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Verne, B. Michael

From: [REDACTED]
Sent: Thursday, April 03, 2008 4:26 PM
To: Verne, B. Michael
Cc: [REDACTED]
Subject: Unproductive Real Property Exemption

Dear Mr. Verne:

Thank you for taking the time today to discuss with us the transaction which is being contemplated by our client. This e-mail is to confirm the facts which we shared with you during our conversation, and your response. Please confirm your agreement with the conclusions and interpretations below, per our discussion.

We represent a client which has proposed one of several competing plans to purchase a debtor-in-possession's assets out of bankruptcy. Company A is the debtor-in-possession, and it has filed for Bankruptcy, as have each of its subsidiaries. The assets being acquired include, in relevant part, timberlands and a mill. Company A owns the mill being acquired and two of its wholly-owned subsidiaries, Company B and Company C, own the timberlands being acquired.

The assets have been the subject of several appraisals and are encumbered by varying amounts of debt. Our client's Plan contemplates the contribution of cash and the assumption or conversion of a portion of the debt obligations of the Debtors and will require bankruptcy court approval to implement the reorganization.

Our client is forming a new LLC investment vehicle, which will combine with one of its pre-existing entities and one of the creditors to form a Newco LLC. We are assuming that each party will meet the size-of-party tests. Under the reorganization plan, all of the Debtors' commercial timberland and lumber mill assets will be transferred to Newco for approximately \$620 million. Our questions focus on whether the value of certain assets are exempt from inclusion in the size of transaction test. The questions involve "intra-company sales" under section 802.2(c)(1) and the applicability to this transaction of the "in conjunction with" language under section 802.2(c)(2)(iii).

Intra-Company Sales

In this transaction, there are two sets of timberlands, owned by two entities.

Company B, a wholly-owned subsidiary of Company A, owns the first set of Timberlands (Timberlands I). Company A harvests and purchases all the logs from Company B's Timberlands. Company A then processes the majority of the logs through its sawmills, although it does sell some logs to third parties, after harvesting and purchasing the Timberlands, without any further processing.

Company C, a wholly-owned subsidiary of Company A, owns the second set of Timberlands (Timberlands II). However, Company B has the exclusive rights to harvest the Timberlands, and operates them. All the timber from Timberlands II is harvested and purchased by Company A under a contract with its wholly-owned subsidiary, Company B.

You confirmed that when one entity harvests and purchases logs from Timberlands owned by its wholly-owned subsidiary, those sales are "intra-company sales" for purposes of § 802.2(c)(1), and therefore:

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- 1) The sales between Company A and Company B of timber from Timberlands I are "intra-company sales" for purposes of § 802.2(c)(1);
- 2) The sales between Company A and Company B of timber from Timberlands II are "intra-company sales" for purposes of § 802.2(c)(1); and
- 3) All of those "intra-company sales" can be excluded when determining whether the property generated total revenues in excess of \$5 million during the last 36 months under § 802.2(c)(1), regardless of what the purchasing entity subsequently does with the logs after purchasing them from an entity within the same ultimate parent entity (whether it processes them through its sawmills or sells them to third parties without further processing).

"In Conjunction With"

In Informal Staff Opinion 0110003, the PNO agreed with the statement that "in an acquisition of timberland, it will suffice to aggregate revenues only from contiguous parcels and that the PNO has not considered the 'used in conjunction with' concept to be applicable in such a transaction." You confirmed that is the case here, where the acquisition would include both timberlands owned by Company B and Company C, and a mill owned and used by Company A to process logs harvested from those timberlands.

Therefore, assuming that Timberlands I and II are otherwise unproductive real property, the concurrent acquisition of the mill does not render the Timberlands productive real property, and the value of the Timberlands can be excluded from the size of transaction.

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AGREE
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