

806.40; 806.11(b)(1) and (2)

March 16, 1999

SENT VIA FACSIMILE TO NO.: 202-326-2624

Richard B. Smith, Esquire
Premerger Notification Office
Bureau of Competition
Federal Trade Commission
Sixth Street and Pennsylvania Avenue N.W.
Washington DC 20580

Dear Mr. Smith:

We seek the staff's determination whether the ultimate parent entity is an individual sole Trustee of a Trust, or the Trust itself. The Trust is a Massachusetts business trust issuing transferable shares, and its only significant asset consists of all voting securities of a corporation ("Seller"). Seller and the Trust have assets of less than \$10 million. Our client ("Purchaser") has assets over \$100 million and is negotiating to purchase substantially all of Seller's assets. If Seller's ultimate parent is the Trust, the size-of-the-person threshold will not be crossed. On the other hand, if Seller's ultimate parent is the individual Trustee, his additional personal business assets will elevate the acquired person over the threshold.

Until January 1, 1999 Seller's voting securities were held by five individuals, four with 15% each and the fifth with 40%. On that date, the five contributed their shares in Seller to a newly created business Trust in exchange for equal numbers of the Trust's transferable shares. This transaction was tax driven.

The former 40% shareholder in Seller and current 40% holder of the Trust's shares is sole Trustee. Under the Declaration of Trust:

The Trustee shall have without further authorization full and absolute power and control and authority over the Trust Property and over the business of this Trust to the same extent as if the Trustee was the sole owner of such property subject only to the limitations herein expressly stated.

Among detailed powers granted to the Trustee, are the power "to vote and exercise all other rights concerning, any shares of stock . . . of any corporation. . . ." Thus, the Trustee controls Seller

Under § 801.1(c) of the HSR regulations, however, as I understand it, that control would not normally result in having the Trustee, rather than the Trust, be deemed to hold Seller's voting securities. The trust is not "a common trust fund or collective investment fund within the meaning of 12 CFR § 9.18(a) . . . [or a] revocable trust or an irrevocable trust in which the settlor retains a reversionary interest in the corpus. . . ." While a section of the trust appears to permit its termination by a vote of three-quarters of the shareholders if they would be adversely affected (without stating what vote is needed if they would not be adversely affected), this provision would not seem to constitute a power of revocation and, in any case, would not place such a power in any one person.

More troublesome is the provision at 43 Fed. Reg. 33459 (July 31, 1978), stating:

Since a Trust does not issue voting securities, under the rules it can be controlled by another entity only if the latter has a contractual power, under the Trust indenture, to designate the Trustee or, if there is more than one, a majority of the Trustees. See §§ 801.1(a)(1) and 801.1(b)(2). For example, if a corporation appoints the Trustees of an employee pension plan organized as a Trust, then the corporation would control the Trust under § 801.1(b)(2), and the Trust would not be a separate "person" under the rules. . . .

Section 801.1(a)(1) of the regulations defines "person" as "an ultimate parent entity and all entities which it controls directly or indirectly." Section 801.1(b)(1) includes within the definition of "control:"

Having the contractual power presently to designate 50 percent or more of the directors of a corporation, or in the case of unincorporated entities, of individuals exercising similar functions.

Because virtually every trust provides some method of designating successor trustees, it seems logical that the power to name replacement or successor trustees should only place control of the trust assets in the person having that power when that person is someone other than the trustee himself. Otherwise, for HSR purposes virtually every trust would have its assets held by the trustee rather than the trust, contrary to the basic thrust of the rule. This problem is recognized in Premerger Notification Manual (ABA 1991), Item 84:

Clearly the settlor's power to designate the trustee in establishing the trust does not confer control. Section 801.1(c)(3)

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specifically identifies the conditions under which the settlor controls. Any third party having the power to designate or replace half or more of the trustees will control. However, it is not clear how this provision relates to the case where a trustee is given the power to designate a replacement trustee. This power adds very little to the actual control that trustee already exercises over the trust assets.

The Manual notes that, "The FTC staff has not stated a position on this issue."

The topic of replacement and successor trustees is treated in §§ 3.6 and 11.2-11.4 of the subject declaration of trust. Generally, the remaining trustees fill vacancies. Although there is only one Trustee at present, § 3.1 permits the Trustee to fix the number of trustees. Also under § 3.6, if no trustee is serving then a named individual, one of the 15% beneficial owners, shall serve as successor trustee. Section 11.2 provides for the removal of trustees by the affirmative vote of not less than three-fourths in interest of the shares then outstanding. Section 11.4 provides that if all trustees shall have died or have become incapacitated and there is no successor trustee serving, new trustees may be elected by the affirmative vote of not less than 60% of the shares outstanding.

We believe that the Trust should be treated as Seller's ultimate parent, rendering it unnecessary to include the Trustee's other assets in applying the size-of-the-person test. As indicated by the above discussion of item 84 in the Manual, however, this conclusion is not free from doubt. Therefore, we respectfully request an informal determination by the staff as to how the rules pertaining to holdings by a Trustee should be applied on these facts.

Please let me know [redacted] whether we should treat the Trustee or the Trust as Seller's UPE. Thank you very much.

Sincerely yours,

[redacted signature]

3/19/99 Advised writer that it has been the long-standing policy of the [redacted] office to treat Mass. Business Trusts as corporations. Formerly of this Trust covered by 801.40 but, not a 100% owner at time of formation (and no 100% power, as well, writer advised) Share of Trust held by minority holders only. The five individuals agreed to appoint the 40% holder as sole trustee (director) through the trust instrument, but no single one of the five made such appointment. Power to revoke trust or remove trustee is not held by any one of the five. On the basis of corporate (rather than trust) control and, in, the corporation (or trust) is its own UPE. (M. U. Grey).
R. B. Smith