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Verne, B. Michael

From: [REDACTED]
Sent: Wednesday, June 27, 2012 5:16 PM
To: Verne, B. Michael
Subject: Proposed Transaction Involving Subleases and Leases of Aircraft

Dear Mike,

Company A and Company B, two large U.S. commercial airline companies, are proposing to enter into various lease arrangements involving 88 aircraft. The other key parties involved in the transactions are Company A's wholly-owned subsidiary ("Sub-A"), and the manufacturer of the 88 aircraft ("Manufacturer").

A. Existing situation

Currently 78 of the 88 aircraft involved in the proposed transaction are owned by affiliates of the Manufacturer (the "Manufacturer Aircraft") and are leased to Sub-A under individual lease agreements with the Manufacturer (the "Manufacturer Leases"). The lease agreements terminate at various times, but all have several more years to run. The useful lives of these 78 aircraft extend well beyond the term of these Manufacturer Leases, and the leases provide that the aircraft will be returned to the Manufacturer at the end of each lease. The lease payments are normal for the industry.

The remaining 10 aircraft are the subject of financing arrangements with third parties (the "Financing Company Aircraft") and are leased to Sub-A under individual lease agreements. These lease agreements terminate in 2017 and 2018; the useful lives of these 10 aircraft extend well beyond these termination dates. Affiliates of Company A will own the Financing Company Aircraft at the end of the term of the financing arrangements. The lease payments for the Financing Company Aircraft are also normal for the industry.

B. Proposed Lease Transactions

Under the proposed lease transactions (which are described in more detail below), Company B will sublease the 88 aircraft from Sub-A for the duration of Sub-A's existing leases. At the end of those leases, Company B will enter into new leases or purchase the aircraft (depending on the options available under the individual leases). The specific transactions are as follows:

1. Between Company B and Sub-A: Company B and Sub-A will enter into an Agreement whereby:

a. Sub-A will sublease the 78 Manufacturer Aircraft to Company B for the remainder of the terms of Sub-A's Manufacturer Leases.

b. Sub-A will, subject to obtaining consents, sublease or otherwise transition its arrangements relating to the 10 Financing Company Aircraft to Company B. The sublease or other arrangements may include a purchase option in favor of Company B for these Financing Company Aircraft at the end of the sublease. If a purchase option is included, the purchase price at the end of the subleases will be set at the then fair market value for each aircraft.

Note: All subleases are intended to be treated as “leases” for U.S. Federal income tax purposes. Under all of the subleases between Company B and Sub-A, Company B (the Lessee) must meet certain requirements set forth in the lease or get prior written consent of Sub-A (the Lessor) before it may sublease or otherwise transfer the aircraft. Company B must maintain the aircraft and is responsible for carrying insurance on the leased aircraft during the terms of these subleases. The subleases would take effect and the aircraft would be transitioned from Sub-A to Company B over a 3 year period beginning in or about August 2013 and ending in or about December 2015.

2. Between Company B and the Manufacturer: Company B will enter into a separate agreement directly with the Manufacturer to lease the 78 Manufacturer Aircraft from the Manufacturer (the “Company B – Manufacturer Leases”) after the original Manufacturer Leases with Sub-A expire (and thus the point at which the aircraft would otherwise be returned to the Manufacturer by Sub-A). The new Company B – Manufacturer Leases will extend for several years, though again not for the useful life of the 78 aircraft. These leases will include a purchase option in favor of Company B at the end of the leases. The purchase price at the end of the leases will be set at the then fair market value for each aircraft.

C. HSR Analysis

We do not believe that any of the proposed lease transactions trigger HSR filing requirements, but wanted to confirm this conclusion with you.

Generally, entering into leases or subleases do not constitute an acquisition of the underlying assets unless the lease amounts to an installment sale of the property, where a lease exhausts the useful life of the property or where the lease otherwise results in the “present acquisition of the underlying asset.” (See interpretations 4, 26 and 97 of the ABA Antitrust Section, Premerger Notification Practice Manual.) Examples of a lease being viewed as a “present acquisition” of the underlying assets referenced in informal interpretations include: an example where an unduly high rental charge is coupled with an option under which the lessee may subsequently purchase the property as a nominal price. On the other hand if the lease agreement provides for normal rental payments and/or a subsequent purchase option at fair market value, the PNO has stated that the transaction is not an “acquisition” subject to HSR. It should be noted that the interpretations indicate that the HSR analysis for entering into a sublease is not affected by whether the sublease payments to the sublessor exceed the payments by the lessee/sublessor to the original lessor.

The interpretations indicate that to distinguish between a “purchase styled as a lease” and a “routine leasing transaction” the PNO looks to see whether the lease amounts to a present transfer of beneficial ownership. The PNO considers such factors as: the duration of the lease (e.g. whether the duration of lease encompasses the useful life of the asset); how the parties to the lease allocate the risk of loss or damage to the underlying property during the lease term; whether the lessee has a right to transfer its interest without the consent of the lessor; whether the lease is or will be shown as an asset on the financial books of either party; and how the lease is treated for tax purposes.

None of the leases or subleases involved in the proposed lease transactions described above constitutes the present transfer of the underlying assets.

As to the Company B - Sub-A subleases: Sub-A, with the knowledge and approval of the Manufacturer (for 78 of the aircraft) and the various Lessors for the Financing Company Aircraft (for the remaining 10 aircraft), is subleasing the 88 aircraft to Company B for the remaining time it has under its original leases. Its original leases and the new subleases are standard commercial leases within the airline industry. The duration

of the leases and proposed subleases are far shorter than the useful life of the aircraft. The sub-lessee (Company B) either has no right to the aircraft after the end of the sublease (in the case of the Manufacturer Aircraft), or can only acquire the aircraft for a payment of fair market value (in the case of the Financing Company Aircraft). The subleases are intended to be treated as leases for tax purposes, and the sub-lessee may not transfer or sublease the aircraft for the duration of the sublease unless it meets certain requirements set forth in the lease or secures Sub-A's consent. All of these factors are characteristic of "routine leasing transactions," not "purchases styled as leases."

As to the Company B - Manufacturer leases: These leases, which are effective for the 78 Manufacturer Aircraft once the Company B - Sub-A subleases expire, are also standard leases within the industry. The duration does not exhaust the remaining useful life of the aircraft, Company B must pay fair market value to the Manufacturer to acquire the aircraft at the end of the lease, and the lease payments are set at normal market rates. Again, these facts are characteristic of "routine leasing transactions."

For the above reasons, we believe that none of these lease transactions trigger HSR filing requirements. Please let us know if you agree with our conclusions.

Thanks very much for your help.

Regards,

[Redacted]

[Redacted]

AGREE
BM
6/28/12

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