

Verne, B. Michael

From: [REDACTED]
 Sent: Thursday, July 20, 2006 11:55 AM
 To: Verne, B. Michael
 Cc: [REDACTED]
 Subject: HSR Advice - Formation of Joint Venture Corporation and Acquisition of Voting Securities and Assets

Set forth below is the description of transaction, analysis, and conclusion with respect to a proposed transaction to form a joint venture corporation and for the new corporation to acquire two related service businesses, which I referenced in a voice mail message this morning.

Please confirm that, based on the facts described, you agree with the conclusions set forth below, or clarify how the proposed transaction should be analyzed for purposes of determining whether some or all of the parties must observe the HSR notification and waiting period requirements.

1. Description of Transaction. Three separate investment funds (individually "Fund" and collectively "Funds"), and an individual who is the sole owner of two related services businesses (collectively "ABC"), have entered in to a letter of intent ("LOI") that provides that they will incorporate a new C-corp. ("ABC I"), that will acquire 100 percent of the ownership interests of ABC for a total purchase price of \$67.5M to \$100M. (All dollar amounts are rounded to the first decimal place for convenience.)

The three Funds will contribute a total of \$24.2M in cash and will acquire approximately 35.5 percent, 11 percent, and 4 percent, respectively, or a total of 50.5 percent of the voting securities of ABC I, valued at \$24.2M. The owner of ABC will contribute 100 percent of the voting securities or membership interests of ABC, and will receive 49.5 percent of the voting securities of ABC I, valued at \$23.7M, and an initial cash payment of \$43.8M (subject to an escrow of 5 percent of that amount). The two entities that comprise ABC are an LLC and an s-corp.; the latter may contribute all of its assets to a wholly-owned LLC, which ABC I will acquire. The total assets of ABC have a book value of approximately \$15M.

The owner of ABC also may receive an additional contingent payment in early 2007 of up to \$30M in cash and \$2.5M in voting securities of ABC I, that depends on ABC I's 2006 EBITDA. Depending on the amount, if any, of the contingent payment to the owner of ABC, the Funds may contribute additional cash in the maximum aggregate amount of \$2.6M, and will receive additional voting securities of ABC I in proportion to their respective ownership interests in ABC I as described above. Thus, the parties' acquisition of additional voting securities of ABC I in early 2007, to the extent this occurs, will not change the proportion of voting securities owned by each of the Funds and the owner of ABC, as described above.

A bank unrelated to the parties ("Bank") will provide senior debt to ABC I in an initial amount of \$22.6M, which may be increased to \$50M to fund the earn-out described above. The Bank will not acquire any voting securities (including convertible voting securities) of ABC I, and the senior debt will be non-recourse to the Funds and the owner of ABC (ie, none of these parties will guarantee repayment of the debt).

The parties expect to fund ABC I and consummate ABC I's acquisition of ABC in a single closing. As such, ABC I will not have a regularly prepared balance sheet at the time of closing.

The LOI provides that the owner of ABC and the Fund that acquires 35.5 percent of ABC I's voting securities each will have the right to appoint two of the five directors of ABC I, and that these two parties must jointly agree on the appointment of the fifth director.

2. Size of Persons for Formation of ABC I. One or more of the Funds has total assets and/or annual net sales in excess of \$113.4M, and the owner of ABC has total assets and annual net sales in excess of \$11.3M.

ABC I will be its own ultimate parent entity because no person will own 50 percent or more of its voting securities or have the contractual power presently to designate 50 percent or more of its directors. ABC I's total assets will exceed \$11.3M for purposes of Rule 801.40, based solely on the initial cash contributions by the Funds. ABC I's total assets for purposes of Rule 801.40 also will include the book value of the total assets of ABC (approximately \$15M), but not the \$22.6M to \$50M of senior debt, because the Bank will not acquire any voting securities, including convertible voting securities, of ABC I.

Accordingly, the parties will satisfy the size of person test in Rule 801.40 with respect to the formation of ABC I.

3. Size of Transaction For Formation of ABC I. Each of the Funds and the owner of ABC will acquire voting securities of ABC I. Under Rule 801.40, each will be deemed an acquiring person and ABC I will be deemed an acquired person.

The LOI provides a capitalization table for ABC I that specifies the sources and use of funds by ABC I, as follows: \$26.8M maximum aggregate capital contribution by the Funds; \$22.6M in senior debt (and the additional senior debt of up to \$27.4M if needed to fund the contingent payment) that ABC I will (or may) borrow; and \$26.2M as the maximum aggregate value of voting securities of ABC I that the owner of ABC may receive. The parties are preparing a definitive agreement that will contain substantially the same terms, which are sufficient to determine the acquisition price for the initial acquisition of voting securities of ABC I under Rule 801.10(a)(2)(i).

Based on the purchase prices specified in the LOI, none of the parties' separate initial acquisitions of voting securities of ABC I will exceed \$56.7M, the current minimum size of transaction threshold under the HSR Act and FTC Premerger Notification Rules.

Depending on ABC I's 2006 EBITDA, the Funds and the owner of ABC also may acquire additional voting securities of ABC I in early 2007. Pursuant to Rule 801.13(a)(2)(ii), the Funds and the owner of ABC each must determine the fair market value of the voting securities of ABC I that they already hold to determine whether each of their separate 2007 acquisitions, when aggregated with the voting securities that each of them already owns, exceeds the \$56.7M size of transaction threshold.

4. ABC I's Size of Person for its Acquisition of ABC. The formation of ABC I as a joint venture corporation, and ABC I's acquisition of voting securities and assets of ABC, are analyzed as separate transactions. ABC I will not have a regularly prepared balance sheet at the time that it acquires ABC. Pursuant to Rule 801.11(e), the total assets of ABC I as an acquiring person with respect to its acquisition of ABC will consist of all assets held by ABC I at the time of the acquisition, less all cash that will be used for the acquisition, including expenses incidental thereto. The only assets that ABC I will hold at the time of its acquisition of ABC will be cash to fund that acquisition or for acquisition-related expenses. Thus, ABC I will not satisfy the \$11.3M size of person test with respect to its acquisition of ABC.

5. Conclusion. Based on the foregoing description of transaction and analysis, the separate initial acquisitions of voting securities of ABC I by the Funds and the owner of ABC will not satisfy the \$56.7M size of transaction test, and ABC I will not satisfy the size of person test with respect to its acquisition of voting securities and assets of ABC. Accordingly, none of the parties to the transaction are required to observe the notification and waiting period requirements of the HSR Act prior to consummating the initial acquisition of voting securities of ABC I or ABC I's acquisition of ABC.

With respect to the possible acquisition of additional voting securities of ABC in early 2007, the Funds and the owner of ABC each must determine the fair market value of the voting securities of ABC I that they already hold to determine whether each such acquisition, when aggregated with the fair market value of the voting securities of ABC I that each of them already holds, will exceed the \$56.7M size of transaction threshold. If so, each such acquiring person also must determine whether the size of person tests are satisfied with respect thereto, using the most recent regularly prepared balance sheet of ABC I as of that time.

Best regards, [REDACTED]

Nancy and I talked this through and agree that this probably isn't reportable, but using a different analysis. We believe that the two transactions you describe (formation of Newco and subsequent acquisition of ABC) are really all part of the 801.40 formation of Newco.

So I don't think your valuations of the voting securities of Newco being acquired by the three funds reflects the fact that Newco holds cash (including the initial \$22.6 MM from the bank, but not the future potential funds from the bank) and the assets of ABC. The current owner of ABC would be exempt under 802.4 for its acquisition of voting securities of Newco because all that is being contributed to the formation, other than ABC, is cash.

Even if the value of Newco voting securities for one or more of the funds exceeds \$56.7 MM, they might also be exempt under 802.4, because the only non-exempt assets Newco would hold are those of ABC. If the book value of those assets is \$15 MM, I'd be surprised if the fair market value is almost four times that.

N. OVUKA AGREES.

B. [Signature]

7/20/06