

REVISED TREATMENT OF LLCs UNDER HART-SCOTT-RODINO ACT

SIMPSON THACHER & BARTLETT LLP

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As of March 1, 1999, the Federal Trade Commission will implement a revised Formal Interpretation of the Hart-Scott-Rodino Act, which concerns the reportability of certain transactions involving the formation of a Limited Liability Company ("LLC"). Under the revised interpretation, the formation of an LLC which combines under common control in the LLC two or more pre-existing businesses will be treated as subject to the requirements of the HSR Act under § 801.2(d) of the HSR rules, 16 CFR § 801.2(d), which governs mergers and consolidations.

This Formal Interpretation changes the treatment of LLC's as follows: The FTC will treat as reportable the formation of an LLC if (1) two or more pre-existing, separately controlled businesses will be contributed, and (2) at least one of the members will control the LLC (i.e., have an interest entitling it to 50 percent of the profits of the LLC or 50 percent of the assets of the LLC upon dissolution). The formation of all other LLCs will be treated similar to the formation of a partnership which, under the FTC's longstanding position on partnership formations, will not be reportable. Post-formation acquisitions of membership interests in LLCs will not be reportable except in two situations: (1) when the acquisition of the membership interest results in the acquiring person, who had not previously filed for and consummated the acquisition of control of that LLC, holding 100 percent of the membership interests of the LLC (similar to the FTC treatment of the acquisition of a partnership interest), and (2) when the acquiring person contributes a business to the LLC in exchange for the LLC membership interest. The FTC will treat this contribution of an additional business to the business(es) already in the LLC as a formation of a new LLC under this Interpretation.

In determining what is a "business" for purposes of this Interpretation, the FTC will look to the definition of "operating unit" under § 801.1(a) of the rules, which includes "assets that are operated . . . as a business undertaking in a particular location or for particular products or services, even though those assets may not be organized as a separate legal entity." In addition, the contribution to an LLC of an interest in intellectual property, such as a patent, a patent license, know-how, and so forth, which is exclusive against all parties including the grantor, is the contribution of a business, whether or not the intellectual property has generated any revenues. To determine whether a filing is required, the parties also must determine the size-of-person and size-of-transaction, as well as whether any exemption in the act or rules makes the acquisition non-reportable.

This Formal Interpretation will not require reporting regarding some LLC formations and some acquisitions of existing LLC interests that would have required reporting under the Interpretation announced by the FTC in October 1998. Unlike the October version, this Formal Interpretation requires reporting only if the formation brings together two formerly separately controlled businesses. In contrast, the October Formal Interpretation would have viewed LLCs that are created solely as financing vehicles as potentially reportable. Under this revised Interpretation, so long as financing transactions do not result in the contribution of a business to the LLC by two or more members, it will not be treated as reportable.

The FTC has also announced its decision not to change its treatment of partnerships at this time, but has raised the possibility that it may reexamine the issue in the future.

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If you would like any additional information regarding the reportability of an LLC transaction under the HSR Act, please call Joe Tringali (455-3840) or Jack D'Angelo (455-2722).

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