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Verne, B. Michael

From: [REDACTED]
Sent: Wednesday, July 18, 2012 10:49 AM
To: Verne, B. Michael
Subject: HSR

Mike:

Buyer and Seller have agreed to a sale of Seller's business, but the structure is unusual, and we want to make sure we are analyzing this correctly. You may assume that the size-of-persons test (if applicable) would be satisfied. (Seller has several owners, and although we do not think this is relevant to the analysis, Seller is controlled for HSR purposes by a single shareholder who holds 50% or more of Seller's voting securities.)

At signing, Buyer acquire an option to purchase Seller's business. The option will be divided into two sequential options. The first option will permit Buyer to acquire up to a 25% interest in Seller's business. This first option is exercisable anytime from now until a specified date in 2017. The second option is exercisable only in 2017 (for a thirty-day period after the exercise period for the first option has run) and permits Buyer to acquire whatever share of the business it has not previously acquired.

Buyer will pay an "upfront amount" for the options; if Buyer exercises options, each exercise will require an "exercise payment." If the second option were exercisable today (which it is not), then the total of these three payments (the upfront payment and the exercise payments) would be below the current size-of-transaction threshold. The exercise payment on the second option is subject to an upward or downward adjustment depending on Seller's financial performance.

Seller is an "S" corporation. For tax reasons, Buyer will not actually acquire any voting securities in the "S" corporation at any time. (Acquiring such securities would disqualify the corporation from "S" treatment for tax purposes and subject it to corporate taxation.) Rather, when Buyer first exercises an option, the S corporation will drop its assets into an LLC. What Buyer will get is either up to 25% of the LLC interests (if it maximizes its exercise of the first option) or 100% of the interests (if it exercises the second option).

At the initial signing (that is, when Buyer has bought the options and made the upfront payment, but before it has exercised the options), Buyer will be entitled to appoint a director to sit on the "S" corporation's board and will be entitled to certain minority-protection rights (such as requiring minority consent to sale of assets or entry into a material contract). If Buyer decides to exercise its first option (for up to a 25% interest in the business), then, Buyer's director seat and minority protection rights will then shift to the LLC, and Buyer will no longer have a Board seat on the "S" corporation board.

We believe that this transaction is not reportable today, because Buyer is not acquiring either voting securities or an LLC interest. Nor is it reportable on exercise of the first option, because Buyer's acquisition of interests will not confer control of the LLC. Exercise of the second option is potentially reportable, because acquisition of the LLC interest will confer control of the LLC. Reportability will depend on the value of the LLC interests that Buyer will hold after exercise of the second option, which would be the sum of (i) the FMV of the any LLC interests that Buyer has previously acquired and still holds, and (ii) the purchase price (if "determined") or FMV (if purchase price is not "determined") for the LLC interests that Buyer acquires through exercise of the second option.

Do you agree?

[REDACTED]

AGREE -
BM
7/18/12
K. WALSH CONCURS.