

Memo



TO The Files, Kansas City/Omaha
FROM Rod Anderson, Kansas City/Omaha
Dave Schaaf, Kansas City/Omaha
Clifton Davis, Kansas City/Omaha
DATE January 11, 2002
SUBJECT Westar Industries, Inc. ("Westar") - Tax Implications of
Acquisition Alternatives for Guardian International, Inc.
("Guardian")
WEX09872

FACTS

Westar Industries, Inc. ("Westar"), a wholly owned subsidiary of Western Resources, Inc. ("WRI"), owns approximately 32% of the voting stock of Guardian International, Inc. ("Guardian").¹

Westar is considering purchasing (with cash, stock, or cash and stock) Guardian with the following objectives:

- Purchase the Guardian holding company and remove the public stub.
- Achieve a stepped-up tax basis in assets.
- Avoid tax leakage.

OTHER ISSUES

1. Regarding consideration, is Westar interested in using WRI or Westar stock?
2. What is the estimated purchase price?
3. What is the estimated inside/outside tax basis in Guardian?²
4. Does WRI have any interest in attempting to posture the acquisition in a form suitable of assisting a future spin-off of Westar? (This idea needs further development prior to confirming its validity).

ACQUISITION ALTERNATIVES

I. *Taxable Asset Acquisition*

Westar acquires the assets of Guardian.

¹ See attached Schedule A detailing Westar's ownership in Guardian.

² Based on Guardian's December 31, 2001 10-K, Guardian's inside tax basis is approximately \$40 million.

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Advantages:

- Step-up in basis - Westar takes a stepped-up basis in the assets acquired equal to the purchase price (consideration plus liabilities assumed).

Disadvantages

- Tax leakage - Guardian's gain from the sale of its assets, the difference between the purchase price of the assets and Guardian's tax basis in its assets, is taxable income to Guardian.
 - Guardian may offset a portion of its gain from the sale of its assets with existing net operating losses ("NOLs"). Guardian had a NOL carryforward of approximately \$4.4 million as of December 31, 2001.³
- Westar does not acquire the Guardian holding company or remove the public stub.

2. Taxable Stock Acquisition

Westar acquires the stock of Guardian.

Advantages:

- Westar acquires the Guardian holding company and removes the public stub.
- Carryover of NOL – Guardian's NOL should carryover to Westar and be available to offset future income of Westar and the WRI consolidated group, subject to limitation (Section 382).

Disadvantages

- Tax Leakage - Guardian's shareholders will recognize a gain or loss from the sale of their Guardian stock equal to the difference between the purchase price of the stock and each shareholder's tax basis in his/her shares of Guardian.
- No Step-up in basis - Westar takes a carry-over basis in the assets acquired.

3. Tax Free Acquisition (Reverse Triangular Merger).

A "Reverse Triangular Merger" requires a corporation to acquire a target by using an existing or transitory subsidiary as the merger vehicle. Target survives the merger. Control of target stock must be acquired in exchange for parent stock. After the transaction, target must own "substantially all" of its properties and the subsidiaries' properties (excluding parent's voting stock used in the transaction).

Advantages:

- Limited tax leakage – To the extent cash is used in the transaction, Guardian's shareholders will recognize gain equal to the lesser of the "boot" received or the gain realized.

³ The estimated NOL is derived by grossing up the deferred tax benefit described in Note 10 of the December 31, 2001 10-K. (\$1,772,000/40%).

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- Westar acquires the Guardian holding company and removes the public stub.
 - Limitation: Guardian shareholders may receive other property (i.e., cash) from Westar or WRI for up to 20% of their Guardian voting stock and 20% of each class of non-voting Guardian stock.
- Carryover of NOL – Guardian's NOL should carryover to Westar and be available to offset future income of Westar and the WRI consolidated group, subject to limitation (Section 382).

Disadvantages

- No Step-up in basis - Westar takes a carry-over basis in the assets acquired.