

OCTOBER 2018

AUTHOR

MICHAEL A. FINIO
MATTHEW S. DRAPER
NICHOLAS C. STEWART

Federal Trade Commission Changes Course on Reportability Analysis for Not-for-Profit Combinations

Board Control is No Longer Dispositive, and FTC Clarifies Differences in Transaction Structures and Exemptions

SUMMARY

On October 26, 2018, the Federal Trade Commission's Premerger Notification Office (the "PNO") issued new guidance on the reportability analysis for transactions involving not-for-profit entities. This new "tip sheet" (a) warns filers against simply relying on basic "control" analysis (i.e., a determination of what person or entity controls a particular board of directors), (b) provides examples of typical not-for-profit transaction structures seen by the PNO, and (c) clarifies and reiterates the PNO's position on exemptions for these often utilized structures.

A. Control Analysis – Focus on Beneficial Ownership, Not Just Board Rights. In the past, PNO guidance on not-for-profit transaction reportability focused on whether a proposed transaction would result in a change of beneficial ownership through a change of control of an entity's board of directors. However, for certain not-for-profit transactions – including hospital "affiliation" deals – this mode of investigation proved lacking, because they often provide for a change in beneficial ownership without affecting board control. The PNO, mindful of the transaction structures currently being utilized in the not-for-profit space, particularly with respect to hospitals, issued the new tip sheet to make clear that beneficial ownership can be achieved by means other than board control.

Prior informal interpretations in the not-for-profit sector conflated the concepts of beneficial ownership and control. The PNO has previously issued informal interpretations for an affiliation between a non-profit and a hospital stating that "the **only** HSR control test applicable to non-stock, non-profit corporations is having the contractual right presently to designate 50% or more of the directors of the not-for-profit corporation." 0705011 Informal Interpretation, May 17, 2007 (emphasis added). The newly issued tip sheet makes clear that while acquiring board control is still meaningful in determining beneficial ownership, it is not dispositive.

Notably, "beneficial ownership" is not defined in the Act or the rules. However, the tip sheet sets forth examples of beneficial ownership for a typical hospital affiliation structure where two (or more) affiliating hospitals create a new not-for-profit holding company for the affiliating hospitals (the "Newco"). In such an arrangement, beneficial ownership may be exhibited without regard to control of the board of directors in the following ways:

- (i) Newco has the right to authorize and/or approve the articles, bylaws, and other governance documents of the affiliating hospital entities;
- (ii) Newco has the right to authorize and/or approve the sale or lease of the affiliating hospital assets;
- (iii) Newco has the right to appoint and/or approve the senior officers of the affiliating hospital entities; or
- (iv) Newco has the right to devise and/or approve the strategic plans, capital budgets and expenditures, and significant contracting of the affiliating hospitals.

Under previously provided PNO guidance, these items would not have been considered in determining reportability; however, the newly promulgated PNO tip sheet makes clear that these factors can lead to the determination that an affiliation results in a reportable transaction, regardless of any change in board control.

B. Discussion of Typical Transactions. The PNO noted that not-for-profit transactions generally come in three varieties: a simple acquisition, a consolidation, and a joint venture formation.¹

- (i) Simple Acquisition: an existing entity (the acquiring person) is deemed to hold assets of an acquired entity as a result of an acquisition transaction.
- (ii) Consolidation: two existing not-for-profit entities consolidate under a Newco (which is also not-for-profit).
- (iii) Joint Venture Formation: two existing not-for-profit entities can form a new entity.

While the above is not an exhaustive list, the PNO's description of typical transactions provides helpful guidance in applying the most likely applicable exemption analysis under 802.40.

C. Exemption Availability for Typical Transaction Structures. A nuanced understanding of the type of not-for-profit transaction being undertaken is key in determining whether a reportability exemption may apply. Depending upon the structure of a transaction, an otherwise reportable transaction may be exempt from reporting requirements. Notably, Rule 802.40 provides an exemption for transactions that involve the formation of not-for-profit entities, such as joint ventures to own and operate an ambulatory surgery center. However, the PNO was clear that this exemption does not apply to transactions that produce a Newco with control over the affiliates' boards or other hallmarks of beneficial ownership. Such transactions are reportable consolidations.

The PNO's on-line posting may be found [here](#), and the tip sheet may be found [here](#).

The Saul Ewing Arnstein & Lehr LLP Hart-Scott team has handled hospital affiliations requiring and not requiring HSR filings, along with FTC inquiries in both cases. Please contact: Mike Finio at (717) 238-7671 or mike.finio@saul.com, Matt Draper at (412) 209-2535 or matt.draper@saul.com, or Nicholas Stewart at (410) 332-8616 or nicholas.stewart@saul.com.

¹ The writers note that in their health care/hospital acquisition experience, virtually everything is termed an "Affiliation Agreement" at the top of page one, or on the cover sheet to the agreement, but that once the content of the "affiliation" is parsed, it is clear not only who is in control, but how.

This Alert was written by Michael A. Finio, Counsel in the Firm's Health Care Practice, Partner Matthew Draper and Associate Nicholas Stewart. Michael can be reached at (717) 238-7671 or mike.finio@saul.com. Matthew can be reached at (412) 209-2535 or matt.draper@saul.com. Nicholas can be reached at (410) 332-8616 or nicholas.stewart@saul.com. This publication has been prepared by the Health Care Practice for information purposes only.

The provision and receipt of the information in this publication (a) should not be considered legal advice, (b) does not create a lawyer-client relationship, and (c) should not be acted on without seeking professional counsel who have been informed of the specific facts. Under the rules of certain jurisdictions, this communication may constitute "Attorney Advertising."