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801.1(b)**Verne, B. Michael**

From: [REDACTED]
Sent: Wednesday, October 28, 2009 12:06 PM
To: Verne, B. Michael
Cc: [REDACTED]
Subject: HSR Question Concerning LLC Formation

Mike, hope all is well with you [REDACTED] and I would appreciate your advice on the transaction described below.

I. Factual Circumstances

Various investors own voting securities in corporations A, B, C, D, and E, companies which own oil and gas exploration assets and certain midstream assets. X is the largest investor but holds less than 50 percent of the voting securities of each company. There is a shareholder agreement concerning each company but under such agreements X only has the right to appoint one of five directors.

The investors want to reorganize and, to that end, are establishing a new limited liability company (the "LLC") to which they will contribute their shares in A, B, C, D, and E (the "Formation") in exchange for interests in the LLC. Following such action, the LLC will be the owner of all of the voting securities of A, B, C, D and E.

The LLC has a complicated membership structure and parallels in many ways the original ownership structures of A, B, C, D, and E. For example, there are fifteen classes of membership units. The first group of units consists of Class-A Preferred units, Class B-Preferred units, Class C-Preferred Units, and Class D-Preferred Units (collectively, the "Preferred Units"). The second group consists of Class A-1 Units, Class A-3 Units, Class B-1 Units, Class B-3 Units, and Class B-5 Units (collectively, the "Common Units"). The final group of units consists of Class A-2 Profits Units, Class A-4 Profits Units, Class B-2 Profits Units, Class B-3 Profits Units, Class B-4 Profits Units, and Class B-5 Profits Units (collectively, the "Incentive Units").

The Preferred Units for the most part will be held by the original investors in A, B, C, D, and E. The holders of the Common Units will be individuals in the management of A, B, C, D, and E, and the holders of the Incentive Units will be those who previously held to stock options in A, B, C, D, and E.

The LLC does not contemplate the payment of "profits" on a regular basis. Rather distributions are expected to be made only on the sale of a subsidiary of the LLC or on the sale of the LLC itself. These distributions, when they occur, will be made according to a detailed eleven step "waterfall" arrangement which, stated in short hand fashion, basically works as follows:

- a. In step one of the waterfall, the holders of the Preferred Units first receive back the original price they paid for the units plus an 8 percent return. The Preferred Units are the only units where the holders have a right not only to the price they paid for the units but to a specified rate of return.
- b. Only after the payout outlined in (a) above is accomplished do certain of the Common Units start getting a return. At this step, Class A-1 and Class B-1 units become entitled to payments on a pro rata basis along with the Preferred Units until all receive a dollar amount per unit specified under that step of the waterfall. The structure of the specific dollar amounts in the waterfall is designed to increase management's proportion of the return as the aggregate amount of distributions increases and is based upon the ownership structures of A, B, C, D and E.
- c. Once step (b) is accomplished, the process continues through a series of eleven steps with various Common Units and Incentive Units joining in after the ones before them have received their specified dollar amount per unit. The Preferred Units participate in all eleven steps of the waterfall.

Under the above-described arrangements, holders of Common Units and Profits Units are subordinate to holders of the Preferred Units, and some of the holders of the Common Units and Profit Units are subordinate to each other.

Payments on liquidation follow the same waterfall arrangement as described above except that the holders of the Class-D Preferred Units receive payments related to those units prior to any payments being made in relation to the other Preferred Units.

II. HSR Analysis

- a. For purposes of determining control of A, B, C, D and E, we understand that we should look to the voting rights

provided in the articles of incorporation, as opposed to the shareholder agreements. Even if that is not correct though, the shareholder agreements allow X to appoint only 1 of 5 directors (2 of the others being appointed by other investors and 2 representing management.) Accordingly, there is no scenario in which X controls A, B, C, D or E for HSR purposes.

b. Based on an earlier telephone discussion which Paul, Anthony and I had with you we understand that the creation of the LLC and the contribution to it of ownership of A, B,C, D, and E would be considered an LLC formation and not an acquisition by the LLC of A, B, C, D, and E.

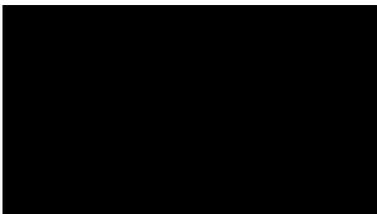
c. The question presented then is whether any one investor in A, B, C, D, and E will acquire control of the LLC for HSR purposes. In that regard, we would view the pay out arrangements with respect to the LLC as variable in nature, with the result that the HSR control test would turn on whether any one investor would have a right to 50 percent or more of the assets of the LLC on liquidation after payment of "debts." 16 C.F.R. 801.1(f). Please confirm if our understanding in that regard is correct.

d. It is our understanding that the rights of the holders of the Preferred Units to repayment of the cost of their initial investment plus a return of 8 percent is considered a "debt" of the LLC for purposes of 16 C.F.R. 801.1(f) (the "Preferred Debt"). If a liquidation were to occur on day 1 after the closing of the Formation, based on asset values expected to be on the balance sheet of the LLC at that time, it is anticipated that step one of the waterfall would not be completed and there would not be enough funds or assets to pay all of the Preferred Debt and other debt (such as accounts payable) ("Other Debt"). As a result, there would be no assets to distribute to the holders of the Common Units and Incentive Units (or Preferred Units participating pro rata with them). In such case, it is our further understanding that no one would be considered to control the LLC, it would be its own ultimate parent, and no HSR filing would be required.

e. Alternatively, if our understanding is incorrect and the payments to the holders of Preferred Units under step one on the waterfall are not viewed as "debt" for purposes of 16 C.F.R. 801.1(f), then if a liquidation were to occur on day 1 after the closing of the Formation, based on asset values expected to be on the balance sheet at that time, it is anticipated that Other Debt would be paid off and there would be assets available for distribution to the Preferred Unit holders in partial fulfillment of step one of the waterfall. Under this scenario, it is expected that X would be entitled to 50 percent or more of such assets and would face an HSR filing requirement in the absence of an applicable exemption.

Could you please advise us of your views on the treatment of obligations owed to the Preferred Unit holders as debt for purposes of 16 C.F.R. 801.1(f)? *YES*

Thank you very much for your assistance in this matter.



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10/28/08*

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Thank You.