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Cross-Border M&A Considerations for Your Next U.S. Acquisition

By Matthew F. Gorra & Thomas S. Pilkerton III

As world markets continue to converge and strategic and financial buyers seek merger & acquisition opportunities on the global stage, many buyers are finding attractive opportunities in the U.S. Whether your goal is to capture the largest consumer market in the world, purchase technology that can be leveraged by your entities outside the U.S., or strike a joint venture with a U.S.-based business, every C-suite and business development executive should consider the issues discussed below during the early stages of transaction planning.

Choosing the Acquisition Structure

Legal and tax structuring should be considered early in the process of any deal. Are you intending to transfer the cash flow from the U.S. operations to your non-U.S. affiliates or shareholders? Or, are you a private equity buyer that seeks to infuse equity and debt capital into the target with visions of a future exit? Answers to these questions will likely have a material impact on the structure of the acquisition and the relationship between the target and your other business interests. Fortunately, the U.S. legal and business culture generally offers acquirers broad flexibility to structure transactions to suit their business goals.

U.S. corporate laws permit you to choose whether your acquisition will be an asset purchase, stock acquisition, merger, joint venture, loan arrangement, or any combination thereof. As with any transaction, you should speak with your tax lawyers and accountants early in the process to help you determine the ideal structure, take into consideration tax transfer pricing alternatives and weigh the benefits, costs and ease of closing the deal under each scenario. Even if you have done prior transactions in the U.S. and believe you have the optimal structure, it is important to regularly check in with your advisors to test your assumptions given the frequent changes in national, state and local laws, including recent changes in the U.S. federal tax regime impacting foreign investments.

Acquisitions are usually accomplished using either a Subchapter C corporation or a pass-through tax entity, such as a limited liability company. Most often, these entities are formed in the State of Delaware to take advantage of its well-developed corporate jurisprudence. Non-U.S. investors should be pleased to learn that these entities provide limited liability protection and their equityholder structures are not generally made available to the public. Rather, ownership ledgers, transfers of equity and changes in director designations are largely maintained as a matter of internal corporate governance.

Negotiating the Deal

Typical rules of engagement apply to transaction negotiations in the U.S. Buyer and seller typically negotiate a non-binding letter of intent with a period of exclusivity, and then seek to reach agreement on the primary business terms and execute definitive agreements during the period specified in the letter of intent. Although there is heavy emphasis placed on legal due diligence, there is equal emphasis placed on the negotiation of representations and warranties and indemnities within the definitive purchase agreement.

An experienced lawyer can be valuable in navigating the nuances of these concepts and advising you on the comparative law differences between what is standard in the U.S. and your home country. For example, one notable difference between U.S. deals and deals in Europe is that U.S. transaction documents typically do not incorporate reference to a data room or a legal or tax advisor's due diligence report as part of, or as general exceptions to, the seller's representations and warranties. Instead, the rights of the parties are contained within the confines of the definitive purchase agreement and its schedules and exhibits. Further, post-closing purchase price adjustments based on trued-up financial statements (e.g. completion accounts) are the market norm in the U.S., whereas the locked-box mechanism is trending in Europe.

With respect to the allocation of liabilities between the parties, within the past three years, we have seen an increasing use of representations and warranties insurance to bridge negotiation gaps related to holdbacks, indemnity baskets and caps, and special indemnity items. Note that the terms and coverage of U.S.-based policies (including deductibles and retentions) often differ from policies underwritten in the U.K. or other jurisdictions and should be carefully reviewed.

You are best served by engaging a legal advisor with experience on a high number of recent merger & acquisition transactions, which should give you access to the firm's institutional knowledge on similar deals in your industry sector. This will give you the confidence that the final deal terms are within market and reflect the best thinking on evolving legal issues.

Regulatory Compliance

If you are a non-U.S. buyer, your legal advisors can help you navigate several U.S. regulatory regimes that apply to U.S. deals. A few of the most frequently encountered are noted below:

a) HSR: The Hart-Scott-Rodino Antitrust Improvements Act of 1976 generally requires parties to transactions exceeding certain thresholds to file premerger notification reports with the Federal Trade Commission and U.S. Department of Justice. The parties must also observe pre-closing waiting periods (typically 30 days) while the transaction is evaluated for any anti-competitive effects or violations of U.S. antitrust laws.

b) CFIUS: The Committee on Foreign Investment in the United States (CFIUS) is provided with broad powers to block and unwind certain types of foreign investment in the U.S. that may impact national security and U.S. critical infrastructure. While the impact on critical infrastructure is determined on a case-by-case basis, the sectors most likely to raise potential issues are energy, defense, telecom, transportation, finance, chemicals, food/water and public health. The filing with CFIUS is a voluntary proceeding and the review period is 30 days, but may be extended for an additional 45 days.

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c) Foreign Asset Control: For foreign policy and national security reasons, the U.S. imposes economic sanctions against various countries, entities, individuals and organisations. The sanctions prohibit certain transactions and may require a freezing of assets. The Office of Foreign Assets Control (OFAC) administers and enforces these sanctions programs, which may impact foreign investments or operations once an investment is made.

d) BEA Filings: Every transaction resulting in a non-U.S. person owning at least 10% of the voting securities of a U.S. business is subject to reporting requirements with the Bureau of Economic Analysis (BEA). The filings include (i) a new investment survey, (ii) quarterly reports, (iii) annual reports, and (iv) quinquennial (five-year) reports. While the reports do require disclosure of equity ownership and certain financial information, including inter-company transactions, each of the reports is confidential and may be used by the BEA only for analytical and statistical purposes.

e) Industry-Specific: Depending on the industry and operations of the target, other regulatory regimes may apply. For example, if the target has classified contracts with the U.S. Government, a FOCI (foreign ownership, control or influence) analysis should be conducted to assess the relevant factors and determine a proper mitigation strategy.

Operational Considerations

Before taking on the responsibility of owning a U.S. company, you need to be aware of the myriad of legal requirements within which the target company must remain in compliance in the operation of its business. The following aspects of U.S. law deserve the attention of non-U.S. buyers due to their impact on the target's operations:

a) Export: The Export Administration Regulations (EAR), International Traffic in Arms Regulations (ITAR) and other U.S. export rules and regulations govern the export and reexport of goods, hardware, software and technology. For example, the EAR contains a list of controlled items requiring an export license and the ITAR imposes strict rules governing the export of defense articles and services, including technical data.

b) Labour: The labour and employment laws of the U.S. are generally employer-friendly. The default principle in most states is that employees are employed "at will" and may be terminated without statutory severance or a works council meeting. However, in connection with a mass layoff or facility closing, certain federal and state laws may apply. For example, the Workers' Adjustment and Retraining Notification Act generally requires an employer with 100 or more employees to provide 60 days' prior notice of termination or else provide pay and benefits when improper notice was given.

c) FCPA: The Foreign Corrupt Practices Act (FCPA) makes it a crime to make a payment to a foreign official for the purpose of obtaining or retaining business for or with, or directing business to, any person, or otherwise influencing such foreign official. The FCPA does not require that a corrupt act succeed in its purpose and the law has been interpreted broadly to cover a wide variety of actions, types of payments and gratuities. Liability under the FCPA also extends to the acts of employees, representatives and affiliates and can cover acts authorised within or outside the U.S.

d) Other: Non-US investors and parent companies should also keep in mind: (i) federal and state environmental regulations, (ii) the Agricultural Foreign Investment Disclosure Act of 1978, (iii) US anti-dumping and countervailing duty laws, and (iv) US immigration laws.

Final Takeaway

You can develop a sound U.S. acquisition strategy by observing the general advice discussed above. Similarly, after you make your acquisition, we recommend that you maintain a regular focus on U.S legal compliance that includes coordination between your internal business teams and outside counsel.

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