November 18, 1986

BY HAND

Linda Heban, Esq.
Premerger Notification Office
Bureau of Competition
Room 301
Federal Trade Commission
6th Street and Pennsylvania Avenue, N.W.
Washington, D. C. 20580

Dear Ms. Heban:

This will serve to summarize our conversations of last week concerning the treatment of leveraged leases or lease financing arrangements under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the "Act") and the regulations promulgated thereunder and to request your response to the issues raised herein in the form of an informal interpretation pursuant to 16 C.F.R. § 803.30.

You confirmed as an initial matter that leveraged leases or lease financing transactions are exempt from the reporting requirements of the Act under § 802.63 of the regulations. Although the exact structure of such transactions may vary in a number of respects from case to case, for purposes of this inquiry such transactions may be defined as the Commission did in the Statement of Basis and Purpose:

> In a common type of lease financing, several equity investors contribute part of the cost of the leased equipment to a trustee (the owner trustee). The owner trustee, usually a commercial bank, then borrows the remaining funds from other investors (usually other institutional investors) and purchases the equipment, which is often leased to the actual user. Often, a second trust is established that takes a security interest in the leased property to protect the rights of the equity investors.

43 Fed. Reg. 33502 (1978).

The Commission concluded that the establishment of such transactions, which involve various "acquisitions", should be exempt from the Act. The Commission recognized that they were a "hybrid credit arrangement" that should not be treated any differently from a more traditional extension of credit. (A copy of the relevant pages from the statement of Basis and Purpose is enclosed).*/

The question I posed to you and that we have discussed is whether the sale or transfer of this transaction from one lessor/creditor to another can similarly be considered exempt from the Act. I explained that these transactions are sold for a variety of reasons completely unrelated to the actual use of the leased asset. Thus, one creditor/lessor may sell the transaction to another because of tax considerations or because it seeks to realize some of the value of the asset immediately rather than awaiting termination of the lease.

The sale of these transactions can generally occur in two ways. First, the asset can simply be sold subject to the existing lease to the actual user and the new creditor/lessor (through the various trust arrangements) steps into the shoes of the previous creditor/lessor. Second, instead of a transfer of the asset per se the acquiring company can simply purchase 100% of the voting securities of the corporation that is acting as creditor/lessor. It is important to understand in this context that lease financing companies often establish specialized subsidiaries, the only function for which is to participate in certain transactions. Thus, hypothetical Lease Financing, Inc. may have a wholly-owned subsidiary, Lease Financing-Sub, Inc.,

.....

*/ Neither the regulations nor the Statement of Basis and Purpose speaks to the sale of lease financing transactions. Example 2 in Section 802.63 deals with the acquisition of assets by a creditor "in a transaction" and states that the subsequent disposition of those assets is not exempt under Section 802.63. This example seems to contemplate the acquisition of assets in a foreclosure or upon default and not as part of the initial transaction. Moreover, in discussing the disposition of the assets it does not contemplate the sale of the asset as part of the sale of the loan arrangement as is the case with lease financing transactions.

whose only assets are its participation in, for example, three lease financing arrangements and whose sole activities are incident to those financing arrangements. Such financing arrangements can be purchased by simply purchasing 100% of the voting securities of Lease Financing-Sub, Inc.

We believe that the Commission's recognition that leveraged leases or lease financing transactions are just another form of credit arrangement should enable the Premerger Office to conclude that the transfer of such arrangements is exempt under the Act. Under subsection (c)(2) of the Act, "acquisitions of bonds, mortgages, deeds of trust, or other obligations which are not voting securities" are exempt. Following the statutory mandate, the Premerger Office has concluded in informal interpretations that the acquisition of mortgage loans and commercial loans are exempt. See American Bar Association, Premerger Notification Practice Manual 14 (1985). A true lease financing transaction is nothing more than an extension of credit to the lessee to finance its use of the asset or equipment being leased. Just as there is no competitive significance in the transfer of a mortgage loan from one mortgagee to another, similarly there is no competitive significance to the transfer of a lease financing transaction from one creditor to another. Although there are legal distinctions between the two transactions -- for example, the creditor in a lease financing transaction actually owns (through a trust arrangement) the asset -- such distinctions are without significance for purposes of the Act. We believe, therefore, that the (c)(2) exemption implicitly if not explicitly exempts the acquisition of lease financing transactions.

As we discussed, in this context the (c)(2) exemption is often also considered in conjunction with (c)(1) "ordinary course of business" exemption. The Premerger Office has previously concluded that the sale of retail notes from one corporation's credit subsidiary to another's finance subsidiary was within the ordinary course of business. See Premerger Notification Practice Manual at 12-13. The relationship between the (c)(1) and the (c)(2) exemptions in the sale of loans was recognized by Senator Hart:

> Section 7A(c)(2) exempts acquisition of bonds, mortgages, deeds of trust, or other obligations which are not voting securities and Section 7A(c)(1) exempts acquisitions of goods or realty transferred in the ordinary course of business. It is the intention of the managers that these provisions exempt consumer receivables and loans or other obligations, which are not voting securities, which are traditional financing arrangements and which normally are sold to banks or other financing agencies and acquired in the normal course of business.

122 Congressional Record S. 15417 (Daily Edition Sept. 9, 1976) (quoted in Statement of Basis and Purpose, 43 Fed. Reg. at 33503).

Although it is becoming far more common for these lease financing transactions to be transferred, there is a problem in using the ordinary course of business exemption as defined in the regulations. As mentioned above, for tax and other reasons, a lease financing company will often establish numerous specialized subsidiaries, the sole function of which is to participate in some financing transactions. It can often be the case, therefore, that when these lease financing transactions are sold they constitute the sale of all or substantially all of the assets of that specialized subsidiary. Such a sale could not be considered in the ordinary course of business by virtue of § 802.1(b) of the regulations. Thus, as currently interpreted, the ordinary course of business exemption may not apply to the sale of some lease financing transactions.

In sum, for the reasons recognized by the Commission in exempting from the Act the establishment of these lease financing transactions, we believe the sale of such transactions should be exempt from the requirements of the Act. The sale of these types of financings does nothing more than replace one creditor with another, leaving undisturbed the actual user of the asset. Accordingly, we respectfully request that you concur in our reading of subsection (c)(2) of the Act as exempting the sale of lease financing transactions, the establishment of which would be exempt under § 802.63. Such an exemption would serve the purposes of the Act and prevent the antitrust agencies from being

inundated with reports on the transfer of these lease financing transactions which have no competitive significance. */

As the sale of these lease financing transactions becomes more common, this issue becomes more important. We are currently working on numerous deals involving the sale of lease financing transactions that for tax reasons must close by year-end. Accordingly, your prompt response to the foregoing would be greatly appreciated. I would also be happy to answer any questions raised by your deliberations.

Sincerely,

[redacted]

[redacted]

*/ We believe the exemption for the sale of lease financing transactions should be without regard to the manner in which they are sold. Thus, the acquisition of lease financing transactions should be exempt even if they constitute all or substantially all of the seller's assets. Similarly, an acquisition of the voting securities of an entity whose assets consist solely of lease financing transactions and assets incident thereto should be deemed an acquisition of lease financing transactions and exempt. Cf. 15 C.F.R. § 802.1(a).

Must use ordinary course exemption analysis.

(c)(4) does not apply because are acquiring an asset.

11/24/86