

TO:

FROM:

DATE:

January 11, 1991

RE:

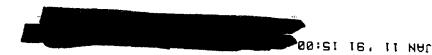
Application of the Jurisdictional Test to Enclosed Fact Pattern

We have several questions about valuing the consideration for the purpose of determining the Size-of-the-Transaction test in the following transaction:

Mr. Jones, an entrepreneur, entered into an agreement several months ago to buy out two subsidiaries from a company owned by him and a single foreign investor. Mr. Jones had sufficient funds to purchase Co. Y, but had to seek funds from other sources for Company X ("CX"). CX's fixed assets were appraised at that time by an industry expert approximately \$15 million and its current assets have been approximately \$6 million, for a total value of approximately \$21 million. However, an allocation was made in that transaction discounting CX's value to approximately \$11.5 million. (Because of assumed liabilities of approximately \$3 million, Mr. Jones' purchase price was approximately \$14.5 million.) In order to close this transaction, for which Hart-Scott notification had been properly made, Mr. Jones was required to borrow \$13,570,000 from a competitor, Comp (this amount included approximately \$2.0 million for a prepayment to the prior owners of CX regarding a covenant not to compete). In exchange for this loan, Mr. Jones agreed to repay the principal and 12% interest within 60 days and to pay a \$500 thousand fee. In the event he failed to make that payment, Comp was given an option to purchase CX's assets for \$14,490,000. Comp also was required to pay CX approximately \$2 million for a non-competition agreement in the event Comp exercised the option to purchase CX's assets.

OUR QUESTIONS RE: SIZE-OF-THE-TRANSACTION TEST:

- 1. Does the \$14,490,000 constitute Fair Market Value under §801.10(c)(3) when an industry expert has appraised the fixed assets at approximately \$6 million above the current purchase price, and the basis for that purchase price was understood to be a discounted value?
- 2. Must the valuation of the consideration in this transaction include the interest on the loan made to Mr. Jones, which has in fact accrued to a value of \$280 thousand, if Comp is willing to forgive that amount?



- 3. Must the valuation of the consideration include the \$2 million for the non-competition agreement to be paid to CX when the option is exercised?
- 4. Would it be permissible for the parties to agree now to reduce the purchase price, in order to get below \$15 million, by Comp's not purchasing approximately \$1.7 million in CX's receivables.

Thank you for your attention to this matter. Please advise as soon as possible. My telephone number is

- 1. Yes. If the finite (3/4,5MM) represents the Board of Directors of the acquiring persons good faith determination them it is the foir market value for those assets. Note: Value of these assets is either the accumition price or the fair market value whichever is higher.
- 2. No. les in the installment contract setting (see S.B.P. for \$861.10(0)(5)) interest should be excluded from the validation of consideration.
- 3. Yes. according to a long standing police, covenants that to compete should be included so part of valuation of costs.
- 4. Yes, If the parties node inch in agreement and Comp would not he getting those receivables through a disquised or share tensection, then it would premiosible to reduce the purchase since.