April 26, 1988

FEDERAL EXPRESS
EXPEDITED ATTENTION REQUESTED

Mr. Wayne Kaplan
Federal Trade Commission
Room 303, Federal Trade Commission
Seventh and Pennsylvania
Washington, D.C. 20580

RE: Pre-Merger Notification Filing--Treatment of Intercompany Sales for Purposes of Application of FTC Rule 802.50

Dear Mr. Kaplan:

This letter is in regard to our telephone conversation concerning the treatment of intercompany sales for the purpose of determining aggregate sales under FTC Rule 802.50. The basic facts of our proposed transactions are as follows:

, the acquiring company, has assets and sales in excess of $100 million. proposes to purchase 100% of the capital stock of a company based and incorporated in the United Kingdom. owns 100% of the capital stock of four separate companies, one incorporated and based in Germany, one in Switzerland, one in Holland, and one in Austria. The Switzerland subsidiary owns 100% of the capital stock of a corporation incorporated and based in the State of North Carolina All of the operating subsidiaries of principally engaged in the business of manufacturing and sell

had sales during 1987 of $18.7 million and had assets at December 31, 1987 of $9.3 million. Neither nor any of its other subsidiaries had significant assets in the U.S. or made sales into the U.S. other than sales made to

manufactures from parts purchased from the German subsidiary of in 198

[redacted] purchased $6.7 worth of parts from the German subsidiary. [redacted] added approximately an additional $5.5 million in labor[1] and materials to those parts in 1987 to produce finished goods.

Applying those facts to Rule 802.50 leads, we believe, to the conclusion that this transaction is exempt from the notification requirement of the Act. Rule 802.50(b) exempts from the Act a U.S. Company's acquisition of stock of a foreign issuer unless either:

1. The foreign issuer has assets in the U.S. in excess of $15 million; or

2. The foreign issuer made aggregate sales in or into the U.S. of $25 million or more during its most recent year.

[redacted] the foreign issuer) total U.S. assets, on an aggregated basis, are $9.3 million; thus subpart 1 is satisfied. Whether subpart 2 is also satisfied depends on whether "aggregate sales" includes the $6.7 million in intercompany sales from [redacted] German subsidiary to [redacted] We believe that intercompany sales should not be included for the following reasons:

1. If intercompany sales are included in aggregate sales, then the intercompany sales will be included twice since [redacted], after additional manufacturing, resells the same items it purchases from the German subsidiary of [redacted]

2. Generally Accepted Accounting Principles ("GAAP") mandate the elimination of intercompany sales when computing the net sales of an entity. On at least three prior occasions the FTC has relied on GAAP in resolving questions concerning the premerger notification rules. See Letter to Barry J. Raingold, December 7, 1978, summarized in Premerger Notification Practice Manual, American Bar Association, ("Practice Manual"), No. 97; Letter to Mr. Thomas Hancock, April 6, 1979, summarized in the Practice Manual, No. 103; Letter

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1 [redacted] cost of sales for 1987 was approximately $12.4 million. Inventory levels at the end of 1987 were not materially different than levels at the beginning of the prior year.

to Dana Abrahamsen, February 1, 1982, summarized in the Practice Manual, No. 107.

3. When employing market share analyses in reviewing mergers under Section 7 of the Clayton Act, courts eliminate the effect of intercompany sales. See In re Corrugated Container Antitrust Litigation, 1981-1 (CCH) Trade Cas. ¶64,114. Cf. United States v Aluminum Corp. of America, 91 F. Supp. 333,356 S.D.N.Y. (1980).

4. FTC Rule 801.11 requires that sales be reported on a consolidated basis, which means the elimination of intercompany sales. If a reporting person does not prepare consolidated financial statements, then the rule requires that it recompute its sales to eliminate sales duplication. Although you questioned whether this Rule applies to transactions involving intercompany sales between a U.S. and a foreign corporation, the Rule clearly evidences the Commission's recognition of the fact that including intercompany sales in sales results in a double counting of sales.

5. The purpose of the Act would not be furthered by requiring the inclusion of intercompany sales in sales. The Act makes it possible for the FTC and the Justice Department to detect mergers that may adversely impact competition by requiring the disclosure of proposed mergers. A company obtains market share, and thus the ability to impact competition, by successfully selling to entities outside of the corporate family, not by shuffling product from one subsidiary to another as part of the process of manufacturing the product for final sale.

For these reasons, we believe that aggregate sales, as used in Rule 802.50(b)(2), do not include intercompany sales. Please advise of the position of your office on this matter. Please give this matter expedited attention and respond to me or [redacted] this office by Monday, May 9, 1988.

Very truly yours,

[redacted]

The letter ignores the Q of the indirect acquisition of the U.S. sub ([redacted]) which may be reportable if its U.S. bmn are over 15.0 MM [redacted] value. Otherwise the transaction is non-reportable pursuant to 802.50 since the import of parts would not be included in the $25.0 MM of U.S. sales or sales into the U.S. Wayne Kaplan 4-29-88.