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Date: Fri, Dec 8, 2000 12:24 PM
Subject: HSR

As I thought about one of our several conversations yesterday and tried to reconstruct the interpretive principles, I found myself getting very confused. May I lay out the following problem in a more methodical way?

Suppose that Company X has 3 directors, elected by the holders of its common stock. Company X is going to issue a new class of preferred stock, the holders of which will elect two new directors, making a total of 5 directors. The holders of Company X common stock will continue to elect the other 3.

Person A will acquire (first case) all the preferred shares. Person A will become a 40% shareholder of Company X. Straightforward.

Person A will acquire (second case) half the preferred shares, plus one share. Assume no cumulative voting. I would have said that Person A becomes a 20% shareholder of Company X, since it will hold half the shares that elect two-fifths of the directors. But I'm confused about your comment yesterday concerning the ability to "seat" directors. Person A in this case presumably has the practical power to elect both of the directors elected by the preferred shareholders. Does that make Person A a 40% shareholder? My answer -- for purposes of determining whether Person A is making a reportable acquisition -- would be no. -- AGREE --

B. Michael Verne
12/12/00

N. OVUICA
T. HANLON
R. SMITH
AGREE.

A modification of my first case: Person A will acquire all the preferred shares, but his purchase contract with the issuer says he gets the right to designate one additional director (out of the 3 otherwise reserved to the common shareholders). We talked about this scenario yesterday. Your answer was that you look to the voting power inherent in the shares, and not to the purchase contract, so Person A is viewed as acquiring 40% (not 60%) of Company X's total outstanding voting securities. AGREE --

If, instead of trying to figure out whether Person A's acquisition is reportable, we're now trying to figure out whether Person A controls Company X after the acquisition is completed, is Person A viewed as having the power to "seat" three of five directors, and therefore as controlling Company X? I would say yes. AGREE --

Return to my second case, in which Person A acquires only just over half the preferred shares. Does Person A control Company X because it has the practical ability to "seat" both of the preferred directors and the additional, appointed director? Or was this your point about not combining voting power with contractual power, and thus that Person A is viewed as being able to "seat" the two preferred directors, but not the additional appointed director? YES - A CONTROLS X

TEST FOR CONTROL
IS THE MAXIMUM
NUMBER OF DIRECTORS
THAT A CAN SEAT
THROUGH THE COMBINATION
OF VOTING ITS STOCK
+ THE CONTRACTUAL
RIGHT TO DESIGNATE.

Sorry to make this complicated, but I think we've both seen variations on each of these variations. Thanks for your help.

[REDACTED]

SINCE THIS IS 3 OF 5,
A CONTROLS.