Walsh, Kathryn E.

From: Verne, B. Michael
Sent: Tuesday, June 24, 2014 10:24 AM
To: [redacted] Walsh, Kathryn E.
Subject: RE: Question Regarding Leveraged Acquisition

[redacted] - on first blush [redacted] description sounded like more than merely arranging (esp. "doing everything"). We didn't realize that we had made such a bright line distinction on the arranging of the loan. That said, we need to be consistent with the April 4, 2012 position unless we have some good basis for changing it, so we stand corrected. Do not include the loan proceeds. Thanks for keeping us on our toes ☺ Best - Mike

---

From: [redacted]
Sent: Tuesday, June 24, 2014 9:59 AM
To: Verne, B. Michael; [redacted] Walsh, Kathryn E.
Subject: RE: Question Regarding Leveraged Acquisition

Mike,

I apologize for jumping in, but because this is a typical LBO scenario, I would appreciate your clarification. Although the buyer is arranging the financing, the buyer is not incurring the loan, making the loan or financing the loan. This is no different than the April 4, 2012 advisory attached to [redacted] e-mail or advisory 0801014. In both cases, the buyer arranged the loan, but that did not make it part of the transaction value. Indeed, in the April 4, 2012 advisory, the PNO stated "Merely arranging the financing is not enough." Please help me understand how this transaction is different.

Thank you,

[redacted]

From: Verne, B. Michael [mailto:MVERNE@ftc.gov]
Sent: Tuesday, June 24, 2014 9:51 AM
To: [redacted] Walsh, Kathryn E.
Cc: [redacted]
Subject: RE: Question Regarding Leveraged Acquisition

[redacted] - based on that, we think that the buyer is involved enough in the loan process to require including the loan proceeds as part of the size of transaction.

From: [redacted]
Sent: Tuesday, June 24, 2014 9:49 AM
To: Verne, B. Michael; Walsh, Kathryn E.

13

Cc: [redacted]
Subject: RE: Question Regarding Leveraged Acquisition

Mike -

My corporate colleague tells me that Buyer essentially is "doing everything" to put the loan in place --- identifying potential lenders, selecting the lenders, negotiating the commitment/indication of interest letters, and negotiating the final terms of the credit agreement.

Please let me know if it would help to have a call with my corporate partner. We could arrange a time when Bob can join us.

Many thanks,

[redacted]

From: Verne, B. Michael [mailto:MVERNE@ftc.gov]
Sent: Tuesday, June 24, 2014 9:35 AM
To: [redacted]; Walsh, Kathryn E.
Cc: [redacted]
Subject: RE: Question Regarding Leveraged Acquisition

[redacted] - what specifically is the buyer doing to "arrange" the third party loan?

From: [redacted]
Sent: Tuesday, June 24, 2014 8:59 AM
To: Verne, B. Michael; Walsh, Kathryn E.
Cc: [redacted]
Subject: RE: Question Regarding Leveraged Acquisition

Mike -

Thanks for your prompt response. Just to clarify -- in our scenario, Buyer is arranging the loan to Target from the third party bank (but not providing the loan or guaranteeing it). Do you still agree that the loan proceeds are not included in the size of transaction?

Many thanks,

[redacted]

From: Verne, B. Michael [mailto:MVERNE@ftc.gov]
Sent: Tuesday, June 24, 2014 8:52 AM
To: [redacted] Walsh, Kathryn E.
Cc: [redacted]
Subject: RE: Question Regarding Leveraged Acquisition

[redacted] We lately have said on several occasions that if the proceeds of the loan are going to the interest holders of the Target, they should be included. But all of them involved the Buyer either arranging the loan, providing the loan, taking on the loan itself or guaranteeing the loan. None of these appear to be the case in this transaction. We agree that the loan proceeds are not included in the size of transaction.

From: [redacted]
Sent: Monday, June 23, 2014 5:09 PM
To: Verne, B. Michael; Walsh, Kathryn E.
Cc: [redacted]
Subject: Question Regarding Leveraged Acquisition

Hi, Mike and Kate -

[redacted] and I are working on the leveraged acquisition of privately-held LLC interests. We would like your guidance as to whether the debt to be incurred by the target ("Target") from a third party bank in connection with the acquisition can be disregarded in determining the purchase price for HSR purposes.

Assume in the following scenario that the size-of-person test is satisfied. Target's equity holders ("Sellers") will form a new LLC ("Holdco") and exchange their interests in Target for interests in Holdco. Target then will borrow approximately $51 million from a third party bank and will distribute the proceeds of the loan to Holdco, which, in turn, will distribute such proceeds to Sellers immediately prior to the transaction. The loan will be secured by Target assets and Target equity and is contingent on the purchase of Holdco LLC interests by the buyer ("Buyer"). Buyer is arranging the financing, but will not guarantee payment of the loan, nor provide funding for the loan. Target would not have incurred the loan but for the sale of Holdco LLC interests to Buyer. Moreover, distribution of the loan proceeds to Sellers is contingent on the purchase of the Holdco LLC interests by Buyer.

Buyer then will acquire 65% of the LLC interests of Holdco for a payment of approximately $52 million to Sellers after payment of transaction expenses. (The purchase agreement provides that the purchase price will be the product of (a) 65% <u>multiplied</u> by (b) the value of 100% of Target interests prior to Target incurring the debt (as agreed by Buyer and Sellers) <u>less</u> the proceeds from the third party bank loan <u>plus</u> Buyer transaction expenses.) Sellers will retain the remaining 35% of the Holdco LLC interests. Consequently, Sellers will receive a total of approximately $103 million combined from the third party loan proceeds and Buyer payment.

In view of the facts that Buyer is not incurring the loan, providing the loan, or guaranteeing the loan, [redacted] believes that the amount of the loan should not be included in the value of the transaction. This conclusion is supported by the attached informal interpretation, dated April 4, 2012, as well as by earlier informal interpretations 0801014 (http://www.ftc.gov/enforcement/premerger-notification-program/informal-interpretations/0801014) and 0404012 (http://www.ftc.gov/enforcement/premerger-notification-program/informal-interpretations/0404012).

Other informal interpretations, however, including the attached LBO scenarios you worked through with [redacted] in 2008 indicate that the loan should be included in the transaction value. See the attached informal interpretation from 2008 and informal interpretation 0909001 (http://www.ftc.gov/enforcement/premerger-notification-program/informal-interpretations/0909001). We note that in each case above, however, the buyer or its subsidiary either incurred the loan, provided the loan, or guaranteed the loan.

Is the attached April 4, 2012 informal interpretation the PNO's current position on leveraged acquisitions such that the purchase price in our scenario described above is $52 million and the transaction, consequently, is not reportable under HSR?

As, always, many thanks for your assistance.

Best,

[redacted]

****

IRS Circular 230 Disclosure:
To ensure compliance with requirements imposed by the U.S. Internal Revenue Service, we inform you that any tax advice contained in this communication (including any attachments) was not intended or written to be used, and cannot be used, by any taxpayer for the purpose of (1) avoiding tax-related penalties under the U.S. Internal Revenue Code or (2) promoting, marketing or recommending to another party any tax-related matters addressed herein.

The information contained in this communication is confidential, may be attorney-client privileged, may constitute inside information, and is intended only for the use of the addressee. It is the property of [redacted] Unauthorized use, disclosure or copying of this communication or any part thereof is strictly prohibited and may be unlawful. If you have received this communication in error, please notify us immediately by return e-mail or by e-mail to [redacted] and destroy this communication and all copies thereof, including all attachments.
****

****

IRS Circular 230 Disclosure:
To ensure compliance with requirements imposed by the U.S. Internal Revenue Service, we inform you that any tax advice contained in this communication (including any attachments) was not intended or written to be used, and cannot be used, by any taxpayer for the purpose of (1) avoiding tax-related penalties under the U.S. Internal Revenue Code or (2) promoting, marketing or recommending to another party any tax-related matters addressed herein.

The information contained in this communication is confidential, may be attorney-client privileged, may constitute inside information, and is intended only for the use of the addressee. It is the property of [redacted] Unauthorized use, disclosure or copying of this communication or any part thereof is strictly prohibited and may be unlawful. If you have received this communication in error, please notify us immediately by return e-mail or by e-mail to [redacted] and destroy this communication and all copies thereof, including all attachments.
****

****

IRS Circular 230 Disclosure:
To ensure compliance with requirements imposed by the U.S. Internal Revenue Service, we inform you that any tax advice contained in this communication (including any attachments) was not intended or written to be used, and cannot be

[redacted]

Fr [redacted]
Sent: Wednesday, April 04, 2012 6:10 PM
To: [redacted]
Subject: LBO Exchange with PNO

Bob: Here's the exchange we had with the PNO. Let me know if you have any questions.

[redacted]

[redacted]

From: Verne, B. Michael [mailto:MVERNE@ftc.gov]
Sent: Wednesday, April 04, 2012 2:42 PM
To: [redacted]
Cc: Pope, Susan H.
Subject: LBO

[redacted] after reading the more detailed hypo, I agree with the conclusion that this is a $35 million deal. My first read of [redacted] description was that the Buyer was providing the $35 million in financing, which would be the same as paying an additional $35 million for the voting securities (i.e., same as $35 million in cash and $35 million in a note). The distinction we make on these LBO transactions is that if the Buyer is providing the financing or guaranteeing it, the amount financed is included in the value of the transaction. If the financing is through a third party and is not guaranteed by the Buyer, it is not included. Merely arranging the financing is not enough.

From: [redacted]
Sent: Tuesday, April 03, 2012 4:30 PM
To: 'spope@ftc.gov'
Cc: [redacted]
Subject: RE: LBO Transaction

Hi Susan –

[redacted] shared your email conversation with me, and I wanted to jump in to make sure that the issues in our transaction were clearly stated. Our client is engaged in what we consider to be a typical lev[illegible]ed buyout transaction. Several informal staff opinions have found such transactions to be non-rep[illegible]ble on similar facts, and our client has asked for confirmation. Your response to [redacted] suggests that the leveraging of a business might be thought of as "consideration." While I think that conclusion could be possible in some cases, I don't think it applies here, and we would like to clarify. Here are the facts of our transaction in a bit more detail:

(1) Buyer and Target will create two transaction vehicles solely for the purposes of this transaction – Sub A to be controlled by Buyer and Sub B to be controlled by Target. Sub B will contain the operating entity that is the subject of the acquisition.

(2) At closing, the parties will engage in a "two step" transaction that will involve (a) an investment by the Buyer and (b) a third-party financing of the operating entity that will leverage the acquired company and allow current shareholders to redeem their own interests. In detail –

(a) Sub B (operating company) will be merged into Sub A;

(b) Buyer will pay $35 million for an equity stake in the merged entity;

(c) Third Party Bank will loan Sub A $35 million against the acquired assets. Buyer is neither providing the financing nor guaranteeing the loan; and

(d) Target shareholders will receive the proceeds of the third-party loan (leveraging the business and reducing its value), the acquisition price from the Buyer, and a minority interest in the now-leveraged Sub A.

As is typical with leveraged buyouts, the result of the transaction is that the value of the acquired company is diminished, and the Buyer's ownership percentage is increased. The value of the Buyer's equity interest ($35m) remains constant.

Analysis:

We consider this transaction to be non-reportable for at least two reasons. First, to state the obvious, the notification requirement is based on the value of the acquired assets or securities. *See* 15 USC 18A(a) (notification required if "as a result of such acquisition, the acquiring person would hold an aggregate total amount of the voting securities and assets of the acquired person ...in excess of [$68.2m])." The value of the acquired securities is determined by the acquisition price or the fair market value. 16 CFR 801.10 and 801.13. In either case, the key consideration is the value of the securities or assets to be held by the acquirer. In our leveraged buyout described above, the value of the security interest to be held by Buyer is precisely $35 million as a result of the transaction. If Buyer were to sell its acquired security interest immediately after the transaction, the Buyer's investment in the leveraged company would still be worth $35 million, regardless of how much value is extracted by the current shareholders due to company leveraging. As such, we conclude that the Buyer's investment is not reportable. This seems to be the exact conclusion reached by the Staff in informal opinion 0801014 (Verne, at http://www.ftc.gov/bc/hsr/informal/opinions/0801014.htm).

Second, any redemption of shares or special dividends to the Target's current shareholders for the purpose of leveraging the company would seem to be exempt as intraperson transactions under 802.30. For example, Target could take out a loan today, distribute the cash to shareholders (or redeem shareholder stock), and thereby leverage the company in a non-reportable transaction. The fact that they would do this as part of a two-step leveraged buyout does not change the exempt nature of the transaction. This also seems to be the conclusion reached by the Staff in informal opinion 404012 (Verne, at http://www.ftc.gov/bc/hsr/informal/opinions/0404012.htm).

Finally, we think it is fairly plain that this sort of transaction structure is not intended as a means of avoidance. Leveraged buyouts are a common and important vehicle for aligning private equity, financial institutions, and shareholders to achieve the most efficient use of capital. Please assume that there are legitimate reasons for this structure when considering whether it is notifiable.

Based on the facts and analysis above, we believe that the Buyer has no obligation to make a notification under the HSR Act. If we have misunderstood the staff opinions referenced above, please let us know. And apologies for our failure to provide a complete analysis in the first instance. If we can provide any additional information or if you would like to discuss, please don't hesitate to ask.

Thanks for your help!

[redacted]

[redacted]

"Verne, B. Michael" <MVERNE@ftc.gov>

05/01/2008 02:46 PM

To [redacted]

cc "Bruno, Marian" <MBRUNO@ftc.gov>, "Berg, Karen E." <KBERG@ftc.gov>, "Walsh, Kathryn" <kwalsh@ftc.gov>

Subject RE: LBOs

[redacted]- sorry to take so long to get back to you. We have discussed this issue among ourselves and have concluded that all of the scenarios should be valued at $100 MM. Here are the factors that we think should lead us to the conclusion that in each of these transactions the value is $100 MM.

1) In each of these scenarios the shareholders of the target are receiving $100 MM for their voting securities. Because these are non-publicly traded issuers, the acquisition price is determined, so a fair market valuation at any point is irrelevant to the value analysis.

2) In each scenario the debt of the target that makes the value of its voting securities $50 MM after closing is not pre-existing debt, but debt that is introduced at closing to help the buyer finance the acquisition.

3) In Scenario 1, the buyer acquires the voting securities of the target (for $50 MM in cash and a $50 MM note) prior to the bank lending the target $50 MM to retire the note. So for an instant, the buyer holds debt free voting securities of the target, valued at $100 MM. The debt is then incurred by the target, reducing its value to $50 MM.

4) In Scenario 2, the loan from the bank is to the buyer, not the target, so at the time the voting securities of the target are acquired, the target is still debt free (and valued at $100 MM). It is only after the buyer merges down into the target that the debt is transferred to the target, reducing its value to $50 MM.

5) In Scenario 3, the analysis is basically the same as Scenario 2, except instead of the buyer directly receiving the loan proceed and then merging down into the target, a new wholly-owned subsidiary of the buyer receives the proceeds and merges down into the target.

I'll be happy to discuss any of these points further if you need to. Regards - Mike

-----Original Message-----
From: [redacted]
Sent: Thursday, May 01, 2008 12:06 PM
To: Verne, B. Michael
Subject: Re: LBOs

I understand. I know you were all busy to meet the Wednesday deadline. If you can have something this afternoon, that would be great. Thanks.

[redacted]

"Verne, B. Michael" <MVERNE@ftc.gov>

05/01/2008 11:04 AM

To [redacted]

cc

Subject LBOs

[redacted]- sorry it's taking a while to get everyone together here. We should have an answer for you this afternoon. Thanks for your patience.

[redacted]

****
The information contained in this communication is confidential, may be attorney-client privileged, may constitute inside information, and is intended only for the use of the addressee. It is the property of [redacted]
Unauthorized use, disclosure or copying of this communication or any part thereof is strictly prohibited and may be unlawful. If you have received this communication in error, please notify us immediately by return e-mail or by e-mail to postmaster@kirkland.com, and destroy this communication and all copies thereof, including all attachments.
****

Hypothetical LBO Transaction Structures

Scenario 1

Buyer and Target (assume no debt outstanding on Target's books pre-transaction)

Shareholders of Target will receive $100 million pursuant to a Stock Purchase Agreement entered into with Buyer

Shareholders receive $100 million
- $50 million in cash from Buyer
- $50 million note from Buyer to Target shareholders

Buyer acquires voting stock of Target

Bank lends $50 million to Target

Buyer immediately pays off note to Target shareholders with borrowings made by Target

Scenario 2

Buyer and Target (assume no debt outstanding on Target's books pre-transaction)

Shareholders of Target will receive $100 million pursuant to a Stock Purchase Agreement entered into with Buyer

Shareholders receive $100 million
- $50 million in cash from Buyer
- $50 million in cash from loan by Bank to Buyer

Buyer acquires voting stock of Target and then merges down into Target with Target surviving.

Scenario 3

Buyer and Target (assume no debt outstanding on Target's books pre-transaction)

Shareholders of Target will receive $100 million for an acquisition of Target stock by Buyer through a merger pursuant to a Merger Agreement

Buyer will form a subsidiary (will be borrower)
- Subsidiary will be merged into Target with Target surviving
- Shareholders receive $100 million (Note: Sometimes the payment is made pre-merger and sometimes it is made post-merger.)
  - $50 million in cash from Buyer
  - $50 million from borrowings of Subsidiary of Buyer

NOTE: In all scenarios, the shareholders of Target receive $100 million for the voting securities of Target (Buyer makes such $100 million payment to Target shareholders and funds such payment through its cash contribution and through borrowings (or causing various entities to assume debt) as described in the above scenarios.); however, if Target was sold again the next day, the new shareholders of Target would receive only $50 million for the voting securities of Target because of the debt put on the books of Target through the leveraged buyout.