Hart-Scott-Rodino
Premerger Notification Program

Introductory Guide II

To File or Not to File
When You Must File a Premerger Notification Report Form

Revised September 2008

FTC.GOV/BC/HSR **FTC Premerger Notification Office** (202) 326-3100

AN OVERVIEW

Guide II is the second in a series of guides prepared by the Federal Trade Commission's Premerger Notification Office ("PNO"). It describes the criteria used to determine whether a transaction is subject to the requirements of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (§ 7A of the Clayton Act or "the Act"), and uses a hypothetical transaction to illustrate the application of the Premerger Notification Rules (the "Rules").

Other Guides in this series provide additional information. Guide I is an overview of the program and the way it operates and Guide III contains "A Model Request for Additional Information and Documentary Material (Second Request)."

The Guides are not intended to address specific proposed transactions. If you are analyzing a transaction, we suggest that you consult the Act, the Rules, and the other Guides in this series, as well as the Federal Trade Commission's website at http://www.ftc.gov/bc/hsr. If you have a specific question on a proposed transaction and your question is not addressed in these reference sources, call the PNO between the hours of 8:30AM and 5:00PM, Monday through Friday, except holidays, at (202) 326-3100.

I. INTRODUCTION

Title II of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 established the Federal Premerger Notification Program (the "Program"). The Program is designed to provide the Federal Trade Commission (the "FTC" or "Commission") and the Department of Justice (the "DOJ") with information about large mergers and acquisitions before they occur. The parties to certain proposed transactions must submit a Notification and Report Form for Certain Mergers and Acquisitions (the "Form")[1] with information about their businesses to the enforcement agencies and wait a specified period of time before consummating the transactions. During that "waiting period," the antitrust enforcement agencies analyze the likely competitive effects of the proposed transaction. If either agency believes that further information is needed in order to complete the competitive analysis, then it may request additional information and documentary material from the parties. Issuance of this "second request" extends the waiting period for a specified period, usually 30 days, after the parties have complied with the request. The additional time provides the reviewing agency with the opportunity to analyze the information and to take appropriate action before the transaction is consummated. If the agency believes that a proposed transaction may violate the antitrust laws, it may seek an injunction in federal district court to prohibit consummation of the acquisition.

The Rules are divided into three parts:[2]

1) Coverage: The first part, 16 C.F.R. Part 801, encompasses the coverage rules. These include definitions of important terms, methods for determining dollar values and percentages, and specific instructions for the treatment of particular types of transactions.

2) Exemptions: The second part, 16 C.F.R. Part 802, contains certain exemptions for types of transactions that otherwise would be reportable. Before filing, you should consult these exemption rules, as well as the exemptions set out in the statute itself, to determine whether any of them apply.

3) Transmittal: The third part, 16 C.F.R. Part 803, sets out premerger notification filing, waiting period and second request procedures.

This Guide focuses primarily on the coverage rules, 16 C.F.R. Part 801.

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[1] FTC Form C4 (rev. 06/06/06).

[2] The Premerger Notification Rules are found at 16 C.F.R. Parts 801, 802 and 803. The Rules also are identified by number, and each Rule beginning with Rule 801.1 corresponds directly with the section number in the C.F.R. (so that Rule 801.40 would be found in 16 C.F.R. § 801.40). In this Guide, the Rules are cited by Rule number.

II. JURISDICTIONAL REQUIREMENTS

For the Act to apply to a particular transaction, it must satisfy three tests: the commerce test of Section 7A(a)(1) as well as the size of transaction test and the size of person test of Section 7A(a)(2).

An acquisition will satisfy the commerce test if either of the parties to a transaction is engaged in commerce or in any activity affecting commerce. The size of transaction test is met if, as a result of the transaction, the acquiring person will hold an aggregate amount of voting securities, non-corporate interests ("NCI") and assets of the acquired person valued at more than $50 million (as adjusted).[3] The size of person test is met if one of the parties has sales or assets of at least $100 million (as adjusted) and the other party has sales or assets of at least $10 million (as adjusted). [4]

III. HYPOTHETICAL TRANSACTION

Throughout this Guide, we will refer to the following hypothetical transaction (italicized in the document). The hypothetical places you in the position of legal counsel to a corporation that is about to be acquired. However, the principles it illustrates should be of use to readers in other circumstances.

The President of Beta Products, Inc., walks into your law office and informs you that the Zed Corporation is acquiring her company. She remarks that Zed Corporation mentioned something about the Hart-Scott-Rodino Act and filing a notification and report form within the next few weeks. Although you have handled certain business transactions for Beta Products in the past, this is the first time that the possibility of a premerger notification filing has been involved. You want to determine, therefore, whether the transaction must be reported, and if so, how.

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[3] The 2000 amendments to the Act require the Commission to revise certain thresholds annually based on the change in the level of gross national product. A parenthetical "(as adjusted)" has been added where necessary throughout the Rules (and in this guide) to indicate where such a change in statutory threshold value occurs. The term "as adjusted" is defined in subsection 801.1 (m) of the Rules and refers to a table of the adjusted values published in the Federal Register notice titled "Revised Jurisdictional Thresholds for Section 7A of the Clayton Act." The notice contains a table showing adjusted values for the rules and is published in January of each year. The values contained therein are effective as of the date published in the Federal Register notice and remain effective until superceded in the next calendar year.

[4] The size of person test is not applicable if, as a result of the transaction, the acquiring person will hold an aggregate amount of voting securities, NCI and/or assets of the acquired person valued in excess of $200 million (as adjusted). *See* § 7A (a)(2) of the Act.

IV. PRELIMINARY QUESTIONS

In determining whether a particular transaction must be reported, you should begin by answering several preliminary questions:

1) What is being acquired?

2) What are the amount and the nature of the consideration?

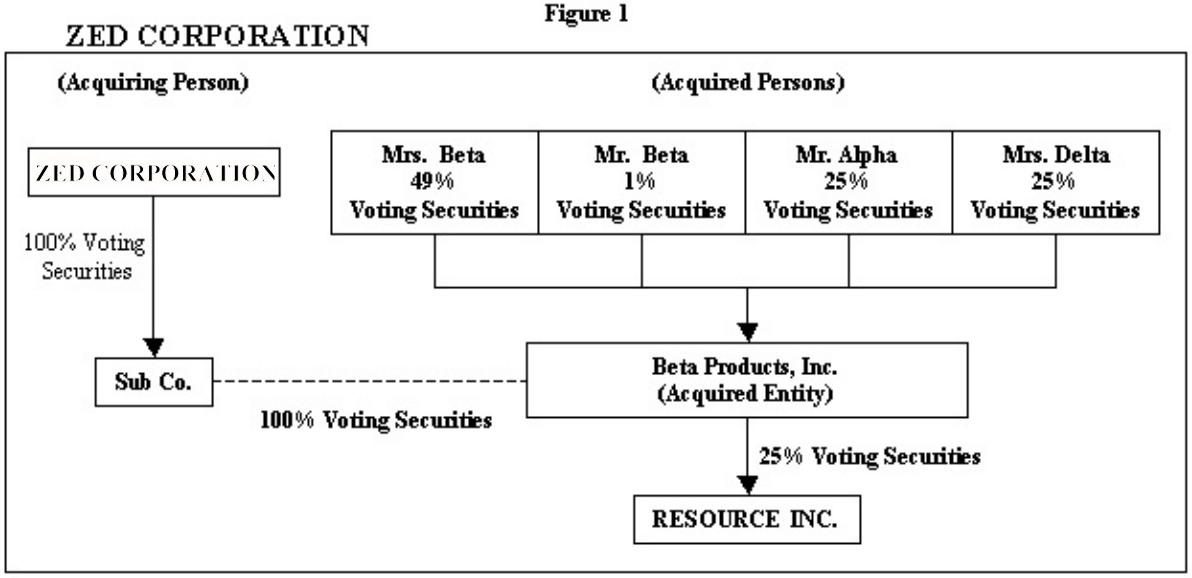
3) Who are the parties involved in the transaction?

4) When and under what conditions will the transaction take place?

In exploring these preliminary questions about the hypothetical transaction, you have learned that Zed Corporation has entered into agreements with the shareholders of Beta Products to buy all of Beta Products' outstanding voting stock for $90 million. Further investigation reveals, however, that Zed Corporation does not plan to purchase the voting stock directly; rather, Zed Corporation's wholly-owned subsidiary, Sub Co., will buy the shares from Beta Products' shareholders. You already know who those shareholders are: Mrs. Beta holds 49 percent of the outstanding voting securities and her husband owns one percent, while Mrs. Delta, her sister-in-law, and Mr. Alpha, an unrelated private investor, each own 25 percent. You also know from your previous work that Beta Products holds 4500 shares of common stock, which constitute 25 percent of the voting securities of Resource Inc. Beta Products is the largest holder of Resource Inc. voting securities.

To clarify the relationships among the parties and the structure of the transaction, it is often helpful to draw a diagram of the transaction such as the one in Figure 1 below. *As you will see*

Figure 1



later, the Rules treat this transaction as two separate acquisitions, either or both of which may be reportable. In both acquisitions, the acquiring person is Zed Corporation. Mrs. and Mr. Beta, together, are the acquired person in the acquisition of Beta Products, Inc. In addition, because the acquisition of Beta Products will result in Zed Corporation holding voting securities of Resource Inc., the Rules treat this aspect of the transaction as a different acquisition in which Resource Inc. also is an acquired person.

V. STEPS TO DETERMINE REPORTABILITY

Once you have outlined the basic transaction, you are ready to analyze it to determine whether it must be reported. The important steps in this process include:

1) Determining the size of the transaction and the relevant reporting threshold;

2) Identifying the acquiring and acquired persons (the "ultimate parent entity") of each party; and

3) Determining the size of each person involved in the transaction.

A. The Size of Transaction Test

The size of transaction test, as its name suggests, is concerned with the value of what is being acquired. Because the objective of the Program is to analyze the effects of combining once separate businesses, the Rules generally require that assets, voting securities or NCI of the acquired person that have already been acquired must be aggregated with those that will be acquired in the proposed transaction. When what has previously been purchased plus what will be bought in the present acquisition meets the size of transaction criteria, the transaction becomes reportable unless an exemption applies.

1. Value of voting securities, NCI and assets to be held

In order to determine whether a transaction meets the size of transaction test, you must compute the value of the voting securities, NCI and assets, which you will hold as a result of the acquisition. The phrase "held as a result of the acquisition" has a technical meaning under the Rules. It includes not only those securities, NCI and assets that are currently being acquired, but also voting securities, NCI, and, in some circumstances, assets previously acquired from the same person. Rule 801.13[5] determines what is held as a result of the acquisition, and Rules 801.13 and 801.14[6] specify how such voting securities, NCI and assets should be aggregated and valued.

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[5] *See* 16 C.F.R. § 801.13.

[6] *See* 16 C.F.R. §§ 801.13, 801.14.

a. "Held as a result of the acquisition"

All voting securities, NCI and assets currently being acquired are held as a result of the acquisition. In addition, Rule 801.13[7] explains when you must aggregate previously-acquired voting securities, NCI or assets with those that you plan to acquire in order to determine what is held as a result of the acquisition. Different principles apply to asset, voting securities and NCI acquisitions.

(1) Aggregating previously-acquired voting securities or NCI

Rule 801.13(a)(1)[8] requires that you add any voting securities that you currently hold of the same issuer to any voting securities that you propose to acquire to determine what voting securities of that issuer will be held as a result of the planned acquisition. There are some special circumstances, however, described in Rule 801.15,[9] in which the prior, simultaneous, or subsequent acquisition is exempt from notification and need not be included in the calculation.

Rule 801.14,[10] requires that you aggregate the value of all of the voting securities of all of the issuers included within the acquired person that you will hold as a result of the acquisition. Thus, if you hold less than 50% of the voting securities of one subsidiary company and plan to acquire voting securities of the parent or a different subsidiary of the same parent, you would aggregate these holdings to determine the value of the securities held.

Rule 801.13(c)(1)[11] requires that you add any NCI that you currently hold of the same non-corporate entity to any NCI that you propose to acquire to determine what NCI will be held as a result of the planned acquisition. Rule 801.14,[12] requires that you aggregate the value of all NCI included within the acquired person that you will hold as a result of the acquisition as determined by Rule 801.13(c). Under Rule 801.13(c)(2),[13] an acquisition of NCI which does not confer control of the unincorporated entity is not aggregated with any other assets or voting securities which have been or are currently being acquired from the same acquired person.

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[7] *See* 16 C.F.R. § 801.13.

[8] *See* 16 C.F.R. § 801.13(a)(1).

[9] *See* 16 C.F.R. § 801.15.

[10] *See* 16 C.F.R. § 801.14.

[11] *See* 16 C.F.R. § 801.13(c)(1).

[12] *See* 16 C.F.R. § 801.14.

[13] *See* 16 C.F.R. § 801.13(c)(2).

(2) Aggregating assets and voting securities

In some circumstances, the size of transaction test requires acquiring persons to add the value of an issuer's voting securities that it holds and will hold with the value of assets that have been acquired or will be acquired from that issuer or the person controlling that issuer. Whether the acquisitions of assets and voting securities are both to be considered "held as a result of the transaction" depends on the order of the transactions. If a noncontrolling percentage of voting securities were purchased in a nonreportable transaction and will be held at the time assets are to be acquired, then both the voting securities and assets are held as a result of the transaction. Their combined value is included to determine if the size of transaction test is satisfied. If, however, the asset transaction precedes the voting securities transaction, then the assets are not held as a result of the later acquisition of voting securities and the value of the assets is not included. The Commission explained the exclusion of assets in the second instance when it promulgated Rule 801.13:[14] "once assets are sold, they confer no continuing ability to participate in the affairs of the acquired person, and so prior acquisitions of assets need not be considered for purposes of subsequent acquisitions of voting securities."[15]

(3) Aggregating previously-acquired assets

Generally, the acquisition by an acquiring person of assets from the same acquired person is not aggregated unless: the second acquisition is made pursuant to a signed letter of intent or agreement, and within the previous 180 days the acquiring person has signed a letter of intent or agreement in principle to acquire assets from the same acquired person, which is still in effect but has not been consummated; or the acquiring person has acquired assets from the same acquired person which it still holds; and the previous acquisition (whether consummated or still contemplated) was not subject to the requirements of the Act.[16] If the previous asset acquisition (or aggregated asset acquisitions) was reported properly to the enforcement agencies, aggregation is not required. In addition, if a single agreement calls for multiple closings on purchases of assets from the same person, the purchases must be aggregated to the extent that those closings are within one year.

b. Valuation

Once you have determined what is held as a result of the acquisition, you must value those securities, NCI and assets. Again, different methods are used for valuation, depending on whether voting securities, NCI or assets will be held as a result of an acquisition.

Voting securities fall into one of two groups for valuation purposes: publicly traded and untraded, *i.e.*, those not traded on a national securities exchange or quoted in NASDAQ. Under

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[14] *See* 16 C.F.R. § 801.13.

[15] *See* 43 Fed. Reg. 33478-9 (1978).

[16] *See* 16 C.F.R. § 801.13 (b)(1) and (b)(2).

the Rules, the value of publicly traded voting securities that are to be acquired is the higher of "market price" or "acquisition price." Thus, if the voting securities are trading at $50 a share, and you have a contract to buy a block for $60 a share, the $60 value is used. If the acquisition price of publicly-traded shares has not been determined, the value is the market price. For non-publicly traded voting securities, the securities are valued at their "acquisition price" or, if the "acquisition price" has not been determined, at "fair market value." Previously acquired securities are valued in similar ways pursuant to Rules 801.10 and 801.13.[17] NCI are valued in the same manner as non-publicly traded voting securities. In an acquisition of assets, Rule 801.10(b)[18] provides that the assets must be valued at their "fair market value" or, "if determined and greater than the fair market value," at their "acquisition price."

The terms "market price," "acquisition price," and "fair market value" are defined for premerger notification purposes in Rule 801.10(c).[19] For useful information concerning the "valuation rule", please visit http://www.ftc.gov/bc/hsr/hsrvaluation.shtm and http://www.ftc.gov/bc/hsr/801.10summary.shtm.

(1) Determining market price

In transactions subject to § 801.30, *e.g.*, open market stock purchases, the "market price" is the lowest closing quotation or bid price within 45 days prior to receipt by the issuer of the notice required by Rule 803.5(a) from the acquiring person, which must be delivered to start the waiting period. In transactions to which Rule § 801.30 does not apply, *e.g.*, purchases from a "controlling" stockholder or directly from the issuer, the "market price" is the lowest closing quotation or bid price within the 45 calendar days preceding the closing of the acquisition, but not extending back prior to the day before execution of the agreement or letter of intent to merge or acquire. The "45-day rule" will enable you to determine whether a particular transaction will meet the size of transaction test even though the price of the voting securities may be fluctuating significantly on the open market.

(2) Determining acquisition price

Rule 801.10(c)(2)[20] states that the "acquisition price" includes the value of all consideration for the voting securities, NCI and assets being acquired. This consideration includes any cash, voting securities, tangible assets, and intangible assets that the acquiring person is exchanging with the seller. In an asset transaction, it also includes the value of any liabilities that the acquiring person will assume. Thus, if you will pay $85 million in cash for a factory and, in

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[17] *See* 16 C.F.R. §§ 801.10 and 801.13.

[18] *See* 16 C.F.R. 801.10(b).

[19] *See* 16 C.F.R. S 801.10(c).

[20] *See* 16 C.F.R. § 801.10(c)(2).

addition, will assume $10 million in liabilities, the acquisition price is $95 million.

(3) Determining fair market value

"Fair market value" must be determined in good faith by the board of directors of the ultimate parent entity of the acquiring person (or the board's designee).[21] Such a determination must be made within 60 days of filing or, if no filing is required, within 60 days of consummation of the acquisition. Thus, if the parties neither file nor consummate within 60 days of the determination, they cannot rely on it. If a filing is made within the 60 days, however, a new fair market value determination is not required regardless of the consummation date.

(4) Voting securities and assets previously acquired

Voting securities that were acquired in an earlier transaction are valued on the basis of their current worth, not their historical purchase price.[22] If the securities are publicly traded, you should use their current market price, as determined by the 45-day rule under Rule 801.10(c)(1).[23] Otherwise, they are valued at their current fair market value, as determined by Rule 801.10(c)(3).[24] NCI are valued in the same manner as non-publicly traded voting securities. Previously acquired assets should be valued according to Rule 801.10(b)[25] at the greater of their current fair market value or the acquisition price at the time they were acquired.

Since Beta Products, Inc., is a closely-held company and the stock is not publicly traded, the applicable Rule is 16 C.F.R. § 801.10(a)(2). This Rule provides that the value of the voting securities will be the acquisition price, if determined, or, if the acquisition price has not been determined, the fair market value of the voting securities as set by the board of directors of the acquiring person. Sub Co. and Beta Products' shareholders have agreed on a total purchase price of $90 million for 100 percent of the voting securities of Beta Products, Inc. Therefore, you will not have to get the board of directors of Zed Corporation to determine the fair market value of Beta Products' stock. Rather, you can rely on the acquisition price of $90 million to conclude that the acquisition meets the size of transaction test.

To determine whether Zed Corporation and Resource Inc. must report, you will have to calculate the value of the voting securities of Resource Inc. that will be held by Zed as a result of acquiring Beta Products. Because the acquisition price of the Resource securities is not

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[21] *See* 16 C.F.R. § 801.10(c)(3).

[22] *See* Rule 801.13(a), 16 C.F.R. § 801.13(a).

[23] *See* 16 C.F.R. § 801.10(c)(1).

[24] *See* 16 C.F.R. § 801.10(c)(3).

[25] *See* 16 C.F.R. § 801.10(b).

separately identified, the Rules require that the value be determined by the market price.[26] *In this transaction, the market price can be determined because the voting securities are publicly traded. Resource shares sell, at the time of your research, for $100 a share; thus, the value of the 4500 Resource shares that Zed will obtain is likely to be about $4.5 million.*[27] *If Zed already owned other Resource voting securities, you would add the current market price of those shares to determine if the total value of the voting securities held as a result of the acquisition meets the size of transaction test. After reviewing Zed's holdings, you determine that it does not hold any other Resource securities. Accordingly, the secondary acquisition does not meet the size of transaction test and is not reportable.*

c. Calculating percentage of voting securities to be acquired

Rule 801.12 sets out a formula to be used whenever the Act or Rules require calculation of the percentage of voting securities of an issuer to be held or acquired, *e.g.*, in determining control.[28] The Rule is designed to recognize weighted voting rights and different classes of voting securities. As illustrated below, the percentage is derived from the ratio of two numbers: the number of votes for directors of the issuer that the holder of a class of voting securities is presently entitled to cast, or, as a result of the acquisition, will become entitled to cast, divided by the total number of votes for directors which presently may be cast by that class, multiplied by the number of directors elected by that class, divided by the total number of directors.

$$\frac{\textit{\# of Votes of Class A Held}}{\textit{Total Votes of Class A}} \times \frac{\textit{Directors Elected by Class A Stock}}{\textit{Total \# of Directors}} = \%$$

The resulting percentage should be calculated separately for each class, and then totaled to determine an acquiring person's voting power. You should omit authorized but unissued voting securities or treasury securities, as well as convertible voting securities that have not yet been converted and do not have a present right to vote, unless you are filing notification for their acquisition or conversion.

2. The Notification Thresholds

Rule 801.1(h), 16 C.F.R. § 801.1(h), establishes five notification thresholds for acquisitions of

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[26] *See* Rule 801.10(a)(1)(ii), 16 C.F.R. § 801.10(a)(1)(ii).

[27] *See* Rule 801.10(c)(1), 16 C.F.R. § 801.10 (c)(1).

[28] *See* 16 C.F.R. § 801.12(b).

voting securities[29]:

a) $50 million (as adjusted);

b) $100 million (as adjusted);

c) $500 million (as adjusted);

d) 25%, if valued at greater than $1 billion (as adjusted); and

e) 50%, if valued at greater than $50 million (as adjusted).

Because the Rules provide that all voting securities held by the acquiring person after an acquisition are "held as a result of the acquisition," the thresholds are designed to act as exemptions to relieve parties of the burden of making another filing every time additional shares of the same person are acquired. As such, when notification is filed, the acquiring person is allowed one year from the end of the waiting period to cross the threshold it indicated in the filing.[30] If within that year the person reaches the stated threshold or any lower threshold, it may continue acquiring shares up to the next threshold for five years measured from the end of the waiting period. The acquiring person must file again, however, before it can cross that next higher threshold. The 50 percent threshold is the highest threshold regardless of the corresponding dollar value, because it indicates the acquisition of control.

Because Zed is acquiring 100% of the voting securities of Beta Products, it will indicate the 50% filing threshold in its filing regardless of the transaction value.

B. Identifying the Acquiring and Acquired Persons

If the hypothetical transaction were valued in excess of $200 million (as adjusted), the transaction would be reportable unless an exemption applied. But, because the hypothetical transaction is valued at $90 million, you must also turn to the size of person test, as you must for all transactions valued in excess of $50 million (as adjusted) but at $200 million (as adjusted) or less. The first step in determining your size of person is to identify the "acquiring person" and the "acquired person." Under the Act, the obligation to report depends on the size of the "persons" involved. "Person" is defined in Rule 801.1 (a)(1) and is the "ultimate parent entity" of the buyer or seller. That is, it is the entity that ultimately controls the buyer or seller.[31]

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[29] The notification thresholds do not apply to acquisitions of assets or NCI.

[30] *See* 803.7.

[31] *See* "control" under 801.1 (b).

1. The Ultimate Parent Entity

An ultimate parent entity or "UPE" is the company, individual or other entity that controls a party to the transaction and is not itself controlled by anyone else. For example, the UPE may be a corporate parent of a subsidiary company that has signed a contract to purchase a plant, or it could be a partnership or an individual that owns a majority of the voting securities of the acquiring company. The ultimate parent entity may be separated from the company whose name appears on the sale agreement by many layers of controlled subsidiaries, or the UPE may actually be entering into the transaction in its own name.

2. Control

Identifying the ultimate parent entity involves tracing the chain of "control," a term defined in Rule 801.1(b).[32] Control is established by the "holding" of 50 percent or more of the outstanding voting securities of an issuer. In the case of an entity that has no outstanding voting securities, control is established by the right to 50 percent or more of the profits, or the right, in the event of dissolution, to 50 percent or more of the assets of the entity. Control also is accomplished by having the contractual power presently to designate 50 percent or more of the board of directors of a corporation.

As a result, more than one person may be deemed to control an entity at the same time. For example, one person may hold 50 percent of the voting securities of the entity while another person has the contractual power to appoint 50 percent of the board of directors.

3. "Hold" and "Beneficial Ownership"

To determine control of a corporation you first must identify the individuals or entities that "hold" its voting securities. The holder of voting securities, according to Rule 801.1(c),[33] is the individual or entity that has beneficial ownership. Although the term "beneficial ownership" is not defined in the Rules, the Statement of Basis and Purpose accompanying the Rules provides examples of some indicators of beneficial ownership, including the right to receive an increase in the value of the voting securities, the right to receive dividends, the obligation to bear the risk of loss, and the right to vote the stock.[34] Thus, a person would be the "holder" of voting securities even though the shares were physically held by the person's stockbroker and listed under the broker's street name.

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[32] *See* 16 C.F.R. § 801.1(b).

[33] *See* 16 C.F.R. § 801.1(c).

[34] *See* The Statement of Basis and Purpose, 43 Fed. Reg. 33458 and subparts 2 through 8 of Rule 801.1(c), 16 C.F.R. § 801.1(c).

In the hypothetical, Sub Co. is not a UPE because Zed Corporation holds 50 percent or more of its outstanding voting securities. Assume that no one person holds as much as 50 percent of Zed Corporation's voting securities nor does anyone have the contractual power to appoint 50 percent of its board of directors. Under the Rules, therefore, Zed Corporation is not controlled by anyone else, and is the UPE of a "person" consisting of Zed Corporation and any other entities that it controls. In this situation, Beta Products, Inc., does not have a single 50 percent shareholder nor does any person have the contractual power to appoint 50 percent of its board of directors. However, our analysis cannot end here. Under Rule 801.1(c)(2),[35] the holdings of spouses and their minor children must be aggregated. Thus, Mrs. Beta and Mr. Beta hold 50 percent of Beta Products, Inc., (49 percent and one percent, respectively), and together are its ultimate parent entity. Because they are individuals, the Betas cannot be controlled by any other entity.

C. The Size of Person Test

1. The basic test

The next step in the analysis is to determine the size of the persons you have defined as the ultimate parent entities of the parties. The basic "size of person test" established by Section 7A(a)(2) of the Act requires a filing in transactions valued in excess of $50 million (as adjusted) but at $200 million (as adjusted) or less only where at least one of the persons involved in the transaction has $100 million (as adjusted) or more in annual net sales or total assets, and the other has $10 million (as adjusted) or more.[36] If these size thresholds are not met, the transaction need not be reported. Thus, for example, filings would not be required for a merger between two $99 million companies.[37]

There is one exception to the basic size of person test. Where an acquired person is not engaged in manufacturing only its total assets (unless its sales are $100 million (as adjusted) or more) are considered in determining its size. In addition, you should be aware that the size of person test is eliminated in transactions valued in excess of $200 million (as adjusted).

2. Calculating annual net sales and total assets

The procedures for calculating the annual net sales and total assets of a person are set out in Rule 801.11.[38] In the majority of cases, you will easily be able to determine whether the size of

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[35] *See* 16 C.F.R. § 801.1(c)(2).

[36] *See* 15 U.S.C. § 18a(a)(2).

[37] Provided, of course, that GDP has not declined resulting in the size of person test consequently declining to less than $99 million.

[38] *See* 16 C.F.R. § 801.11.

person test is satisfied. Generally, a person's annual net sales[39] and total assets are as stated on its last regularly prepared annual statement of income and last regularly prepared balance sheet. These financial statements must be as of a date not more than 15 months old, and have been prepared in accordance with procedures normally used by the filing person.[40]

A person should continue to rely on its regularly prepared financial statements until the next regularly prepared statements are available, even if subsequent changes in income or assets have occurred. For example, the most recently prepared statements may show $9 million in annual net sales and $8 million in total assets in the previous year, although the person's sales have increased in the current fiscal year such that its annual revenue will exceed $10 million (as adjusted) when its next statement is issued. For premerger notification purposes, however, the person will not be considered a $10 million (as adjusted) person until the annual income statement reflecting the increased revenue is prepared. The same analysis would be applied, however, if sales in the current fiscal year have decreased. A company's sales and assets may not be relied on until they are reflected in regularly prepared financial statements.

a. Including controlled entities

The size of person test includes the sales and assets of all entities, both domestic and foreign, included within the person. Any entities controlled by the UPE whose sales and assets are not consolidated in its financial statements must be added to determine the total size of the person. Unconsolidated sales and assets should be added, however, only to the extent that such additions are "nonduplicative." If the UPE's interest in the subsidiary is already reflected on the parent's balance sheet as an asset, then adding together the total assets of the subsidiary and the total assets of the parent would result in double counting at least part of the value of the subsidiary's assets. Accordingly, you should add only the subsidiary's total assets after subtracting the value of the interest in the subsidiary as it is carried on the parent's balance sheet.[41]

b. Natural persons

The total assets of a natural person include his or her investment assets (cash, deposits in financial institutions, other money market instruments, and instruments evidencing government obligations), voting securities, and other income-producing property, together with the total assets of any entity he or she controls. Property is income-producing if it is held either for

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[39] As used in the rule, "net sales" means gross revenues less returns, discounts, excise taxes, and the like. "Net sales" is not the equivalent of profits or "net income," however, and therefore the cost of raw materials, wages, interest, and other expenses may not be deducted. *See* The Statement of Basis and Purpose at 43 Fed. Reg. 33472-73.

[40] *See* 16 C.F.R. § 801.11(b)(2).

[41] *See* the statement of basis and purpose at 43 Fed. Reg. 33473 which provides additional information concerning consolidating a person's sales or assets.

investment or for the production of income, whether or not it actually produces income. You will have to refer to the definitions of "hold" and "control" to determine whether the individual (together with spouse and minor children) "holds" such property and to determine what entities he or she may "control." You may omit from the calculation the value of residences, cars, and personal property not held for the purpose of producing income. The annual net sales of an individual are the sum of the net sales of the entities he or she controls, including proprietorships, as well as income derived from investments.

c. Newly-formed person

A newly formed person, who has not yet prepared financial statements, may need to prepare a special statement of its sales and assets in order to calculate its size. Typically, these entities are formed for the purpose of making an acquisition. Under 801.11(e), a UPE without a regularly prepared balance sheet may exclude funds which will be used to make an acquisition in determining its size.[42] The Rule applies until the UPE, or any entity within it, has a regularly prepared balance sheet.

In the hypothetical, you have already identified Zed Corporation as its own ultimate parent entity and have concluded that Mr. and Mrs. Beta together are the ultimate parent entity of Beta Products, Inc. Assume that you also know that Zed Corporation is a large diversified company which probably has several hundred million dollars in annual sales. To be certain, you can consult Zed Corporation's annual report and refer to the 10-K and 10-Q reports that the company has filed with the Securities and Exchange Commission. In this instance, assume that Zed Corporation's annual report confirms that last year the company had annual revenues of $545 million. Since the current year has not yet ended and Zed Corporation used the calendar year for accounting purposes, there is no more recent annual income figure. Thus, Zed Corporation is clearly a $100 million (as adjusted) person. If it were necessary to consider total assets, you would want to look for the company's most recent regularly prepared balance sheet showing total assets. Note, however, that the balance sheets included in the firm's annual report or SEC filing may not be the company's most recent regularly prepared statements, since many corporations prepare quarterly or monthly statements of assets apart from those filed.

Applying the size of person test to Mr. and Mrs. Beta is a bit more involved since neither regularly prepares a financial statement. A good starting point, though, would be to add together the sales and assets of all the companies they control. You would not include the sales and assets of Resource Inc. because the Betas do not control that company but hold only a minority interest with no contractual power to appoint 50 percent or more of the board of directors. Assume here that Beta Products, Inc., is the only company controlled by Mr. and Mrs. Beta. Accordingly, you need not consolidate on one balance sheet the sales and assets of several entities. The minimum annual net sales for Mr. and Mrs. Beta can thus be found in the annual revenue figure from Beta Products' yearly statement of income. Assume that statement shows

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[42] *See* 16 C.F.R. § 801.11(e).

sales to be $9 million. It also shows total assets to be $9 million. If either figure had been $10 million (as adjusted), you could have stopped there and concluded that the size of person in the case of Mr. and Mrs. Beta was at least $10 million (as adjusted).

In the absence of such a simple solution, however, you must next consider the value of any additional investments owned by Mr. and Mrs. Beta, and any additional revenues these may generate. As provided by Rule 801.11 (d),[43] you should not consider Mr. Beta's country residence or the sports car he drives in computing his total assets; similarly, the value of Mrs. Beta's luxury condominium should be omitted from the calculation of her total assets. You should also exclude the value of the Resource Inc. voting securities because, although they are investment assets, their value is already reflected on Beta Products' balance sheet.

However, Mr. and Mrs. Beta also hold in their own names some voting securities in other corporations, a vacation cottage that is rented out during the summer months, and a racehorse. Since these assets are all held to produce income or as investments, you will have to determine their value and include them in your calculation of the value of Mr. and Mrs. Beta's total assets.

You determine that these additional voting securities and income producing properties are worth at least $10 million. Adding this to the total assets of Beta Products, Inc., puts Mr. and Mrs. Beta's total assets over $10 million (as adjusted). You conclude, therefore, that Mr. and Mrs. Beta together satisfy the size of person requirement. Because you have now determined that the acquiring person is a $100 million (as adjusted) person and the acquired person is a $10 million (as adjusted) person (they will need to stipulate to this size of person in their filing), you know that the parties to the proposed transaction meet the size of person test.

Zed's acquisition of Beta is valued at $90 million and the parties meet the size of person test. Thus, unless an exemption applies, the parties in this hypothetical transaction must file and observe the statutory waiting period.

VI. ADDITIONAL CONSIDERATIONS

Note that this Guide does not cover all reporting obligations. The formation of corporate joint ventures and unincorporated entities may be reportable if the parties and the newly-formed entities meet certain criteria.[44] Also, transactions involving foreign businesses are subject to distinct treatment under the Rules.[45]

You also should be aware of Rule 801.90, which is designed to limit the ability of parties to

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[43] *See* 16 C.F.R. § 801.11 (d).

[44] *See* Rule 801.40 - 801.50, 16 C.F.R. § 801.40 - 801.50.

[45] *See* Rules 802.50 - 802.53, 16 C.F.R. §§ 802.50 - 802.53.

evade the Act's filing requirements. It states that: "Any transaction(s) or other device(s) entered into or employed for the purpose of avoiding the obligation to comply with the requirements of the act shall be disregarded, and the obligation to comply shall be determined by applying the act and these rules to the substance of the transaction."[46]

Finally, it is important to consider the many exemptions provided in the Act and the Rules. The Program is designed to facilitate antitrust review. It, therefore, does not require notification for transactions that have been determined to be unlikely to violate the antitrust laws. For example:

1) Stock splits that do not increase the percentages owned by any person are exempt;[47]

2) Acquisitions of small percentages of an issuer's voting securities solely for the purpose of investment are exempt;[48]

3) Acquisitions of additional voting securities by persons who already hold 50 percent of the voting shares of an issuer are not reportable;[49]

4) Acquisitions in the ordinary course of business, such as purchases of current supplies and used durable goods also are exempt;[50]

5) Acquisitions of several categories of real property, such as unproductive real property, office and residential property, and hotels are not reportable.[51]

6) Acquisitions in regulated industries, whose competitive effects are reviewed by other agencies, may be exempt or subject to modified reporting requirements.[52]

Although the premerger notification Rules tend to be complex and technical, the discussion in this Guide should help you determine whether a particular transaction must be reported. That

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[46] *See* Rule 801.90, 16 C.F.R. § 801.90.

[47] *See* § 7A(c)(10), 15 U.S.C. § 18a(c)(10), and Rule 802.10, 16 C.F.R.§ 802.10.

[48] *See* § 7A(c)(9), 15 U.S.C. § 18a(c)(9), and Rule 802.9, 16 C.F.R. § 802.9.

[49] *See* § 7A(c)(3), 15 U.S.C. § 18a(c)(3), and Rule 802.30, 16 C.F.R. § 802.30.

[50] *See* § 7A(c) (1), 15 U.S.C. § 18a (c)(1) and Rules 802.1(b), 802.1(c), 16 C.F.R. § 802.1(b), § 802.1(c)

[51] *See* § 7A(d)(2)(B), 15 U.S.C. § 18A(d)(2)(B); and Rules 802.2(c), 802.2(d), 802.2(e), 16 C.F.R. § 802.2(c), 802.2(d), 802.2(e).

[52] *See* § 7A(c)(6), 15 U.S.C. § 18a(c)(6), and Rule 802.6, 16 C.F.R. § 802.6.

said, you should not rely on this Guide alone to determine your filing obligation. As indicated earlier, you should refer to the Act, the relevant Rules and the Formal Interpretations of the Rules to understand points that are not discussed in this general introduction. Appendix 1, below, provides a quick reference to certain Rules relevant to determining reportability.

If you conclude that a transaction must be reported, you may want to consult the Federal Trade Commission's website at http://www.ftc.gov/bc/hsr for help in completing the Form. In addition, take the time to read the instructions to the Form carefully. They have been written to help you avoid the most common mistakes.

After consulting each of the sources mentioned here and in Guide I, if you still have questions, contact the PNO at (202) 326-3100.

Appendix 1: Relevant Rule – Quick Reference

Identifying Acquiring and Acquired Persons	
"UPE"	§ 801.1(a)(3)
"Person"	§ 801.1(a)(1)
"Control"	§ 801.1(b)
"Hold"	§ 801.1(c)

Size of Transaction Test	
Aggregation of Holdings	§§ 801.13 - 801.15
Value of Acquisition	§ 801.10
Percentage of Voting Securities	§ 801.12
Notification Thresholds	§ 801.1(h)

Size of Person Test	
Annual Net Sales and Total Assets	§ 801.11

Other Considerations	
Exemptions:	
Investment Only	§ 7A(c)(9); § 802.9
Intraperson	§ 7A(c)(3); § 802.30
Ordinary Course of Business	§ 7A(c)(1); § 802.1
Real Property	§ 802.2; § 802.5
Regulated Industries	§ 7A(c)(6); § 802.6
Foreign Transactions	§ § 802.50 - 802.53
Secondary Acquisitions	§ 801.4
Joint Venture Formations:	
Corporations	§ 801.40
Unincorporated Entities	§ 801.50
Avoidance	§ 801.90