801.40

**Michael Verne**

**From:** [redacted]
**Sent:** Wednesday, December 18, 2002 2:55 PM
**To:** Michael Verne
**Subject:** Follow-up on prior call

Mike - per my voice mail - a month ago we discussed a transaction (on which you consulted with Nancy Ovuka). I wanted to follow up on a twist. There are 4 physician practices that are going to create a new "parent." By way of background, the 4 practices have different structures. 1 is a NFP Corp., 2 are for profit corporations, and the last is a taxable NFP corporation (whatever that is). They intend to form a new "Parent," which will happen on Day 1 (more on its structure later). Each of the 4 practices will get some position (i.e., board rights / voting rights) in the Parent. The 4 practices are going to, in essence, give control of their operations to the new Parent several months after Day 1. This likely will happen by having the Parent become the sole corporate member of the NFP Corp, and be given contractual governance rights to the three other corporations which will! "mirror" the rights it has as the sole corporate member of the NFP Corp. You advised that if the Parent is a not-for-profit corporation, the Premerger office would treat this as exempt by analogy to Rule 802.40, which exempts the formation of not-for-profit joint ventures. The whole transaction, including the Parent formation and its subsequent acquisition, several months after its formation, of sole corporate membership of the NFP Corp. and contractual control rights of the other for-profit practice groups (all of which are contemplated at the time of the formation), would be exempt. The key to this analysis, I think was the fact that Parent was a NFP (and the structure of the existing practices did not matter). Please let me know if you think I've missed anything on this.

I just learned that there may be a slight wrinkle. I don't think it should change the analysis, but wanted to run it past you. The parties contemplate the structure above. However, Parent, after being created as a NFP under state law, will need to apply to be treated as a tax exempt entity under 501(c)(3) or 501(c)(4). That application likely would not be made for months after its formation, and the IRS determination likely would not be made for something like a year following the formation of Parent. I don't think that should matter -- if the parties, acting in good faith, form it as a not for profit venture, I think that should be sufficient even if it later needs to be converted into a for profit venture. That is, the formation is the potentially reportable event, and it was exempt when formed. Do you concur with that?

Alternatively, in the "worst case," this could be viewed as an 801.40 joint venture formation. Each of the 4 practices contributing would need to determine the fair market value of the interest it was taking back in the Parent (which would be viewed as holding any rights it will be acquiring in each of the 4 practices when those contributions are made). If none of those interests in the parent would be worth $50 million, then no filing would be required. No further analysis would need to be done when the parent took the contractual control rights / became the sole corporate member of Parent, as those "acquisitions" would be events in the formation (even though occurring after the date of formation). Here, the Parent is going to have control rights, but essentially no financial interest in the four practices that it will control. Essentially all of the revenues derived at the practice level w! ill be taken out at the practice level (either as expenses, or as salary / profits by the physician owners of the practices), and would never be available to / for the benefit of Parent. Thus, it seems very unlikely that anyone would view its shareholding in a for-profit Parent has having any significant value (and not approaching the $50 million threshold), but each of the four practice groups would need to make such a determination under the HSR rules.

Do you see any flaws in this analysis, or anything I am missing? Please feel free to send a note back, or call me if there is anything of significance that you think needs to be discussed.

As always, thanks for your help.

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email:

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For more information on N[redacted]& [redacted]ease visit our website at:

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AGREE -
B. Mc[illegible]
12/20/02