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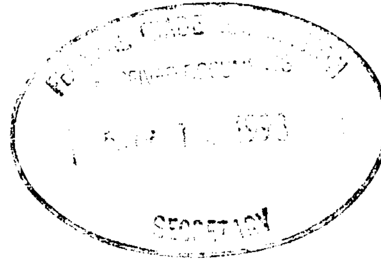

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November 12, 1998

FEDERAL TRADE COMMISSION
PREMERGER NOTIFICATION OFFICE
1998 NOV 12 A 9:01

Mr. Joseph G. Krauss
Assistant Director for the Premerger
Notification Office
Bureau of Competition, Room 301
Federal Trade Commission
Pennsylvania Avenue & 6th Street NW
Washington, D.C. 20580

Dear Mr. Krauss:

This responds to your request for comments on your recent, formal HSR interpretation regarding the formation of LLCs and your more general inquiry about the formation of partnerships. What follows are, principally, my views on these issues. They are not client sponsored. Nor did I have an opportunity to give them wide circulation within our firm.

By way of background and thus perspective, I am a transactional lawyer. I focus on acquisitions and joint ventures. I have worked extensively with the HSR regime for the two-plus decades it has existed.

Here are my thoughts:

Combinations of Pre-Existing Businesses

I welcome the approach you adopted in your interpretation about LLCs, your focusing on transactions that unite independently owned businesses under common control. As with all rules that attempt to divide myriad events into categories, this one, too, will present knotty issues. But, in my view, your sorting joint ventures based on whether they unite existing businesses correlates well with what should be important to you. Joint ventures that combine businesses are, obviously, far more likely to present antitrust issues than ventures which, for example, simply pool the participants' cash and credit to launch or acquire new businesses. Although the latter could have antitrust significance, your rules necessarily deal with levels of probability. And, of course, non-reportable transactions are not antitrust immune.

But Why Different Treatment for Different Types of Entities?

Let me step back from LLCs, now, and treat the broader subject of joint venture formation. Even as I applaud your "uniting" approach, I believe you are headed down (indeed, are already far down) a path in which you are making formal distinctions among types of entities that have little relevance to antitrust. Let me explain.

- In my view and those of most everyone I have discussed this issue with since 1977, your predecessors relied on shaky assumptions when, in Rule 801.40, they divided the universe of joint ventures into corporate joint ventures and all others.

- CEOs and other business people who make the decision to form a joint venture want to form a joint venture. Business being their business, they focus on the business deal. They typically have little idea (or, with respect, are sometimes ill-informed about) whether they should use a corporation, a partnership, an LLC or something else to house the joint venture. In the end, they leave those second order decisions to lawyers, accountants and others like me. And we, in turn, make those decisions based on criteria (for example, tax transparency) that do not correlate with competitive considerations.

- In other words, at least in my experience, there is little correlation between antitrust sensitivity and form of entity.

- Contrary to the rule makers' perception in 1977, big partnerships (by "partnership" I mean <u>entities</u> formed under statutes that require formal filings, as in the case of limited partnerships, and <u>entities</u> formed under statutes that do not require formal filings, as in the case of many general partnerships), are not formed casually or accidentally. Large partnerships are formed with deliberation and clear purpose. I say that fully mindful of the occasional lawsuit brought by creditors that imposes partnership status (essentially, cross-liability and cross-agency) on parties that thought they were independent actors. I am not concerned that you will attempt to impose HSR sanctions on that sort of forced or unintended relationship.

- Nor, as has been suggested, should the difficulty of your monitoring compliance dictate the contours of your rules, whether with respect to this or any other HSR subject matter. By now, the transaction bar is pretty sophisticated about HSR. For the most part, we are doing our job. Most transaction lawyers are or have access to an HSR expert. And our clients do file if we tell them to file.

- Enter, now, the LLC. From an HSR perspective, the invention of LLCs should have been a trivial event. LLCs present little more than another choice of vehicle for the lawyers and others who make the less important decisions. The important decisions (which joint ventures to proceed with) continue to be made by business people based on business and other criteria.

- You nevertheless are struggling with LLCs. The reason is that you inherited Rule 801.40. Because that rule lacks a sound rationale, you had no ready

foundation to shape an LLC rule.*

- In all events, we now have three very different HSR rules that govern the formation of joint ventures. For corporations, the size and dollar criteria of Rule 801.40(c) govern. For LLCs, those criteria plus the unification-of-businesses principle plus the common control principle govern. For partnerships, the "never file" rule governs.

If I am right that there is little relationship between antitrust substance and choice of joint venture entity, this is, I submit, an awful lot of rule making and line drawing to little useful end. Where will we go when the business and tax bars invent a next species of entity? That will happen.

The Burden Issue and a Suggestion

You asked about burden. Obviously any expansion of your coverage will increase burden -- more $45,000 filing fees, more legal fees, more management time, more government time. Right now, the principal cause for burden is the very low filing thresholds. Although I did not check inflation indices, I will guess that 15 million 1976 dollars equates with something like 6 million 1998 dollars. Your remedying that problem (lowered thresholds) across the board for all voting security and asset acquisitions should be your number one "burden" project.

What it would take to achieve such a change, I do not know. But let me suggest a first, baby step. In the limited context of joint venture formation, I suggest that you consider:

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* Indeed, I believe that, lacking such a foundation and because you felt compelled to position LLCs rationally between corporations and partnerships, your original treatment of LLCs may have been backwards as tested by antitrust principles. As I understand it, before your recent interpretation, the formation of an LLC with outside directors ("managers" in LLC parlance) was more likely to require filings than the formation of an LLC with inside directors (i.e., employees of the LLC's equity holders). Ceteris paribus, outside directors are probably more likely to run a business as an independent profit center and competitor than are employees of the parties that formed the LLC.

- common rules for the formation of all types of joint venture entities
- tied to the parties' uniting existing businesses under common control (some version of your new LLC approach)
- but with higher dollar thresholds.

This sort of approach would:

- dispense with formal distinctions among entity types that have little antitrust relevance
- divide the universe of joint ventures into those that pose the greater threats to competition and those that pose far lesser threats
- yet not impose an undue tax (burden).

Rule 801.90 Issues

Let me, finally, share a thought regarding the application of Rule 801.90 in this area. I was perplexed by the reference to Rule 801.90 in example 2 in your LLC interpretation.

As you know, a Rule 801.90 violation requires two elements. First, the parties need to employ a "transaction" or "device" for the purpose of avoiding coverage. If they do, then, second, you disregard the transaction or device and apply the act and rules to the "substance" of the transaction.

Please consider what that means in the context of the rules now in place for joint ventures. Assume, for example, that two parties form a partnership joint venture rather than a corporate joint venture solely for the purpose of avoiding filings. That, I assume you believe, would be a transaction or device. Yet the second part of the test would not be satisfied. Your rule (the partnership exception) is the substance in this context. You defined that substance by your rule, a rule that treats form as substance. Rule 801.90 thus does not apply.

Contrary to example 2 in your LLC interpretation, that same conclusion (no HSR coverage) should follow if the parties select a 49/49/2 ownership split for an LLC rather than a 50/50 split. That is no different than if the parties reduce an

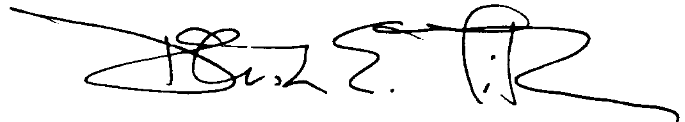
acquisition price by $100 to bring an acquisition below a controlling $15 million threshold. You cannot, I submit, have things both ways -- write a quantitative or form-focused rule and then ignore that rule yourselves. If, behind the wheel, I hold my speed to 64 mph in order to avoid a ticket (i.e., employ a device for that purpose), that is okay. I am not speeding.

I believe, therefore, that if you retain joint venture rules linked to types of entities or percentage ownership splits, you should back off references to Rule 801.90 like the one in example 2.

* * *

I hope this letter is helpful. I wish you well in this endeavor. Comments come easily. Good rule writing is far harder.

Very truly yours,



Daniel E. Titelbaum