

KIRKLAND ALERT

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Increasing U.S., Global Scrutiny of Foreign Investment: Things to Watch

In the past several weeks, stakeholders on both sides of the Atlantic have voiced increasing skepticism and concern regarding the potential impact of foreign investment on national security.

For example:

- **Germany.** On Wednesday, July 12, the German Federal Government Cabinet adopted a new directive increasing the German government's power to scrutinize acquisitions and public takeovers of German companies, with a focus on those operating in "critical infrastructure" sectors (e.g., software, telecom, energy).¹
- **France.** French president Emmanuel Macron has called for the EU to consider regional measures to investigate and block acquisitions by non-EU investors.²
- **United States.** In June, Rep. Rosa DeLauro (D-CT) introduced a bill that would require the Committee on Foreign Investment in the United States ("CFIUS") to undertake a "net benefit" assessment for all transactions that it reviews, and specifically consider a transaction's impact on U.S. food safety, public health, productivity, and economic activity.³ Separately, Sen. John Cornyn (R-TX) stated he will propose legislation to expand CFIUS' authority.⁴
- **Canada.** Canada's Conservative leader Andrew Scheer recently criticized a Chinese takeover of a Canadian satellite technology and technology company, stating that "*Canada's defense policy cannot include selling national-security secrets to appease communist dictatorships.*"⁵

Notably, the prospects of formal regulatory changes outside of Germany remain uncertain. Nevertheless, the possible secondary effects of the changing global policy and political environment, including planning for longer transaction review timelines and practical considerations for managing uncertainty (e.g., outside termination dates), on individual transactions should be considered and proactively addressed. But, these impacts can often be mitigated with careful advance planning, and may present opportunities for creative solutions to transaction challenges.

We summarize below four key items for our clients to consider in the near term.

1. **Transactions with a China nexus may create particular challenges for deal timing and certainty, especially if a prospective Chinese investor may gain access to export-controlled or "bleeding edge" technologies.**

Global debate over balancing foreign investment and national security continues to affect the environment for cross-border transactions.

- The U.S. government [has warned](#) that Chinese investors are targeting U.S. artificial intelligence capabilities through transactions not notified to CFIUS and of which CFIUS may not easily become aware, including smaller investments and investments in third-country companies.
- Germany's directive is generally considered to express a reaction to 2016's wave of takeovers of German companies by Chinese investors. Notably, Germany was the largest EU recipient of Chinese investment in 2016.⁶
- Risks may arise not only from pure-play acquisitions by Chinese buyers, but also from syndication to Chinese investors and use of Chinese banks (state-owned or private) to secure deal financing.
 - In this regard, it is worth noting that President Obama's executive order blocking the takeover of Aixtron SE's U.S. business by a consortium of Chinese investors [specifically cited financing](#) from a Chinese state-owned bank as a source of national security risk.

National security risk may arise in industries that have not been traditionally considered "sensitive," as well as from minority investments.

2. There is increasing recognition that national security risk may arise outside of traditional transaction structures and "change of control" transactions.

- The new German directive permits investigations of "indirect acquisitions," i.e., transactions involving EU-incorporated vehicles ultimately funded by non-EU sources.⁷
- During a recent Senate Intelligence Committee hearing, Central Intelligence Agency Director Mike Pompeo suggested that "*there are many . . . ways one could invest in an entity here in the United States and exert significant control over that entity,*" and that such transactions should also fall within CFIUS' purview.⁸

3. U.S. and EU stakeholders increasingly perceive national security risk as arising in sectors that have not historically been considered sensitive, or from economic factors.

- For example, there is a growing consensus that food security is a key part of U.S. national security:
 - On March 14, 2017, Senators Grassley (R-IA) and Stabenow (D-MI) [introduced a bill](#) that would add the Secretary of Agriculture and Secretary of Health and Human Services as permanent members of CFIUS.
 - Secretary of Commerce Wilbur Ross affirmed during his confirmation testimony that "*[f]ood is certainly an element of national security by any measure.*"⁹
- Germany's Minister of Economics highlighted a lack of investment reciprocity in acquirers' home countries as justification for the new directive.¹⁰

4. But, the concept of national security is not without limits.

- In contrast to Rep. DeLauro's call for CFIUS to evaluate the potential impact of a transaction on U.S. economic security, Secretary of the Treasury and chair of CFIUS, Secretary Mnuchin, has emphasized that, "*Fundamentally, we want to keep CFIUS as a national security review and we want to deal with economic issues separately. We don't want to confuse those issues.*"¹¹

Looking forward to 2H17 and beyond, interested parties should carefully evaluate the dynamic, multijurisdictional foreign investment clearance landscape at the outset of any potential transaction. Careful planning for investment clearances early in the deal process is critical to maximize competitive positioning, and to minimize the likelihood of adverse consequences on deal feasibility, timing, certainty, and cost.

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¹ Guy Chazan, "Germany Expands Powers to Block Takeovers," *Financial Times* (Jul. 12, 2017), available at <https://www.ft.com/content/5087c106-66fc-11e7-9a66-93fb352ba1fe?mhq5j=e2>.

² "France's Macron: EU needs to screen foreign investment," *Reuters* (Jun. 22, 2017), available at <http://uk.reuters.com/article/uk-eu-trade-macron-idUKKBN19D1KR>.

³ H.R. 2932, *Foreign Investment and National Security Act of 2017* (Jun. 16, 2017).

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- ⁴ Saleha Mohsin, “Mnuchin Seeks Greater Scrutiny of Chinese Investments in U.S.,” *Bloomberg Politics* (Jun. 14, 2017), available at <https://www.bloomberg.com/news/articles/2017-06-14/mnuchin-seeks-greater-scrutiny-of-chinese-investments-in-u-s>.
- ⁵ Robert Fife and Steven Chase, “U.S. Rebukes Canada over Chinese takeover of Norsat,” *The Globe and Mail* (Jun. 12, 2017), available at <https://beta.theglobeandmail.com/news/politics/us-rebuked-canada-over-chinese-takeover-of-norsat/article35294914/>.
- ⁶ Thilo Hanemann and Mikko Huotari, “Record Flows and Growing Imbalances: Chinese Investment in Europe in 2016,” The Rhodium Group (Jan. 10, 2017), available at <http://rhg.com/reports/record-flows-and-growing-imbances-chinese-investment-in-europe-in-2016>.
- ⁷ Chazan, *supra* n. 1.
- ⁸ Senate Intelligence Committee Hearing (May 11, 2017), available at www.washingtonpost.com/news/politics/wp/2017/05/11/full-transcript-acting-fbi-director-mccabe-and-others-testify-before-the-senate-intelligence-committee/?hpid=hp_hp-top-table-main-mccabe-testify%3Ahomepage%2Ft-home&hpid=hp_hp-top-table-main-mccabe-testify%3Ahomepage%2Ft-home.
- ⁹ *Hearing on the Nomination of Wilbur Ross to Be Secretary of Commerce Before the H. Comm. on Commerce, Science and Transportation*, 114th Cong. (2017) (statement of Wilbur Ross, Nominee for Secretary of Commerce).
- ¹⁰ Chazan, *supra* n. 1.
- ¹¹ Saleha Mohsin, “Mnuchin Seeks Lawmakers’ Help to Fix Foreign Investment Panel,” *Bloomberg*, June 6, 2017, available at <https://www.bloomberg.com/politics/articles/2017-06-06/mnuchin-seeks-lawmakers-help-to-fix-foreign-investment-panel>.

If you have any questions about the matters addressed in this *Kirkland Alert*, please contact the following Kirkland authors or your regular Kirkland contact.

Mario Mancuso, P.C.
Kirkland & Ellis LLP
655 Fifteenth Street, N.W.
Washington, D.C. 20005
www.kirkland.com/mmancuso
+1 202 879 5070

Dr. Anna Schwander
Kirkland & Ellis International LLP
Maximilianstrasse 11
80539 Munich
Germany
www.kirkland.com/aschwander
+49 89 2030 6044

Luci Hague
Kirkland & Ellis LLP
655 Fifteenth Street, N.W.
Washington, D.C. 20005
www.kirkland.com/lhague
+1 202 879 5195

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