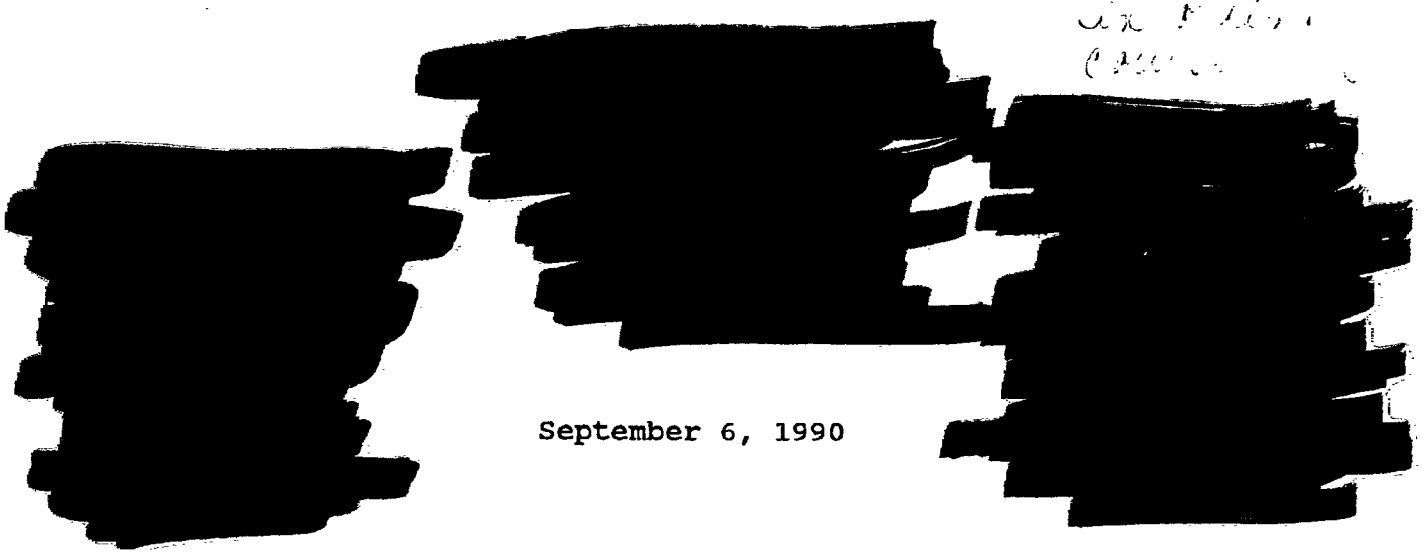

September 6, 1990

VIA OVERNIGHT COURIER

Premerger Notification Office
Bureau of Competition
Room 303
Federal Trade Commission
Washington, D.C. 20580

Attention: Ms. Nancy Ovuka

Re: Section 802.63 Exemption

Dear Ms. Ovuka:

As you may recall, I had several telephone conversations last month with Dick Smith and you regarding the applicability of the Section 802.63 exemption to certain types of sale-leaseback transactions routinely consummated by our client, a corporation that qualifies as a "real estate investment trust" or "REIT" under the Internal Revenue Code ("Code"). The purpose of this letter is to provide you with additional detail regarding our client and the specifics of a pending sale-leaseback transaction and to confirm your concurrence in our view that such a transaction is exempt from the reporting requirements of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the "HSR Act").

I. The Section 802.63 Exemption

Section 802.63(a) provides in pertinent part:

> An acquisition . . . in connection with the establishment of a lease financing . . . shall be exempt from the requirements of the act if made by a creditor in a bona fide credit transaction entered into in the ordinary course of the creditor's business.

I understand from our recent telephone conversations as well as a similar telephone conversation I had with Dick Smith in November 1989 that the Premerger Notification Office has concluded that Section 802.63 exempts sale-leaseback transactions as long as the acquiring person (1) takes title to the property and then leases the property back to the seller in a bona fide transaction, (2) engages in such sale-leaseback transactions in the ordinary course of its business, and (3) does not compete with the person to whom the property is leased.

II. [redacted]
Business

Our client, [redacted] ([redacted]), is a corporation engaged in the business of making passive investments in health care facilities and qualifies as a REIT under the Code. When considering the applicability of the Section 802.63 exemption, it is important to understand the significance and implications of what it means to be a qualifying REIT under the Code.

Generally speaking, a qualifying REIT under the Code is one that engages in long-term passive investments in real estate on behalf of a relatively large number of small investors. The Code provides special tax treatment for qualifying REITs. The principal feature of this special tax treatment is the absence of taxation at the corporate level -- that is, a qualifying REIT is not required to pay income taxes to the extent that it currently distributes its income to its shareholders.

The purpose of this special tax treatment is to encourage and facilitate long-term passive investments in real estate by small investors. In order to ensure that this broad purpose is achieved, Sections 856 through 860 of the Code and the regulations promulgated thereunder require that a corporation comply with a complex and technical set of rules before it is deemed a qualifying REIT eligible for the favored tax treatment.

As set forth below, these rules greatly restrict the business activities in which a qualifying REIT may engage.

In order to qualify as a REIT for a taxable year, the Code requires generally that (1) at least 75 percent of the total assets of the REIT must consist of real estate assets, cash, or governmental securities; (2) at least 75 percent of the REIT's gross income must be derived from real estate activities, including rents from real property and interest on mortgage obligations; (3) at least 95 percent of the REIT's gross income must consist of gross income derived from real estate activities plus dividends, interest, or gains from disposing of securities; and (4) gross income from the sale or other disposition of real property held for less than four years or from the sale of certain securities must comprise less than 30 percent of the gross income of the REIT.

In order for a REIT's income to qualify as "rents from real property," (1) the REIT may not own, directly or indirectly, ten percent or more of any entity that is its lessee; and (2) amounts received with respect to the leased property may not depend on the income or profits of the lessee. These requirements are intended to ensure that the REIT will not have a proprietary interest in the operation of the leased property.

The Code also discourages a REIT from buying and selling property as a dealer by imposing a 100 percent tax on the net income (not reduced by losses) from such sales with some limited exceptions and, in addition, extensive dealer activities could jeopardize the company's ability to maintain its status as a REIT under the Code.

The practical consequence of all of these provisions is that the business activities of a REIT are limited to investing on a long-term basis in mortgages or investing in real estate for the purpose of renting such real estate on an arm's-length basis to unrelated entities.

The REIT provisions in the Code also prohibit a REIT from actively managing or operating its property, either directly or indirectly through a property manager. Income from the operation or management of its property would not be qualifying income to a REIT under the 95 percent gross income test discussed above. Thus, even a small amount of such activity could

jeopardize its status as a REIT under the Code.[1/] In addition, with respect to property that a REIT leases to another entity, the REIT is restricted to providing only those services to its tenants that a tax-exempt organization may provide to its tenants without causing its rental income to be "unrelated business income." Generally, the services under this standard are those services which relate to the maintenance of the property itself, rather than services rendered to the lessee or with respect to the business of the lessee. As a result, a REIT generally must refrain from providing services for the benefit of its lessees or such lessees' businesses or it must employ an independent property manager to provide such services.

The failure to qualify as a REIT during any taxable year would have a material adverse effect on the REIT and its shareholders. The REIT would be subject to federal income tax at corporate rates on all of its taxable income and would not be able to deduct the dividends it paid, which could result in a discontinuation of or substantial reduction in dividends to shareholders. Dividends would also be subject to the regular tax

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1. There is one exception to this 95 percent gross income test limitation. Income derived by a REIT from the operation of "foreclosure property" will be treated as qualifying income under the 95 percent gross income test. A REIT may elect to treat as foreclosure property, property it acquires as a result of a foreclosure on a lease of the property or on a loan which was secured by the property. Property may qualify as foreclosure property for up to two years, unless extended with the permission of the Internal Revenue Service. A REIT may directly operate foreclosure property for no more then 90 days after the property is acquired by foreclosure and thereafter, the REIT may operate the property only through an independent property manager. The purpose of the foreclosure property provision is to allow a REIT to operate property it acquires through foreclosure while the REIT is attempting to re-lease or sell the property. REITs are discouraged from electing foreclosure property treatment because, while qualifying REITs generally are not subject to corporate income tax on income currently distributed to their shareholders, they are subject to tax on their net income from foreclosure property at the highest corporate tax rate. HCPI currently owns and operates, through independent property managers, two properties which qualify as foreclosure property. All of the other properties owned by HCPI are leased to unrelated lessees, and HCPI is attempting to re-lease these two foreclosure properties.

rules applicable to dividends received by shareholders of corporations.

The Code also requires that the shares of a REIT be held by at least 100 shareholders and that five or fewer individuals may not own more than 50 percent, in value, of the REIT's outstanding shares. As a result, no one shareholder can "control," within the meaning of the HSR Act, a qualifying REIT, and a qualifying REIT is always its own ultimate parent entity.

As mentioned above, [redacted] is in the business of making long-term passive investments in health care facilities. These investments are made in various forms, with each transaction being structured to provide a current return to HCPI's shareholders and to comply with the REIT provisions under the Code. Nearly all of such investments are sale-leaseback arrangements in which [redacted] acquires a health care facility from the owner of the facility and [redacted] then leases the facility back to the owner who will operate the facility. As a result of such a transaction, [redacted] acquires title to the property and derives rental income from the lease. From the operator's perspective, the sale-leaseback arrangement serves, in many respects, as a financing mechanism.

Once it acquires a health care facility, [redacted] does not (and could not without placing its REIT status in jeopardy) operate or manage the facility. As discussed above, [redacted] must lease the facility on an arm's-length basis to a third party and the REIT rules greatly limit HCPI's ability to provide services to its lessee. In fact, all of the properties currently leased by HCPI have been leased on a triple net basis whereby [redacted] provides no services to the lessees.

In sum, [redacted] routinely enters into sale-leaseback arrangements with operators of health care facilities. In these transactions, [redacted] acquires title to the real property and leases the property back to the operators in a bona fide lease. [redacted] is not in the business of operating or managing the health care facilities, but instead is in the business of investing, on a long-term basis, in the real property.

III. [redacted] Pending Sale-Leaseback Transaction With [redacted]

[redacted] and [redacted] ([redacted]) have recently signed a letter of intent that provides for the sale and leaseback of 15 health care facilities currently owned and operated by [redacted] and/or its affiliates. The total purchase price is $112.3 million, and the parties expect to close on ten of the properties as early as September 18, 1990, and on the remaining properties some time between February 15 and March 31, 1991, if certain conditions are met. This proposed transaction is typical of the type of sale-leaseback arrangements entered into by [redacted], as described in more detail in Part II above. A complete copy of the letter of intent is attached hereto as Exhibit A. We would ask that you maintain the confidentiality of the letter of intent and not disclose it to any third parties.

IV. Applicability of the Section 802.63 Exemption to the Sale-Leaseback Transaction Between [redacted]

Based on our understanding of Section 802.63 and our discussions with Dick Smith and you regarding this exemption, we believe that the sale-leaseback transaction between [redacted] and [redacted] is exempt from the reporting requirements of the HSR Act. First, in this sale-leaseback transaction, [redacted] will purchase and take title to all 15 health care facilities and will, in turn, lease the facilities back to [redacted] pursuant to bona fide leases. Second, this transaction is part of [redacted] ordinary course of business in that it is similar to the many other sale-leaseback transactions into which [redacted] has entered. As mentioned above, in order to qualify as a REIT under the Code, [redacted] must maintain certain long-term investments in real estate but is effectively prevented from operating or managing the real property in which it has invested. Sale-leaseback transactions are the logical result of the REIT restrictions. Third, because [redacted] is not (and cannot be) in the business of operating or managing health care facilities, [redacted] does not compete with [redacted] with respect to the operation of health care facilities. For all of these reasons, we believe that this pending transaction satisfies all of the elements of the Section 802.63 exemption.

We would greatly appreciate your concurrence in our application of the Section 802.63 exemption to the pending transaction between [redacted]. If you have any questions about [redacted] or this transaction, please do not hesitate to contact me at [redacted]

We look forward to hearing from you at your earliest convenience.

Sincerely,

[redacted]