

801.1 (C)

[REDACTED]

with effect from November 23, 1992
the confidentiality provision of
Section 7a (b) of the Clayton Act
which restricts release under the
Freedom of Information Act

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FEDERAL TRADE COMMISSION
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VIA FACSIMILE

Richard Smith, Esq.
Premerger Notification Office
Federal Trade Commission
Washington, D.C. 20580

Re: HSR filing requirements in sale-lease back
transaction

Dear Mr. Smith:

We spoke last week concerning a proposed transaction
wherein title to [REDACTED] will be transferred from
three special purpose trusts, which presently hold title to the
vessels, to our client [REDACTED].
[REDACTED] presently operates the [REDACTED] under 25 year leases (so-
called [REDACTED]) and has done so since the [REDACTED]
were built and commissioned ten years ago. The [REDACTED]
[REDACTED] is the trustee of the trusts, and [REDACTED]
[REDACTED] and [REDACTED] are
the trustor-beneficiaries of the trusts. These relationships
are more fully explained below.

In the late 1970's, [REDACTED] contracted with [REDACTED]
to build three new [REDACTED] to modernize
[REDACTED]. The [REDACTED] were designed by [REDACTED] and built to its
specifications for the particular needs of its [REDACTED] operations.
[REDACTED] paid all progress payments due to the [REDACTED] except for
the final delivery payment, which was financed by [REDACTED] and [REDACTED]
[REDACTED] as explained below. In 1982, the first of these [REDACTED]
was completed and commissioned the [REDACTED]. Later
in 1982 and in 1983, the [REDACTED]
[REDACTED] were completed and commissioned. Immediately prior
to delivery, [REDACTED] assigned the construction contracts to special
purpose trusts. Upon completion, the [REDACTED] were "delivered"
to the trusts by transfer of title from the [REDACTED] and
immediately leased back to [REDACTED] for 25 years (the statutory

[REDACTED]

economic life of the [REDACTED] with renewal options. *Since their commissioning, the [REDACTED] have been in [REDACTED] sole possession, and it has had complete control over the deployment of the [REDACTED] which it has used continuously in its own [REDACTED] operations.*

In the early 1980's, the most economical way for [REDACTED] to acquire the three [REDACTED] for its [REDACTED] was to finance them through tax advantaged leveraged lease transactions which were popular at the time. In such transactions, financial intermediaries (such as [REDACTED] and [REDACTED]) financed the acquisition of the [REDACTED]. These transactions allowed [REDACTED] as the operator-beneficial owner of the [REDACTED] to finance the acquisition of the [REDACTED] at a lower cost than would be available through simple mortgage borrowing by permitting large financial institutions to employ the tax advantages attributable to being the "titled owner" of the assets. An additional factor here is that the bonds issued to finance the acquisition are guaranteed by the U.S. Government under a program administered by [REDACTED].

The leases in these transactions are often referred to as "net net leases" or "hell and high water leases." [REDACTED] as the lessee, is responsible for all maintenance, manning and insurance costs of any kind associated with the ownership and operation of the [REDACTED]. Furthermore, [REDACTED] is obliged to pay the lease hire whether or not it has use of the [REDACTED] in order to assure the stream of cash necessary to repay the financing. The owner-lessors have no responsibilities other than to collect rent which is applied to the reduction of the Government-guaranteed bonds. Although the United States tax authorities consider the lessors to be the taxable owners of the [REDACTED] for purposes of receiving the tax benefits associated with the [REDACTED] these financing entities have no control over the deployment of the [REDACTED].

The leases in question extend for a period of 25 years from delivery of the [REDACTED]. This period coincides with the statutory life of the [REDACTED] for purposes of the [REDACTED]. [REDACTED] accounts for the [REDACTED] as capital assets owned by [REDACTED] on its financial reports and depreciates them accordingly for accounting purposes on its books.

The operational control of the [REDACTED] here has always rested solely with [REDACTED], and the transfer of "legal title" to the [REDACTED] from the trusts to [REDACTED] will not change the substance of what has been the case since the [REDACTED] were first built and [REDACTED]. In these circumstances, the transfer of title to the [REDACTED] to [REDACTED] is exempt from the HSR filing requirements [REDACTED].

because [redacted] has always held "beneficial ownership" of the [redacted] and because the technical passage of title is in the ordinary course of business and exempt under section 802.1(b) of the FTC's Rules (16 CFR § 802.1(b)).

Set forth below is a more detailed description of the pertinent facts which support the conclusion that no HSR filing is required in the circumstances present here.¹

Description of the transactions

1. The [redacted] were built under contracts between [redacted] and the [redacted] according to [redacted] design and specifications. The [redacted] were designed to meet the particular needs of [redacted] operations. Construction of the [redacted] was supervised by [redacted] and it was solely responsible for payments under those contracts.

2. When the [redacted] were completed satisfactorily, physical possession of the [redacted] was "delivered" to [redacted] pursuant to long-term leases of the [redacted].

3. Upon delivery, title to the [redacted] was passed to special purpose trusts, which were a common form of financing vehicle for durable goods in the 1980's. The trust structure allowed for investment tax credits and certain tax deductions for depreciation to flow to [redacted] and [redacted] as the beneficiaries of the trusts. The tax deductions result in lower lease hire rates being charged to [redacted] for its operation of the [redacted]. In order to achieve the tax benefits, title to the [redacted] must be held by the trusts, with [redacted] and [redacted] considered the trustor-beneficiaries under the trust agreement and the tax code. Once a [redacted] is sold or otherwise disposed of, the trusts are dissolved.

4. Under the trust structure, the [redacted] serves as the trustee. It has no interest in the corpus of the trust itself but acts as a fiduciary, receives payments from [redacted] under the lease, and pays out the moneys in accordance with the financing requirements.

¹ We understand that based on the facts outlined in the letter to Mr. Sipple, dated November 21, 1990, which we obtained through a FOIA request, the Premerger Notification Office concluded that a filing was not required in connection with a sale-lease back transaction. The facts relating to this transaction parallel those set forth in that letter very closely.

[redacted]

5. [redacted] and [redacted] are in the business of financing the construction and acquisition of durable goods such as [redacted] that require substantial capital outlays. They have no interest in possessing or operating those assets. In reliance on [redacted] credit, [redacted] and [redacted] put up approximately 25% of the money to finance the [redacted], and the rest was financed by Government guaranteed bonds under a program administered by [redacted]. The bonds are secured exclusively by the guarantee of the U.S. Government. The Government's interest is secured by a mortgage on the [redacted] an assignment of [redacted] obligations under the leases, and [redacted] general credit.

6. As the guarantor of the bonds, the U.S. Government through [redacted] is the sole secured creditor. There are separate collateral and security arrangements (including UCC filings) between [redacted] and [redacted] regarding the vessels while they are operated by [redacted].

7. Immediately upon delivery of the [redacted] from the shipyard, [redacted] entered into a lease-back of the [redacted] with the trusts. The leases are for 25 years each, which is the statutory useful life of the [redacted] under [redacted] regulations.² The leases also provide for renewals to [redacted] for one or more additional periods of not less than two nor more than ten years. [redacted] has the right to sub-lease the [redacted] under certain conditions.

8. [redacted] makes lease payments semi-annually. The lease payments cover the principal and interest payments on the bonds, the fee charged by the Government for its guarantee, a return on [redacted] and [redacted] equity in the [redacted], and the administrative costs and charges of the trustee.

9. As lessee of the [redacted] is free to use the [redacted] in its operations with virtually no limitations, other than [redacted] short of using the [redacted] in a dangerous manner or in a hazardous or illegal activity. [redacted] is

² Under these laws, [redacted] is entitled to receive certain subsidies in connection with the operation of these [redacted] until such time as they reach 25 years of age. Because of this subsidy limitation, [redacted] has always disposed of its [redacted] on or before they reach the age of 25 years. Thus, as a practical matter, the 25 year lease term here is the full useful life of the [redacted] to [redacted].

alone responsible for providing all the cargo to make the commercial utilization of the [REDACTED] successful.

10. [REDACTED] possesses all the indicia of the owner-operator of the [REDACTED] and must alone bear all the operating costs:

- (a) [REDACTED] named the [REDACTED]
- (b) [REDACTED] outfitted the [REDACTED] with the equipment it deems necessary (and may change the equipment as it wants).
- (c) [REDACTED] painted the [REDACTED] the colors it wanted.
- (d) [REDACTED] may modify the [REDACTED] as it sees fit (including major structural changes such as inserting an [REDACTED] [REDACTED] so long as it does not reduce the value of the [REDACTED])
- (e) [REDACTED] is solely responsible for the [REDACTED] of the [REDACTED] and the costs thereof.
- (f) [REDACTED] must pay all documentation and inspection costs.
- (g) [REDACTED] must pay all maintenance and repair costs.

11. [REDACTED] is required to pay for all insurance on the [REDACTED] for loss or damage. The named insureds include the U.S. Government, the trust, [REDACTED] or [REDACTED] as the case may be, and [REDACTED] as the lessee. [REDACTED] pays all the premiums and the policies provide there is no recourse by the insurance carrier to any of the other named insureds for any premium payments under the policies. If the [REDACTED] were destroyed, [REDACTED] would still be responsible for paying off the security interests in the [REDACTED] should the insurance proceeds fall short. On the other hand, any funds remaining from the insurance proceeds after the interests of the secured creditors were paid would go to [REDACTED]

12. Financial and other covenants normally imposed on the borrower in asset financing are imposed solely upon [REDACTED] so long as the bonds with which the vessels were financed remain outstanding.

Discussion

1. Since their commissioning, [REDACTED] has controlled and operated the [REDACTED] and is responsible for all costs of operation. Title to the [REDACTED] passed to the trusts solely for the purposes of financing and utilizing certain tax incentives available under the then-existing law. [REDACTED] has always been the sole operator and has complete control over how the [REDACTED] are going to be deployed in the competitive arena for the full statutory [REDACTED] life of 25 years or longer. It carries the [REDACTED] as assets on its financial statements and depreciates them for accounting and financial reporting purposes. The success or failure of the deployment of the [REDACTED] in the [REDACTED]

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competitive arena has always rested and continues to rest with [REDACTED]. As long as the financing entities receive their payments under the financing agreements, they have no economic interest in the productive value or deployment of the [REDACTED]. In taking title, [REDACTED] is merely buying out the intermediary financing entities.

2. There is little question that each step in the evolution of this transaction has been or will be in the ordinary course of business for each of the parties. When [REDACTED] bought the [REDACTED] from the [REDACTED] the transaction was in the ordinary course of business of the [REDACTED] under Rules section 802.1(b). The financing of the [REDACTED] was in the ordinary course of the business of [REDACTED]. Financing the acquisition of new capital goods is what they do.³ The technical passage of title is part and parcel of the financing requirements. It has nothing to do with control over the productive utilization of the assets in the competitive processes and should be considered exempt under Rules section 802.1(b).⁴

For the foregoing reasons, the proposed transaction is exempt and no filing is required.

If there are any additional questions, please do not hesitate to call me at the above-noted telephone number. Time is of

3 Indeed, the revenues associated with the leases at issue here would be reported by the financing entities under SIC code 6159, Miscellaneous Business Credit Institutions, not any of the codes associated with [REDACTED] which is how the revenues from the operation of the [REDACTED] here would be reported by [REDACTED].

4 If the financing of these [REDACTED] could have been accomplished without the passage of title, the substance of the transaction would not have changed and there would be no question that there would be no filing required. Both Rules sections 802.1 and 802.30 look to the substance of transactions in granting exclusions. The substance here is the technical passage of title purely for financing reasons. There is no transfer of the economic or competitive value of the assets. Those values have always been held by [REDACTED].

[REDACTED]

the essence here and we would greatly appreciate an early response.

Very truly yours,

[REDACTED]
[REDACTED]
[REDACTED]
11/30/92 - Advised [REDACTED] that, under the particular facts of this situation, there is no need for Lessee to file for taking of title to [REDACTED] from Lessor. Under the present lease, we are of the view that Lessee holds the assets. This determination is based on the facts that: (1) the [REDACTED] were built to Lessee's design and specifications; (2) the 25 year lease term is, for Lessee, the full useful life of the [REDACTED] to the Lessee; (3) the [REDACTED] are under the full control of the Lessee, which is responsible for their maintenance, marring and insurance; (4) the Lessee carries [REDACTED] as capital assets on its books and depreciates them; (5) the Lessee may modify [REDACTED] as long as their value is not reduced and; (6) title to the [REDACTED] is being taken by the Lessee purely for financial reasons. As to the disposal of the [REDACTED] by the Lessee before they reach the age of 25 years (as noted in Article 2 of the letter), the Lease does not specifically address which party will shift from the sale of the [REDACTED] for more than the Lessee owes the Lessor or which party will absorb the loss of the [REDACTED] are sold for less than what the Lessee owes the Lessor. These situations will be resolved through negotiation between the Lessor and Lessee.

RRSmith