

April 24, 1973

PLAINTIFF'S
EXHIBIT

WRG-709

MEMORANDUM TO THE BOARD

Subject: Construction Products Division
New Vermiculite Mill - Libby, Montana
Industrial Development Revenue Bonds

SUMMARY

Authorization is requested to finance \$5,950,000 of the new \$7,600,000 mill at Zonolite's Libby, Montana vermiculite mine with Industrial Development Revenue Bonds (IDRB's). W. R. Grace & Co. has received a ruling from the Internal Revenue Service confirming that interest income earned on IDRB's used to finance \$5,950,000 of the new mill would be exempt from federal income taxes provided the IDRB's are issued in the name of Lincoln County, Montana. Under today's market conditions, the IDRB's would carry a coupon rate of 5 7/8% per annum which compares favorably to a coupon rate of approximately 7 7/8% per annum on a conventional industrial bond of similar maturity. The favorable interest rate differential on the tax-exempt IDRB's would provide an interest saving to W. R. Grace & Co. of approximately pre-tax \$119,000 a year. The IDRB's would be issued for a period of 25 years with principal payments beginning in year 11, resulting in an average life for the IDRB's of about 19 years. W. R. Grace & Co. has the necessary leeway under its Senior Loan Agreement (the "Met" Agreement) to accommodate this financing.

BACKGROUND

On May 10, 1971 and November 2, 1972 the Board approved Construction Products RCA's #12 and #12-1 which requested authority to construct for \$7,600,000 a new mill at Zonolite's Libby, Montana vermiculite mine to replace the existing mill in order to:

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1. comply with State and Federal pollution control requirements.

The existing mill was releasing particulate emissions (dust) and asbestos (tremolite) fibers into the air in amounts in excess of State and Federal standards. In addition, waste material slimes from the existing mill were polluting a nearby river.

2. reduce the mill production costs which had risen at 10.1% per year from 1966 to 1971.
3. increase Zonolite's ore milling capacity by 34%.

Under the Internal Revenue Code, locally authorized government bodies may issue tax-exempt IDRB's for the purpose of industrial development and pollution control. Within certain limitations, interest income from IDRB's is exempt from federal taxation in a manner similar to the treatment of municipal bonds. The interest cost of such borrowings is therefore lower than the cost of similar borrowings on a taxable basis.

In the case of the new Libby mill, Montana law authorizes Lincoln County, within whose jurisdiction the mine is located, to issue IDRB's to help finance industrial development and pollution control. Acting within this authority, Lincoln County has passed a resolution to issue IDRB's for the purpose of financing a portion of the new Libby mill. The Internal Revenue Service has ruled that \$5,950,000 to be expended for the new mill meets the tax-exempt tests as follows:

1. \$1,000,000 per location limitation - An authorized government body may raise funds in its name for any one industrial user within its jurisdiction up to \$1.0 million for any purpose (up to \$5.0 million under certain restrictive circumstances which

cannot be complied with in the case of the new Libby mill). The \$1.0 million per location rule allows Lincoln County to issue up to a lifetime maximum of \$1.0 million of tax-exempt IDRB's to finance development of the Libby operation. The Internal Revenue Service has ruled that Lincoln County may issue tax-exempt IDRB's totalling \$1.0 million for the purpose of financing the \$1.1 million Ore Stockpile and Blending Facility which is being constructed to insure uniform vermiculite feed to the new Libby mill.

2. \$4,950,000 for pollution control - Tax-exempt status is unlimited for amounts expended on air and water pollution control facilities. In the case of the new Libby mill, the Internal Revenue Service has ruled that \$4,950,000 of total expenditures on the new mill are for the purpose of pollution control. Consequently, this amount satisfies the tax-exempt test.

DETAILS OF IDRB FINANCING

The firm of Blyth Eastman Dillon & Co. has agreed to underwrite the issue of \$5,950,000 of IDRB's. The IDRB's would be marketed as one issue. However, for legal reasons the \$5,950,000 would be composed of two issues, \$4,950,000 of pollution control IDRB's for the new mill and \$1,000,000 small issue (per location limitation) for the Ore Stockpile & Blending Facility. The IDRB's would be issued with a 25 year maturity. The repayment schedule would be interest only for the first 10 years and level debt repayment during the remaining 15 years, resulting in an average life of approximately 19 years for the entire issue. On the basis of today's market conditions, for a Baa rated issue the IDRB's would carry a coupon rate of approximately 5 7/8% or about 2% under the rate on a non tax-exempt issue of like maturity. The

final pricing would be fixed at the time the IDRB's are marketed. The following schedule gives a breakdown of the anticipated costs to Grace for the \$5,950,000 IDRB issue:

(See table on the next page)

Blyth Eastman Dillon
Cost Estimate
for IDRB Issues Totalling
\$5,950,000

\$4,950,000 Pollution Related Issue
+
\$1,000,000 Small Issue

Dated Date of Issues	5/1/73	(1)
Due Date	5/1/84 - 5/1/98	(2)
Coupon	5 7/8% p.a.	(3)
Average Life	19 yrs. 0 mos. 21 days	
Underwriters Fee	\$89,250	(4)
Effective Interest Cost per annum		
- Interest & Underwriters Fee Only	5.9537%	
- All Estimated Costs Included	5.9940%	(5)

(1) IDRB's will be marketed following Board action

(2) Level Debt Sinking Fund

(3) Based on current market conditions for Baa rated bonds

(4) \$15.00 per \$1,000 of IDRB's

(5) Other Estimated costs applicable to issue

Printing	\$10,000
Bond Attorney	14,000
Price Waterhouse Statement	15,000
Trustee (initial fee)	3,000
Miscellaneous	<u>3,750</u>
Total	<u><u>\$45,750</u></u>

The firm of Chapman and Cutler (Chicago), who are recognized Bond Counsel, have, on the strength of the Internal Revenue Service ruling received by W. R. Grace & Co., indicated agreement to issue opinions stating that \$4,950,000 being expended on the new mill for the purpose of pollution control and \$1.0 million being spent for the Ore Stockpile & Blending Facility are exempt from federal income taxes. The IDRB's would be issued in the name of Lincoln County. A W. R. Grace & Co. guarantee on the IDRB's would be required. The new mill, the Ore Stockpile & Blending Facility and the underlying land would be leased to Lincoln County by W. R. Grace & Co. and would serve as collateral for the IDRB's. The facilities and land would be sublet back to W. R. Grace & Co. at exactly the same terms as required to service and retire the IDRB's. No additional administrative or other charges would be included in the lease payments to Lincoln County except that the usual property taxes would be assessed. The lease arrangement between W. R. Grace & Co. and Lincoln County would expire when the IDRB's have been retired. In the event of default, Lincoln County would have the right to sublet the facilities and land to a third party until all of the outstanding IDRB's have been retired. Lincoln County would assign its rights under the lease agreements to

. The bank would act as

Trustee and would administer the lease agreements and would handle the servicing and amortization of the IDRB's. W. R. Grace & Co. would bear the cost of the Trustee.

TAX EFFECTS OF IDRB'S TO W. R. GRACE & CO.

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For tax purposes, W. R. Grace & Co. would capitalize the cost of the new mill and the Ore Stockpile & Blending facility and depreciate them using current depreciation schedules. Also, W. R. Grace & Co. would expense on a current basis that portion of the lease payments which corresponded to interest payments on the IDRB's as well as the payment of property taxes, the cost of the Trustee and all other incidental expenses associated with W. R. Grace & Co.'s

financing arrangement with Lincoln County.

W. R. GRACE'S SENIOR LOAN AGREEMENT

The issuance of IDRB's to finance a portion of the Libby project would constitute secured debt in W. R. Grace & Co.'s accounts. On this basis the \$5,950,000 of IDRB's would be subject to Section 10(B)(5) of W. R. Grace & Co.'s Senior Loan Agreement (the "Net" Agreement). The lenders under the "Net" Agreement have recently agreed to increase the 10(B)(5) limitation on secured debt for domestic and Canadian subsidiaries from \$25.0 million to \$45.0 million. It was agreed with the lenders that the revised \$45.0 million limitation could be applied up to a maximum of \$25.0 million for general unspecified purposes or the full \$45.0 million for pollution related expenditures. Consequently, W. R. Grace & Co. can accommodate the \$5,950,000 of IDRB's for the Libby project under the "Net" Agreement (to be revised by F. Brennan).

REQUIRED BOARD ACTION

The documentation for the \$4,950,000 pollution control issue and the \$1,000,000 small issue have been reviewed by the Corporate Legal Department. The Board is asked to approve resolutions which essentially cover the following matters:

(To be drafted by Gail Wood)