The Latest Developments in Cross-Border Transactions

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This issue of the Bloomberg Law Special Reports offers the latest insights on how new policy, regulations, and court actions are impacting international corporate transactions. We look at key areas of uncertainty, including Brexit and the European Union, and the coming impact on business and law practice.

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Greater Scrutiny Awaits Foreign Investment in U.S.

By Ellen Sheng

The Foreign Investment Risk Review Modernization Act, which passed Congress last August, widened the scope of foreign investment activity that can be scrutinized for national security concerns. While primarily aimed at Chinese investments, the new review process by the Committee on Foreign Investment in the U.S. has broad implications for U.S. law practices, especially in technology-related and other sensitive areas.

The committee's heightened influence means companies and law firms working on cross-border deals need to have a good understanding of CFIUS. Many companies, anticipating regulatory pushback, are taking precautions to structure their deals in a way that doesn't raise concerns.

The new law expands the purview of CFIUS, according to Bloomberg Law.

"Since the second half of the Obama administration, CFIUS has been marching toward a broader and broader conception of what are sensitive transactions," said Scott Flicker, partner at Paul Hastings and chair of the firm's Washington, D.C., office. "The statute is a validation of that broader concept of sensitivity that CFIUS had been already busy implementing."

Once a relatively obscure body, CFIUS now looms larger than ever in foreign investment deals in the U.S. The committee has always presided over deals involving sensitive technology, such as anything involving the military. The new law expands CFIUS's purview, according to Bloomberg Law, to include foreign investment in a U.S. business that "maintains or collects sensitive personal data of U.S. citizens that may be exploited in a manner that threatens national security."

Concern over personal data is why Beijing Kunlun Tech now needs to sell the popular gay dating app Grindr. FIRRMA also introduces mandatory filing requirements, including fines for noncompliance, for deals that meet certain criteria and are in one of 27 industries.

More and more companies involved in cross-border M&A need to take CFIUS guidelines into consideration. Many are restructuring deals by coming up with mitigating measures: limiting the board presence of foreign investors, limiting foreign access to sensitive information, spinning off or excluding businesses that could be sensitive, making smaller investments, and other adjustments.

"Deals will continue to get done, but what you are seeing is another year of an unprecedented number of transactions going through the committee for review," said John Carlin, who chairs Morrison Foerster's global risk and crisis management practice group and is a former assistant attorney general for the Department of Justice's national security division.

CFIUS, an interagency committee created in 1975, has long had the authority to intervene in any transaction that fell within its purview. It previously did not require companies to file before a transaction. Companies could close their transaction and face the possibility that the committee might intervene after the fact.

Now, transactions involving a foreign government and certain sensitive sectors such as critical infrastructure, critical technologies, or sensitive, nonpublic information on U.S. citizens need to file with CFIUS. The penalty for not filing is a hefty fine that can be as much as the amount of the acquisition.

The act implemented a pilot program last November that includes the new mandatory filing requirement. The pilot is in place until the Treasury Department, which chairs CFIUS, releases regulations that will likely include all of FIRRMA as well as things not included in the pilot program.

The committee came to the forefront amid heightened nationalism and an increasing number of foreign investments from China, sparking concerns about leaking technology secrets to foreign investors. Chinese investment in the U.S. rose to an all-time high of $46.5 billion in 2016, then dropped to $29.7 billion in 2017 and $4.8 billion in 2018, according to the Rhodium Group.

Driving the decline were changes in domestic Chinese policy that cracked down on outbound investment, increased friction in the U.S.-China relationship, and heightened scrutiny by CFIUS.

The committee's workload increased from 100 cases in 2010 to 238 in 2017. With the new mandatory filing procedures, CFIUS expects 1,000 cases in 2020. The committee now has more staff and more money to help wield its authority. Its budget more than doubled to $15 million for fiscal 2019, and the committee has requested a budget of $35 million for 2020.

CFIUS can take a few years to clear a filing.

The increased scrutiny is expected to put even more of a damper on Chinese investment in the U.S. "While FIRRMA applies to all non-U.S. buyers, it will make it even harder – for indirect as well as direct – China deals," said Mario Mancuso, partner at Kirkland & Ellis. Mancuso, as a former U.S. under secretary of Commerce for industry and security, was a decision-maker in CFIUS and is also the author of *A Dealmaker's Guide to CFIUS*.

Given how long it can take CFIUS to accept and clear a filing, which can be anywhere from three months to a few years, companies are being proactive in taking precautions.

Flicker says he's seeing more companies trying to engage in prophylactic mitigation. That could mean restricting the ability of a foreign investor to get information that a company might have. A company might also impose requirements that only U.S. citizens on the board or in the executive suite be empowered to protect information from the foreign investor.

Companies might go ahead and try to close a deal before getting CFIUS approval, then point to mitigating measures in case CFIUS has reservations. In addition to CFIUS, companies need to watch out for new interpretations of what regulatory bodies might consider sensitive to national security.

The Export Control Reform Act of 2018 started a process to identify and control "emerging" and "foundational" technologies that are essential to national security. The Department of Commerce is expected to issue guidelines on what technologies will fall into this category and be subject to export controls.

AT A GLANCE:
Key Changes Under FIRRMA

- Lowered threshold for control and expanded categories of covered transactions
- Changes to investor rights and arrangements designed to evade CFIUS covered
- Certain real estate transactions are covered transactions
- New short filing format
- New mandatory filing requirements
- CFIUS authorized to conduct pilot programs under FIRRMA

In this changing environment, with the new authority granted to CFIUS and other regulatory authorities, companies can expect increased scrutiny over foreign investment deals.

"There is now unprecedented use of resources, new authority to impose penalties," Carlin said. "If you're doing cross-border deals, you need to know CFIUS well enough."

Ellen Sheng is a writer and editor with a focus on business, finance, fintech, and U.S.-Asia investments.

Complications Multiply for Cross-Border M&A

By Katherine Gustafson

Merger and acquisition activity has been at record highs for the past two years, but the volume and size of deals are both declining in 2019. The value of M&A transactions in the first quarter — at $876.7 billion — was down 9.1 percent from the same period in 2018, and reflected 333 fewer transactions.

A slow first quarter is common in international dealmaking, however, and M&A activity often picks up later in the year, according to Bloomberg Law. Further, despite this recent cool-off, there's plenty of money available for new transactions, even as various global forces affect the cross-border M&A landscape. These include national security concerns focused on Chinese investment, uncertainties about Brexit and slow growth in Europe, and the volatility stemming from a potential trade war or government shutdown in the U.S.

U.S. lawmakers and regulators have been working to define and regulate technology that presents potential national security risks in today's interconnected world.

In August, Congress passed the Foreign Investment Risk Review Modernization Act, which authorizes the Committee on Foreign Investment in the United States to conduct a pilot program to discern how to control foreign investment in "critical technologies." These might include defense, telecommunications, and aerospace, as well as essential infrastructure such as utilities and health care.

M&A activity often picks up after the first quarter, according to Bloomberg Law.

The program requires certain international transactions to be declared 45 days before closing, after which CFIUS has 30 days to act. Failure to declare prompts a penalty up to the value of the transaction. In the past, CFIUS reviews were voluntary and involved no waiting periods or fines.

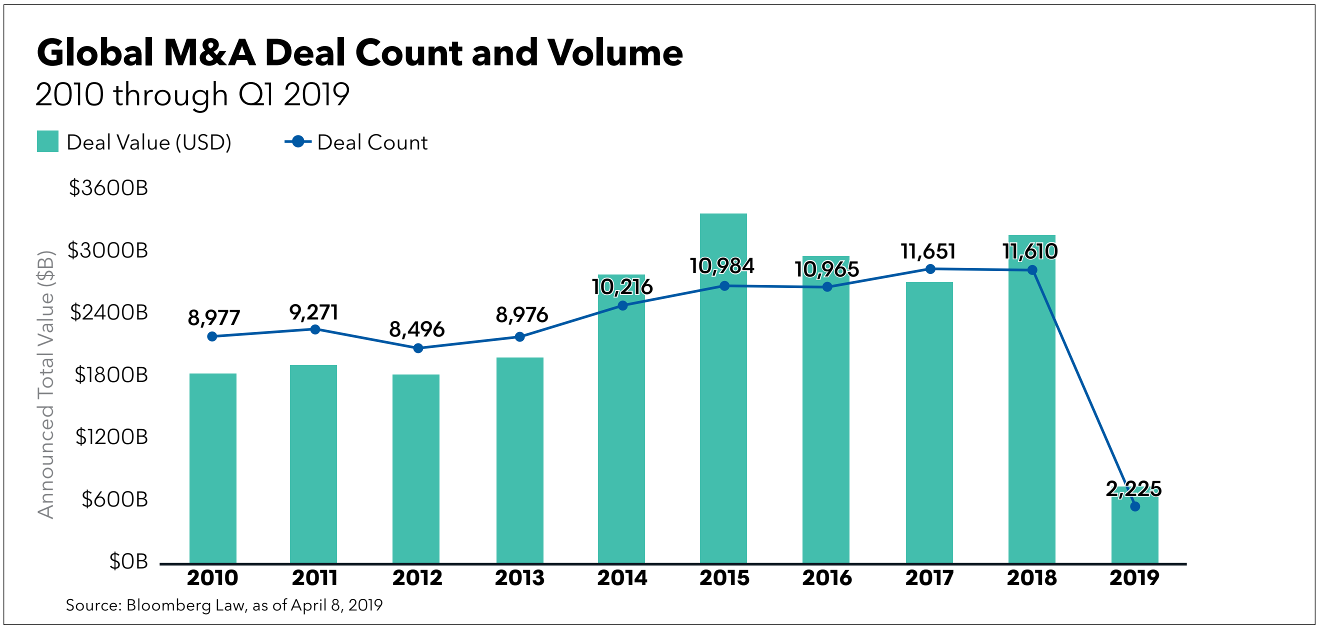
This new approach reflects a growing concern over international actors using investment in U.S. technology to gain leverage that may threaten national security. The rules will prompt declarations for transactions that would previously have gone unnoticed because they would have been considered lower-risk. This expanded, mandatory review is driving Chinese investors away as the Trump administration gets aggressive in relations and trade with the Asian superpower.

"The foreign investments climate in the U.S. is pretty open for people from every place in the world except for China," said Adam Emmerich, partner at Wachtell, Lipton, Rosen & Katz. "There is no Chinese M&A activity in the U.S. People don't even bother to apply. Perhaps things will change if and when there's a trade deal."

Instead, Chinese investors are looking to Europe, which also is trying to restrict investment in critical technologies. In March, the European Union introduced a framework for screening deals with foreign buyers, which member states must now enact as law. Restrictions on international deals are likely to ripple across the M&A landscape.

"I think it's good that we're being careful that companies are not being misallocated through foreign investments," said Jan Willem van Drimmelen, global head of corporate client services at Intertrust. "But this will also have a meaningful impact on M&A activity, at least from a process perspective. It'll be a more intense, more time-consuming process."

Political uncertainty and sluggish economic growth are also part of the near-term picture for cross-border M&A. Experts point to a sense of hesitancy in M&A due to ongoing questions about how political developments will play out and what effect they'll have on markets.



The continuing doubt about Brexit and slow growth across Europe are contributing to a stressed European business climate. Despite a generally strong M&A showing on the global stage, European dealmaking is said to be "in credit-crisis-level doldrums," with European M&A down by 35 percent compared to this time last year. The first quarter of this year was the worst quarter for M&A activity in Europe since 2013, according to Bloomberg.

Brexit in particular is creating a sense of suspended animation among dealmakers as they await clarity. Other investors, however, are motivated by the perceived insecurity; as some European economies evince weakness, investors are alert to good deals.

"Transactions still occur in times of uncertainty, and great fortunes have been won by bravery amidst chaos and fear," Emmerich said. "But most people look at Brexit and say, 'Gosh, what is the long-run future? If the U.K. economy ends up being a tattered ruin as a result of Brexit, anything I buy in the U.K. is going to be worthless.'"

It's certainly true that the near-term outlook for cross-border M&A incorporates its share of tumult. But that factor's also present in equity markets, which has bumped up interest in M&A among some companies looking for an exit. Both valuations and volatility are high enough that some companies are finding M&A more attractive than an initial public offering.

Accordingly, an emerging trend in 2019 is "dual-tracking" – companies simultaneously preparing for an IPO and pursuing an M&A deal, usually via auction.

"Some companies that were thinking of doing an IPO are now flipping into M&A," said Michal Berkner, a partner at Cooley LLP in London. "We didn't see that as a prominent trend last year, but definitely this year."

While a dual-track process likely involves more complication, resource expenditure, and risk than choosing one or the other, it allows companies to pursue the highest bidder. In some situations, they can get double the anticipated IPO amount through an M&A.

This trend is partly due to the U.S. government shutdown early in 2019 that halted ongoing IPOs and bought time for buyers to approach companies about M&A possibilities. In an uncertain climate characterized by the chaotic forces inherent in ongoing trade wars, potential sellers may be more aware of IPOs' disadvantages in relation to the attractive cut-and-dried nature of M&A – namely, that an IPO is not a complete exit and will likely include lockups on share sales.

"For founders, there's an advantage of doing a deal," Berkner said.

National security and uncertainty are defining the dynamics of M&A in 2019. While they haven't dampened international dealmaking enthusiasm in any substantial way, at least outside Europe, these forces are sure to have an effect on M&A for the remainder of the year and beyond.

Katherine Gustafson is a writer specializing in business topics including accounting, management, and innovation.

U.S. Litigation Poses Risks to Foreign Companies

By Lisa Singh

For foreign firms with U.S. operations, the prospect of U.S. litigation is increasing, along with a wide range of regulatory requirements in different industries. To manage the risk, businesses will need to start with a comprehensive legal strategy.

The threat of U.S. litigation is increasingly real.

"The ever-changing and increasingly complex body of regulation and case law in the U.S., coupled with the broad reach of U.S. regulators and courts, is making it more challenging for foreign companies to navigate," said Edward Kirk, a partner in Clyde & Co's New York office.

In dealing with globalization, intellectual property issues, and policy uncertainty, both stateside and abroad, companies face a widening range of worldwide liability – hastened in some cases by the growth of litigation funding vehicles, notes Andrea Neuman, partner with Gibson, Dunn & Crutcher.

In this environment, the threat of U.S. litigation is increasingly real for nearly any business with stateside operations.

"The more business you do in the United States, the more likely it is that you'll be sued here," said Atif Khawaja, partner at Kirkland & Ellis in New York. However, the effects of litigation will vary across industries.

"A new, foreign entrant in our consumer goods market is likely to find itself facing a products liability suit one day," Khawaja said. Industries with a few large players will continue to spark antitrust attention, he added, while companies on the cutting edge of science and technology will face additional intellectual property disputes.

In the decade since the financial crisis, regulatory reach has broadened to include scrutiny of foreign firms with operations in the U.S.

"Many of the largest U.S. regulatory settlements involving violations of the Foreign Corrupt Practices Act, anti-money laundering, sanctions, and other regulations have been paid by companies based outside of the U.S.," Kirk of Clyde noted. Companies that issue securities on a U.S. exchange or that engage in U.S. transactions regarding other securities are increasingly likely to face a U.S. securities class action, he added.

Nor do litigation risks show any signs of abating under the current administration, as demonstrated by various sanctions regimes spearheaded by the Office of Foreign Assets Control.

"The threat of U.S. litigation to enforce the U.S. criminal and civil laws incident to trading with OFAC-sanctioned countries cuts across all industries of international stature within each sanctioned country, and remains a significant commercial risk," said J.P. Douglas-Henry, global co-chair of DLA Piper's litigation and regulatory practice.

The impact of lawsuits is likely to be felt almost immediately, according to Bloomberg Law.

The recent decision by the Trump administration to implement Title III of the Helms-Burton Act, allowing U.S. nationals to seek damages in U.S. courts from foreign companies that operate on properties seized by the Cuban government, also holds far-reaching implications.

Even as lawsuits may consume years in the legal system, their impact is likely to be felt almost immediately, said Peter Harrell, a fellow at the Center for a New American Security, a Washington-based research group, as reported by Bloomberg Law.

As regulations increase litigation risk, companies may face potentially onerous discovery obligations that can occur on several fronts.

Despite varying case law, U.S. courts continue to grant application for discovery under Section 1782, in some cases to a foreign-based subsidiary, involving documents used in foreign proceedings. "1782 presents ongoing and expanding risk because, as the U.S. follows the possession, custody, and control rule, a lot of companies, for business reasons, are moving to unified platforms for information sharing," Neuman of Gibson Dunn said.

Meanwhile, mounting U.S. litigation risk ensures discovery will remain a challenge for foreign firms – compounded by the prospect for conflicts with home country legal systems, particularly where data privacy laws diverge.

"In the United States, broad rights [of litigation parties to] compel each other to produce large amounts of records pose potential problems with, for example, European companies whose records may be subject to the GDPR," Khawaja said. Even stateside, companies face conflicting legal requirements that heighten litigation risk.

Divergent privacy laws may drive conflicts with home country legal systems.

"In areas where there is no overarching federal law, foreign companies may find it particularly difficult to understand the applicability of state laws and their interplay with federal regulations," Kirk said, citing varying data breach disclosure and notification laws. "As customers may reside in various states, companies may be subject to a wide range of different rules and regulations."

Formulating a coherent legal strategy at the outset is essential, experts say. This is imperative as companies often underestimate the fees associated with managing litigation requirements. "While the complexity of the case will determine the likely costs of discovery, those costs frequently exceed parties' expectations," Douglas-Henry said.

"The key really is proactive planning [across] three areas," Neuman said, citing jurisdiction, corporate separateness, and information management considerations. "It's critical to be well-informed on the rules of engagement, both locally and globally."

As a first measure, companies should monitor and understand their level of contacts with the U.S. – for example, whether a company has a physical presence and customers stateside, Khawaja said. He stresses that the obligation to preserve evidence exists where there is even reasonable anticipation of litigation.

Further, beyond retaining counsel with cross-border litigation expertise, companies can minimize cost and exposure through due diligence.

"A lot of litigation can be avoided with advance planning," Khawaja said, "and by paying closer attention to U.S. law before a dispute ripens into a full lawsuit."

Lisa Singh is a writer specializing in business and technology matters.

International Dispute Resolution Poised for More Growth

By Shaheen Pasha

Dispute resolution is a growth area for international law firms, as globalized business creates opportunities for specialization and an influx of litigation finance players helps fund plaintiffs to pursue cross-border legal action.

With businesses spread across different markets, it is common for legal cases to have some international component to them. But dedicated cross-border litigation and arbitration remain fairly niche practices, divided among a small group of international law firms.

The exclusivity of the practice is with good reason. Transnational cases are often complex and high profile, involving multiple legal jurisdictions, evolving international treaties, and high political stakes, impacting both international commercial entities and sovereign states.

The Apple-Qualcomm case involved more than 100 legal proceedings around the globe, according to Bloomberg Law.

A dedicated practice with expertise in the local culture, language, and legal complexities of any foreign market is a competitive advantage for law firms. It's an area with immense opportunity, legal experts say.

"The global economy is of course increasingly interconnected, and as more and more commerce happens across borders, disputes will arise," said Daniel Gonzalez, partner at Hogan Lovells in Miami.

And international disputes often end up in the news, especially when they deal with matters of intellectual property and patent law in the technology sector.

The recently resolved Apple-Qualcomm case, for instance, was a particularly prominent international legal battle, spanning two years and involving billions of dollars in technology licensing fees. While the two tech giants – represented respectively by the law firms of Fish & Richardson and Cravath, Swaine & Moore – did not reveal the deal's financial terms, they announced they were dismissing global litigation related to the case. The battle between the corporations involved more than 100 legal proceedings around the globe, according to Bloomberg Law.

Such wide-ranging and prolonged cases are expensive to pursue. That's where litigation finance comes in, serving as a growth driver for the international dispute resolution practice. Litigation finance firm Vannin Capital projected dispute funding by litigation finance companies would grow 20 percent to 30 percent each year, reaching $2.1 billion to $2.7 billion by 2021, according to a special report by Bloomberg Law.

The growth in litigation finance, especially financing for international arbitration, has resulted "in a number of claims being brought that could not have been brought previously because of a lack of resources," Gonzalez said. International arbitration is growing at a faster clip than litigation, he added, driven in part by challenges to enforcement of litigation judgments across borders.

The Convention on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the New York Convention, ensures the recognition and enforcement of foreign arbitral awards among its signatories. Arbitration centers are becoming more common globally, and not just in power locations such as Paris and Stockholm. That portends more growth in arbitration as an international dispute resolution practice.

"When you see (markets) such as Singapore, Dubai, and Hong Kong opening up arbitration centers, it's an indication that they think this will be the wave of the future," said Timothy Webster, associate professor and director of Asian Legal Studies at Case Western Reserve University. "Arbitration seems to be a growth area globally," due to its enforceability across borders.

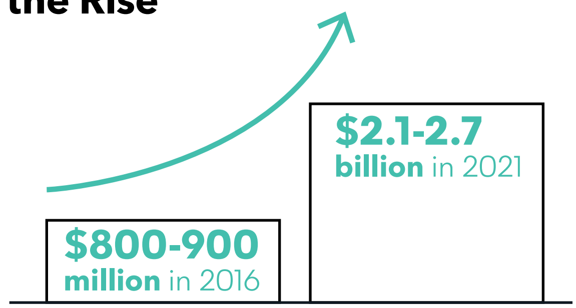
But when it comes to litigation, there are no similar international treaties to ensure foreign countries abide by judgments. In a vibrantly growing economic market like China, for instance, that can be problematic, Webster said. Though China is a signatory of the New York Convention, unless a Chinese company has assets in the U.S. or another country, such as the U.K. or South Korea, that enforces U.S. judgments, there will be little financial benefit to winning a judgment in a U.S. court.

International law firms can find profitable opportunities.

There is hope, however. The 2017 fraud case *Liu Li v. Tao Li and Tong Wu* out of China made headlines in the legal world after Wuhan Intermediate People's Court took the unprecedented step of enforcing an American judgment. After a California judge ordered compensation of almost $150,000 to settle the claim for a fabricated share transfer, Liu filed in Wuhan Court to enforce the judgment, as both plaintiffs held assets in China. Legal experts saw the Wuhan Court's decision as a potential opening in China's policy toward acceptance of foreign judgments.

But even without a giant shift in enforcement policies or any international treaties recognizing judgments, international law firms can find profitable opportunities. Jef Klazen, partner at Kobre & Kim in New York, said a number of corporates are beginning to appreciate the need for counsel specializing in high-end collections and enforcement of judgments and arbitration awards.

Global Dispute Spending by Litigation Finance Firms on the Rise



Source: Vannin Capital

Collections and enforcement work within international dispute resolution can involve going after specific assets to collect on an award or, in some cases, gathering evidence and information to initiate proceedings in jurisdictions friendlier to enforcement.

"In such cases, we have done things like freezing international bank accounts, foreclosing on luxury mansions, and putting a debtor's offshore companies into liquidation," Klazen said.

Such legal work is a "growing area because there's somewhat of an unfulfilled need for it, and the market is catching up to an increase in demand," he added. "Many clients may not even know at the beginning that the right solution for their particular case may involve taking legal action across several jurisdictions."

Shaheen Pasha is a writer and journalism professor, focusing on legal and financial issues.

WTO Decision May Set Confrontation With U.S. Tariffs

By Stephanie Cohen

A recent landmark decision by a panel of the World Trade Organization could mean a showdown over President Trump's authority to impose tariffs on steel and aluminum.

The WTO's affirmation of its right to review "emergency" retaliatory trade measures in response to national security concerns stemmed from a 2016 case in which Ukraine accused Russia of restricting the movement of goods that passed through the Russian Federation to other nations, including Kazakhstan and the Kyrgyz Republic. Russia argued that such restrictions are not subject to WTO scrutiny. The WTO rejected that position in an April decision, before agreeing with Russia's argument that the situation between the two countries constituted an "emergency in international relations" — as outlined in the articles of the General Agreement on Tariffs and Trade.

"Russia lost the argument [over WTO jurisdiction] but won the case," said William Reinsch, a chair at the Center for Strategic and International Studies and a senior adviser at international law firm Kelley Drye & Warren.

The president has relied on Section 232 to restrict imports, according to Bloomberg Law.

The panel's decision may open the door for more countries, including the U.S., to claim retaliatory trade measures are a response to self-determined national security concerns. But the WTO also concluded that an essential security exception can be objectively reviewed by a panel to determine whether it was made in good faith, a position at odds with the Trump administration's assertion that such matters can only be determined by nations themselves.

The administration called the ruling "seriously flawed." The U.S. has argued GATT Article XXI's drafting history shows the intent to prevent the WTO from substituting its judgment regarding the validity of a national security justification for that of member countries, according to the Congressional Research Service. The Trump administration also sees national security as a broad and powerful tool when it comes to shaping trade policies.

The president has relied on Section 232 of the Trade Expansion Act of 1962 to restrict imports of products he sees as a threat to U.S. national security, according to Bloomberg Law. Trump imposed additional tariffs of 25 percent and 10 percent on steel and aluminum imports for most countries beginning in June 2018, following a Section 232 determination. In November 2018, the WTO Dispute Settlement Body agreed to requests from seven members to establish panels to hear the case over these Section 232 tariffs and retaliatory countermeasures, which is the first step in the formal dispute process.

The WTO panel decision in the Russia-Ukraine case is not a binding precedent, which leaves the panels reviewing U.S. cases to make their own determinations, but Reinsch said it is reasonable to assume the WTO panels will not take up the U.S. matter "in a vacuum." The U.S. could argue the WTO panel went beyond its mandate in establishing authority to review these matters, Reinsch said.

In fact, WTO Director-General Roberto Azevedo called the panel's decision to intervene in a regional security matter such as the Russia-Ukraine conflict a "very dangerous development," saying, "Issues that are sensitive enough to bring up national security concerns should be treated politically and not technically at the dispute settlement mechanism of the WTO."

The WTO decision in the Russia-Ukraine case puts GATT members on notice to act in good faith and not just relabel a protectionist trade measure as a national security interest, said Thomas Allen, a shareholder in Greenberg Traurig's International Arbitration & Litigation practice. Allen thinks the U.S. "has a harder path to convincing a WTO panel that it has acted properly under Article XXI."

The U.S. steel and aluminum tariff issues before the WTO probably won't be decided until after the 2020 presidential election. "The WTO process doesn't move that fast," said Lewis Leibowitz, an international trade attorney. A WTO panel decision should not be expected until late 2019, at the earliest, and if the U.S. loses there, it will still have the right to appeal the decision before the WTO Appellate Body, Leibowitz said. "The current uncertainty about the continued functioning of the Appellate Body after 2019 could mean that the appeals will take much longer than is customary."

The Russia-Ukraine decision puts GATT members on notice to act in good faith.

Trump's position that he has unilateral power to impose tariffs received support stateside from a March 25 Court of International Trade decision in *American Institute for International Steel, Sim-Tex, and Kurt Orban Partners v. United States*. The court rejected a constitutional challenge to Section 232 tariffs on imports of steel and aluminum products brought by the AIIS.

AIIS challenged the "essentially unlimited definition of national security" in this statute and its "limitless grant of discretionary remedial powers," according to a March 27 trade report from Sandler, Travis & Rosenberg. In its decision affirming the tariffs, the court noted that it was bound by a 43-year-old Supreme Court precedent set by *Federal Energy Administration v. Algonquin SNG*, which gives the president substantial flexibility under Section 232 to "regulate commerce by way of means reserved for Congress, leaving very few tools beyond his reach."

Assuming the decision is not overturned, it could "increase the likelihood of additional Section 232 tariffs on automobiles and auto parts and other products," according to Sandler, Travis & Rosenberg.

The CIT decision "is likely to give more urgency" to efforts in Congress to move legislation that would restrict the president's Section 232 authority, according to a trade update by law firm Neville Peterson.

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