From: Storm, Evan
To: [redacted]
Cc: [redacted]
Subject: RE: Question about application of 802.2(c) and 802.2(a)
Date: Thursday, May 05, 2016 11:18:56 AM

[redacted]

This would qualify as unproductive real property under 802.2(c) based on the equipment and work needed to complete the hospital.

Regards

Evan

From: [redacted]
Sent: Thursday, May 05, 2016 9:11 AM
To: Walsh, Kathryn E.; Shaffer, Kristin; Storm, Evan; Whitehead, Nora
Cc: [redacted]
Subject: Question about application of 802.2(c) and 802.2(a)

Hi all,

I would like to confirm the applicability of two alternative 802.2 exemptions applicable to the acquisition of a newly constructed but partially completed acute care hospital building ("Building"). Buyer would acquire the Building in the context of bankruptcy proceedings for approximately $115 million.

The first possible exemption is 802.2(c) (unproductive real property). The Building has not yet opened for operation and currently has some of the operating equipment necessary to operate as an acute care hospital but the equipment is not part of the bankruptcy sale and even if it can be acquired it is not sufficient to operate the hospital. Even if Buyer does acquire the equipment existing in the Building, they would need to spend approximately $14 million to install additional equipment to get the hospital operational. The time to install the equipment after close would be approximately 3 to 4 months. Additional expenses and time would be incurred for completing the facilities' mechanical systems, IT build out and obtaining necessary licenses. Although 802.2(c)(2)(i) states that this exemption does not apply to facilities that have not yet begun operation, the FTC Statement of Basis and Purpose applicable to 802.2(c) states that this exclusion of new facilities from the 802.2(c) unproductive real property exemption is "intended to apply to 'turnkey' facilities, i.e., new facilities capable of commencing operations immediately with minimal additional capital expenditure. . . . A new facility that is partially complete, is not ready to commence operation in the immediate future and requires substantial additional capital investment is not yet a manufacturing or non-manufacturing facility within the meaning of 802.2(c)(2)(i). Such a facility may qualify as unproductive real property." Further, example 6 to 802.2 indicates that if the building "does not contain the equipment" necessary to operate and "requires significant capital investment before it can be used" then it may qualify as unproductive real property. See also https://www.ftc.gov/enforcement/premerger-notification-program/informal-interpretations/1511001 ("To determine whether 802.2(c) applies, we look to whether the structure is a facility, meaning it is capable of commencing operations immediately with minimal additional capital investment."). Would you agree that given the time and expense necessary to commence operations the Building is not a facility under 802.2(c), and thus qualifies for the 802.2.(c) exception?

Alternatively, if the Building is deemed a facility not exempt under 802.2(c), we are of the view that it should be exempt under 802.2(a) (new facilities held for sale by the acquired person). Here, the Building was constructed and held for the purpose of leasing to a third party hospital operator, although the terms of the lease are such that the lease should be treated as the transfer of beneficial ownership of the Building (i.e., a sale) as discussed in informal opinion 24 in the PNO Manual 5th edition. The lease that the Seller had contemplated prior to entering bankruptcy was a long term 20 year lease, with a tenant right to sublease. The leased premises consist of: certain land, the Building and other improvements to be constructed on the land, and the machinery and equipment paid for and installed by landlord, attached to the Improvements in such a manner as to become fixtures. Tenant could not terminate the lease over this 20 year period and tenant had the sole right to extend for up to 2 consecutive 5-year periods, resulting in a 30 year lease approximating the vast majority of the useful life of the Building. The lease is a triple net lease meaning that the tenant is responsible for all costs including taxes, insurance and maintenance. Assuming the Building does not qualify for the unproductive real property exemption but is instead a new facility, given the duration of the lease and the allocation of costs and risks to the tenant, would you agree that its acquisition is exempt under 802.2(a) as the nature of the contemplated lease is such that the Building was held by the acquired person (Seller) at all times solely for what is essentially sale?

Many thanks,

[redacted]