Managed Funds Association
The Voice of the Global Alternative Investment Industry
Washington, D.C. | New York

February 1, 2021

Via Online Submission

April Tabor
Federal Trade Commission
Office of the Secretary
600 Pennsylvania Avenue, NW
Suite CC-5610 (Annex J)
Washington, DC 20580

Re: 16 C.F.R. Parts 801-803: Hart-Scott-Rodino Coverage, Exemption, and Transmittal Rules
Project No. P110014

Dear Ms. Tabor:

Managed Funds Association[1] ("MFA") welcomes the opportunity to comment on the proposed amendments to the premerger notification rules ("the Rules") that implement the Hart-Scott-Rodino Antitrust Improvements Act ("HSR Act") as published in the notice of proposed rulemaking ("NPRM") issued by the Federal Trade Commission ("FTC" or "Commission") on December 1, 2020.[2]

MFA appreciates the Commission's efforts to update the current Rules to increase the efficiency and effectiveness of the Premerger Notification Program, more accurately respond to current-day market realities, and provide the FTC and the Antitrust Division of the Department of Justice ("DOJ" or "Antitrust Division") (together, the "Agencies") with information necessary to assess transactions that may harm competition. MFA supports the proposal of a new *de minimis* exemption, a proposal for which MFA has long advocated. The proposed *de minimis* exemption would remove significant burdens on investment management firms, their clients, and issuers, as well as contribute to the efficient operation of public markets, without posing any increased harm to competition. However, MFA has strong concerns that the many exceptions to the proposed exemption would make the exemption unavailable to many investment managers. In addition, MFA is concerned that the proposal to aggregate multiple entities for purposes of HSR reporting

[1] MFA represents the global alternative investment industry and its investors by advocating for public policies that foster efficient, transparent, fair capital markets, and competitive tax and regulatory structures. MFA supports member business strategy and growth via proprietary access to subject matter experts, peer-to-peer networking, and best practices. MFA's more than 140 member firms collectively manage nearly $1.6 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has a global presence and is active in Washington, London, Brussels, and Asia, supporting a global policy environment that fosters growth in the alternative investment industry.
[2] 85 Fed. Reg. 77053 (Dec. 1, 2020).

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will be impractical and unduly burdensome in many instances, and in particular the inclusion of "associates" in the definition of "person" under the Rules will often be unworkable for investment management firms. Limiting the availability of the proposed exemption will inhibit the types of engagement between investors and issuers that serve important public policy goals such as increasing issuer accountability on environmental, social, and governance ("ESG") matters. The Securities and Exchange Commission ("SEC") and many other constituencies support constructive engagement on ESG matters, and it is readily distinguished from the type of engagement which is of antitrust concern to the Agencies.

As noted in the NPRM,[3] the Commission, with the concurrence of the Assistant Attorney General of the Antitrust Division, can exempt classes of transactions not likely to violate the antitrust laws from the requirements of the HSR Act.[4] The Agencies recognize that their mission is best served by focusing their finite resources on transactions that pose a potential threat to competition, and not on *pro forma* filings for transactions very unlikely to harm competition and that impose significant burdens and costs on investors and issuers.[5] Unfortunately, we are of the view that the Rules will not achieve the Commission's objectives, but, to the contrary, will result in a significant number of unnecessary filings and increased burden on both the Commission staff and investors.

I. Executive Summary

MFA supports the Commission's efforts to update current Rules but we are concerned that the proposed Rules do not consider important features of the investment management industry that would make aspects of the Rules challenging and impractical to implement. MFA welcomes the opportunity to continue working with the Commission to refine the Rules. To this end, MFA provides the following comments and recommendations:

- MFA strongly supports the proposed *de minimis* rule, with modifications as proposed below, as exempting from review those transactions least likely to harm competition, while removing significant burdens on investors, issuers, and the Agencies, and fostering beneficial engagement between shareholders and management.

Aggregation

- The proposal to aggregate different funds under common management for purposes of determining when an HSR notification is required should be deleted from the final rule. This proposal is unworkable and would impose significant burdens on investment

[3] *Id*. at 77054.
[4] 18 U.S.C. § 18(d)(2)(B).
[5] 85 Fed. Reg. 77053, 77055 (Dec. 1, 2020) ("The Agencies have a strong interest in receiving HSR filings that contain enough information to conduct a preliminary assessment of whether the proposed transaction presents competition concerns, while at the same time not receiving filings related to acquisitions that are very unlikely to raise competition concerns.").

management firms and their clients. Additionally, this requirement would distort markets and increase HSR filings for investments that present no potential for competitive harm.

- If any aggregation is adopted, it should not be accomplished by recourse to redefining "person" to include associates. To do so would upend the over 40-year reliance on the concept of ultimate parent entity for reporting purposes and would have unintended consequences for other aspects of HSR regulations and the applicability of important exemptions.
- If the proposed definition of "person" is adopted, an exception for investment management firms should be provided. Minority investments by such firms are especially unlikely to negatively harm competition.

Common Ownership Exception

- The 1% common ownership exception to the proposed *de minimis* exemption should be eliminated. There is no substantial basis for concluding that common ownership facilitates competitive harm. This exception would make the exemption unavailable to many investment management firms, for whom the rule is most appropriate.
- In the alternative, the common ownership exception should be raised to 10%, or, at a minimum, 5%.

Definition of "Competitor"

- Instead of the proposed definition of "competitor," the Commission should adopt the Clayton Act § 8 definition of "competitor," including both its safe harbor for *de minimis* competition and the requirement that the competition must occur in the same geographic location. The definition as proposed is unduly burdensome on investors, who may not be able to accurately determine NAICS codes of companies, and, because NAICS codes are often much broader than antitrust markets, scopes in companies that do not actually compete.

Vendor/Vendee Relationships

- The exception in the proposed *de minimis* exemption concerning vendor/vendee relationships should be eliminated. There is no basis for presuming that a vendor/vendee relationship should preclude use of the proposed exemption, and the inclusion of this exception would significantly limit use of the proposed exemption by large institutional investors.

II. Aggregation Should Not Be Required

We appreciate the Commission's concerns that it does not have sufficient visibility into shareholdings by associates of certain types of entities, such as private equity funds and master limited partnerships. The Agencies' efforts for greater visibility of the holdings of associates when an acquiring person, as currently defined, makes an acquisition are understandable. We believe the best way for the Agencies to address this concern is to modify or expand the information that is required on the Notification and Report Form ("HSR Form" or "Form") for transactions that are reportable based upon the acquisition made by a single ultimate parent. For the entire history of the HSR Act, reportability has been determined on the basis of beneficial ownership, and not on

contractual relationships.[6] This was a carefully considered decision by the Agencies in promulgating the original rules, and should not be altered without thoughtful consideration of all of the potential implications on the entire regulatory framework that was built upon that foundation, including other definitions, provisions, and exemptions.

Aside from the general problems entailed in any attempt to change the current definition of "person" to encompass a wider number of entities based on contractual relationships, the Commission's specific proposal in the NPRM to expand the definition of "person"[7] to encompass more than one ultimate parent entity[8] ("UPE") by including "associates"[9] in the definition of the filing person is problematic. Basing reportability other than on beneficial ownership of an UPE would upend the entire HSR framework. The idea of redefining "person" by reference to associates seems to rely on a simplified and static understanding of how funds are structured and operate over time. While the term "associate" is adequate for the purpose of determining at a specific point in time what information should be disclosed about certain entities beyond the specific acquiring person in the HSR Form required to be submitted under the HSR Act, the term is wholly unsuited for use in determining which transactions should be reported and who holds the right to make acquisitions over the five year period after reporting, as explained in further detail below.

MFA has strong concerns about the increased burden this proposal would impose on investment management firms and their clients. The justification for the proposal appears wholly hypothetical, as MFA is unaware of any enforcement actions because of an associate's holding in an issuer. As will be discussed in greater detail below, the costs and burdens of tracking very small shareholdings across multiple funds are steep, and place a significant and potentially unmanageable burden on investment advisers and their investors. Such costs and burdens include the significant practical issues to determine when a filing is required, the difficulty of detecting very small shareholding amounts across multiple funds, and steep compliance costs from systems and personnel that track the information as well as increased filing fees and attorney costs.

As we will discuss below, statistics demonstrate that holdings of 10% or less do not give rise to competitive harm. Thus, given the dramatically increased costs to investment management firms from aggregation, balanced by a negligible or nonexistent benefit to the Agencies from

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[6] With rare exception, such as control via irrevocable proxies to appoint a majority of a corporation's board of directors.

[7] 16 C.F.R. § 801.1(a)(1) "Except as provided in paragraphs (a) and (b) of §801.12, the term person means an ultimate parent entity and all entities which it controls directly or indirectly."

[8] 16 C.F.R. § 801.1(a)(3) "The term ultimate parent entity means an entity which is not controlled by any other entity."

[9] 16 C.F.R. § 801.1(d)(2) "*Associate*. For purposes of Items 6 and 7 of the Form, an associate of an acquiring person shall be an entity that is not an affiliate of such person but: (A) Has the right, directly or indirectly, to manage the operations or investment decisions of an acquiring entity (a 'managing entity'); or (B) Has its operations or investment decisions, directly or indirectly, managed by the acquiring person; or (C) Directly or indirectly controls, is controlled by, or is under common control with a managing entity; or (D) Directly or indirectly manages, is managed by, or is under common operational or investment decision management with a managing entity."

increased insight into transactions unlikely to pose harm to competition, there is no justification for expanding filings for such *de minimis* holdings. For these reasons, we believe that aggregation should continue to be avoided for investment management firms. Below, we elaborate on our objections to aggregation, and suggest some alternative approaches.

a. If the New Definition Is Adopted, Certain Types of Investment Funds Should Be Excepted

If the proposed definition of "person" includes funds or entities other than a single UPE, an exception should exist for the types of investment management firms that comprise MFA's membership. Investment management firms actively buy and sell voting securities, but in terms of how the companies that issue those voting securities are managed, many are passive investors who seek to obtain positive returns for their clients over the period the voting securities are held, rather than to take a majority stake or influence the basic business decisions of the companies. Further, funds within such firms generally have varying investment goals independent from the goals of other funds within the fund family—in fact, such variety serves a primary purpose of diversifying the offerings of asset management companies. Nevertheless, under the proposed definition of "person," all such funds would be included in the acquiring person because the same UPE typically owns the investment managers of the various funds.

Given this independence and the varying goals among funds within a larger investment management firm, there is limited incentive to share information and coordinate investment strategies between funds. Indeed, the funds may be siloed from each other for sharing information, and it may not be permissible under company policy to share certain details about holdings in issuers, as well as facts and documents related to investments, particularly if the funds or their managers are aware of material nonpublic information about the companies in which they invest. Thus, having one person certify the correctness and completeness of the information on the HSR Form, as well as the documents submitted thereto, creates a risk for that certifying official.

For these reasons, if the proposed definition of "person" is adopted, an exception for investment management firms should be provided.

b. "Associate" Is Currently Used to Describe Information an Acquiring Person Must Report on Its HSR Notification Form

The current HSR Form requires information about holdings of associates in the issuer whose shares are to be acquired, or in issuers reporting revenues in the same six-digit NAICS codes as the target issuer. The definition of "associates" is broad, and, for the types of private equity funds and master limited partnerships discussed in the NPRM, it generally encompasses all entities that are part of the same private equity fund family. This information permits the Agencies to evaluate the combined shareholding in the target issuer, as well as holdings in companies in the same or similar businesses. Because there is currently no requirement to report holdings of associates under 5% on the HSR Form, the filing person can ignore small accounts. Given that most managers of investment funds want a diverse portfolio of investments, they rarely would hold

more than $94 million or 5% or more of an issuer in more than a handful of their larger funds, and it is less likely that a 5% or more holding in a large cap issuer would be held within a managed account or fund that is owned by a single investor, which makes the information currently required of associates generally easy to monitor for HSR compliance—particularly given that this information only needs to be collected when a single fund exceeding the size-of-transaction threshold triggers an HSR filing. In addition, because HSR reporting is based on the concept of the UPE, the current HSR reporting obligation for a managed account or fund of one[10] rests with the investor, and not the fund manager.

Importantly, at present, a reportable transaction is first determined by looking at the acquisition of the voting securities of an issuer by each acquiring person, which is ordinarily a single limited partnership fund that is not "controlled" by any other person or entity. Once that acquiring person and its fund manager are identified, the associates of the fund and its manager are determined and reported on the Form where applicable. At present, the only tripwire necessary for determining whether an HSR filing is required is that a UPE crosses the size of transaction threshold (and the parties meet the size-of-person test). As it now stands, the determination of associates, and the interdependence of persons and their associates, and associates of their associates, is not required in order to determine whether a transaction is reportable under the HSR Act.

c. The Proposed Aggregation Rule Relies on Simplified Assumptions About Fund Structures, and the Associate Concept Breaks Down If There Is No One-to-One Match-Up of Fund Managers to Funds

In the NPRM, the Commission describes in both its explanation and the example the following simple structure:

> Parent Fund creates Fund Vehicle 1, Fund Vehicle 2, and Fund Vehicle 3, each a non-corporate entity. No one controls these non-corporate entities, so each fund vehicle is its own UPE even though they exist within the same family of funds.[11]

This describes a common private equity fund structure where the manager forms the entities that will acquire control of portfolio operating companies or invest in venture capital start-up companies, and raises funds largely from institutional investors who become limited partners of multiple investor fund entities. This is likely the most common structure the Commission sees in HSR filings, because only associates holding more than 5% of the issuer being acquired, or

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[10] A managed account or fund of one is by definition owned 50% or more by the account holder or sole fund owner, and therefore is included within the UPE of its owner, and its holdings are aggregated with any other holdings of that owner. Because a fund manager will not know all of the other holdings of such investors, generally fund managers do not monitor such managed accounts and funds for HSR compliance unless the account/fund managed by that manager itself exceeds the HSR size of transaction threshold. A more detailed discussion of managed accounts and funds of one are provided below at p. 7.

[11] 85 Fed. Reg. 77053, 77055 (Dec. 1, 2020).

other issuers in the same NAICS code, are reported. This 5% threshold generally excludes smaller funds that are under a common investment manager, such as funds that individual investors beneficially own (so-called co-investments) that are also invested in the issuer being acquired or other issuers that share the same NAICS code.

Crucially, many other types of funds have more complex structures that do not look at all like the example the Commission assumes in the discussion of the new rules and the reporting examples that it provides.

Asset managers who manage funds that invest in these other types of non-control investments, including minority shareholding positions in publicly traded securities, ordinarily have more complex structures. Indeed, some asset and fund managers have organizational charts that run hundreds of pages, as different entities are created to accommodate different investors, tax consequences, limit liability, provide discrete collateral pools for debt financing, and segregate different investment strategies or risk profiles. At present, only the associate entities large enough to hold potentially 5% or more of a single issuer need to be considered for the HSR Form, which would exclude all but a handful of funds when looking across a fund family set of organizational charts.

While a discussion of all of the different varieties of fund arrangements would be too voluminous for inclusion in this comment, we highlight as examples the following complexities that the Commission seems to ignore in its simplified view of fund families:

> (1) Managed Accounts: A managed account is an investment account that a single institutional or individual investor owns, such as a pension fund or insurance company. A professional money manager is hired by the investor to oversee the account. The manager has discretionary authority over the account, and makes investment decisions pertinent to the client. A managed account may contain financial assets, cash, or titles to property. The investment manager has the authority to buy and sell assets without the client's prior approval, as long as it acts according to its fiduciary duty and the client's objectives. *Under the proposed redefinition of "person," all of the UPE owners of managed accounts would be considered associates of the fund manager. A fund manager with hundreds of managed accounts would have hundreds of UPEs within its person!*
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> (2) Funds of One: A fund of one is an investment fund, usually a limited partnership, that has a single investor, often a large institutional or sovereign wealth fund investor. Investing in a commingled fund exposes investors to fund performance risk if the manager receives redemption requests and is required to force sell positions. With a fund of one, investors are insulated from that commingled risk. Funds of one have become increasingly popular. *The UPE of a fund of one is the investor, so, under the proposed redefinition of "person," each fund of one investor UPE would become an associate within the same person as the fund manager.*

(3) Segregated Portfolio Companies: A segregated portfolio company ("SPC") is usually a single limited partnership fund entity that treats each portfolio (also called a sleeve or a series) as a sub-fund within the SPC. Adding to their complexity, an SPC may have a different manager for each series within it. According to informal guidance by the PNO, the UPE of an SPC organized as a limited partnership is the SPC itself if it has no single investor entitled to 50% more of its profits or assets on dissolution, and series are ignored. *Under the proposed redefinition of "person," if the UPE SPC has several different managers, each SPC manager would be an associate of the fund, and every other fund that each of the managers manage would also be an associate of each manager.*

(4) Subadvisors: A fund subadvisor is a third-party money manager hired by a fund management company to manage an investment portfolio at the direction of the primary investment manager. Typically, a subadvisor is brought in because of that manager's expertise in managing a certain area of the market or specific strategy. *Under the proposed redefinition of "person," each primary investment manager and subadvisor would be an associate of the subadvised fund, and any other fund that the investment manager or subadvisor also advises would be an associate within that same person.*

As the above examples reveal, it is quite common for one fund to have more than one manager, and for one manager to manage more than one fund. Further, large institutional investors, who are the UPEs of funds of one and managed accounts, ordinarily invest with more than one manager to manage their extensive portfolios, in addition to some investing funds using their own in-house fund managers. There is often no "one-to-one" match of investment managers to funds as in the simplified example on which the Commission relies. Given this fact, if the proposed redefinition of "person" is adopted, there will be many situations where there are a number of "persons" that can be created using different combinations of funds and managers that own shares in the same issuer, or may acquire shares in that issuer in the future.

The multiplicity of "person" permutations created by the inclusion of associates in the definition of "person" leads to very real compliance problems. Under the proposed redefinition of "person," each fund, large investor, and fund manager will need to determine all of the possible combinations that could constitute a person by performing this exercise: start with each manager and fund entity and then determine the associates for each. Then, once all of the possible person permutations are determined, someone will need to aggregate and track all of the voting security holdings in the specific issuer under consideration held in each of the UPE entities included within each of the possible persons. As discussed above, this type of aggregation and sharing of proprietary information raises problems, as separate funds typically do not disclose their positions to other funds. Further, as various combinations trip the HSR filing thresholds, sequential HSR filings will need to be made as each potential person crosses the reporting thresholds for each issuer, so that no potential associate holding or acquiring shares in the relevant issuer remains uncovered by an HSR filing. Lawyers, and those who fill out forms, will benefit; the Commission and consumers will be harmed by added filings of no competitive consequence and the additional, wasted costs imposed on both the filing firms and the Agencies.

d. The Proposed Aggregation Rule Relies on the Assumption That the Identity of Associates Is Static and Does Not Change Over Time; this Associate Concept Does Not Work If the Members of the "Person" Are Constantly Changing

The determination of associates is currently used for determining what information needs to be included on an HSR Form at a particular point in time (i.e., the day an HSR filing is made). A transaction is reportable based solely with respect to a specific UPE seeking to exceed the size-of-transaction threshold and meeting the size-of-parties test. When the HSR waiting period expires or is terminated early, the UPE may then acquire voting securities up to the thresholds for which the filing was made for the following five years if the holdings of the UPE cross the applicable threshold within one year. Under current rules, the number or identity of the other UPEs with which a UPE associates does not affect its right to acquire additional shares over that five-year period.[12]

If the new definition of "person" is adopted, in addition to the complexity of determining the identity of associates **at a specific point in time**, there is the issue of how the identity of associates, and therefore the members of a person, are determined **over a period of time**. In other words, assume Person I is composed of: (a) Investment Manager; (b) Mr. Savvy, a 50% owner of the Investment Manager entity and the individual who does the management; (c) Fund Vehicle 1; (d) Private University (a UPE within the Person because it has a fund of one that Investment Manager manages); and (e) Company Pension Fund (making Company a UPE within the Person because it has a managed account that Investment Manager manages). Person I files an HSR to acquire over $50 million but less than $100 million of Issuer D, and the waiting period expires. Person I may now acquire up to $100 million of Issuer D over the next five years, so long as it crosses the $50 million threshold within one year.

All fine and good so far. Now suppose that Mr. Savvy sells his 50% interest in the Investment Manager to the other principals because he wants to start a new investment company. And let's assume that Private University no longer wants to invest with Investment Manager because it liked Mr. Savvy, and liquidates its fund of one. Also, Company Pension Fund is taken private by a private equity fund and is no longer its own UPE, but part of another fund family, and retains its managed account with Investment Manager. And Investment Manager gets a new investor who opens a managed account, the Visionary Foundation.

After these changes, what does the HSR filing made for Person I mean?

1. Can Fund Vehicle 1 still acquire up to $100 million of Issuer D under the HSR filed by Person I?

[12] If a person other than the one that filed the HSR becomes the UPE, then that new UPE would need to file an HSR to acquire the shares held.

2. Does it matter what the entities that were associates at the time that the HSR filing was made currently hold (and does it matter if they are still associates of Fund Vehicle 1)?
3. Does Fund Vehicle 1 need to re-determine its associates each time it makes an acquisition and make a new HSR filing as part of each different Person that can be constructed?
4. What if Person I only crossed the $50 million threshold within one year based solely on acquisitions by Private University's fund of one, which is no longer an associate within Person I? Does the HSR right to acquire follow Private University and is no longer applicable to others in Person I?
5. Can Visionary Foundation acquire $51 million of Issuer D without reporting if all of the other original members of Person I hold less than $49 million, even if it was not a member of Person I when it filed?

This example highlights the fact that the expiration of the HSR waiting period grants the recipient the right to acquire shares up to the next threshold for five years without being subject to civil penalties of $1.3 million per month.[13] When that right is granted to a UPE, that right belongs to a legal entity or natural person. That UPE retains that right irrespective of the identity of other parties with which it associates or has contractual relations. If the HSR right to acquire is granted to a person as redefined under the proposal, that right belongs to a collection of entities that are separate UPEs, and no one natural person or legal entity owns that right. Therefore, if that collection of entities changes, it is unclear what happens to that right.

Investment fund managers add and lose investors all the time, and larger institutional investors add and change investment managers continuously. It is not clear under the proposal whether each different permutation of associates results in an ever-changing person. If so, then either it is not clear to whom the right to exceed the HSR size of transaction thresholds applies when UPEs depart or are added, or whether every single acquisition will require a new HSR analysis and potential new filing, even if one or more associates were listed as members of a person on a prior HSR filing.

To summarize, as currently used for determining what information needs to be included on an HSR Form at a particular point in time (the day an HSR filing is made) and starting with a specific UPE as the acquiring person, the concept of associate works. Once these conditions are relaxed, however, the associate term is no longer a useful basis for determining when an HSR filing is required, and whether a prior filing by a person that included a particular UPE covers a

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[13] The daily HSR maximum civil penalty of $43,792 x 30 days. When a filing obligation is determined after closing, either by the party or the Commission, a party will then file and be subject to a 30-day HSR Act waiting period. We understand the policy of the Commission is not to grant early termination to remedial filings, so the minimum civil penalty exposure to a missed HSR filing is $1.3 million.

subsequent acquisition. We include additional examples of the problems created by redefinition of "person" to include associates in Appendix A.

Accordingly, the proposal to redefine "person" by reference to associates should be deleted from the final rule.

e. Defining "Person" Beyond Individual UPEs Is Overly Burdensome

The term "person" appears throughout the HSR Act and Rules. Redefining "person" to include other funds or entities other than a single UPE would impact not only aggregation of shareholdings and information required on the HSR Form, but also many other aspects of premerger notification. At its most basic, the HSR Act provides thresholds for certain transactions involving acquiring persons who will hold "an aggregate total amount of the voting securities and assets of the acquired person."[14] The revised definition of "person" would presumably apply to an "acquired person" as well, making the determination of an acquiring person's aggregate holdings across an issuer and all issuers controlled by its associates overwhelmingly challenging, if not impossible, to determine.

Including more than a single UPE in the definition of "person" would dramatically increase the number of HSR filings by many investment funds. Beyond the practical problems with identifying the scope of the acquiring person as discussed above, the requirement to survey the holdings of multiple funds with disparate investing strategies and provide separate financial reports, revenues, lists of controlled entities, and other detailed information for each will raise compliance costs for funds significantly. In contrast to the simplified private equity and master limited partnership structures in the hypotheticals included in the NPRM, large investment funds typically encompass significantly greater numbers of investing funds of much broader complexity, with structures that shift over time, making gathering and reporting such information overwhelmingly challenging.

The SEC aggregates shareholdings across common managers when a filing is required because SEC filings provide public disclosure of significant shareholdings by an investor in an issuer. Filings made to the SEC are simple lists that can be prepared automatically using computer programs that download data. Further, Form 13D and 13G SEC filings provide after the fact notice of an acquisition. HSR filings, by contrast, require the submission of extensive data and documents, and are intended to allow the Agencies to review proposed acquisitions in issuers in advance of such transactions for potential competitive harm. Due to the waiting period and the perceived significance of a competitive review of a proposed transaction, HSR filings impose a much greater burden on investors and can have much more significant distortive effects on markets. Greatly expanding the scope of proposed transactions that would require HSR filings to include proposed acquisitions in which competitive harm is extremely unlikely will not offer nearly enough benefits to offset these large costs.

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[14] 15 U.S.C. § 18a(a)(2).

For all of these reasons as well as additional reasons set out in Parts III and IV below pertaining to the proposed *de minimis* exemption, the increased burden and complexity of preparing an HSR filing for such funds outweighs any potential benefit to the Agencies from greater insight into investments that are mostly minority shareholdings and very unlikely to impact competition negatively. The burden of the increase in filings would fall on both the filing parties and the Agencies alike, as well as potentially result in significant distortions in the markets. Examining hundreds or thousands of additional filings each year from investment management funds for what are mostly minority shareholdings will not further the Agencies' goal of using resources effectively to protect competition.

f. Alternate Methods Could Be Used to Obtain the Information Provided

In the NPRM,[15] the Commission requests additional information about how index funds and exchange-traded funds might be exempted from the requirement to aggregate, implicitly acknowledging that aggregation may be an overly blunt instrument for certain types of investors.

While it may be challenging to draw bright lines between these types of investing funds and private equity funds, the conclusion does not necessarily follow that the best solution is to require reporting by all investment funds on an aggregated basis. Given the potential for massive over-reporting by investment management firms that could result from aggregation and the accompanying burdens on investors, issuers, and the Agencies, it is necessary to think creatively about solutions that could enable such firms to continue with their investments without crippling regulatory burdens, and enable the Agencies to obtain the information needed in other ways. The Rules already exempt many classes of acquisitions from notification requirements under the Act where the cost of compliance is high and the potential benefit to the Agencies is relatively small because of the low likelihood of potential for competitive harm, such as transactions below a certain size and acquisitions of certain types of assets such as real estate. Minority acquisitions by investment management firms are the sort of transactions for which special exemptions make sense.

For example, if the Agencies seek more information about share ownership across associates when competitive harm is unlikely and has not been found in the past, they could require that investors provide a notice filing that is purely a disclosure of beneficial ownership by a shareholder and its associates without requiring that an acquisition be delayed until the termination of a review period.

Alternately, SEC filings provide a wealth of information about shareholdings in public companies by investment management firms. The Agencies could consider an exemption from filing requirements under the HSR Act for any such firms that make SEC filings for beneficial ownership of voting securities up to a certain threshold, perhaps of up to 15%. HSR Rule 802.64

[15] 85 Fed. Reg. 77053, 77058 (Dec. 1, 2020).

currently permits the acquisition of holdings in an issuer of up to 15% by certain institutional investors, reflecting a policy judgment that 15% shareholdings by certain types of investors are very unlikely to cause competitive harm. The Rules provide many exemptions from filing requirements when the burden of filing far outweighs the risk of competitive harm by the type of transaction exempted. MFA respectfully submits that acquisitions of voting securities of 15% or less by investment management firms are precisely the type of transaction that should benefit from such an exemption. Given that the acquisition is of a minority stake, if an anticompetitive situation arose as a result of such a shareholding, divestiture could be ordered.

Finally, if no clear exemptions can be found that would apply to investment management firms, we urge the Agencies to take the time necessary to devise alternative ways to obtain the information sought rather than enact the proposed aggregation rule now when it will impose large costs and practically unworkable processes on investment management firms without a countervailing benefit sufficient to justify the burden.

g. Concluding Remarks on Aggregation

Although the investment landscape has experienced many changes since the inception of the premerger notification program, the purpose and structure of investment management funds have largely remained the same. Today, as in 1978, the primary purpose of such funds is to increase returns to clients, not to participate in the day-to-day operations of the issuers whose shares they hold. Holdings by such funds have historically not posed a threat to competition, and that fact remains true. The primary changes related to investment management funds has not been to the structure or purpose of such funds, but rather the increased participation in such funds by investors at large. As such, applying the proposed definition of "person," largely designed for private equity funds and master limited partnerships, is not only unjustified, but will also be quite harmful.

III. Reasons for Support of a *De Minimis* Exemption

Investment managers invest more than $3 trillion through private investment funds on behalf of sophisticated institutional investors, much of which comes from pension plans, university, and other nonprofit endowments. Institutional investors have recognized the value of diversification and have increased allocation to alternative investment management funds. Requiring notification under the HSR Act for *de minimis* acquisitions of shares by such funds imposes tremendous burdens and costs on the funds and their investors. The proposed exemption would decrease unnecessary filings, and reduce burden to the Agencies and investors. It would also permit the kinds of communications widely recognized as serving broader social aims, such as when an investor advocates for specific diverse candidates for board director positions in furtherance of ESG goals.

We express our broad support for the proposed *de minimis* exemption in the NPRM. A *de minimis* exemption for acquisitions of up to 10% of an issuer that does not rely on investor intent

would significantly reduce burdens on investors, issuers, and the Agencies; serve important public policy aims; and exempt from review those transactions least likely to harm competition.

a. *De Minimis* Acquisitions Pose No Potential Harm to Competition

The Commission "has long contemplated the exemption of acquisitions of 10% or less of the voting securities of an issuer,"[16] including a blanket exemption for all acquisitions of 10% or less of an issuer's voting securities, "regardless of the intent of the acquired person."[17] Indeed, MFA and others have long argued that the Rules impose overly broad filing requirements for investments of 10% or less of the voting securities of an issuer, as such investments do not threaten competition.[18] The Commission clearly agrees, stating that "[i]n the Agencies' experience, these filings almost never present competition concerns."[19]

The past decade and a half has clearly put any lingering empirical debate to rest given that, as the NPRM crucially notes, from FY 2001 to FY 2017 "the Agencies did not challenge any acquisitions involving a stake of 10% or less."[20] Premerger filing data shows both that the Agencies did not challenge any acquisitions of 10% or less of an issuer's voting securities from 1981 to 1986, and that from October 1986 to January 2001 acquisitions of 15% or less of an issuer's voting securities did not, except under extremely limited circumstances,[21] raise competitive concerns.

Past FTC Commissioners have acknowledged that these *de minimis* acquisitions do not pose harm to competition. In the *Third Point* matter, the dissenting Commissioners stated that substantive antitrust concerns are "highly unlikely" to arise under Section 7 of the Clayton Act from acquisitions of 10% or less of an issuer's voting securities.[22] The majority statement did not dispute that conclusion, and explicitly recognized "Congress's considered judgment that '*de minimis* non-control' stock acquisitions may be safely excepted from the notification requirements."[23]

The existing § 802.9 exemption, which does not require filings for shareholdings of 10% or less when the investor holds the shares solely for the purpose of investment, is of course consistent with the lack of competitive concern associated with these acquisitions. The proposed

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[16] *Id*. at 77058.
[17] 53 Fed. Reg. 36831, 36840 (Sept. 22, 1988).
[18] *See, e.g.*, Letter from MFA to Donald S. Clark, Regarding Competition and Consumer Protection in the 21st Century Hearings, Project Number P181201—Investment Community Request for HSR Reform (Aug. 13, 2018).
[19] 85 Fed. Reg. 77053, 77055 (Dec. 1, 2020).
[20] 85 Fed. Reg. 77053, 77055 n.1 (Dec. 1, 2020).
[21] In three out of four cases, a larger transaction was also challenged. *See* Bilal Sayyed, *A "Sound Basis" Exists for Revising the HSR Act's Investment-Only Exemption*, 12(4) ANTITRUST SOURCE 1, 10, 13, 14 at n.75 (Apr. 2013).
[22] Dissenting Statement of Commissioners Maureen K. Ohlhausen and Joshua D. Wright at 3, *In the Matter of Third Point*, FTC No. 121-0019 (Aug. 24, 2015).
[23] Statement of the Federal Trade Commission at 2-3, *In the Matter of Third Point*, FTC No. 121-0019 (Aug. 24, 2015).

§ 802.15 exemption, however, better coheres not only with a much larger and long-standing trend to craft antitrust rules that eschew consideration of firm intent, but also with the purpose of the HSR Act—to facilitate enforcement of Section 7 of the Clayton Act and to prohibit only transactions that may result in a substantial lessening of competition.[24]

For these reasons, the proposed § 802.15 exemption for shareholdings of 10% is a welcome reprieve from the burdens and costs associated with making HSR filings for such *de minimis* holdings.

b. Asset Managers Have Significantly Increased Engagement with Companies Since Promulgation of the Rules, Serving Public Policy Goals

The level of shareholder engagement with issuers has expanded significantly since promulgation of the Rules. The former Chairman of the SEC, Jay Clayton, noted the "dramatic increase in the number of U.S. companies reporting shareholder engagement, with 72% of S&P 500 companies reporting engagement with shareholders in 2017, compared to just 6% in 2010."[25] MFA believes without question that if shareholder engagement was measured between 1978, when the Rules were initially promulgated, and today, the increase would be even more dramatic.

Shareholder communication with issuers now covers multiple activities not inconsistent with an investment purpose as stated in the 1978 Statement of Basis and Purpose ("SBP").[26] The Commission itself acknowledges in the NPRM that "a great deal of potential shareholder engagement involves more than merely holding (and potentially selling) stock, but does not encompass what the 1978 SBP discusses."[27] Indeed, clients today expect that asset managers will regularly monitor their investments and engage with company management on business decisions like executive pay and other corporate governance issues. This type of stewardship reflects ordinary-course shareholder engagement, and is a key part of providing services to fund clients that drive value and increase returns.

Engagement with issuer management also serves important public policy goals like corporate accountability. For example, the so-called "say-on-pay" vote has resulted in corporate boards soliciting with greater frequency the views of institutional investors on executive

[24] 15 U.S.C. § 18.
[25] Chairman Jay Clayton, *Statement Announcing SEC Staff Roundtable on the Proxy Process*, SEC. & EXCH. COMM'N (July 30, 2018) (citation omitted).
[26] The acts specifically enumerated in the SBP as being "evidence of an intent inconsistent with an investment purpose" include (but are not limited to): "(1) Nominating a candidate for the board of directors of the Issuer; (2) proposing corporate action requiring shareholder approval; (3) soliciting proxies; (4) having a controlling shareholder, director, officer or employee simultaneously serving as an officer or director of the Issuer; (5) being a competitor of the Issuer; or (6) doing any of the foregoing with respect to any entity directly or indirectly controlling the Issuer. The facts and circumstances of each case will be evaluated whenever any of these actions have been taken by a person claiming that voting securities are held or acquired solely for the purpose of investment and thus not subject to the act's requirements." 43 Fed. Reg. 33450, 33465 (July 31, 1978).
[27] 85 Fed. Reg. 77053, 77059 (Dec. 1, 2020) (citation omitted).

compensation plans. Many companies have responded to the increased desire of shareholders for engagement by offering more shareholder meetings and conference calls, as well as providing more detailed disclosures.[28] Business leaders have also called for broader communication of a board's decision-making to shareholders, as well as active engagement from asset managers to represent the interests of their clients and understand company perspectives.[29] SEC commissioners,[30] the business community,[31] and empirical studies[32] all support enhancing shareholder engagement as critical for investor protection.

Importantly, investment management firms do not communicate with management to participate in the basic business decisions of the issuer, nor to attempt to exercise control over the issuer's decisions. Rather, their primary purpose is to ensure that the company is run responsibly to deliver maximum value to shareholders. Such stewardship and oversight by fund managers serves all clients who invest in such funds—namely, the majority of workers and retirees today as well as other shareholders of companies, who benefit from increased transparency when companies respond to communications with investment management firms.

As presently construed, § 802.9 is arguably too narrow to permit a large portion of ordinary-course shareholder communication with management that benefits both investors and issuers, and thus deprives shareholders of reliance upon the investment-purpose-only exemption.[33] Recent enforcement actions in *Third Point*[34] and *Value Act*,[35] along with statements by agency officials, have created uncertainty about the line between good shareholder stewardship and actions incompatible with an investment-only intent. As the Commission recognizes in the NPRM,

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[28] *See* James Kim & Jason D. Schloetzer, *Global Trends in Board-Shareholder Engagement*, THE CONFERENCE BOARD (Oct. 2013) (finding that companies including Coca Cola, Pfizer, Allstate, Johnson & Johnson and Prudential Financial have been increasing shareholder engagement by increasing shareholder meetings, conference calls, letters, disclosures, and other means of interacting with shareholders). [consider a more recent citation]

[29] *See* "Commonsense Principles of Corporate Governance" (July 2016) §§ II.a, VIII.a, https://www.governanceprinciples.org/wp-content/uploads/2018/10/CommonsensePrinciples2.0.pdf.

[30] *See, e.g.*, Statement by Daniel M. Gallagher, former SEC Commissioner, Activism, Short-Termism, and the SEC: Remarks at the 21st Annual Stanford Directors' College (June 23, 2015) ("If companies are republics, then management and even at times boards need to engage with shareholders with the same vigor that politicians engage with their constituents. Clearly communicating your company's strategy and how the board is overseeing management's execution of that strategy to investors, and in turn hearing what's on your investors' minds, can help demonstrate to the SEC that boards are a tool for investor protection, not an impediment to it.").

[31] *See, e.g.*, BUSINESS ROUNDTABLE, STATEMENT ON THE PURPOSE OF A CORPORATION (Aug. 19, 2019) (committing to "[g]enerating long-term value for shareholders, who provide the capital that allows companies to invest to invest grow and innovate. We are committed to transparency and effective engagement with shareholders").

[32] *See, e.g.*, Matthew R. Denes, Jonathan M. Karpoff, & Victoria B. McWilliams, *Thirty Years of Shareholder Activism: A Survey of Empirical Research*, 44 J. CORP. FIN. 404, 417 (June 2017) (concluding that "activism that adopts some of the investment-intensive aspects of corporate takeovers, such as hedge fund activism, is associated with improvements in target firms' values and operations").

[33] *See* Debbie Feinstein, Ken Libby & Jennifer Lee, "*Investment-only" means just that*, F.T.C. BLOG (Aug. 24, 2015) ("*[A]ny investor who is considering engaging with management . . . should proceed with caution* when relying on the investment-only exemption.") (emphasis added), https://www.ftc.gov/news-events/blogs/competition-matters/2015/08/investment-only-means-just.

[34] *See generally* U.S. v. Third Point Offshore Fund, Ltd. *et al.*, Docket No. 1:15-cv-01366-KBJ (Dec. 18, 2015).

[35] *See generally* U.S. v. VA Partners I, LLC, *et al.*, Docket No. 3:16-cv-01672-WHA (Nov. 1, 2016).

"even the simplest of topics can present subtleties that complicate whether § 802.9 might exempt an acquisition of 10% or less of an issuer's voting securities."[36] And the stakes are high: the penalty for inadvertently violating the HSR Act and Rules by improperly relying on the exemption contained in § 802.9 currently is a fine of $43,280/day for each day the investor is not in compliance. As a result, investors must choose either to forgo beneficial shareholder-issuer communications or to make unnecessary HSR notifications with the resultant costs.

In addition, the current ambiguity around the type of shareholder engagement considered consistent with § 802.9 serves to chill shareholder ESG engagement with issuers. For example, in *Third Point*, the Commission prohibited behavior it saw as inconsistent with § 802.9, including inquiring of third parties their interest in serving on the board of an issuer or communicating with the issuer regarding a person it believes is worthy of advancement to the issuer's board.[37] When such communication is not related to an investor seeking to change the basic business decisions of the issuer, but to help the issuer add diversity to its board, the HSR Act should not stand as an impediment.

The creation of a *de minimis* exemption for shareholdings of 10% or less would remove this uncertainty, eliminate unnecessary compliance costs, and permit shareholders to be better stewards of their investments.

c. The Proposed Exemption Reduces Costs for Institutional Investors and Their Clients

MFA members manage the assets of a broad range of institutional investors, such as pension funds, charitable foundations, and university endowments. MFA members seek to further their clients' goals of providing retirement security for workers, income for retirees, and increasing resources for charities, foundations, and endowments. The requirement to make *pro forma* (from an antitrust perspective) HSR filings for small shareholdings can increase, sometimes significantly, the costs of investing for institutional investors, which ultimately reduces investment returns to these investors and their beneficiaries.

These costs occur in multiple ways. First, share prices for a target issuer may rise during the HSR waiting period (either 15 or 30 days after filing). Further, if the investment management firm opts to request early termination of the waiting period under the HSR Act and the request is granted, the fact that it has filed a premerger notification will become publicly announced, which can result in other investors attempting to take advantage of the firm's intended trading strategy, thereby driving up the cost of acquiring the shares, or misinterpretation of the reason for the filing. Importantly, the issuer may incorrectly believe that an HSR filing indicates that the firm intends to take a hostilely activist approach toward the issuer, potentially causing management to become less willing to communicate with the firm that has made an HSR filing. Finally, the fees associated

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[36] 85 Fed. Reg. 77053, 77059 (Dec. 1, 2020).
[37] Final Judgment at IV (G) and (H), *In the Matter of Third Point*, FTC No. 121-0019 (Aug. 24, 2015), https://www.ftc.gov/system/files/documents/cases/151218thirdpointjudgment.pdf.

with notifying a transaction under the HSR Act are not trivial, and include attorney fees as well as filing fees ranging from $45,000 to $280,000 per filing. The clients of the investment management firms bear these additional expenses, which reduce clients' overall investment returns.

d. The Proposed Exemption Increases the Efficiency of Public Markets

Major investors, such as the alternative investment funds that comprise MFA's membership, move in and out of positions in issuers regularly. This is especially so for funds tied to a particular stock index (for example, the S&P 500), in which the rebalancing of a fund's holdings to mirror the index happens frequently. The requirement for such funds to prepare an HSR filing and observe the waiting period for these frequent and small adjustments affects the liquidity of the issuer's stock during the HSR waiting period by depressing demand artificially during that period. The delay also affects the fund's ability accurately and timely to mirror the index in question, which can harm fund performance.

Finally, and crucially, requiring HSR filings for 10% or less of an issuer's shares can send erroneous signals that the investor is activist or may turn hostile. These false signals increase the amount of "noise" in the market, and depress market accuracy and efficiency. The proposed *de minimis* exemption would permit a safe harbor for investments by such funds, greatly increasing the efficiency of the funds themselves as well as the markets for public companies.

e. The Proposed Exemption Frees Scarce Agency Resources

The Commission notes in the NPRM that, to use their resources as effectively as possible, the Agencies "have a strong interest . . . in eliminating filings for categories of acquisitions that are unlikely to create competitive concerns."[38] The Commission cites filings for acquisitions of 10% or less of an issuer as one of two categories of filings that "make it difficult for the Agencies to focus their resources effectively."[39] With the proposed addition of aggregation of funds under common management, the number of HSR filings not presenting substantive issues could increase significantly. The proposed *de minimis* exemption will help the Agencies focus their limited resources on reviewing the transactions most likely to harm competition.

IV. Suggested Changes to the *De Minimis* Exemption

From the NPRM and the two Q&A calls hosted by Commission staff regarding the proposed changes to the HSR Rules, it is clear that the Agencies desire feedback regarding all aspects of the proposed changes. MFA appreciates the Commission's openness on the form of the proposed *de minimis* exemption, and proposes the following changes.

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[38] 85 Fed. Reg. 77053, 77058 (Dec. 1, 2020).
[39] *Id*. at 77055.

a. The "Common Ownership Exception" Lacks Evidentiary Support and a Solid Policy Foundation; Its Goals Can Be Obtained by Other Means

When a common owner has minority stakes in competing firms, the empirical evidence provides no substantial basis that competitive concerns could exist to support a common ownership exception to the FTC's admirable effort toward minimizing the costs imposed on parties engaging in *de minimis* acquisitions. Thus, the common ownership exception to the proposed *de minimis* rule should be struck.

Antitrust rules exist to protect competition and consumer welfare as informed by the best economic learning. While some analysis has shown the potential for antitrust concerns from "common ownership," these studies have generated significant controversy and many experts do not believe they reflect actual market realities. Without a sound empirical foundation, crafting legal rules to address merely theoretical concerns could harm, rather than help, consumers in the real world. The history of the antitrust laws, especially with mergers, makes this abundantly clear: most economists once believed that mergers increasing market concentration to levels today regarded as non-problematic would harm competition. A troubling, anti-consumer enforcement program followed,[40] ultimately rejected by empirical work that gave rise to the modern consumer welfare standard.[41]

This history is instructive when considering the Agencies' decision to exclude from an otherwise laudable proposed *de minimis* exemption transactions in which the acquirer also holds more than 1% of any competitor of the issuer.[42] Although economists have long recognized that partial acquisitions of a competitor not made solely for investment can be anticompetitive, even without a controlling financial interest,[43] from FY 2001 to FY 2017, the antitrust agencies received 1,804 filings for acquisitions of less than a 10% financial interest and did not challenge *any* as anticompetitive.[44] The implication of this result is clear: in practice, the antitrust agencies do not think that *de minimis* partial acquisitions of this kind pose antitrust concerns. In fact, antitrust enforcement during the years in which those statistics were compiled reflects a long-standing, aggressive approach to challenging potentially anticompetitive mergers and acquisitions, codified in the Obama Administration's 2010 Merger Guidelines,[45] including challenging partial acquisitions deemed anticompetitive.[46]

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[40] *See, e.g.*, United States v. Von's Grocery Co., 384 U.S. 270 (1966).
[41] *See, e.g.*, Harold Demsetz, *Two Systems of Belief about Monopoly*, *in* INDUS. CONCENTRATION, THE NEW LEARNING 167 (Harvey J. Goldschmid et al. eds, 1974).
[42] 85 Fed. Reg. 77053, 77061 (Dec. 1 2020).
[43] *See, e.g.*, Steven C. Salop & Daniel P. O'Brien, *Competitive Effects of Partial Ownership: Financial Interest and Corporate Control*, 67 ANTITRUST L.J. 559 (2000).
[44] 85 Fed. Reg. 77053, 77055 n.1 (Dec. 1, 2020).
[45] U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 13 (2010).
[46] *See, e.g.*, United States v. Dairy Farmers of America, 426 F.3d 850 (6th Cir. 2005) (finding 50% non-controlling interest could be unlawful); *In re* TC Group, L.L.C., No. 061-0197 (Jan. 25, 2007) (Decision and Order) (requiring remedies for acquisition of 22.6% non-controlling interest).

The view that there is no substantial basis for concluding that common ownership facilitates competitive harm is not merely the view of one cadre of commentators who have contributed to the economic literature. Just a little over three years ago, the Organization for Economic Cooperation and Development held a hearing on common ownership, inviting the United States to comment. The FTC and DOJ reviewed the economic literature and related policy proposals, with unequivocal findings:

> Given the ongoing academic research and debate, and its early stage of development, the U.S. antitrust agencies *are not prepared at this time to make any changes* to their policies or practices with respect to common ownership by institutional investors.[47]

In the short time since this submission, nothing has changed to justify the Agencies to reverse their conclusion. Although the literature remains inconclusive,[48] the Agencies now propose to use it for exactly the purpose they claimed in November 2017 it would not support, namely, as justification for an important new policy.

Tellingly, one reason that there is no consensus in the empirical literature regarding the competitive effects of common ownership is that neither proponents nor opponents have been able to document a mechanism by which minority owners could exercise sufficient control to cause anticompetitive effects.[49] This knowledge gap, of course, is crucial for antitrust law: any increases in concentration that are found to be associated with common ownership could have efficiency explanations. Moreover, commentators have continued to emphasize how possible mechanisms of control identified by theorists may not represent rational conduct.[50] Perhaps most important, the purpose of the Rules is to empower the Agencies to challenge mergers—the extreme case of common ownership—without having to "unscramble the eggs." But this concern is inapposite to *de minimis* partial acquisitions by non-competitors, where the firms remain separate, making both Sherman Act § 1 and FTC Act § 5 more than sufficient to police concerted and unilateral collusive conduct.

The burden is on those proposing a common ownership exception to the FTC's 10% exemption to the HSR Act for non-competitive acquisitions to establish its appropriateness, and those proponents have failed resoundingly in light of the purpose of the Rules and the lack of a robust understanding of how minority owners exercise control to harm competition. Unless or

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[47] DEP'T OF JUSTICE & FED. TRADE COMM'N, COMMON OWNERSHIP BY INSTITUTIONAL INVESTORS AND ITS IMPACT ON COMPETITION (Nov. 2017) (emphasis added).

[48] *Compare* Lysle Boller & Fiona Scott Morton, *Testing the Theory of Common Stock Ownership*, NBER Working Paper No. 27515 (2020) (finding that common ownership may be associated with anticompetitive effects), *with* Andrew Koch, Marios A. Panayides & Shawn Thomas, *Common Ownership and Competition in Product Markets*, __ J. FINANCIAL ECON. __ (2020) (challenging the link between common ownership and anticompetitive effects).

[49] *See, e.g.*, Boller & Scott Morton, *supra* note X, at 58.

[50] *See* C. Scott Hemphill & Marcel Kahan, *The Strategies of Anticompetitive Common Ownership*, 129 YALE L.J. 1392, 1400 (2018) ("Our main conclusion is that, for most mechanisms, there is either no strong theoretical basis for believing that institutional [common owners] could or would want to employ them, no significant evidence suggesting that they do employ them, or both.").

until that burden is met, implementing regulations grounded in rejected policies and unsupported theories would be arbitrary and capricious.

MFA respectfully recommends that the Commission eliminate the 1% common ownership exception to the proposed *de minimis* exemption.

b. There Is No Empirical Basis for a 1% Threshold, and It Would Result in More Harm Than Good

If the problem is the example we have occasionally heard—a common owner investing up to 10% in multiple competing firms—the solution should be narrowly tailored to this specific concern. But instead the proposed rule goes much further, and requires filings by a common owner who owns up to 10% of one firm but only 1% or more of a competitor. Relative to a comprehensive 10% threshold, such a rule would considerably increase the filings required under the HSR Act, and therefore the costs borne by the investment and business communities. Moreover, the implication of the FTC's inclusion of a 1% threshold would, of course, appear to be that *de minimis* overlaps are viewed as inherently raising potential competitive concerns by giving investors the ability to exercise control through even the most minute minority holdings—rather than, as in the scenario noted above, a nearly 10% stake in competitors. Indeed, the latter much more closely accords with what some commentators have suggested as a safe harbor for minority investments, and therefore what could be properly exempted from HSR filing requirements.[51]

Here again, proponents of such an exception have not carried their burden. A 1% threshold represented what Commissioner Noah Phillips identified as one of the more "dramatic"[52] policy proposals from commentators, preventing a common owner from holding more than 1% in two or more competing firms in oligopoly markets.[53] The purported rationale for this test draws upon previous concentration measures developed in the partial-ownership literature for determining anticompetitive effects, and sees as its marginal case a hypothetical world where five large institutional investors all own 1% of each of four equally sized firms making up an oligopoly industry. Yet, if this is the policy concern underlying the rule, the effect is vastly overbroad, as the rule would require filings by all investors, large and small, when they have *any* overlaps of competing firms with a stake of 1% or more no matter how many firms exist in the relevant industry. A view that anticompetitive effects from common ownership become more plausible at this 1% threshold lacks empirical support, and instead is an arbitrary line that some commentators believe would make antitrust enforcement against common ownership more administrable—thus putting the remedial cart entirely before what remains an anticompetitive unicorn.

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[51] *See, e.g.*, Edward B. Rock & Daniel L. Rubinfeld, *Defusing the Antitrust Threat to Institutional Investor Involvement in Corporate Governance*, NYU Law and Economics Research Paper No. 17-05, at 29 (Mar. 1, 2017) (proposing a 15% safe harbor).
[52] *See* Noah J. Phillips, Comm'r, Fed. Trade Comm'n, Taking Stock: Assessing Common Ownership, Remarks before the Concurrences Review and NYU Stern Global Antitrust Economics Conference, at 2 (June 1, 2018).
[53] *See* Eric A. Posner, Fiona Scott Morton, & E. Glen Weyl, *A Proposal to Limit the Anticompetitive Power of Institutional Investors*, 81 ANTITRUST L.J. 669 (2017).

c. The 1% Threshold Creates Numerous Practical and Costly Problems

Given the significant increase in investments by the general public in managed funds since the promulgation of the Rules, the aggregate holdings of funds under management in any given issuer can easily reach a level of 1%. Setting the common ownership exception at this low level would thus effectively place the proposed exemption out of reach of many large institutional investors and managed funds—swallowing, as it were, the broader exemption and again leaving investors with a regime that, on the one hand, chills beneficial shareholder engagement or, on the other, imposes administrative burdens in no way commensurate with the likelihood of competitive harm.

Investing broadly across major companies, including in companies that compete with each other, is a method commonly used by large fund managers to reduce risk through diversification, which remains crucial toward safeguarding investor returns. The 1% threshold exception, particularly when combined with aggregation, will thus raise the costs for firms to diversify, and incentivize managers toward sub-optimal portfolios. In addition, more diversified investors would be at a disadvantage to those less diversified, harming clients of the more diversified funds.

Frequent rebalancing of portfolios by such investors, as a way to track indexes that the investment funds are designed to mirror or for other reasons, means that filings will need to be made with much greater frequency as holdings fluctuate around a 1% threshold, raising costs and burdens for investors and issuers alike. Moreover, many of MFA's members have concerns about the feasibility and burden of creating tracking systems to monitor shareholdings of less than 1% across thousands of issuers and multiple funds based on whether those issuers could be deemed "competitors" of one another according to the broad definition proposed. At a minimum, the time spent tracking this information would mean that fund administration costs would be raised significantly, reducing returns to investors. In addition, small incremental changes to rebalance or diversify fund holdings would require a new HSR waiting period, in practice greatly increasing the difficulty of large fund managers in managing portfolio risk through diversification or hedging. It is more likely that these fund managers would instead forgo communications with issuers rather than bear the burdens and opportunity costs associated with making frequent filings. Further, if the proposed aggregation rules were to be adopted, information necessary to determine whether the 1% threshold is exceeded by a "person"[54] that includes multiple ultimate parent entities, or an ultimate parent entity that is a part of multiple persons, may not be determinable.

Although we do not believe that a common ownership exception is necessary, if one is to be included in the final rule, a threshold of 10% would be more appropriate. There is no rationale for asymmetry between the levels of holdings—if a holding of 10% or less does not confer sufficient control to be of concern, as the proposed rule assumes and history demonstrates, there is no justification for a 1% threshold for a holding in a competitor. Setting the *de minimis*

[54] 16 C.F.R. § 801.1(a)(1) "Except as provided in paragraphs (a) and (b) of §801.12, the term person means an ultimate parent entity and all entities which it controls directly or indirectly."

exemption at 10% while having a 1% cap on investments in a competitor also creates logical inconsistencies. If Fund X holds 2% of Company A and 0.75% of Company B, which are considered "competitors," the holding in Company A is eligible for the *de minimis* exemption for shareholdings up to 10%, but the holding in Company B is not, given the 2% shareholding in Company A and the common ownership exception of 1%. Thus, in practice, investors must choose one investment only to qualify for the exemption, and keep investments in all competing firms below 1%.

If the Commission will not raise the amount of the common ownership exception to 10%, the threshold should, at a minimum, be raised to 5%. This percentage tracks a reporting threshold from the SEC, and reflects data that large fund investors already track.[55] If an anticompetitive situation were to arise from common ownership, which we view as highly unlikely, divestiture or other remedies could be ordered for the minority stake held. And to the extent that impermissible agreements between parties or other anticompetitive actions arise involving common ownership, Sherman Act § 1 and FTC Act § 5 provide a remedy.

Thus, in the alternative, MFA recommends that the Commission raise the common ownership exception to 10%, or, at a minimum, 5%.

d. The Definition of "Competitor" as Proposed Is Unworkable

Finally, the proposed definition of "competitor," defined to include both a six-digit NAICS code-based overlap and the phrase "competes in any line of commerce," are both overly broad and extremely challenging to apply and track accurately. The ambiguity from the proposed "competitor" definition would cause unnecessary filings by investors, and/or a chilling effect on communications between institutional investors and issuer management. As we argue below, in contrast to all of the complexity, uncertainty, and implementation problems identified above with the proposed HSR definition of "competitor," the definition of "competitor" under Clayton Act § 8 is a long-used definition that would be understood by investors and issuers alike.

MFA disagrees with the assertion in the NPRM that six-digit NAICS codes are "objective and easy to administer"[56] in the context of minority investments in an issuer, given that the NAICS codes that an issuer uses are not publicly available and issuers are under no legal obligation to provide their NAICS codes to investors. Basing HSR filing obligations, and potential penalties of $1.3 million per month, even as part of an exemption, on information to which the acquiring person may not have access creates significant compliance risk that vitiates the exemption.

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[55] We note that the Commission staff have expressed resistance to use of SEC reporting criteria because they were not designed for antitrust enforcement. Nevertheless, we note that the use of information collected for purposes other than antitrust has not prevented the Commission from using NAICS codes developed by the Department of Commerce in Item 5 of the HSR Form.

[56] 85 Fed. Reg. 77053, 77061 (Dec. 1, 2020).

The difficulty in assessing another company's NAICS codes from the outside stems from two primary considerations:

(1) Issuers that are operating companies may use multiple NAICS codes, and larger diversified companies or conglomerates easily could use dozens of codes, making it more likely that the issuer reports under NAICS codes activities that are not material enough to be described in publicly available materials, such as annual reports or 10K filings with the SEC; and

(2) There are numerous common NAICS codes that companies frequently use across all industries that are unrelated to their core operations. Often these are administrative in nature, and an outsider may have no ability to determine whether they apply from publicly available information. Examples include:

NAICS	Description	Examples of Use
523910	Miscellaneous intermediation	Investment of excess cash held by the company not being used for operations
524128	Other direct insurance (except life, health, and medical) carriers	Companies that create a captive insurance business entity to obtain tax benefits
531120	Lessors of non-residential buildings (except miniwarehouses)	Companies that lease excess office space or other real estate they are not occupying

Thus, to an outsider, such as an investor planning to acquire less than 10% of an issuer's stock, even knowing all of the markets in which the issuer competes will not guarantee that the investor can determine all of the NAICS codes used by the issuer. The risk and consequences of missing just one of these codes, no matter how *de minimis* or competitively insignificant, when civil penalties accrue at a rate of $1.3 million per month, will certainly chill any reliance on the proposed exemption by investors.

In the November 9, 2020 virtual workshop, Commission staff said that its enforcement approach with respect to the proposed 10% exemption would not be "some sort of gotcha to trip people up who are acting in good faith."[57] Under the proposed exemption, however, many investors may not be willing to rely on a good faith estimate on an issuer's NAICS codes and the good graces of the Agencies if each investment subjects them to a minimum exposure of a $1.3 million per month civil penalty for HSR violations. There is also a risk that the Agencies may be tempted to bring HSR Act technical violation actions based on disqualifying NAICS codes in lieu

[57] Real time transcript from Federal Trade Commission virtual workshop on the Proposed Amendments to HSR Rules (Nov. 9, 2000).

of litigating more complex or defensible antitrust allegations on the merits when bringing cases, or using the prospect of multi-million dollar HSR Act fines on such good faith errors as a means of pressuring settlement on other claims. We believe the best way to avoid "gotcha" situations is to implement regulations that can be easily complied with by investors exercising good faith, and for which compliance can be determined using publicly available information.

Further, even if a less than 10% investor is able to guess accurately or obtain the cooperation of an issuer in which it plans to invest to correctly determine all of an issuer's NAICS codes, as well as all of the codes of the issuers in which it also invests 1% or more, which could number in the hundreds, these codes were not designed to identify antitrust markets or competitive overlaps, and are manifestly overbroad for this purpose. There are three primary reasons why NAICS codes are overbroad and should not be used to determine the identity of competitors:

(1) Manufacturing NAICS codes are broad categories at the six-digit level, which is why the agencies require 10-digit codes for manufactured items. Accordingly, 10-digit NAPCS codes are better suited to identifying manufacturing competitors. For example, the six-digit codes for pharmaceuticals illustrate the lack of alignment between NAICS codes and actual competitive overlap: code 325412, Pharmaceutical Preparation Manufacturing, includes prescription medications, over-the-counter medications, veterinary medications, cough drops, and vitamins, products that encompass hundreds of separate antitrust markets.

(2) As described above, some administrative activities common to businesses across all industries result in the reporting of NAICS code revenue by issuers. Accordingly, any 1% or greater investment in an issuer that invests excess cash (523910, Miscellaneous Intermediation), has a captive insurance subsidiary (524128, Other Direct Insurance Carriers), or leases temporarily vacant office or warehouse space (531120, Lessors of Non-residential Buildings) would effectively prevent the use of the exemption for investments in completely unrelated issuers that do not compete against each other.

(3) Some NAICS codes are based on the manner in which services are performed, and not the functions that the services provide or the customers that they serve. Examples that cover a large number of companies currently popular with investors include:

> Code 454111—Internet Retail Sales. This code covers everything that an issuer may sell over the internet, from meal kits to exercise equipment, even if the issuer's primary sales are brick and mortar. Particularly given the effects of COVID, almost all retailers now sell over the internet. As a practical matter, the use of NAICS codes means that no investor holding 1% of any retailer is likely to be able to use the exemption for any company that sells directly to consumers.

> Code 511210—Software Publishers. This code covers any software services no matter the function, market, or customer served. This code covers a broad swath of the economy,

including ride share companies, app developers, food delivery companies, video games, and business and educational software. As a practical matter, the use of NAICS codes means that no investor holding 1% of any software company is likely to be able to use the exemption for a vast number of issuers in a diverse portfolio.

Code 541711—Research and Development in Biotechnology. The code covers an industry that has attracted considerable investment over the past few years and encompasses a broad range of medical, animal, plant, and other product research and development. Biotech research is being done across a broad range of technologies, from developing COVID vaccines to plant-based meat substitutes. Given that some investment funds focus on this sector, the use of NAICS codes means that no fund focused on biotech is likely to be able to use the exemption, even if the issuers in which they invest are a diversified portfolio of companies that research different diseases and applications.

On the other hand, as the NPRM itself notes, NAICS codes can sometimes be too narrow for antitrust purposes, as "competitors sometimes use different NAICS codes to describe the same line of business."[58] A proxy that is both over- and under-inclusive is thus a poor vehicle for measuring actual competition between two entities. Further, if the definition of "competitor" also covers companies that actually compete in fact, then, as a matter of logic, the additional inclusion of overlapping NAICS codes adds to the definition of "competitor" only those "companies that share the same NAICS code and do not compete." We believe there is no justification for including companies that do not compete within the definition of "competitor."

The second prong of the test, "competes in any line of commerce," also lacks specificity. The phrasing is vague, and provides no safe harbor for any level of "competing" revenues, as Clayton Act § 8 does.[59] Also, in the November 9, 2020 FTC virtual workshop, FTC staff stated that the omission of a geographic requirement for competition is "intentional."[60] We wish to emphasize that competition within the same geographic location should be a requirement for inclusion in the definition of "competitor." An issuer that only owns a chain of restaurants in Maine cannot reasonably be considered a competitor to another issuer that operates only in California. Given that no 10% or less acquisitions have ever been challenged, it does not make sense to include as competitors issuers who are in the same industry but do not compete in the

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[58] *Id*. at 77056.

[59] 15 U.S.C. § 19. Section 8 of the Clayton Act prohibits an officer or director, or officers or directors from the same company, from serving on the boards of competing issuers. Competition is defined as operating businesses "so that the elimination of competition by agreement between them would constitute a violation of any of the antitrust laws." Notwithstanding that prohibition, the prohibition does not apply to companies if: "(A) the competitive sales of either corporation are less than $1,000,000, as adjusted pursuant to paragraph (5) of this subsection; (B) the competitive sales of either corporation are less than 2 per centum of that corporation's total sales; or (C) the competitive sales of each corporation are less than 4 per centum of that corporation's total sales."

[60] Real time transcript from Federal Trade Commission virtual workshop on the Proposed Amendments to HSR Rules (Nov. 9, 2000). To the extent that the Commission has a particular concern with hospitals or other particular industries in which geographic markets are "highly contested," such narrow concern would be better addressed by carving them out of a geographic requirement. We also note that none of the hospital mergers challenged by the Agencies have involved acquisitions of 10% or less of their voting securities by investors who do not control other hospitals.

same geographic areas. We believe that the use of the Clayton Act § 8 definition, which includes a location requirement, would avoid making the proposed definition of "competitor" overbroad.

MFA recommends that the Commission abandon any use of NAICS codes and the proposed "any line of commerce" test divorced from geography with respect to the proposed 10% exemption and adopt the Clayton Act § 8 definition of "competitor," including both its safe harbor for *de minimis* competition and the requirement that the competition must occur in the same geographic location.

e. The Vendor/Vendee Exception Does Not Make Sense, and the Amount ($10 million) Would Punish Large Institutional Investors

Finally, MFA believes the exception in proposed § 802.15 for a vendor/vendee relationship between the investor and the issuer of $10 million or more is not justified. MFA recommends eliminating this exception, as there is no clear evidence that a vendor/vendee relationship negatively impacts competition when one holds shares of the other. In fact, one would expect a vendee to have incentives for its vendor to provide more competitive pricing toward the vendee/investor. If the vendor/vendee exception to the exemption remains, MFA suggests raising the threshold to $75 million, as the currently proposed level could easily render the exemption unavailable for large investors/investment managers that engage in significant transactions with counterparties in the ordinary course of business. For example, if a large investor/investment manager has a prime brokerage account with a global financial institution through which it pays more than $10 million in fees, this exception would assume that the investor may be engaging in anti-competitive behavior if it then acquires a 1% position in the stock of another large financial institution. There is no basis for such an assumption. Further, the exception could inhibit investment in vendors, as large investors may simply choose not to invest in the types of entities with which they regularly do business, such as banks, health insurance companies, and accounting firms, rather than risk violating the proposed exemption.

Thus, MFA recommends eliminating the exception in proposed § 802.15 concerning vendor/vendee relationships.

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In sum, MFA respectfully submits that the goals of the proposed *de minimis* exemption would be frustrated given the market realities large investment management firms face if the rule is adopted as currently proposed. Some of the proposals rely on assumptions that lack foundation in law, economics, policy, or current business practice. We propose the following modifications to the proposed regulations:

802.15(b)(ii) Eliminate; in the alternative, change references to 1% to 10%

802.15(b)(v) Eliminate; in the alternative, change reference to $10 million to $75 million

801.1(r) Change entire provision to read "*Competitor*. For purposes of these rules, the term *competitor* means any person that would be in violation of 15 U.S.C. § 19 if it shared a common director or officer with the issuer."

V. Conclusion

For the reasons we describe, the proposal to redefine a person under the HSR Act to include associates is unworkable because there is often no one-to-one match of investments managers and funds/investors and because basing the composition of a filing person on a potentially multiple and changing mix of UPEs would upend the entire HSR framework. Further, expanding the definition of "person" to include associates is unnecessary and would create incredible burdens on investment management firms and their clients, distort markets, and cause a significant increase in HSR filings for many proposed investments that have been proven not to cause competitive harm, even when paired with the *de minimis* exemption. If the proposed definition of "person" is adopted, an exception for minority investments by investment management firms should be provided.

Importantly, a 10% *de minimis* exemption, with modifications as proposed, will eliminate unnecessary and over-inclusive HSR filings, foster desirable ordinary-course engagement between shareholders and management, and reduce costs and burdens on investors and the Agencies alike. Any exceptions to the *de minimis* exemption should provide for practical application by the industry, should be logically consistent, should be based on actual situations in which competitive harm could occur, and should not discriminate against large institutions based solely on their size. Thus, the 1% common ownership exception to the proposed exemption should be eliminated, or raised to 10%, or rather to 5%. The proposed definition of "competitor" should be eliminated as impractical to determine and unduly burdensome, and instead the Agencies should adopt the Clayton Act § 8 definition of "competitor" for this purpose, including its safe harbor for *de minimis* competition as well as the requirement that competition occur in the same geographic region.

Finally, as there is no basis for presuming that a vendor/vendee relationship should negate the use of the proposed exemption, this exception to the proposed rule should be eliminated or, at a minimum, raised to $75 million in order to not discriminate against large institutional investors.

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MFA appreciates the opportunity to provide these comments to the Commission in response to the proposed amendments to the HSR Rules. If you have any questions about these comments, or if we can provide additional information, please do not hesitate to contact the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Jennifer W. Han

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Appendix A – Examples to Illustrate the Unworkability of Redefining "Person" to Include Associates

To illustrate the unworkability of the proposed definition of "person" based on associate relationships, consider the following example:

1. Investment Manager A manages a fund of one for Private University and a fund of one for Company Pension Fund. The manager and the two funds investors are each their own ultimate parent entities, and associates of each other under the Rules. If the new definition of "person" is implemented, then Private University, Company Pension Fund, Investment Manager A, and each of their associates constitute "Person I." They hold the following voting securities of Issuer D:

    - Private University holds $10 million in the fund of one managed by Investment Manager A, and $15 million in a separate managed account with Investment Manager B, Fund Vehicle 1B.
    - Company Pension Fund holds $8 million in the managed account under Investment Manager A, and $5 million in a separate account managed by Investment Manager C.

    Person I holds $38 million of Issuer D.

2. Investment Manager B manages Fund Vehicle 1B, a managed account for Private University, and a managed account for the Narnia Sovereign Wealth Fund. Investment Manager 1B is controlled 50%-50% by two principals, Mr. Wise and Ms. Savvy. The manager, its principals, the fund, and Private University are each their own ultimate parent entities, and associates of each other under the rules. Narnia Sovereign Wealth Fund does not count as an associate because foreign countries are not Persons under HSR. If the new definition of "person" is implemented, then Private University, Fund Vehicle 1B, Investment Manager B, Mr. Wise, and Ms. Savvy are all associates and constitute "Person II." They hold the following voting securities of Issuer D:

    - Private University holds $10 million in the fund of one managed by Investment Manager A, and $20 million in a managed account with Investment Manager B.
    - Narnia Sovereign Wealth Fund holds $50 million (but does not count because foreign countries are not Persons under HSR).[61]
    - Fund Vehicle 1B holds $15 million.

[61] 16 C.F.R. 801.1(a)(2).

- Mr. Wise and Ms. Savvy, to show to their investors that they have "skin in the game," each personally co-invest their own money at 0.01% of the assets under management of Fund Vehicle 1A. Accordingly, each hold $150,000.

Person II holds $45.3 million of Issuer D.

3. Investment Manager C manages Fund Vehicle 1C, and a managed account for Company Pension Fund. The investment manager is controlled by Ms. Smith. The Investment Manager, Ms. Smith (including Mr. Smith, her spouse, and Grace, their minor child), Fund Vehicle 1C, and Company Pension Fund are each their own ultimate parent entities, and associates of each other under the rules. If the new definition of "person" is implemented, then Company Pension Fund, Fund Vehicle 1B, Ms. Smith, Mr. Smith, Grace, Investment Manager C, and each of their associates constitute "Person III."

- Company Pension Fund holds $8 million in managed account under Investment manager A, and $5 million with Investment Manager C.
- Fund Vehicle 1C holds $37 million
- Ms. Smith and her immediate family currently hold no shares.

Person III holds $50 million of Issuer D.

This fact pattern is used to illustrate some of the problems with the prosed definition of "person" including Associates:

Scenario 1. The identity of associates is not fixed, and because a person under the new definition will consist of multiple independent UPEs, advance coordination of their acquisitions will be exceedingly difficult.

- If Company Pension Fund wants to acquire $5 million more of Issuer D through a managed account with another fund manager, it will cause Person III to need to file under HSR, because Company Pension Fund is an associate included within Person III, and Person III would hold $55 million of Issuer D as a result of the transaction.

- If Company Pension Fund wants to acquire an additional $13 million of Issuer D two months later, Person I will need to file, and Person III does not need to file as it had previously filed to cross the $50 million size of transaction threshold.

Note that it is incumbent upon Company Pension Fund to, at a minimum, inform Investment Manager A, Investment Manager C, the fund managers of any accounts it hires them to manage,

including the manager of the new account making the acquisition about its current and planned holdings in Issuer D so that they can check with all associates within each person to determine their current and planned holdings in Issuer D. Indeed, all members of a Person will need to be in contact and report all of their holdings to each other on a continual real-time basis in order to properly monitor whether any new purchase risks putting a person to which they belong over the $50 million threshold.

So in this case, if Company Pension Fund does not provide information about these purchases of Issuer D to an entity within any person it is a member of by virtue of being an associate, then those persons may unknowingly violate the HSR Act and become subject to a $1.3 million per month penalty. (Intent is not a requirement for violation of HSR reporting obligations.)

If HSR civil penalty liability is joint and several, then Investment Manager A, Private University, Investment Manager C, Ms. Smith, Fund Vehicle 1C, and any other associates within Person I and Person III, whether or not they own shares in Issuer D, are each potentially subject to this $1.3 million penalty as persons in violation of the HSR Act. (Because "person" as redefined under the proposed rule is not a single legal entity, but a collection of legal entities that may change over time, presumably multi-UPE persons cannot be assessed an HSR civil penalty for failure to file—only legal entities can be made subject to civil penalties.)

Scenario 2. The new definition will have an effect on how exemptions are applied to UPEs and persons under the proposed definition, and how the one year and five year limits will apply.

Assume Scenario 1 has not occurred. Suppose Issuer D issues a new round of voting securities, and allows its existing shareholders to participate pro-rata in the new issuance. Under 15 U.S.C. §18a(c)(10), such acquisitions are exempt if the acquiring person's per centum share does not increase as a result of the acquisition. Within Person I, Private University participates and acquires pro rata shares, but Company Pension Fund does not. Within Person II, Private University, Fund Vehicle 1B, Ms. Savvy and Mr. Wise all purchase the pro rata shares. The value of the shares acquired by Private University are $6 million. The value of the pro rata shares acquired by Fund Vehicle 1B, Ms. Savvy, and Mr. Wise collectively add up to $3.1 million.

Question: Would the (c)(10) pro rata exemption apply to Person I and Person II collectively? Under the plain language of the HSR statute, the answer is yes because the exemption applies to a "person." In other words, if Company Pension Fund does not participate in the new pro rata distribution, fellow associate Private University may acquire the additional shares that Company Pension fund declines to acquire under the exemption, without filing under HSR, if the exemption collectively applies to all of the associates within Person I, as Person I would not increase its percentage held of Issuer D. However, if Private University does take the extra shares it is entitled to acquire under the exemption as a member of Person I, then that would cause Person II to acquire more voting securities of Issuer D than permitted under the exemption. In that case, all of the other Person II associates who only took their pro rata allocation (thinking they were exempt) would

need to be part of an HSR filing as Person II. This shows that the new rule can deny Fund Vehicle 1B, Ms. Savvy and Mr. Wise the pro rata exemption based solely on the behavior of parties they do not control.

Scenario 3. The New Definition will affect who has the right to acquire shares under the one year and five year HSR periods.

Assume Scenarios 1 and 2 have not occurred. Company Pension Fund decides it may want to acquire $61 million more of Issuer D. So Company Pension Fund has Person I, Person III, and 10 other persons (the Company Pension Fund has funds under management by 10 other fund managers, and therefore must file for all persons crossing an HSR reporting threshold, including each person that includes each of the other investment managers that manage Company Pension Fund funds, whether or not their other associates also hold shares in Issuer D) file under HSR to exceed the $100 million threshold and observes the waiting period.[62] A week after the HSR waiting period expires, Company Pension Fund acquires the $61 million of Issuer D shares. However, unbeknownst to Company, during the HSR waiting period, Private University sold all $30 million of shares in Issuer D out of its accounts managed by Investment Manager A and Investment Manager B. As a result, Person I crossed the $50 million threshold (holding $74 million in Issuer D), but not the $100 million threshold. However, Person III crossed the $100 million threshold (holding $111 million in Issuer D.) A year passes, and now Person I is permitted under the HSR rules to acquire more than $50 million, but not more than $100 million. Person III is allowed to acquire up to $500 million.

Two years later, Company Pension Fund buys another $120 million in Issuer D shares, believing it is entitled to acquire up to $500 million as an associate of Person I and Person III. But because Private University's sale caused the $100 million threshold not to be crossed for Person I, now Person I is in violation of the HSR Act, and all of its associates are subject to a $1.3 million per month civil penalty.

We note that in this example, Private University's sale of shares of Issuer D caused Person I's holdings to decrease. However, the same result would occur if Private University ceased being a member of Person I by liquidating its account and withdrawing its money from Investment Manager A and moving the proceeds to another manager. If Private University broke off all ties with Investment Manager A, it would no longer be an associate within Person I.

We are uncertain whether under the proposed definition of "person," where the membership of Person I was determined by a snapshot of its associates at a certain point of time and that associate mix later changes, Person I remains Person I if any of its associates depart or if new associates are added, and how that would be determined. If the existence of Person I has no continuity, an

[62] We note that since Company Pension Fund would now itself hold over $50 million in Issuer D, this will cause all Persons in which it is an associate to exceed the $50 million HSR filing threshold.

investment manager that gains and loses investors may need to re-file HSR for the same issuer prior to each purchase. Also, for such fluid associate compositions as would often be the case for investment managers, it is not clear under the proposed associate definition what happens if new associates are added or depart between the date an HSR filing is made and when the waiting period expires, let alone by the time the one year and five periods are reached.

The potential changing of membership over time of a person under the proposed definition of "person" as a collection of associates seems to put the Agencies on the horns of a dilemma, forcing them to either: (a) allow a person who has filed and observed the waiting period under the HSR Act to continue to acquire voting securities in an issuer regardless as to whether it adds or subtracts associates after a filing is made (assuming there is some way to determine what collection of entities are a successor to the person that previously filed), in which case the purpose of the aggregation rule, namely, to provide the Agencies with clearer information on related holdings of associates, falls apart; or (b) require a new HSR filing for every unique associate combination person, in which case thousands more filings will be required, potentially in advance of each and every proposed voting security purchase involving large fund managers.