801.10

[redacted]

[redacted]

September 17, 2001

Ms. Nancy M. Ovuka
Premerger Notification Office
Bureau of Competition
Federal Trade Commission
6th Street & Pennsylvania Avenue, N.W.
Washington, D.C. 20580

Re: <u>Advice Concerning Size of the Transaction</u>

Dear Ms. Ovuka:

As a follow-up to our conversation of August 20, 2001, we seek confirmation that the transaction described below would not necessitate the filing of Premerger Notification and Report Forms under the Hart-Scott-Rodino Antitrust Improvement Act of 1976, as amended.

[redacted]) leases or leased about 59 operating facilities (the "<u>Facilities</u>") from [redacted] and owns the leasehold improvements, equipment and other tangible assets located at those Facilities.[1] In Septembe[redacted]nd subsidiaries of [redacted] (collectively, [redacted] entered into a number of substantially similar sublease agreements (the "<u>Subleases</u>") under which [redacted] subleased all of [redacted] rights in the leases relating to the Facilities and the leasehold improvements, equipment and other tangible assets at the Facilities. Since September 199[redacted] has been making periodic rental payments to [redacted] under the Subleases and conducting [redacted] operations at a large portion of the Facilities.

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[1] In addition, [redacted] currently owns one parcel of real property which it leases [redacted] also leases from [redacted] the related improvements, equipment and other tangible assets located at this property). This property leased from [redacted] by [redacted] and the related improvements, equipment and other tangible assets are also subject to a Purchase Option in favor of [redacted] similar to that described herein.

[redacted]

Each Sublease has a term of six years (or shorter in some cases), and, in most cases, contains a purchase option (a "Purchase Option"), which is exercisable by [redacted]t any time during the term of the Sublease and for a short period after the expiration of the term.[2] All of the Purchase Options are linked, such that if any are exercised all must be exercised. Upon the exercise by [redacted] of these Purchase Options, in exchange for the payment of a specified dollar amount (the "Purchase Price"), [redacted] will assign t[redacted] all of [redacted] right, title and interest in the leases, leasehold improvements, equipment and other tangible assets that are the subject of the Subleases and the Subleases will terminate in accordance with their terms. The Purchase Price under each Sublease was calculated under a formula which was intended to result in a Purchase Option exercise price equal to fair market value of the assets covered by the Purchase Option at the time of exercise. [redacted]currently intends to exercise the Purchase Options contained in all of the Subleases. Subsequent to exercise of the Purchase Options, [redacted] as the lessee under the leases, will pay the rent due under the leases with respect to the Facilities directly to the third party landlords. (These rental payments are not included in the aggregate Purchase Price.)

The aggregate Purchase Price which would be payable by [redacted] to [redacted]oday under all of the Subleases in consideration of [redacted] exercise of all of the Purchase Options is approximately $30.5 million[3]. [redacted] would pay the aggregate Purchase Price to [redacted] in cash, by assumption of [redacted] senior secured term debt, by assumption of certain other liabilities o[redacted] or by a combination of the foregoing methods. For the purposes of this letter, please assume that the approximate fair market value of the Facilities does not exceed $30.5 million.

Certain of the Facilities which are currently the subject of Subleases are idle, and are not being put to use by [redacted] or [redacted] (the "Idle Facilities"). Nonetheless, due to the linked nature of the Purchase Options, [redacted] will be required, and intends, to exercise the Purchase Options under the Subleases which relate to the Idle Facilities. However, [redacted] intends to account for the future rent payable to the landlords under the acquired leases relating to the Idle Facilities on its financial statements in a particular manner which is different from the manner in which it will account for the leases which it assumes that relate to Facilities which are not Idle Facilities. Prior to the exercise by [redacted] of the Purchase Options, [redacted]will treat the leases relating to the

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2 The purchase options were issued to [redacted] May of [redacted]95. Premerger Notification and Report Forms were filed by [redacted], the ultimate parent entity o[redacted] 1995, and [redacted]oration ("Holdings") in connection with a series of transactions between [redacted]nd [redacted] and its subsidiaries and certain other parties.

3 The facility owned by [redacted]nd leased to [redacted]hat is mentioned in Note 2 is included in the $30.5 million Purchase Price.

[redacted]

Idle Facilities as effectively worthless and therefore recognize a one-time expense equal to the present value of the future rent for the Idle Facilities and book a related reserve of its balance sheet for a liability in the same amount. In accounting for the Purchase Option exercises, [redacted] will book a balance sheet reserve relating to the Idle Facilities in an amount equal to that booked by [redacted] will in fact continue to make periodic payments of rent to the landlords on the Idle Facilities when such rent is due under the terms of the applicable leases. However, as such rent is paid, rather than recognize an expense on its income statement with respect to these rent payments, [redacted]ill reduce the balance sheet reserve relating to the Idle Facilities. In the event that an Idle Facility is ultimately put to valuable use by [redacted] the accounting treatment of the rent payments relating to such Idle Facility may be modified and the balance sheet reserve reduced accordingly.[4]

The issue on which we have previously solicited your advice is whether the amount of the liability relating to the Idle Facilities which [redacted] will book on its balance sheet should be properly treated as purchase price for the purposes of determining the aggregate acquisition price to be paid by [redacted]pon the exercise of the Purchase Options (*i.e.*, for the purposes of the so called "size of the transaction" test). In our telephone conversation, you indicated that, in your opinion, the balance sheet liability to be booked by [redacted] does not need to be aggregated to the acquisition price for the purposes of the "size of the transaction" test, but rather, that on the basis of the foregoing facts, you would consider the "size of the transaction" to be the $30.5 million acquisition price, exclusive of the balance reserve for the future rent on the Idle Facilities as described above. With regard to determining the "size of the transactions" test, I would very

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[4] In accounting for the Purchase Option exercises, [redacted]will also record credit balances equal to those currently recorded o[redacted]alance sheet that relate to the expense recognition for the leases to be acquired by [redacted] One such balance tha[redacted]ill record at the time of the Purchase Option exercises is a "deferred rent payable" currently recorded on[redacted]alance sheet. Where cash rental payments vary significantly over the term of a lease, generally accepted accounting principles [redacted] require the recognition of the rent expense on an even basis over the lease term. Accordingly, [redacted]as recorded a deferred credit on its balance sheet for the leases to be assigned to [redacted] These credit balances will be recognized by [redacted]t the time of the Purchase Option exercise. [redacted] will recognize a portion of that balance each month as a credit to rent expense over the remaining lease term. In accounting for the Purchase Option exercises, [redacted]will record a total "deferred rent payable" relating to the acquired leases of approximately $11.6 million. By doing so, [redacted]ill avoid recording rent expense already required by [redacted]o be recognized by [redacted]in the early portion of the lease terms when it is paid in the future.

[redacted]will also record a credit of approximately $9.3 million arising from the accounting by [redacted] for certain of the leases to be acquired by [redacted]hich were included in a previous [redacted]le leaseback transaction. This balance, a deferred gain, will be recognized by [redacted]ion of rent expense paid over the remaining term of the leases that comprised the sale leaseback transaction.

much appreciate it if you would (i) reconfirm your position that the balance sheet reserve described above would not need to be aggregated to the acquisition price and (ii) confirm that [redacted] recordation of the credit balances described in Note 4 of this letter would not require [redacted] aggregate the value of such credit balances with the acquisition price.

If I can address any additional questions or concerns, please do not hesitate to contact me.

Very truly [redacted]

cc [redacted]

09/26
Confirmed advice w/ writer

MV concurs

[redacted]