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Verne, B. Michael

From: [REDACTED]
Sent: Wednesday, October 28, 2009 4:46 PM
To: Verne, B. Michael
Cc: [REDACTED]
Subject: HSR Question

Michael,

I would appreciate your input on an HSR issue relating to the treatment of personal goodwill for valuation purposes.

Step 1: Company B and Company C will contribute certain assets and liabilities to a newly formed NEWCO LLC in return for 100% of the membership interests in the new entity. Natural Person B is the indirect owner of Company B (through a trust) and is the UPE of NEWCO LLC. The formation of NEWCO LLC is not a reportable transaction as its value does not cross the filing threshold for the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended ("HSR Act").

Step 2: Pursuant to a membership interest purchase agreement, our client, Company A, intends to acquire 100% of the membership interests of NEWCO LLC from Company B and Company C. In addition, pursuant to a separate goodwill purchase agreement, Company A intends to acquire from Natural Person B his personal goodwill, which Company A intends to exploit in furtherance of the business of NEWCO LLC.

The estimated aggregate purchase price for both the membership interest purchase agreement and the goodwill purchase agreement, including an estimate of the potential earnout payment thereunder, is approximately \$110 million, of which less than \$25 million will be payable to Company B and Company C for the membership interests under the membership interest purchase agreement, and more than \$85 million will be payable to Natural Person B under the goodwill purchase agreement. The personal goodwill belongs to Natural Person B and is not an asset on the balance sheet of Company B or NEWCO LLC. The personal goodwill is separate and distinct from the assets of Company B, and its value was determined by independent appraisal.

My question is whether the personal goodwill of the owner/UPE of Company B should be counted as an asset for HSR valuation purposes. If the goodwill is excluded, the proposed transaction to acquire the LLC interests will not be reportable because its value is below the \$65.2 million threshold.

Natural Person B has personally created, developed, and is the exclusive owner of the goodwill, which is the class of intangibles comprised of his name, reputation, relationships, contacts, trade secrets, and related intellectual property (the "Goodwill"). The Goodwill has previously benefited Company B, and is expected to be valuable to any other similar business with which it is associated, including NEWCO LLC. In purchasing the Goodwill, Company A is purchasing the class of intangibles comprised of the name, reputation, relationships and knowledge of Natural Person B.

We do not think this Goodwill is analogous to the type of goodwill that often appears as a line item on a company's balance sheet or the type that has been addressed in some of the FTC's informal interpretations on goodwill. See, e.g., Opinions no. 0810010, no. 0806014, and no. 0706007. As such, we think that the acquisition of this Goodwill is not a reportable transaction under the HSR Act based on the following two lines of reasoning.

First, the value of the Goodwill is determined by independent appraisal, separate and apart from the assets of Company B. (Our understanding is that goodwill usually represents the difference between the book value of the assets and the fair market value of the business). As such, it seems that the monetary figure is properly analogous to cash or a cash equivalent. Under the HSR Act, neither cash nor a cash equivalent is an asset when it is acquired. See Rule 801.21. In addition, under the HSR Act, cash and a cash equivalent are properly excluded from the valuation of non-exempt assets. See Rule 802.4. Accordingly, it seems that this acquisition of Goodwill, which has been given a cash valuation, is arguably not an HSR Act reportable transaction.

Second, the cash value for the Goodwill is specifically related to the personal intangibles of Natural Person B, separate and distinct from the assets of Company B. (As an aside, Natural Person B is also entering into a separate employment agreement and noncompetition agreement with Company A and/or NEWCO LLC). The HSR Act definition of assets does not usually include personal intangibles or qualities; nor does the act cover the acquisition of or payment for such intangibles. Accordingly, it seems that Goodwill as defined here and as directly related to personal intangibles and qualities is beyond the scope of the HSR Act.

We would be happy to discuss this transaction further with you to the extent there is any additional information that would be helpful to your determination. Please let me know if there is a time this Thursday (October 28) that would be convenient to set up a call.

Thank you in advance for your assistance in this matter. I look forward to speaking with you.

[REDACTED]

AGREE -
DO NOT INCLUDE
PERSONAL GOODWILL
RJ
10/28/09

[REDACTED]

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