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# Reminder: Equity Compensation May Require HSR Filings for Executives of REITs or Other Companies

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Common equity-based compensation-related transactions, such as restricted stock grants, settlement of restricted stock units (RSUs), exchange of operating partnership units (OP units) and option exercises, may trigger filing obligations under the Hart-Scott-Rodino Antitrust Improvements Act (HSR Act) for executives of REITs or other companies who own significant amounts of their company's stock. Executives should be aware of how these filing requirements may apply to them, as filing fees are not insignificant ($45,000 or more) and failing to make a required filing can bring about stiff consequences, including fines of up to $40,000 per day, a governmental inquiry, and potential embarrassment.

This alert discusses how the HSR filing requirements apply, in general, to executives of REITs or other companies in the context of common equity compensation-related transactions.

## THE RULE

The HSR Act requires that acquisitions of voting securities, non-corporate (LLC/LP) interests, or assets which meet certain monetary thresholds be notified to the Federal Trade Commission (FTC) and Department of Justice (DOJ) before closing. As a result, parties to mergers and acquisitions may be required to file a notification under the HSR Act.

The law is equally clear that acquisitions of voting stock by individual executives – whether the stock is acquired through grants of restricted stock, settlement of RSUs, exchange of OP units, option exercises, open market purchases or any other means – can also trigger an HSR filing obligation. An executive may be required to make an HSR filing even if he or she will hold 5% or less of the company's total outstanding voting stock after the acquisition.

> ***Company executives who will hold more than $80.8 million of stock after acquiring additional shares by any means will often have an HSR Act filing requirement.***[1]
>
> ***There are also additional, higher dollar thresholds that can trigger a filing – even if an executive has previously filed to report acquiring a minority stake that crossed a lower threshold.*** These higher thresholds are $161.5 million and $807.5 million.[2]

## HOW TO CALCULATE THE TRANSACTION VALUE?

These filing thresholds are based on the total aggregate amount of stock that a person will hold ***after*** making an acquisition (even though a filing must be made ***before*** the acquisition). The total value of stock that will be held as a result of an acquisition is based on the current fair market value of the person's present holdings plus the price that will be paid to acquire the new shares. However, if the company is publicly traded, then the acquisition price for the new shares is the higher of the current fair market value (based on the stock's recent trading price) or the price that will be paid to acquire the new shares. In other words, an executive cannot rely on the price he or she previously paid to acquire current holdings of company stock. Instead, he or she must mark-to-market the value of the current holdings. An executive of a public company also cannot rely on the strike price for the options he or she intends to exercise. Again, he or she must determine the current fair market value. If the fair market value is higher than the strike price, then the value of what the executive will hold for HSR purposes is the combined fair market value of the current holdings plus the fair market value of what he or she will acquire. An HSR filing may be necessary if this combined fair market value is greater than the now-applicable size-of-transaction threshold of $80.8 million (note that the thresholds are adjusted annually).

### HOW TO CALCULATE THE SIZE-OF-PERSON REQUIREMENT?

For transactions that are valued at less than $323 million, HSR filings are only required if one of the filing thresholds set forth above is met **and** the additional size-of-person requirement is met (importantly, note that HSR filings may be required if the total value of voting stock that an executive will hold is $323 million, even if the size-of-person requirement is not satisfied). The size-of-person requirement generally will be met if:

- the company has more than $161.5 million in total assets or annual net sales; and
- the executive holds at least $16.2 million in total investment assets, voting securities, options, warrants and income-producing property.

Given the $80.8 million size-of-transaction threshold, it is very unlikely that a transaction by an executive that exceeds the size-of-transaction threshold would not also exceed the size-of-person requirement

### WHY DOES THIS MATTER?

An acquisition that is subject to notification may not be completed until the acquiring person pays the filing fee and the 30-day statutory waiting period either expires without action or is terminated early by the agencies.[3] The failure to make a required HSR filing can subject the executive to civil monetary penalties of up to $40,000 per day, and the FTC has imposed significant fines in the hundreds of thousands of dollars on individual investors in recent years. In 2016, the FTC obtained a $480,000 fine from Caledonia Investments for failing to report the acquisition of voting shares as a result of the vesting of restricted stock units in Bristow Group, Inc. Also in 2016, the FTC obtained a $720,000 fine from entrepreneur Mitchell P. Rales for shares that his wife purchased in Colfax Corporation. In 2011, the FTC imposed a penalty of $500,000 on Comcast CEO Brian Roberts when he failed to report acquiring additional stock in 2008 as the result of the vesting of RSUs. Roberts had previously filed notification in 2002 to report acquiring Comcast stock, but that filing was more than five years old and therefore expired at the time Roberts acquired additional stock in 2008 (see **FTC Obtains $500,000 Penalty for Premerger Reporting Act Violations**.)

### ARE THERE EXEMPTIONS THAT MAY APPLY TO EXECUTIVES OF REITS?

If the size-of-person requirement and one of the filing thresholds are met, the transaction will nevertheless be exempt if the fair market value of the company's non-exempt assets is $80.8 million or less. Most typical real estate assets of REITs will fit within one of the categories of exempt assets under the HSR Act. However, there are some commonly held types of assets that are non-exempt, such as trademarks, fund management operations, third-party property management businesses, value of management rights for assets that are not majority owned, and property that is used to conduct a business (e.g., pay parking lots open to the public). Given that a REIT must only hold $80.8 million in total non-exempt assets in order to lose the benefit of the exemption, executives should not presume that this exemption will be available. A detailed assessment of a REIT's assets may be required to establish that this exemption exists. Furthermore, if a REIT acquires non-exempt assets in excess of the threshold at a time when an executive has already exceeded the filing threshold, then an executive's acquisition of even a single share of stock will trigger a filing requirement. As a result, executives seeking to rely upon this exemption will need to monitor the value of the REIT's non-exempt assets on an ongoing basis.

**TYPICAL SCENARIOS**

The following address the HSR filing implications of a number of typical equity-based compensation-related transactions for REIT executives, assuming that the size-of-person test described above is met and the REIT has at least $80.8 million of non-exempt assets:

What happens if:

1. **an executive receives a grant of restricted stock that would put the executive over the threshold?**
   Unvested restricted stock, which entitles the executive to vote for the election of directors, is included in determining whether the executive holds more than $80.8 million of total voting stock. As a result, a grant of unvested restricted stock that puts the executive over the threshold typically will require the executive to make an HSR filing.

2. **an executive vests in restricted stock that puts the executive over the threshold?**
   The HSR requirements apply any time an executive acquires stock that confers the right to vote for the election of directors. For restricted stock, the event that can trigger an HSR filing requirement takes place when the restricted stock that entitles the holder to vote for the election of directors is granted to the executive. The executive is deemed to hold voting stock as a result of the grant, and therefore the subsequent vesting of the restricted stock does not trigger any HSR filing obligation.

3. **an executive receives an RSU that would put the executive over the threshold if the underlying shares were owned?**
   RSUs, which do not entitle the executive to vote for the election of directors, do not count toward the $80.8 million size of transaction threshold. The RSU vesting terms (performance-based hurdles or continued employment) do not affect this determination. Therefore, the grant of RSUs does not trigger an HSR filing requirement. However, the subsequent settlement of RSUs after vesting may require an HSR filing since, upon settlement, the executive will acquire stock that entitles the holder to vote for the election of directors. Prior to the time any RSU settlement takes place, it is important to determine whether the executive will hold more than $80.8 million of voting stock upon the settlement of the RSUs. RSUs or shares of stock that are retained to satisfy tax withholding or that the executive intends to sell immediately upon settlement will not count toward the $80.8 million threshold.

4. **an executive receives shares of stock upon the settlement of an RSU that puts the executive over the threshold?**
   The acquisition of voting stock upon settlement of an RSU that results in the executive holding more than $80.8 million of total voting securities typically will require an HSR filing unless the executive intends to sell the stock acquired upon settlement of the RSU immediately upon settlement.

5. **an executive receives LTIP units or other OP units in the operating partnership of the REIT that would put the executive over the threshold if the underlying shares were owned?**
   The acquisition of interests in a partnership is not subject to the HSR reporting requirements so long as

the executive will not acquire the right to 50% of the partnership's profits or assets upon dissolution. There is no limit to the value of the partnership interests an executive can acquire if the executive will not receive the right to 50% of the profits or assets upon dissolution. As a result, in almost all realistic scenarios, the receipt of LTIP units or other OP units will not trigger an HSR filing. LTIP units or other OP units held by an executive do not count as voting securities of the REIT and, as a result, do not count toward the $80.8 million threshold that may trigger an HSR filing.

6. **an executive receives shares of stock in exchange for OP units in the operating partnership that put the executive over the threshold?**
   The acquisition of voting stock in exchange for OP units in the operating partnership typically will require an HSR filing if as a result the executive will hold company voting securities that have a total value of more than $80.8 million (including the fair market value of any voting securities, including unvested restricted stock, the executive holds prior to the exchange) unless the executive intends to immediately sell the stock upon acquisition.

7. **an executive receives an option for a number of shares that, if exercised, would put the executive over the HSR threshold?**
   The acquisition of an option to acquire shares upon exercise does not require an HSR filing. An HSR filing may be required upon the exercise of the option into voting securities, but the option grant itself does not trigger any filing requirement.

8. **an executive exercises an option that puts the executive over the threshold?**
   The exercise of an option that results in the executive holding voting stock that has a total value of more than $80.8 million (including the fair market value of any voting securities the executive holds prior to the exercise) typically will require the executive to make an HSR filing unless the executive intends to sell the stock acquired immediately upon exercise (e.g., pursuant to a broker-assisted cashless exercise).

Given that a number of common equity-based compensation-related transactions can trigger HSR filing obligations for executives of REITs and other companies who currently own or may acquire voting securities of their company with a value in excess of $80.8 million, these executives should ensure that they are receiving expert advice to make sure that they do not inadvertently overlook these obligations and consider negotiating contractual protections relating to these filing obligations.

[1] The FTC adjusts the HSR thresholds annually in the first quarter according to changes in GNP.
[2] The FTC adjusts the HSR thresholds annually in the first quarter according to changes in GNP.
[3] The filing fee is: $45,000 for transactions valued at more than $80.8 million but not more than $161.5 million; $125,000 for transactions valued at more than $161.5 million but not more than $807.5 million; and $280,000 for transactions valued at more than $807.5 million.

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