

801.40; 801.11(e)

[REDACTED]

[REDACTED]

[REDACTED]

May 19, 1998

VIA TELEFACSIMILE

Richard B. Smith, Esq.
Federal Trade Commission
Washington, D.C. 20580

Dear Mr. Smith:

Following our phone conversation yesterday, and in view of the facts recently learned and verbally communicated to you in that conversation, plus others, please consider this letter a total replacement of the letter from [REDACTED] of this Firm, dated May 14, 1998, relating to the same subject as this letter.

This transaction is in the nature of a leveraged buy-out in which two venture capital entities will join with a number of other investors, and with the current management of an unincorporated division ("Division") of a U.S. company with assets and sales exceeding \$100 million ("Company"), to acquire for \$45 million the Division's assets. The acquisition will be effected through an acquisition vehicle recently incorporated ("Newco").

Another entity ("Debt Fund") will provide subordinated debt financing to Newco and will receive market rate interest, plus an "equity kicker", in the form of non-voting preferred stock. This stock can be converted into voting shares in Newco. Debt Fund will provide no equity capital.

A financing institution ("Bank") will provide senior debt financing and a revolving line of credit. The Bank will also purchase a small amount of voting stock of Newco.

None of the entities (except the Division) has or will have an ultimate parent entity, and none of the investors are affiliated with each other within the meaning of HSR.

Immediately prior to the closing of the proposed transactions, Newco will have no regularly prepared balance sheet or assets other than its rights under an acquisition agreement to purchase the Division's assets.

[REDACTED]

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Specifically:

1. Each of the two venture capital entities referred to above ("Equity Fund I" and "Equity Fund II" collectively, the "Equity Funds"), and the Debt Fund is an equity investment limited partnership.
2. The other investors will (a) include two special purpose entities ("Investment Fund I" and "Investment Fund II"; collectively, the "Investment Funds") through which various individuals will invest in the equity of Newco, (b) possibly several other investors, who will invest directly in the equity of Newco, and (c) the Bank.
3. The investors will enter into an agreement to purchase the voting securities of newly created Newco, from Newco.
4. Equity Fund I has gross assets greater than \$10 million, but less than \$100 million, as determined by its most recent regularly prepared balance sheet. Equity Fund II does not have gross assets or net sales greater than \$10 million, as determined by its most recent regularly prepared balance sheet.
5. It is possible that more than one of the other investors will have gross assets exceeding \$10 million, but, so far as we are aware, less than \$100 million.
6. We assume that the Bank has assets exceeding \$10 million, and probably has assets exceeding \$100 million.
7. Equity Fund I will contribute slightly less than \$4 million in cash to Newco in exchange for less than 40% of its voting shares. Equity Fund II will contribute the difference between the amount that the Equity Fund I actually contributes and \$4,000,000, for less than 1% of Newco's voting shares.
8. The other non-management investors, including the Bank, will contribute approximately an aggregate of \$5.75 million in cash.
9. The management individuals will contribute cash and non-cash consideration with an aggregate value of up to \$ 1 million for the balance of Newco's voting shares (but not more than an aggregate of 10% thereof).

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10. Neither of the Equity Funds, the Investment Funds, nor any ^{more than} of the other investors will acquire voting shares of Newco which have a value of \$15 million or more.
11. No individual or entity will own 50% or more of Newco's voting shares.
12. Debt Fund will lend \$20 million to Newco at prevailing market interest rates, on a long term, subordinated basis. In connection with the loan, it will receive non-voting preferred stock which will be convertible into less than 50% of Newco's voting shares, with a value of less than \$15 Million, but will not make a capital contribution, as such, to Newco.
13. In addition to its equity investment, the Bank will make a \$10 million term loan to Newco, at prevailing interest rates and on a senior debt, long-term basis.
14. The Bank also will provide Newco with a revolving line of credit of \$20 million at prevailing interest rates. \$5 million of this revolving line of credit will be used as part of the \$45 million purchase price for the Division's asset and another \$2.5 million for acquisition fees and expenses. The balance of this credit line (\$12.5 million) will be available for working capital and other proper corporate purposes, but not to repay any of the equity investors. This line of credit will permit its draw down in its entirety as of the date of the closing, but Newco does not intend to draw more than \$7.5 million down on the closing (the \$5 million for part of the purchase price and \$2.5 million for acquisition fees and expenses). Newco is likely to draw down more of the credit line, and may draw down the entire balance thereof, shortly thereafter. If and when drawn down, that balance would be used for whatever corporate needs might then exist. This could conceivably include the purchase of other assets, but not from the Company.
15. In effect, on the closing, Newco will (a) receive about \$10.75 million in equity contributions, (b) an additional \$30 million in borrowed cash, plus (c) a contractual obligation of the Bank to provide another \$20 million on a revolving credit line of which not more than \$7.5 million will be drawn down at that time.
16. On the closing, Newco will use all of its equity capital (\$10.75 million), all of its borrowed funds (\$30 million) and \$7.5 million of its line of credit, aggregating \$48.25 million, to acquire the Division's assets and to pay acquisition fees and expenses, leaving it with the right to draw on the \$12.5 million balance of the revolving credit line.

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Based upon these facts, we would like your views on the following:

- (a) Is the formation of Newco a transaction subject to notification?
- (b) If so, by whom?
- (c) Is the acquisition of the Division's assets by Newco subject to notification?
- (d) If so, by whom?

Please accept my thanks in advance for your views on this matter. I am not looking for a formal opinion, but only your guidance, and will be happy to take it on the telephone.

Sincerely,

[Redacted signature]

cc: [Redacted]

5/20/98. Writer confirmed that Newco will be formed just before the acquisition. Since nobody controls ~~Newco~~ ~~Newco~~ ~~Newco~~ and since nobody will take back voting stock of Newco valued in excess of 15M, Newco's formation is non-reportable (But Debt Fund and Bond are doing money to Newco (which would be included in its assets) but since loans are at prevailing market interest rates they would not affect the value of the voting stock being bought) Newco also is able to use 801.11(e) for its purchase of the Division's assets, giving it no size. However, any redemptible debt securities would require Newco to also a put from balance sheet to see if this (and other factors) make such transaction reportable.

RS Smith