

January 13, 2005

Marian R. Bruno, Esq.  
Assistant Director  
Federal Trade Commission  
Premerger Notification Office  
Bureau of Competition  
600 Pennsylvania Avenue, N.W.  
Washington D.C. 20580

Dear Ms. Bruno:

The purpose of this letter is to request a formal interpretation of Section 7A(a)(2) of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended (the "Act") and 17 C.F.R. §801.13 as these provisions apply to "Rollover Shares" (as defined below).

We represent a number of private equity funds (each, a "Sponsor"), which often use a newly-formed acquisition entity ("Newco") to acquire all of the voting securities of a privately-held entity (a "Target") by either (a) purchasing all of the equity securities of Target or (b) merging a wholly-owned subsidiary of Newco with Target (each, an "Acquisition"). As a result of an Acquisition, Target becomes a wholly-owned subsidiary of Newco, and the sole asset of Newco following the Acquisition is the equity securities of Target held by Newco. Newco typically is capitalized immediately prior to the Acquisition by (i) cash contributed by Sponsor in exchange for voting securities of Newco, and (ii) certain voting securities of Target contributed by certain existing shareholders of Target (the "Rollover Shareholders"), who are typically management employees of Target, in exchange for voting securities of Newco (the "Rollover Shares"). After the Acquisition, voting securities of Newco are held by Sponsor and the Rollover Shareholders.

The question has repeatedly arisen as to whether the Rollover Shares should be deemed "voting securities held as a result of the acquisition" in the transaction described above. We believe that, for the purposes of Section 7A(a)(2) of the Act and 17 C.F.R. §801.13, the term "voting securities" should be construed to specifically exclude any security which an existing equityholder of a privately-held acquired person exchanges for any security of a newly-formed acquisition entity (formed solely for the purpose of effecting an acquisition of such acquired person) if the sole asset of such newly-formed acquisition entity following the acquisition is the securities of the acquired person.

The reason for this request is to clarify the rules set forth in Section 7A(a)(2) of the Act and 17 C.F.R. §801.13 in light of the economic effect of the Acquisition transaction described above. Specifically, the change of control effected by the Acquisition could have alternatively been effected through a recapitalization of Target by Target's redemption of substantially all securities of Target held by existing equityholders and Sponsor's simultaneous purchase of newly issued voting securities of Target from Target (a "Recapitalization"). After the Recapitalization, in addition to the voting securities held by Sponsor, certain existing shareholders (the "Continuing Shareholders") would continue to own voting securities of Target (the "Retained Shares"). In a Recapitalization, the Retained Shares are not transferred, exchanged or converted, and would not constitute voting securities held by the acquiring person under Section 7A(a)(2) of the Act and 17 C.F.R. §801.13.

Although there may be differing rationales that would lead a Sponsor to choose between an Acquisition structure and a Recapitalization structure (including, without limitation, business, tax or accounting reasons), the economic effect of both the Acquisition and the Recapitalization is the same. In each case, the effective result of the transaction is that certain existing shareholders directly or indirectly maintain their ownership in the Target, and Sponsor directly or indirectly acquires a controlling interest in Target.

It is an anomalous result, in our view, that Retained Shares held by Continuing Shareholders in a Recapitalization are not "voting securities held as a result of the acquisition" but that Rollover Shares held by Rollover Shareholders in an Acquisition are "voting securities held as a result of the acquisition" simply because, in the latter case, the Rollover Shareholders physically exchange shares of Target voting securities for voting securities of Newco. In an Acquisition, Newco is merely a holding company whose only asset following the Acquisition is securities of Target. The Acquisition does not change the operations or value of Target, rather it only creates a holding company in which the securities of Target are held. After the Acquisition, Newco's equity value is equivalent to the equity value of Target. Therefore, in our view, the Rollover Shares in an Acquisition should be analyzed in the same manner as the Retained Shares in a Recapitalization for Hart-Scott-Rodino purposes.

#### **An Example of Disparate Hart-Scott-Rodino Treatment of a Recapitalization Compared to an Acquisition**

Assume for the purposes of this section that (a) Sponsor intends to directly or indirectly acquire voting securities of Target in exchange for cash of \$40 million, (b) existing equityholders of Target will continue to hold \$15 million in voting

securities of Target (either directly as Retained Shares or indirectly as Rollover Shares), (c) Target is a privately-held entity, (d) Newco is a newly-formed acquisition entity formed solely for the purpose of effecting the acquisition of Target, and (e) the Act's "Size-of-Parties" and "commerce" tests are met.

If the transaction is structured as a Recapitalization, Sponsor would purchase shares of Target from Target in exchange for \$40 million in cash. The Recapitalization would have no effect on the Retained Shares and the Continuing Shareholders would continue to hold voting securities in Target having a value of \$15 million. Under this structure, no Notification Filing would be required because the Size-of-Transaction test set forth in Section 7A(a)(2) of the Act would not be met.

If the transaction is structured as an Acquisition, immediately prior to the Acquisition Sponsor would contribute cash in the amount of \$40 million to Newco in exchange for voting securities of Newco, and the Rollover Shareholders would contribute their Rollover Shares of Target to Newco in exchange for shares of voting securities of Newco. Newco would acquire the remaining voting securities of Target (by purchase or merger). Following the Acquisition, Target would be a wholly-owned subsidiary of Newco and the only asset held by Newco would be the securities of Target.

17 C.F.R. §801.13 requires that "all voting securities of an issuer held by the acquiring person after the consummation of an acquisition . . . be deemed voting securities held as a result of the acquisition." Because the Rollover Shareholders contribute their Rollover Shares of Target to Newco in exchange for shares of voting securities of Newco, a literal reading of this provision would seem to require that the Rollover Shares would be considered "voting securities held as a result of the acquisition." Applying this literal reading of 17 C.F.R. §801.13 to the Rollover Shares would result in the Size-of-Transaction test set forth in Section 7A(a)(2) of the Act being met and a Notification Filing being required.

This disparate treatment under the Act of the Acquisition and the Recapitalization transactions results solely from a structural difference in the transactions. Moreover, since the Rollover Shareholders and the Continuing Shareholders in both transactions effectively continue to hold a direct or indirect equity interest in Target, the structural difference does not seem to warrant different treatment under the Act. Under the foregoing facts, the Rollover Shares in the Acquisition should be construed as a continuing equity interest in Target (since Newco has no other assets) by the Rollover Shareholders rather than a new investment in Newco.

Federal Trade Commission  
January 13, 2005  
Page 4

### The Need for Issuance of a Formal Interpretation

We believe that Rollover Shares should be excluded from "voting securities held as a result of the acquisition" for the purposes of Section 7A(a)(2) of the Act and 17 C.F.R. §801.13 in the following, narrowly-tailored set of circumstances: (a) Target is a privately-held entity, (b) Newco is a newly formed entity formed for the purposes of effecting an acquisition of Target, and (c) as a result of such acquisition, Target will be a wholly-owned subsidiary of Newco and Newco's sole asset will be the securities of Target held by it.

A literal application of Section 7A(a)(2) of the Act and 17 C.F.R. §801.13 results in different treatment for the Acquisition transaction solely due to a structural difference in how the transaction was effected. This disparate treatment places onerous and costly filing requirements on Sponsor which would not be necessary if Sponsor structured the transaction as a Recapitalization. As the structural differences between the Acquisition and the Recapitalization do not appear to warrant different treatment under the Act, it seems important to have clear guidelines as to how Section 7A(a)(2) of the Act and 17 C.F.R. §801.13 should be applied as to Rollover Shares.

Very truly yours,

ADVISED THAT AS LONG AS NEWCO IS A SHELL HOLDING NOTHING OTHER THAN THE VLS OF TARGET, AND THE ROLLOVER SHAREHOLDERS HOLD THE SAME PERCENTAGE (OR LESS) OF NEWCO VLS THAT THEY HELD IN TARGET, THE ACQUISITION OF NEWCO VLS WOULD BE EXEMPT UNDER 7A(C)(10). ONLY SPONSOR HAS A POTENTIAL FILING OBLIGATION. M. BAUNO CONCURS.

B. Muehl  
1/19/05