801.40; 802.60

February 5, 1992

BY FAX AND BY MAIL

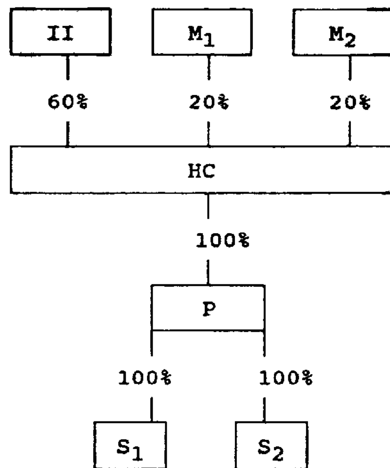
Richard B. Smith, Esquire
Federal Trade Commission
Premerger Notification Office, Rm. 398
6th Street and Pennsylvania Avenue, NW
Washington, DC 20580

Dear Mr. Smith:

I would like to discuss with you whether we are correct in concluding that the transaction described below is not reportable under the Hart-Scott-Rodino Antitrust Improvements Act of 1976.

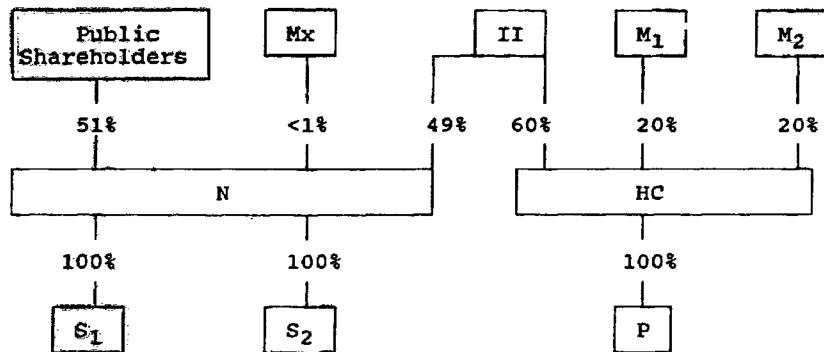
The transaction is essentially a spin-off, through a public offering, of two corporate subsidiaries into a new entity, with a corresponding reduction of the pre-transaction ultimate parent's interest in the entity controlling those subsidiaries from 60% to 49%. The proceeds of the public offering will be used largely to repay certain obligations of the subsidiaries and its pre-transaction parent company. The transaction will consist of a series of steps outlined in the enclosed Description of Transaction. However, all of these steps are necessary parts of a single, indivisible transaction, and none of these steps can or will occur independently of any of the others. We therefore think it proper to view the transaction as a single, indivisible transaction, rather than analyze each intermediate step separately. See ABA Premerger Notification Practice Manual, 1991 Edition, #70.

The two subsidiaries in question (S_1 and S_2) are currently wholly owned by a parent company (P), which is in turn wholly owned by a holding company (HC). The voting securities of HC are held by an institutional investor (II) and two individuals (M_1 and M_2), in the following proportions: II = 60%, M_1 = 20%, M_2 = 20%. The structure can be visualized as follows:



The spin-off of S_1 and S_2 will be accomplished by forming a new company (N), whose shares will be held by II (@ 49%), certain managers of S_1 and S_2 (not M_1 or M_2) (< 1%) and public shareholders (@ 51%), giving rise to the following structure:

Post-Acquisition Structure



We think the resulting change in structure should not be reportable under the following analysis:

1. The acquisition of N shares by management shareholders (M_x), none of whom will at any time hold 50% or more of N's outstanding voting shares, and all of whom in the aggregate will have paid only $150,200 for their shares, will be exempt under 16 C.F.R. 802.20.

2. The acquisition of shares of N by the underwriters in the public offering will be exempt under 16 C.F.R. 802.60.

3. The reduction of II's percentage of indirect ownership in S_1 and S_2 from 60% to 49% should be exempt under 15 U.S.C. 18A(c)(10), since as a result of the transaction "the voting securities acquired do not increase directly <u>or indirectly</u>, the acquiring person's per centum share of outstanding voting securities of the issuer."

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Id.[1] Note that S_1 and S_2 are the same issuers both before and after the transaction, as they are the surviving companies in their respective mergers so that II's percentage of indirect ownership in the same issuers is being reduced.

I would appreciate your calling me after you have had a chance to review this analysis, so that we can discuss it.

Sincerely,

[redacted]

[redacted]

Enclosure

2/5/92 - talked to [redacted]. As to conclusion 2, pg 3., advised that, although underwriters are exempt under 802.60, if they are part of the formation of N, their contributions should be included in N's size and they are "acquiring persons" for purposes of 801.40 (and thus will change the conclusion of footnote 1 below). Also in conclusion 3, pg. 3, (c)(10) is not applicable since II will not control N and thus does not hold the voting stock of S_1 or S_2. The mergers of NS_1 and NS_2 into S_1 and S_2 may also be reportable as acquisitions by N. RBSmith

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1. The acquisition by II of 49% of N's voting securities, even if considered separately rather than as one step in a single transaction, would not be reportable. Such an acquisition is properly viewed as a step in the formation of N prior to the public offering, in which case the requirements of 801.40 will not be satisfied because none of the other acquiring-person managers will meet the $10 million size-of-person requirement. See 16 C.F.R. 801.40(1)(iii). However, this would still leave the mergers of NS_1 and NS_2 into S_1 and S_2. Should the staff not agree with the analysis of paragraph 3 above, this merger would appear to be the only reportable event in the transaction.

Description of Transaction

This memorandum summarizes the proposed spin-off of S_1 and S_2 by P and the concurrent initial public offering of approximately 51% of the common stock of N. It assumes that the value of S_1 and S_2 on a debt-free basis is approximately $104 million. The transaction will be carried out in the following steps:

1. Management of S_1 and S_2 together with II (an institutional investor) will form N. N will be initially capitalized with approximately $200,000 of cash, approximately 24.9% of which will be supplied by II in exchange for an equal percentage of the stock of the outstanding N stock.

2. N will, in turn, form two wholly-owned subsidiaries, NS_1 and NS_2.

3. Lender L will lend to S_1 and S_2 approximately $46.3 million, the proceeds of which will be transferred to P in consideration for the release of S_1 and S_2 from its obligations under the Credit Agreement between P and its subsidiaries with L (the "Credit Agreement"). P, in turn, will use the proceeds to reduce its debt to L under the Credit Agreement.

4. L will transfer to II approximately $39 million principal amount of its note receivable from P under the Credit Agreement.

5. II will transfer to N the $39 million note receivable from P in exchange for 49% of the N common stock.

6. N will issue 51% of its common stock to the public in an initial public offering ("IPO") for proceeds of approximately $40.6 million before related expenses.

7. NS_1 will merge into S_1 and NS_2 will merge into S_2. S_1 and S_2 will each be the surviving corporations in the mergers. Pursuant to the mergers, P will exchange its interests in S_1 and S_2 for $55.9 million, $16.9 million in cash raised in the IPO and $39 million in satisfaction of the P note receivable held by N.

8. The $16.9 million cash proceeds received by P from the mergers (less any amounts reserved for related tax costs) will be applied by P to reduce its debt owed to L.

9. Of the remaining $23.7 million cash raised in the IPO, $20.3 million will be paid to L in reduction of the S_1

and S_2 debt created in step 3 (reducing that debt to $25.0 million) and $3.4 million will be used to pay expenses.

If more than $39 million is raised in the IPO, the principal amount of the P debt obligation to be used by II to purchase N common stock will increase proportionately and the amount paid by NS_1 and NS_2 to P in the mergers will also increase proportionately.