would control the unincorporated entity. The new rules no longer require the contribution of two pre-existing, separately controlled businesses. The formation of an unincorporated entity (other than in connection with a consolidation) is reportable merely if one party will hold a controlling interest and the transaction otherwise meets the jurisdictional requirements and no exemptions apply. Contributors to the new unincorporated entity file notification as

"Control" of a Non-Corporate Entity		
The right to 50% or more of the profits	or	The right to 50% or more of the assets in a dissolution

Reportable Acquisitions of Non-Corporate Interests	
Old Rule	New Rule
Acquisitions of less than a 100% interest in an unincorporated entity <u>are not</u> reportable	Acquisitions of a "controlling" "non-corporate interest" <u>are</u> reportable

acquiring persons only (despite technically being an acquired person with respect to contributed assets) and the new entity need not file as the acquired person. Furthermore, the newly formed unincorporated entity is not required to file as an acquiring person with respect to the contributions made for its formation.

Exemptions

There are several new rules affecting exemptions from filing. Most of the new rules expand prior exemptions applicable only in the context of corporations to cover unincorporated entities. In addition, there are two new exemptions: the acquisition of non-corporate interests in a financing transaction and the formation of a not-for-profit corporation or unincorporated entity.

Some of the prior exemptions expanded to cover unincorporated entities include the exemption for acquisitions of voting securities of a corporation the purchase of whose assets would be exempt, the exemption for acquisitions of certain real estate assets, the exemption for reorganizations, and the intraperson exemption.

Other Noteworthy Changes

Consolidation. The new rules codify a long-standing informal staff position that the combination of any two entities into a new holding company is the equivalent of a consolidation and thus reportable. Each consolidating entity will be both an acquiring and an acquired person.

Aggregation of Assets. An acquiring person must aggregate a current asset acquisition with a non-reportable previously contemplated asset acquisition from the same entity where the letter of intent or agreement for the previously contemplated acquisition is still in effect at the time the HSR filing is made for the current asset acquisition.

Timberland. The acquisition of timberland is now subject to the HSR Act.

Conditions for New Exemption for Non-Corporate Financing Transactions

- investor is contributing only cash to the formation of the unincorporated entity;
- cash is contributed for the purpose of providing financing; and
- terms of the financing agreement are such that the investor will no longer control the entity after the investor realizes its preferred return.

Examples of Exemptions Expanded to Cover Non-Corporate Entities

802.10(b) Reorganizations. Expands the exemption for the acquisition of voting securities pursuant to a stock split or pro rata stock dividend to cover the acquisition of non-corporate interests or voting securities as a result of reorganization of either a corporation or an unincorporated entity into a new entity if (i) no new assets are contributed to the new entity; and (ii) either (a) the acquiring person's interests in the new entity are pro rata or less than the person's holdings in the original entity or (b) the acquiring person was in control of the original entity.

802.30 Intraperson Transactions. Expands the exemption for a transfer of assets/voting securities from a corporation to a controlling shareholder, or the transfer of assets/voting securities from one corporate subsidiary to another corporate subsidiary of the same parent, to cover similar transactions involving unincorporated entities.

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