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Verne, B. Michael

From: [redacted]
Sent: Wednesday, May 23, 2007 3:22 PM
To: Verne, B. Michael
Cc: [redacted]
Subject: HSR question

Mike,

Thanks again for taking the time to review the below scenario with us. As we discussed, the purchase price for the transaction is determined and below the statutory size-of-transaction test, so no filing is required. Please let us know if our understanding is incorrect.

The particular facts are as follows:

Through an investment banking firm, the target solicited and received multiple proposals for an acquisition of voting securities via a reverse triangular merger. The request for proposals provided that the tax benefits from the target's activities prior to closing were to be retained by the selling shareholders and option holders and that these tax benefits would not be available to the acquirer.

The target selected a successful candidate from among the bidders. The acquirer will pay a purchase price of $59.5 million in cash for the voting securities of the target. The agreement includes some additional features that we wish to confirm will not constitute part of the acquisition price.

First, to ensure that the tax benefits for pre-closing activities will be retained by the selling shareholders and option holders, the target will declare a dividend prior to closing that assigns to the selling shareholders the value of those tax benefits. The purchase price allocation formula will be calculated so that option holders, whose options will be canceled at closing, also share in the amount of those pre-closing tax benefits. By this means, the tax benefits will no longer be assets of the target as of the closing. The tax benefits consist primarily of tax refunds that have been claimed for research tax credits and loss carrybacks arising from the deduction of employee stock option benefits. The total value of the tax benefits to be distributed is approximately $2.4 million.

Second, the merger agreement contains an adjustment based on a comparison of the target's actual working capital as of closing against the parties' current forecast of the working capital as of closing. The $59.5 million purchase price is based on an assumed working capital balance at closing of $5 million, an amount that is consistent with the target's recent history. The target plans to dividend or retain cash as necessary to minimize the amount of any working capital adjustment. If working capital is below $5 million at closing, the seller owes the difference to the acquirer. If working capital is above $5 million, the acquirer owes the difference to the seller. The parties reasonably believe that the adjustment will be zero, a belief that is reinforced by the ability to control the adjustment by managing cash through dividends or accumulation. Also, the transaction will close on or before June 30, so we do not expect any material changes in company operations in the short pre-closing period.

Regards,

[redacted]

AGREE
BV 5/23/07

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