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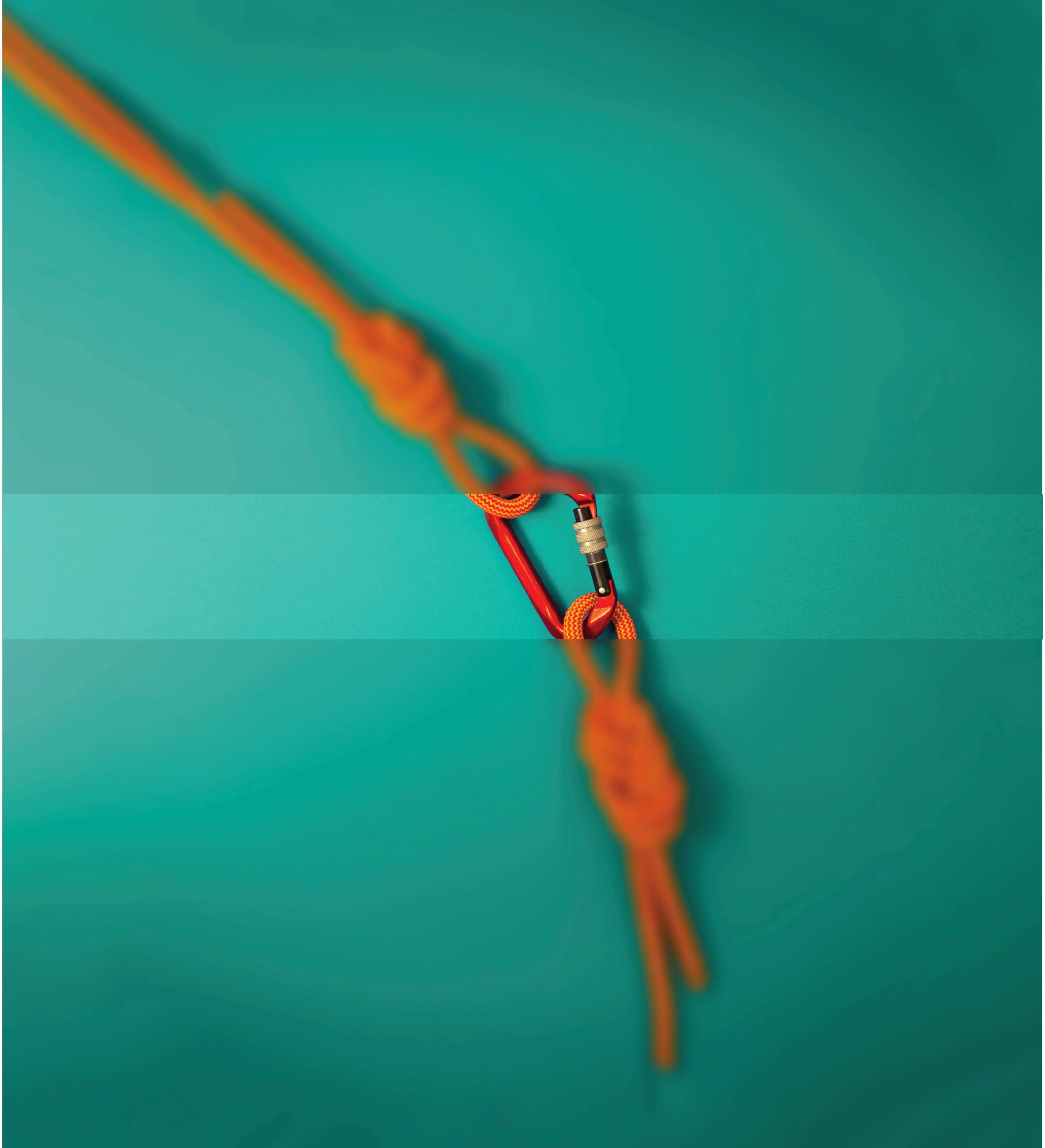

CROSS-BORDER M&A:
A CHECKLIST OF US ISSUES FOR NON-US ACQUIRORS

CONTENTS

CROSS-BORDER M&A: A CHECKLIST OF US ISSUES FOR NON-US ACQUIRORS

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Summary

In contrast to purely domestic M&A, cross-border M&A involves an additional array of legal, jurisdictional, cultural, and commercial nuances that must be navigated. To assist non-US acquirors who are interested in making strategic or other investments in the United States, this article offers a practical guide and covers topics ranging from acquisition structures to regulatory compliance to representations and warranty insurance, among others. While each M&A transaction will present bespoke issues, some of which are likely to be unfamiliar to non-US acquirors, a foundational familiarity with the most common issues that underlie and accompany US M&A deals will help secure successful outcomes.

1. Cross-Border M&A: A Checklist of US Issues for Non-US Acquirors

Cross-border merger and acquisition ("***M&A***") transactions can be far more complex than purely domestic transactions. With advanced planning and careful consideration of relevant issues, however, it is possible to navigate this complexity successfully and achieve the parties' commercial objectives. This article presents an overview of certain key issues that should be considered by non-US acquirors contemplating acquisitions or other strategic investments in the United States.

Global M&A activity peaked during 2021, but volumes normalized in 2022 in a year marked by inflation, progressively increasing interest rates, Russia's invasion of Ukraine, ongoing supply chain disruptions and food and energy insecurity, and the continuation of the COVID-19 pandemic. In particular, cross-border M&A activity has remained relatively stable, painting a more certain picture for global dealmakers than has recently been the case.

2 Deal Structure: Tax, Acquisition Finance, and Other Considerations

2.1 Primary Acquisition Structures

The choice of acquisition structure in M&A is typically driven by the characteristics of entities involved in the transaction, including their respective entity type (under local law), entity classification (for US tax purposes), jurisdictions of organizations, and the nature of their capital structures and related shareholder base, together with the unique tax considerations of the deal and the parties' commercial objectives.

Acquisitions of US public companies are usually structured as either a statutory merger or a tender offer (which is followed by a second-step statutory merger to "squeeze out" any remaining stockholders of the target company who do not participate in the first-step tender offer), both of which are subject to various regulatory requirements and review by the US Securities and Exchange Commission (the "***SEC***"). Acquisitions of US private companies, by contrast, provide far greater structuring flexibility because they generally are not subject to the same regulatory requirements or SEC review that apply to takeovers of public companies. Accordingly, while acquisitions of private companies can (and often do) take the form of a statutory merger (tender offers are rare), direct acquisitions of stock and assets are equally common.

Subject to certain exceptions, parties to a transaction that is structured as an acquisition of assets have the ability to select the assets and liabilities to be transferred to the acquiror and to be retained by the seller. An acquiror of assets generally does not inherit the US tax basis of the seller in the assets being sold. Accordingly, asset acquisitions are often thought to facilitate tax efficiencies for the acquiror because if the acquiror is able to obtain a "step-up" in the tax basis of the acquired assets, then the acquiror should be able to further depreciate those assets over time as well as reduce the acquiror's tax liability related to a future sale of those assets.

By contrast, parties to a transaction that is structured as a merger or an acquisition of stock do not have this ability because the target company in those cases (which is the seller in an asset deal) continues to own the same assets both before and after the closing. Accordingly, in deals structured as a merger or an acquisition of stock, the target company's historic liabilities, including liabilities for unpaid US taxes as well as its US federal income tax attributes (such as net operating losses), generally remain with the target company (although subject to certain requirements, certain tax elections can be made to treat the purchase of stock as a purchase of assets). If an acquisition is structured as a share-for-share merger, then the target company's historic tax liabilities as well as its US federal income tax attributes generally shift to the acquiror.

2.2 Acquisition Vehicles

Non-US acquirors need to carefully consider the choice of acquisition vehicle, which will be based in part on the potential tax treatment of both the contemplated transaction and the combined business after the closing. Non-US acquirors typically use a US corporation as the acquisition vehicle for asset acquisitions of a US business because it allows non-US acquirors to avoid being treated as being directly engaged in a US trade or business (which can introduce significant tax complexities), and non-US acquirors can instead have the US corporation make all required US tax filings and payments. Alternatively, non-US acquirors can also use non-US corporations (or non-corporate US entities) as the acquisition vehicle for acquisitions of stock of a US target company. If a non-US acquiror acquires the stock of a US target company, and the non-US acquiror is eligible for the benefits of an applicable tax treaty with the United States, then dividends, interest, or royalties that the non-US acquiror receives from the US target company may be subject to reduced rates of US withholding taxes (or such taxes might be eliminated entirely).

Accordingly, tax planning in the context of determining a transaction structure should take into account not only the tax consequences of the transaction itself (*e.g.*, whether the transaction is intended to be taxable or tax-deferred), but also the implications of operating the newly-acquired US business after the closing (*e.g.*, cross-border flows of goods and services, the repatriation of cash and other distributions, the availability of US tax treaties, etc.). Careful tax structuring is important because the applicable taxing authority (*e.g.*, the US Internal Revenue Service) can challenge the tax characterization of a transaction if it does not agree that the characterization reflects the substance of that transaction.

2.3 Effects of Tax Reform

Tax reform in the United States in 2017 has had, and will continue to have, a profound effect on cross-border M&A activity, as will the Inflation Reduction Act of 2022 (the "***IRA***") and, if enacted by Congress, recent Biden Administration tax proposals. The centrepiece of the 2017 reform was the federal reduction in the corporate tax rate from 35% to 21%. The Biden Administration has proposed an increase to 28% in its budget proposal for fiscal year 2024, although the probability for that becoming law in the near term does not appear high.

The IRA created a corporate alternative minimum tax, which imposes a 15% minimum tax on the net income of large US corporations (with certain adjustments) starting in 2023. This tax generally applies to US corporations with average net income (subject to adjustments) exceeding USD 1 billion, as well as US members of non-US-parented groups if the worldwide group's average net income (subject to adjustments) exceeds USD 1 billion and the average net income of the US members of the group exceeds USD 100 million. The IRA also created a stock buyback excise tax, which among other things applies to repurchases by US affiliates of shares of publicly traded non-US corporations, as well as to certain repurchases by publicly traded non-US corporations that have US subsidiaries of the stock of such non-US corporations. The amount of tax imposed is generally 1% of the fair market value of the repurchased shares. In IRS guidance, this tax applies to a range of M&A transactions, including leveraged acquisitions where consideration is paid from the proceeds of debt incurred by the target corporation. The Biden Administration's budget proposal would increase this tax from 1% to 4%.

The Biden Administration's budget proposal also includes a number of changes to other tax rules that are sometimes applicable in cross-border M&A. Notably, it would impose added limits (beyond those in current law) on inversions (*i.e.*, relocations (on paper) of US-based companies overseas to reduce their US tax burden) and bring US tax rules closer to compliance with The Organization for Economic Co-operation and Development's global international tax reform initiative known as "Pillar 2." The goal of Pillar 2 is to establish a coordinated multinational system of taxation to ensure large multinational companies with international operations pay a minimum level of tax (15%) in each country where they do business. Pursuant to a recent European Union directive, Pillar 2 is slated to be implemented by European Union member states this year, and the Biden Administration is seeking to change the US tax system to be more aligned with the new laws expected to be adopted in the European Union and similar laws in other countries.

Because US taxes can have a significant impact on the global effective tax rate of non-US acquirors with significant US operations, it is essential to model the impact of these and other key features of the US tax law regime using company-specific facts prior to committing to any US investment or related acquisition structures.

2.4 Acquisition Finance

After years of low interest rates and robust borrowing, the recent increase in interest rates, challenging debt markets, and faltering confidence in the banking sector, have led to a significant slowdown in borrowing. As a result, many acquirors are pursuing alternative acquisition financing options, including partnering with direct lenders such as sovereign wealth funds, accepting seller financing, or increasing equity financing (most frequently in the private equity context). Not surprisingly, cash has remained the currency of choice, particularly in cross-border transactions in which equity of non-US acquirors is often viewed by US sellers as less attractive (notwithstanding potential upside).

In contrast to the United Kingdom and many other non-US jurisdictions, the United States does not have a "certain funds" obligation requiring acquirors to demonstrate that they have sufficient funds to complete an acquisition. In practice, however, sellers in most transactions in the United States require that that the acquiror show that it has sufficient financing to complete the acquisition or has otherwise entered into commitment papers with one or more lenders pursuant to which such lenders provide a firm commitment when the acquisition agreement is executed to provide the necessary financing for the acquisition to close, subject to what are known as "SunGard conditions," which mirror as much as possible the conditions in the acquisition agreement. From the non-US acquiror's perspective, obtaining such commitments prior to the execution of the acquisition agreement is critical because in the US market acquisition agreements only rarely condition the acquiror's obligation to close the transaction on the ability of the acquiror to obtain financing. Definitive financing agreements are then negotiated between signing and closing based on the commitment papers executed at signing.

Lenders may seek to include provisions in the commitment papers to reduce the risk that they will have to fund a loan pursuant to the commitment papers, including market flex and securities demand provisions. Market flex provisions permit lenders to adjust financial terms of the commitment within a certain pre-agreed range in order for the committed lenders to achieve a successful syndication, which is defined as the lenders holding no more than a certain negotiated amount of the commitment or loan, often USD 0. Securities demand provisions permit the lenders to compel the acquiror to issue debt securities to fund the acquisition or to replace a bridge loan that funded an acquisition.

Tax considerations can also affect the method of acquisition financing used by a non-US acquiror. If debt is used, then debt placement and collateral security should be carefully planned, and limits on the deductibility of interest should be carefully considered, to fit the overall structure and related tax modelling. If intercompany debt is used or debt is "pushed down" from a non-US parent to a US subsidiary, then complex conduit financing rules, tax treaty considerations, and rules on recharacterization of debt will need to be taken into account. If the acquisition is funded by issuing common or preferred equity, then dividend withholding rates and tax treaties applicable to the non-US acquiror will need to be considered.

Additional considerations that apply to acquisitions being funded with equity or other securities are set out below in Section 6 (*Securities Laws and Mandatory Offer Requirements*).

2.5 Other Considerations

If the contemplated transaction is potentially politically sensitive or likely to face regulatory resistance, alternative structural considerations may include one or more of the following:

- minority or other non-controlling investments;
- joint ventures;
- contractual partnerships with a US company or management team or partnering with a US source of financing or co-investor (such as a private equity firm);
- utilizing a controlled or partly controlled US acquisition vehicle, including a board of directors largely comprised of US citizens; or
- implementing bespoke governance structures (such as a US proxy board) with respect to specific sensitive subsidiaries or businesses of the target company.

There are pros and cons associated with each of these structures, but depending on the commercial objectives of the parties, each one of these structures could potentially help to facilitate a deal.

3 Foreign Investment Review (CFIUS)

3.1 CFIUS Regulatory Regime

The Committee on Foreign Investment in the United States ("***CFIUS***") is an interagency committee authorized to review certain transactions involving non-US investment in the United States and certain real estate transactions in the United States involving non-US persons, in order to determine the effect of such transactions on the national security interests of the United States. Industries that have historically drawn the greatest scrutiny from CFIUS include defence, aerospace, computers and electronics, heavy machinery, software publishing, utilities, and mining. More recently, transactions involving critical technology, critical infrastructure, and sensitive personal data of US persons (referred to as "***TID US businesses***") are of heightened interest to CFIUS, with semiconductors and 5G technology being leading examples.

CFIUS filings are sometimes mandatory, but often are made on a voluntary basis as well. If the parties make a CFIUS filing regarding their transaction and CFIUS notifies the parties that it is satisfied that the filing contains all required information, an initial review period of up to forty-five days is commenced.[1] After the initial review period, CFIUS will either clear the transaction if it concludes that it does not present any national security risks or, if it cannot do so, initiate a subsequent investigation that may last up to an additional forty-five days.[2] If after further review CFIUS concludes that the transaction presents national security risks, then CFIUS may request the parties to agree to mitigation measures prior to closing, impose conditions on the acquiror's post-closing operation of the acquired business or, in the worst case, refuse to clear the transaction. The range of mitigation measures that CFIUS can impose is intentionally broad and the actual measures sought to be imposed by CFIUS will depend on the risk profile of the deal. If CFIUS enters into a mitigation agreement with parties to resolve identified concerns, it will issue a clearance letter and conclude its investigation. Alternatively, at the conclusion of the investigation stage, CFIUS may refer the matter to the President of the United States (generally with a recommendation to prohibit or "block" the transaction), and the President will have fifteen calendar days to make a decision. Presidential action is rare, however, and CFIUS clears most transactions without conditions. Nonetheless, careful advanced planning, which often includes designing both a legal and a political strategy

1 If the parties submit a Joint Voluntary Notice ("***JVN***"), the initial review period ends no later than 45 calendar days after it has commenced. If the parties submit a "***Declaration***" pursuant to an abbreviated filing process, the initial review period ends no later than 30 calendar days after it has commenced. in contrast to JVNs, there is no secondary "investigation" period for Declarations. See footnote 5 below.

2 If parties submit a short-form Declaration (instead of a JVN), CFIUS will, at the end of the thirty-day review period, issue a decision and choose to either: (1) clear the transaction; (2) direct the parties to file a full JVN; or (3) issue an "No Action" letter without clearing the transaction, thereby leaving the parties to decide whether to close the transaction without filing a JVN and without the formal certainty of clearance.

(including by "pre-conditioning" CFIUS), greatly enhances the likelihood of a successful outcome.

3.2 Recent Developments

The CFIUS landscape has changed dramatically in recent years, including with respect to the US Foreign Investment Risk Review Modernization Act of 2018 ("***FIRRMA***"), which fully took effect on 13 February 2020. Under FIRRMA, CFIUS has jurisdiction to review any transaction that could result in "***control***" of a US business by a non-US person. "Control," however, is not limited to majority ownership, but rather includes any "power, direct or indirect, whether or not exercised, through the ownership of a majority or a dominant minority of the total outstanding voting interest in an entity, board representation, proxy voting, a special share, contractual arrangements, formal or informal arrangements to act in concert, or other means, to determine, direct, or decide important matters affecting an entity."[3] Mandatory filings are required for certain investments which would confer "control" to a non-US acquiror over a TID US business that meets the TID criteria based on the "critical technology" prong.[4] Acquisitions of TID US businesses that meet the TID criteria based on the "critical infrastructure" or "sensitive personal data" prongs only require mandatory filings if the non-US acquiror is a governmental entity acquiring a "substantial interest." Otherwise, the parties may consider a voluntary filing.

Because CFIUS's definition of a critical technology TID US business is now based on export control licensing requirements rather than sector-based industry codes, parties' due diligence costs have increased considerably with the broad range of potentially implicated technologies requiring a high-level classification review when the target business does not have export control classification readily available. Qualifying foreign investors[5] from "excepted foreign states" (which currently includes Australia, Canada, New Zealand, and the United Kingdom) are currently exempt from CFIUS's regulations in limited instances.[6]

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3 31 CFR 800.208.

4 In general, "critical technologies" consist of (i) defense articles or services included on the United States Munitions List set forth in the International Traffic in Arms Regulations; (ii) items included on the Commerce Control List set forth in the Export Administration Regulations (15 CFR parts 730-774) and controlled pursuant to multilateral regimes (including for reasons relating to national security, chemical and biological weapons proliferation, nuclear nonproliferation, or missile technology) or for reasons relating to regional stability or surreptitious listening; (iii) certain nuclear equipment, facilities, components, materials, software, and technologies; and (iv) certain agents and toxins.

5 "Excepted foreign investors" generally include non-US investors that (a) are organized under the laws of an excepted foreign state, (b) have their principal place of business in an excepted foreign state or in the United States and (c) have a board of directors (or equivalent), at least 75% of which is comprised of nationals from excepted foreign states or the United States.

6 They will continue to be subject to CFIUS jurisdiction, however, for investments that result in non-US control of a US business.

Even in situations where a transaction falls outside the scope of CFIUS's mandatory filing regime, there may still be a powerful incentive for parties to seek clearance in order to preclude CFIUS from seeking to require the non-US acquiror to divest the US business after the acquisition has closed.[7] The US Department of the Treasury established the Office of Investment Security Monitoring and Enforcement (the "***Office***"), which is responsible for identifying transactions not notified to CFIUS that may pose national security concerns. The Office uses various means to identify transactions, including tips from the public, interagency referrals, media reports, commercial databases, and congressional notifications.[8] For example, in December 2022, the China-based IoT platform solution provider, Borqs Technologies, announced that CFIUS reviewed its 2021 acquisition of majority ownership in Holu Hou Energy, a US energy storage company, and required it to fully divest its related ownership interests and rights due to national security concerns.[9]

While CFIUS officially states that specific countries are not singled out for enhanced review, CFIUS's most recent divestiture orders suggest that there will likely continue to be heightened scrutiny when Chinese investors are involved. In many situations, including those involving Chinese investors, it has become increasingly popular to try to address the risk of failing to obtain CFIUS clearance through the use of termination fees payable by the non-US acquiror if clearance is not obtained.[10]

4 Merger Control

4.1 Merger Control Regulatory Regime

The Antitrust Division of the US Department of Justice (the "***DOJ***") and the US Federal Trade Commission (the "***FTC***") have the power to review the competitive aspects of proposed transactions – even transactions that do not result in changes of control or involve US companies.

Transactions that exceed certain reporting thresholds are subject to mandatory premerger notification requirements under the US Hart-Scott-

7 While historically unusual, this has occurred with greater frequency in recent years (*e.g.*, in connection with (1) the 2019 acquisition by Beijing Kunlun Tech of an interest in Grindr, (2) the 2019 acquisition by iCarbonX of an interest in PatientsLikeMe, (3) the 2012 acquisition by Ralls Corporation of four wind-farm projects in Oregon, and (4) the 2011 acquisition by Huawei of operating assets from 3Leaf computing). Note that the non-US acquiror in each of these cases was Chinese.

8 In October 2022, the US Department of the Treasury published its first enforcement guidelines regarding mandatory filing requirements, including those related to US businesses critical technologies, and compliance with mitigation agreements. Assistant Secretary for Investment Security Paul Rosen stated that CFIUS "will not hesitate to use all of its tools and take enforcement action."

9 *See* https://www.globenewswire.com/news-release/2022/12/19/2576679/0/ en/Borqs-to-Establish-with-the-U-S-Government-a-Plan-to-Divest-its-Ownership-of-Holu-Hou-Energy-Due-to-DeemedCritical-Technology.html.

10 Non-US acquirors based in countries that restrict or otherwise regulate the flow of capital in connection with outbound investments may be subject to requests from US sellers to secure the payment of these types of reverse termination fees through the use of US collateral structures, including US dollar denominated escrow accounts held in the United States by US banks.

Rodino Antitrust Improvements Act of 1976, as amended (the "***HSR Act***"). If a notification is required, a formal filing must be submitted to both the DOJ and the FTC, and the parties must wait thirty calendar days (fifteen calendar days in the case of cash tender offers and certain bankruptcy situations) after the filing to complete the transaction (the so-called "waiting period"). Either the FTC or the DOJ may request additional information (a so-called "second request") from the parties and extend the waiting period an additional thirty calendar days (ten calendar days in the case of cash tender offers and certain bankruptcy situations). For an indefinite period, the FTC has suspended temporarily requests for early termination of the waiting period, leading to transactional delays even for innocuous transactions.

The fees required to be paid in connection with such filings changed significantly this year, with the lower end of the range being marginally reduced and the upper end of the range (for transactions over USD 1 billion) being raised significantly.

4.2 Other Considerations

Coordinating antitrust/merger control filings and substantive strategies across multiple jurisdictions can be a substantial undertaking and the commercial and timing implications for the deal can be significant. In some cases, for example, the DOJ or FTC might challenge a transaction as anticompetitive and sue to block the deal, which is what occurred in 2018–2019 with AT&T's USD 85 billion acquisition of Time Warner,[11] in November 2020 with Visa's proposed USD 5.3 billion acquisition of Plaid, and in 2021–2022 with UnitedHealth Group's USD 13 billion acquisition of Change Healthcare. The DOJ publicly claims to no longer accept remedies. However, the DOJ will accept a "fix-it-first" solution in which the parties, after having made their initial filings pursuant to the HSR Act, propose a remedy, effect the remedy and then re-file their modified transaction under the HSR Act, which filing will reflect the remedy undertaken by the parties to secure clearance. The FTC, by contrast, is still accepting structural remedies, but has hinted publicly that it is moving toward the DOJ's position. Because of these implications, non-US investors will want to have a good understanding of the substantive risk profile of the proposed transaction, and the remedies most likely to be sought by the DOJ and FTC, when negotiating so-called "hell or high water,"[12] reverse termination fee, and other risk-shifting provisions.

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11 Unlike horizontal mergers, vertical mergers (such as the AT&T-Time Warner merger) are challenged much less commonly and any such challenges prior to AT&T-Time Warner have always been resolved in the form of settlements and concessions negotiated outside the courtroom. While the DOJ ultimately lost the suit against AT&T and Time Warner, both the DOJ and the FTC have since announced plans to issue new vertical merger guidelines. Accordingly, it is not prudent for parties to assume that vertical mergers are subject to less scrutiny than horizontal mergers.

12 A "hell or high water" provision shifts the risk related to obtaining antitrust clearance to the acquiror by obligating the acquiror to do whatever is required to obtain clearance, including by agreeing to any divestment or other remedy proposed by the DOJ or FTC.

5 Regulated Industries

In addition to CFIUS and merger control requirements, various US federal and state regulatory requirements (including regulatory filing and consent requirements) may apply to acquisitions of companies operating in particular sectors, including, for example, registered investment funds/advisers, banking/financial institutions, energy, power and natural resources, maritime, utilities, communications, aviation, transportation, gaming, defence, and insurance. In such cases, complying with such requirements, including seeking and obtaining any related approvals, can sometimes be cumbersome and time-consuming and accordingly be factored into any related deal timelines.

6 Securities Laws and Mandatory Offer Requirements

6.1 General

Non-US acquirors that intend to offer and sell securities in the United States in connection with a US investment may become subject to the SEC's registration requirements, which is an expensive and time-consuming process, and consequently the SEC's ongoing periodic reporting requirements. Under the US Securities Act of 1933 (the "***Securities Act***"), the offer and sale of securities must be registered with the SEC unless the securities being offered and sold, or the related transaction pursuant to which they are offered and sold, is specifically exempted. The most commonly used exemptions for acquisitions of privately held target companies are so-called "private placement" exemptions for transactions that do not involve a public offering of securities.[13] Non-US acquirors seeking to use their stock as consideration in an acquisition of a private company may be able to qualify for such private placement exemptions, which eliminates the time and expense associated with a registered transaction. Non-US acquirors seeking to use their stock as consideration in an acquisition of a US public company, however, will not be able to take advantage of the private placement exemptions and therefore will be required to register with the SEC the offer and sale of their stock in the acquisition.

Additionally, registration requirements under the securities laws of each state (known as "blue sky" laws) involved in the particular transaction apply to the offer and sale of securities unless an exemption is available. Notably, securities offered and sold through certain private placements and securities listed on a US stock exchange (*e.g.*, NASDAQ or NYSE) are exempt from state blue sky laws, though certain notice filings, consent to service of process, and payment of filing fees may apply.

13 Section 4(a)(2) of the Securities Act exempts from registration transactions by an issuer that do not involve a public offering of securities. Most private placement offerings today are conducted under Rule 506 of Regulation D of the Securities Act, which is considered a "safe harbor" under Section 4(a)(2) because it sets out certain standards that, if met, allow an issuer to satisfy the requirements of a Section 4(a)(2) exemption.

6.2 Education/Transparency

Non-US acquirors seeking to offer and sell securities in the United States as deal consideration should also keep in mind that for some shareholders of US target companies, particularly shareholders of US public companies that are accustomed to US securities laws and stock exchange listing rules that are designed to promote transparency and disclosure, additional coordination and planning may be needed to help educate those shareholders in respect of the disclosure regime of the non-US acquiror that would apply if the target company's shareholders were to accept the shares of such non-US acquiror. Even in the case of a non-US acquiror that is, or becomes, a so-called "foreign private issuer" for US securities law purposes, it is not required to comply with the US proxy rules, to file the same periodic reports with the SEC, or to have a majority of its directors be independent, all of which are required of US domiciled, SEC-registered reporting companies.

6.3 Insider Trading; Stakebuilding; Disclosure Requirements

Non-US acquirors seeking to purchase stakes in US public companies must, among other things, take into account the restrictions on insider trading imposed pursuant to Rule 10b-5 under the US Securities Exchange Act of 1934 (the "***Exchange Act***"), the potential requirement to publicly report beneficial ownership of shares (and other information about the acquiror and its intentions with respect to the target company) in excess of 5% pursuant to section 13(d) of the Exchange Act and the "short-swing profits" rules imposed by section 16(b) of the Exchange Act (which potentially can require disgorgement of profits from trading after the acquiror's position in the target company's shares exceeds 10%). Moreover, US federal laws (such as the HSR Act), the laws of the state of the target company's domicile (such as "anti-takeover" laws) and the target company's governance documents may contain provisions that limit the number of shares that can be acquired, or require certain approvals to be obtained, in connection with such acquisitions.

6.4 Mandatory Offer Requirements

There are no mandatory offer requirements in the United States, but non-US acquirors should take care to ensure that any share purchases do not constitute a *de facto* or "creeping" tender offer that would be subject to US tender offer rules.

7 Corrupt Business Practices and Economic Sanctions

7.1 Corrupt Business Practices

Regulators around the world continue to focus on corrupt business practices. First-time investors in the United States should appreciate that their exposure to risk under the US Foreign Corrupt Practices Act (the "***FCPA***") could increase significantly if they acquire a US business. If a non-US acquiror is required to register its shares with the SEC in the United States, including in connection with any listing on a US stock exchange in connection with an acquisition of a US target company, it will invariably become subject to the FCPA. Absent a US listing, a non-US acquiror may also become subject to the FCPA depending on the levels of entanglement between the US target company and its affiliates and the nature of the group's business and geographic exposure.

Among other things, the FCPA makes it unlawful for subject persons and entities to make certain payments or provide anything else of value to a non-US government official for the purpose of obtaining or retaining business for or with, or directing business to, any other person. These provisions also apply to non-US companies and their representatives who take any action in furtherance of such corrupt conduct while in the United States. Importantly, the FCPA's application to non-US government officials is broadly interpreted by US authorities and can include officials and employees of state-owned enterprises.

7.2 Economic Sanctions

US businesses also must comply with US economic sanctions, which can extend to non-US acquirors if their activities involve US businesses or they otherwise have certain requisite touchpoints with the United States. US economic sanctions are primarily administered by the Office of Foreign Assets Control ("***OFAC***") of the US Department of the Treasury and are designed to further US foreign policy and its national security interests and objectives. Accordingly, economic sanctions are generally targeted at non-US countries and regimes, terrorists, narcotics traffickers, human rights violators, and those engaged in activities related to the proliferation of weapons of mass destruction and similar perceived threats to the national security, foreign policy, or economic interests of the United States.

Among other things, OFAC's sanctions make it unlawful for a non-US acquiror to involve US companies (and sometimes their non-US subsidiaries), individual US citizens and US green-card holder directors and employees, and anyone physically located in the United States, in business with OFAC-sanctioned countries or other OFAC-prohibited business, unless an OFAC license or exemption applies.

8 Director Fiduciary Duties

Although M&A deals are typically proposed by the senior executive team, the board of directors (or equivalent) of the US target company/seller often must determine whether a potential transaction can proceed beyond an initial exploratory phase. In making their determination, directors of Delaware corporations[14] are subject to, and guided by, two primary fiduciary duties: the duty of care and the duty of loyalty. The duty of care requires directors to engage in an informed and deliberate decision-making process based on all material information reasonably available to them. The duty of loyalty requires directors to act on a disinterested and independent basis, in good faith and with an honest belief that the action proposed to be taken is in the best interest of the corporation and its stockholders. Notably, when a corporation becomes insolvent, the directors' fiduciary duties shift, and the directors have a responsibility to direct the affairs of the corporation to maximize value for the benefit of the corporation and its creditors.[15]

In general, under a standard of judicial review referred to as the "business judgment rule," directors are entitled to a rebuttable presumption that in making decisions they acted in accordance with their fiduciary duties. If the business judgment rule is not rebutted by plaintiffs, it prevents a court from second-guessing board decisions on business matters, including M&A transactions, as long as those decisions are attributed to any rational business purpose. In M&A transactions, however, courts may more carefully scrutinize the decisions of the board and examine the overall decision-making process, including the quality of information consulted, the procedures followed, and the reasonableness of a board's actions.[16]

While fiduciary duties apply to directors of both private and public corporations, if the target company is a public company, there are many formalities and procedural protections that guide a board of directors' participation in an M&A process, including, for example, with respect to the use of outside legal counsel, one or more outside financial advisors and independent committees, or even obtaining an informed vote of minority shareholders. These formalities and procedures are designed to help directors satisfy their fiduciary duties as well as protect the transaction against heightened judicial scrutiny if it is ever challenged in court, but it can sometimes be difficult for non-US acquirors to understand all of the nuanced requirements. As a result, non-US acquirors need to be well-advised as to the role

14 While not always the case, it is common for US target companies/ sellers to be corporations organized under the laws of the State of Delaware. Directors of US corporations that are organized under the laws of US states other than the State of Delaware will be subject to similar fiduciary duties if the state in which they are organized follows Delaware law in this area. If they do not, or if the applicable target company/seller is a non-corporate legal entity, then different considerations may apply.

15 Unlike certain jurisdictions, under US law, directors of an insolvent company do not have a duty to place the company into a bankruptcy or insolvency process, and insolvent companies are permitted to continue conducting business.

16 In certain circumstances that are beyond the scope of this article, directors may be subject to more demanding standards of judicial review when determining whether they discharged their fiduciary duties in the context of an M&A transaction.

of US public company boards and the legal, regulatory, and litigation framework and risks that drive a target company board's actions.

9 Litigation

The United States is known to be one of the most litigious countries in the world. As a result, companies that are investing, or otherwise conducting business in the United States, must be prepared to defend themselves within that system against a wide range of potential complaints relating to their business operations. This can also sometimes be the case with respect to M&A activity, particularly in uncertain economic times, as market volatility tends to embolden activist shareholders.

While litigation related to takeovers of US private companies is rare, litigation related to takeovers of US public companies is common, though generally not a cause for concern. Excluding situations involving competing bids, where litigation may play a direct role in the contest, and going-private or other "conflict" transactions initiated by controlling shareholders or management of the target company, there are very few examples of major acquisitions of US public companies failing due to litigation, or of materially increased costs arising out of litigation being imposed on arm's-length acquirors. Nevertheless, most acquisitions of US public companies involve state law claims by shareholders of the public company related to alleged breaches of fiduciary duties by the public company's board of directors. These claims typically assert that the sales process undertaken by the board of directors and its advisers was insufficient or otherwise flawed, that the price is too low and that deal protection measures to which the company agreed either discourage or prevent third parties from making superior competing bids. These claims, together with claims under US federal securities laws, also typically assert that the disclosure made by the company regarding the transaction in documents used to solicit shareholder approvals was inaccurate or otherwise misleading. While certainly a nuisance, these types of claims, in which shareholders generally seek to delay or prevent the deal and related damages, are usually easily resolved.

10 Human Resources Considerations

Navigating US labour and employment-related considerations can sometimes be a challenge for non-US acquirors, particularly in cases where human capital represents a large percentage of the deal value. In addition to legal and regulatory compliance (such as benefit plan operational concerns and deferred compensation issues), and integration of employees following the transaction, one of the most significant employment considerations is how to compensate and retain key employees of the target company. This issue is often particularly acute when ultimate ownership changes from a US to a non-US jurisdiction.

Developing solid people-management plans that are put into effect at the outset of the transaction and carried out through closing and into the post-closing integration phase can be critically important. Consider the following key points:

- Acquirors commonly enter into new employment arrangements with key members of the target company's management team in connection with an acquisition to help ensure a smooth transition and stable post-closing leadership.

- Most US sellers insist that acquirors maintain a level of employee compensation and benefits (often including performance incentives and severance) – that is similar to the target company's existing compensation and benefits structure – for a transitional period after the closing (typically 12–24 months).

- US employers often use non-compete agreements as a method of preserving critical human capital. The enforceability of these non-compete agreements is, and historically has been, a facts-and-circumstances analysis that varies from state to state. In general, states typically provide that a non-compete agreement is enforceable if it is reasonable in scope and duration and is bargained for in exchange for consideration. The most notable exception to this general rule of enforceability is in the State of California, where non-compete provisions in the employment arena are generally not enforceable by law (however, in certain circumstances, non-compete agreements bargained for in connection with the sale of a business may be enforceable against a key employee who is also a seller of that business). The law in this area continues to evolve, however, and some state legislatures, including in the Commonwealth of Massachusetts, have passed laws that are designed to promote competition and therefore tend to be more favorable to employees. Needless to say, companies with a multi-state workforce cannot take a one-size-fits-all approach to non-compete agreements, and well-advised non-US acquirors carefully tailor non-compete agreements and other restrictive covenant agreements based on the nuanced rules in each jurisdiction.

- Cash and equity incentive plans, including transaction-related bonuses, are often implemented by non-US acquirors and US target companies to stabilize the workforce in connection with a transaction. Establishing these types of programs on a tax-efficient basis is critical. Many US target companies will have existing arrangements for management that will need to be terminated, or in certain transaction structures assumed or otherwise kept in place, upon closing. Costs associated with the termination, cash settlement, or other treatment of a target company's equity or other incentive awards should be considered when a non-US acquiror is negotiating its own incentive compensation arrangements for retained executives, and also should be taken into account when determining the purchase price.

- If a non-US acquiror is seeking to carry out headcount reductions, it may be relatively easier to do so in the United States than in many non-US countries. In contrast to many non-US countries in which employers may only terminate employees for cause, employment in the United States is predominantly "at-will," which means, as a general matter, that an employer can terminate an employee or otherwise change the terms of the employee's employment relationship at any time in its sole and absolute discretion. Although both common law and statutory exceptions to the at-will rule exist, at-will employment is a bedrock principle in the United States. If headcount reductions will be large scale in nature or result in the closing of a particular worksite, there are notification requirements that might be triggered under US federal and state employment laws.

- Trade unions, works councils, and other employee representative bodies are far more common outside the United States than in the United States. Where trade unions are involved, however, there can be significant additional obligations and requirements under the law and any collective bargaining agreements between the employer and the unions. A non-US acquiror will also want to understand the potential costs around any promised increases in benefits or compensation under the terms of a collective bargaining agreement or any such increases that might result from negotiations around the renewal of an expiring collective bargaining agreement.

- Due to employee uncertainties raised by the prospect of a change in control and new ownership, as well as the additional efforts of employees to close a proposed transaction, sellers and acquirors often adopt retention bonus arrangements to incentivize employees to remain employed through, and for a short period of time after, the closing (*e.g.*, 6-12 months).

11 Intellectual Property and Data Protection

11.1 Intellectual Property

Intellectual property ("***IP***") is protected in the United States by a well-developed body of statutory and common law that is designed to protect the owner's right to use IP as well as to prevent the unauthorized exploitation of IP by others. The scope and strength of the protection, however, differ depending on the nature of the IP right. In the case of software products, for example, the protection offered varies significantly if the IP is an unregistered trade secret, statutory copyright, or patent. The industry in which the owner of the IP operates also influences the degree of protection, so the extent and depth of legal due diligence need to be calibrated accordingly. For example, IP due diligence for a biotechnology company is likely to focus on a small handful of patents, whereas IP due diligence for a software company is likely to focus on the processes for ensuring that ownership of IP created by employees and outside developers vests in the target company. Because the default laws designed to allocate ownership of IP rights are not harmonized across jurisdictions or across the different types of IP, the processes for conferring valid ownership of IP in the United States do not necessarily ensure that the target company will enjoy valid ownership of the IP outside of the United States. Consequently, if a non-US acquiror's business plan depends on certain IP rights conferring protection over a particular technology, the acquiror should carefully consider how that technology is, or can be, protected both within and outside of the United States.

In addition to IP owned by a US target company, companies also in-license IP from third parties, in some cases to incorporate into their customer-facing products and services, and in virtually all cases to provide back-office support and technology. In the United States, the default rules for assignability of IP license agreements differ from the treatment of assignability of many other commercial contracts. Diligence on business-critical IP licenses therefore needs to address the possible outcomes, whether the IP license can come across with the business of the target, whether adequate rights can be provided on a transitional basis, or whether a new IP license or alternative arrangements need to be put in place prior to closing the transaction.

11.2 Data Protection

In contrast to some non-US jurisdictions, the United States does not have a single comprehensive federal data privacy and data security law. Instead, there is a fragmented and dynamic patchwork of federal laws and regulations (including a number of sector-specific requirements), state laws, and industry standards or "best practices" that apply differently across jurisdictions, industries, and data subjects.

Since the European Union's General Data Protection Regulation ("***GDPR***") took effect in 2018, however, the data regulatory landscape in the United States has begun to shift significantly towards a more comprehensive regulatory regime.

Starting with the California Consumer Privacy Act, which took effect on 1 January 2020, other US states have adopted their own data protection laws, including Colorado, Connecticut, Utah, and Virginia. Meanwhile, momentum continues to build for a comprehensive federal law.

In light of the increased regulatory push and several largescale data breaches that have occurred in recent years, and given that the non-US acquiror will often assume the liabilities of the US target company for past non-compliance with privacy laws, potential acquirors must tailor their due diligence exercise to the risk profile of the target company. Often, an acquiror's due diligence should focus not only on the jurisdiction in which the target company is domiciled, but also and often more importantly on the jurisdictions and industries in which the target company operates, collects personal data, processes such data, offers products or services, and monitors individuals. For instance, given the GDPR's extraterritorial scope and increased fines for non-compliance, it is important to assess the potential applicability of the GDPR even for US target companies that do not have a strong nexus to the European Union.

Acquisitions in certain industries may also warrant additional scrutiny. For example, even though the US does not have a comprehensive federal data privacy law, it does have a relatively well-developed set of laws that protect financial data and health data maintained by hospitals and their service providers. There are also rules in place that protect children's data, so companies that target products and services at children may carry higher data protection risk.

The USD 123 million fine on Marriott under the GDPR regime for the Starwood data breach, which was already ongoing prior to Marriott's purchase of Starwood in 2016, serves as a reminder to potential non-US acquirors of US businesses to fully investigate the data privacy and data security risks of their targets inside and outside of the United States.

12 Politics and Local Market Practice

12.1 Politics

The role of politics in cross-border M&A varies greatly. Especially in the current post-pandemic climate, it is likely that we will continue to see increasing political intervention in cross-border transactions and heightened levels of regulatory scrutiny and nationalism. This means that non-US investors may need to rethink their approach to and timeline for a transaction, as well as prepare a narrative that is convincing to applicable regulators and other political stakeholders. It is critical to remember for this purpose that "politics" extends beyond federal and state regulators, and includes other constituencies such as key customers, suppliers, and employees, and any such narratives should be tailored accordingly. The importance of identifying in advance the key constituencies that could influence the success of the transaction and figuring out how best to address their potential concerns should not be underestimated. In some cases, particularly in the case of a high-profile transaction in a sensitive sector, or in a situation involving a state-owned enterprise, politics (separate and apart from CFIUS) need to be carefully and thoroughly considered before making any public announcements concerning the deal.

12.2 Local Market Practice

In the same vein, understanding and accepting local market M&A practice can help to ensure a smooth process and, particularly in a competitive auction setting, help to put a non-US acquiror on equal footing with its US competition. While there may be situations in which it is appropriate to depart from market custom and practice, non-US acquirors who blindly insist on doing it "the way we do it at home" often find it difficult to succeed.

Patient and experienced advisers can be useful in this regard. Conforming to local market custom and practice rarely results in unacceptable levels of risk and may even result in better outcomes than can be expected in the home market. And while it is natural for non-US acquirors to want to engage legal, financial, accounting, and other advisers with whom they have worked in the past in their home markets, it is almost always advisable also to engage local US advisers (beginning with the US colleagues of trusted non-US advisers, if applicable) who are familiar with US concepts. These include, for example, US generally accepted accounting principles and common approaches to purchase price adjustments, as well as US market practice more generally, including as it relates to auction practice, disclosure practice, and various other aspects of M&A practice that is detailed elsewhere in this article.

13 Representations and Warranty and Other Transactional Risk Insurance Products

13.1 RWI Overview

Representation and warranty insurance ("***RWI***") has become increasingly popular in the United States, particularly in the private M&A space, and obtaining (or, at least, considering obtaining) an RWI policy is now standard market practice for private transactions. Market acceptance has increased, in part, due to a maturity in the RWI market in which valid claims against RWI policies have been efficiently paid by RWI insurance providers. With the growth in the market and increased competition among underwriters, RWI policies are more affordable and prevalent, and can be implemented on an expedited basis in parallel with the primary deal negotiations. Rarely does the RWI process slow down deal timing; rather, as RWI coverage helps address what are often complex transaction negotiations around post-closing indemnification and other rights, RWI often helps accelerate the primary deal negotiations.

In addition to standard RWI coverage of between 10%-20% of transaction value, larger limits are being placed through the use of "tower" structures, where multiple RWI providers participate using a layered or stacking approach, and the insured receives the benefit of a blended premium rate as the RWI providers higher in the tower charge lower premiums because providers lower in the tower have greater exposure. As the primary RWI insurer leads the RWI process, the use of a tower structure does not typically add any significant burden on the acquiror. More recently, there has been increased demand for RWI that covers true fundamental representations and warranties (*e.g.*, organization, power and authority, capitalization, and brokers fees) with limits often up to purchase price. These "fundamental only" policies are excess to the primary policy and cover losses for breaches of the fundamental representations and warranties after the policy limits on the primary RWI policy have been exhausted.

13.2 RWI Benefits and Limits

The key benefit of RWI to the seller is obvious – the limitation or elimination of the seller's liability for losses incurred by the acquiror after the closing that result from breaches of representations and warranties by sellers or target companies (so-called "no survival deals"). But using RWI can also benefit non-US acquirors:

- RWI can help make the acquiror's bid in an auction process more attractive and, in many cases, obtaining RWI is a requirement imposed by the seller in connection with the auction process in any event.
- RWI can sometimes meaningfully reduce time and effort spent on negotiating the acquisition agreement, which can be a critical factor in a competitive process.
- RWI can be helpful in cases where the acquiror would like to preserve important post-closing relationships with the seller by allowing the acquiror to seek to recover its losses from a creditworthy insurer under its RWI policy instead of directly from the seller.
- The seller may be more willing to expand the substantive coverage of its representations and warranties and reduce the use of knowledge and materiality qualifiers, thereby expanding the acquiror's basis for recovery under the RWI policy.

RWI, however, has its limits. As the name suggests, RWI only covers the acquiror's losses that result from unknown breaches of the seller's/target company's representations and warranties and not losses that result from breaches of the seller's/target company's covenants. RWI also does not cover known issues or matters that are the subject of a deal specific indemnity, and typically does not cover other types of known risks, contingent or otherwise.[17]

RWI has successfully been used in connection with transactions involving distressed assets and sales in the bankruptcy context (*i.e.*, Section 363 sales), which are addressed briefly below in Section 14 (*Distressed*

17 There are certain exceptions to this general rule, but they are beyond the scope of this article.

Acquisitions). While each distressed situation involves certain complexities and, therefore, more scrutiny is likely to be given by the RWI provider in connect with the sale of a distressed asset, particularly outside of the formal bankruptcy process, RWI has been and can be obtained in such situations. It is worth noting that to the extent the RWI providers see a transaction as more likely to attract a claim against the RWI policy, the pricing of any RWI policy is likely to be higher than the typical RWI policy.

Often, an RWI policy covers a pre-closing tax indemnity if contained in the underlying purchase agreement, or it will contain a "synthetic" pre-closing tax indemnity, providing coverage for a target company's pre-closing taxes. However, such coverage normally will not cover taxes that are accrued but not yet payable for pre-closing periods, transfer taxes, or known tax issues.

13.3 Tax Insurance

Both in the context of a transaction or otherwise, tax issues may arise. In order to limit a non-US acquiror's (or taxpayer's) potential downside risk if there is an adverse determination by a taxing authority, the use of tax insurance has become more prevalent in recent years. Tax insurance policies cover, for example, matters like the tax-free nature of a transaction or the tax consequences of a pre-closing reorganization. Such policies are often used, in the transaction context, if an uncertain tax risk is not covered under the RWI policy. Whether tax insurance will be available for any particular matter is a very fact specific inquiry and will depend, in large part, on how comfortable the tax insurance provider is that the tax matter will not result in a loss under the policy in excess of the retention.

13.4 Contingent Risk Insurance

Another type of transaction risk insurance that is sometimes used is contingent risk insurance. This type of insurance is used to cover the potential loss associated with a known contingent liability, such as an adverse determination in a pending lawsuit, that would typically not be covered by RWI. Because the risk is known, contingent risk insurance tends to be expensive compared to RWI or tax insurance policies. But in the right situation it can protect a non-US acquiror against potentially significant losses if the risk actually materializes. Similar to tax insurance, whether contingent liability insurance will be available for any particular matter is a very fact specific inquiry and will depend, in large part, how comfortable the contingent risk insurer provider is that the contingent liability will not result in a loss under the policy in excess of the retention.

14 Distressed Acquisitions[18]

A financially distressed US target company may present opportunities for non-US acquirors to invest in the United States on financially attractive terms, but these types of transactions can also present significant risks. For example, an acquiror seeking to purchase assets from a financially distressed company should be aware that the transaction may be subject to unwinding if the seller files for bankruptcy after the sale and the seller (i) sold the assets with the actual intent to hinder, delay, or defraud creditors, or (ii) received less than reasonably equivalent value in exchange for its assets and was insolvent at the time or became insolvent as a result of the sale. The potential lookback period to unwind the transaction ranges from two to six years, depending on applicable state law. Additionally, if a seller files for bankruptcy after signing a purchase agreement, but prior to closing the sale, it may have the opportunity to reject, or repudiate, the purchase agreement. Further, even if the transaction closed prior to the bankruptcy filing, the seller could seek to reject related transaction documents that include ongoing post-closing obligations such as guarantees, transitional services arrangements, or other commercial agreements entered into as part of the transaction. A counterparty to a rejected agreement is generally entitled only to an unsecured damages claim, which claims often receive little to no value in a bankruptcy. While certain mitigations may be available in these circumstances, it is usually not possible to eliminate these risks entirely.

Given these challenges, potential acquirors sometimes seek to purchase a distressed target company's assets through a US bankruptcy process commonly referred to as a "363 sale" or a plan of reorganization. Pursuant to the US Bankruptcy Code, a debtor can sell its assets "free and clear" of all liens, claims, and encumbrances, which provides significant protection against post-closing "successor liability" claims against the acquiror and the risk that the transaction will be unwound. In addition, acquiring assets through such a bankruptcy process eliminates the requirement to obtain third-party consents to assign certain leases and contracts, provides an expedited waiting period under the HSR Act (as described above), exempts sales from certain state laws, including bulk sales and stockholder approval, and exempts plan sales from transfer taxes. However, bankruptcy sales also generally require broad public notice, a robust marketing process, and a public auction to ensure that the ultimate sale price reflects the "highest and best" offer available. While sales in bankruptcy can be accomplished efficiently, these requirements can cause delay, increased costs and competition, and third-party scrutiny.

Another route to acquisition of a distressed US target company is a "loan-to-own" strategy, which involves lending to the distressed target company or purchasing a controlling amount of the outstanding debt of the distressed target company

18 Please note that the US bankruptcy laws are complex and the discussion herein is general and does not cover all aspects of US bankruptcy laws or exceptions from general principles.

(generally at a discount), in either case with the goal of acquiring the target company through an in-court or out-of-court debt-to-equity conversion or purchasing the target company's assets through a partial or full credit bid. An acquiror may leverage its creditor position to exert control over the restructuring process, including through threat of foreclosure. Executing on a loan-to-own strategy can be complex, and if not done properly, can result in recharacterization of the debt as equity, subordination of the debt, limitations on credit bidding, and lender liability, among other things.

15. CONCLUSION

Non-US acquirors seeking to invest in the United States can navigate the related jurisdictional, cultural, and commercial complexities with proper planning and consideration of the relevant issues. While each cross-border M&A transaction will present a set of unique considerations, an awareness of, and flexible and creative approach to, the most common issues that accompany US M&A deals, will help secure a successful outcome and achieve the parties' commercial objectives.

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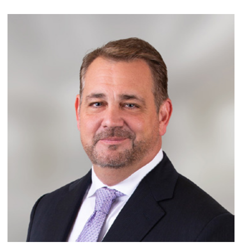

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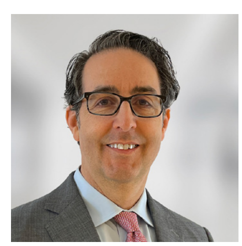

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