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ACQUISITIONS BY CHINESE COMPANIES IN THE UNITED STATES

Chinese company acquisitions of U.S. businesses, fueled by China's growing economic power, are on the rise. Such transactions require regulatory approvals in China and in some cases may be blocked in the U.S. by national security concerns or fears of job loss. Given their very different culture and relative inexperience in the U.S. market, Chinese buyers will need expert advice on the U.S. deal-making process and U.S. sellers may seek special protective measures to enforce their rights and collect post-closing amounts due them from Chinese buyers.

By Andrew M. Ross *

The People's Republic of China and the United States of America are key trading partners, with economies that are intertwined and interdependent. The relationship has been growing as a result of numerous factors and will certainly continue to grow substantially. This is to be expected not only with respect to Chinese foreign direct investment (FDI) in the United States generally – which is already quite significant in investments such as U.S. government securities – but with respect to acquisitions by Chinese businesses of U.S. businesses.

This article will review the trend of China's business acquisitions in the U.S., discuss some of the major factors unique to such transactions, and suggest possible deal terms the parties should bear in mind in order to achieve their objectives. As this article will make clear, although such acquisitions are subject to particular challenges, with the use of experienced acquisition advisors both in preparation for and execution of a deal,

the transactions can be completed and the principals achieve their business objectives.

ACQUISITION DATA AND RECENT TRENDS

Historically, China had not engaged in making substantial FDI. This began to change in approximately 2001.¹ For the period of 2000-2007, China's worldwide FDI is estimated at U.S. \$68 billion,² an amount reflecting dramatic growth and a very significant amount

¹ Karl P. Sauvant, *Is the United States ready for foreign direct investment from emerging markets? The case of China*, in Karl P. Sauvant, Wolfgang A. Maschek, and Geraldine McAllister, eds., *Foreign Direct Investment from Emerging Markets: The Challenges Ahead* (New York: Palgrave Macmillan), chapter 18 (forthcoming).

² Sauvant, *supra* note 1.

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for traditional, less developed countries, although still a small amount as compared with FDI by many developed nations. There have been various factors identified as being key drivers in China's growing FDI. In particular, there is the desire of Chinese companies, supported by ministries of the Chinese government, to secure raw materials and energy supplies, and to enhance China's prestige.³ Other factors are also becoming important.

Most China FDI to date is reported to have taken place in less developed nations and in a few developed countries such as Australia and Canada. However, this geographic locus appears to be broadening.⁴ Although reliable data regarding the magnitude of China US FDI, much less China worldwide FDI, are often limited and on occasion inconsistent, they seem clear as to underlying trends and informative as to rough magnitudes. The worldwide economic downturn, China's favorable export balance, its supply of foreign currency, including U.S. dollars, its businesses' strong balance sheets, and its interest in investing in countries that are politically and economically stable have facilitated and will result in further China FDI in developed nations. This will enhance opportunities for Chinese companies to invest in or acquire companies that have recognized international brands (including perhaps ones for which Chinese buyers serve as original equipment manufacturers), established distribution channels, valuable intellectual property, and research and development facilities.⁵ FDI made in the form of

minority investments, whether through the public markets or in private transactions, has accounted for most China FDI in businesses in the United States to date. For example, China Investment Corporation (CIC) (just one source of China government financing, in addition to other government entities, state-owned entities (SOEs), and private companies) acquired over \$9 billion worth of United States shares in 2009.⁶ Some current limitations should be noted. While China "greenfield" investments in the United States are being actively sought by many states and localities, such investments have not been substantial.⁷ Acquisitions or control investments also have been few and small in aggregate dollar amount in comparison to minority investments in the U. S. Also, Chinese acquisitions in the U.S. are small in comparison to acquisitions from many other countries. However, the number of control acquisitions – including investments which result in a change of control even if not 100% ownership – both pursued but not consummated and those consummated, has been increasing and there is noteworthy public discussion and expectation in both China and the U.S. that the rate of growth will increase dramatically.⁸

Appendix A lists publicly announced Chinese acquisitions (as well as failed acquisitions) of U.S. businesses from 2004 through 2009. (References in

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Global: Examining China's Outbound Investment, China Insights, January 2010.

⁶ *In Disclosure to S.E.C., China Lists \$9.6 Billion in Shares of U.S. Companies*, The New York Times, February 9, 2010 at B4; see also Clarence Kwan, *Chinese Outbound Investment – Now a Headline Story*, Deloitte U.S. China Services Group, October 2009 (research suggests that Chinese companies may have invested \$7-10 billion in the U.S. to date).

⁷ Kathy Chen, *U.S. Cities Seek to Woo Chinese Investment*, The Wall Street Journal, April 6, 2010.

⁸ Luo, *supra* note 4; Sauvant, *supra* note 1; UCLA, *supra* note 5; RSM McGladrey, *supra* note 3. Some commentators question less the trend of FDI, but its future growth rate. See Chen, *supra* note 7.

³ RSM McGladrey, *From Inbound to Outbound: The Gradual Shift of Chinese Business Investments*; The New York Times, February 9, 2010, p. B4.

⁴ Zhongwei Luo, *China Overseas Investment Characteristics and Strategy*, China Securities Daily, November 5, 2009; Financial Times Limited, reprinted Chinadaily.com, December 4, 2009.

⁵ Luo, *supra* note 4; Sauvant, *supra* note 1; UCLA Asian American Studies Center, *Foreign Direct Investment (FDI), U.S./China media brief*, 2010; Chen Weihua, *Hard Journey for Chinese Investment in U.S.*, China Daily, December 4, 2009, reprinted from Financial Times Information; Derek Scissors, *Drowning in Cash, Chinese Foreign Investment: Who, What and Why*, The Heritage Foundation, June 15, 2009; Benesch Friedlander Coplan & Aronoff LLP ("BFCA"), *China Goes*

Appendix A and in this article to “acquisitions” mean “control acquisitions.”)

Appendix A was compiled by the author and does not purport to necessarily be a complete list of all such acquisitions. The number of both attempted and successful acquisitions, as well as the dollar amount involved, are small compared with Chinese minority FDI in the U.S. over this period. The table does support the fact that the number of acquisitions is growing. For example, while there was only one completed transaction from 2004-2006, there were nine in 2009. Most of the recent acquisitions have been for small or middle market businesses, and those that were consummated have generally not been high profile transactions. In fact, higher profile transactions may face more potential obstacles, as discussed below, although most such obstacles can be overcome, also as discussed below. As Appendix A also illustrates, deals done to date appear to be for strategic business, rather than financial, purposes.

FACTORS DIFFERENTIATING CHINESE ACQUISITIONS

Chinese acquisitions of United States businesses basically involve all the U.S. regulatory issues and other considerations as any U.S.-inbound cross-border transaction. However, there are additional considerations and extra sensitivities pertaining to Chinese acquisitions that do not bear upon typical inbound acquisitions by companies based in developed countries. These are discussed below.

China Regulatory Approvals

China FDI is subject to a complex opaque regulatory system, but one that is becoming easier to work with and more supportive of FDI. Three major China national government bodies that must potentially approve transactions are the Ministry of Commerce (MOFCOM), the State Administration of Foreign Exchange, and the National Development and Reform Committee.⁹ Approval can pertain to both the acquisition itself and the right to export foreign currency. The approval of provincial authorities and industry-specific authorities may also be required in various instances. For smaller and less sensitive transactions, much approval authority has been shifted from national to provincial authorities. In the case of industry approvals, industries are divided into three categories: those in which FDI is encouraged; those in which it is permitted; and those in which it is

prohibited (generally those involving unique national interests). For example, in the case of a national SOE, the approval of a national ministry is necessary, while for a provincial SOE, the appropriate provincial authority must approve. In many cases, approvals can be obtained on a pre-transaction basis (*e.g.*, based on a letter of intent), which is some evidence of China’s goal of facilitating FDI, and otherwise after the definitive purchase agreement is signed. As part of the approval process, the Chinese buyer must provide information regarding the target and the terms of the transaction. It used to be, but is generally understood to no longer be the case, that the buyer also had to demonstrate the economic benefits and efficiencies to be derived from the transaction. New MOFCOM regulations were adopted in 2009 to encourage and facilitate FDI and they may in fact have effectively obviated this former requirement.¹⁰ Nevertheless, while many commentators are of the view that the Chinese government’s goal is to support acquisitions generally, including in the United States, especially by government entities and SOEs, the approval process is still often considered to be multi-tiered and viewed as incorporating vague subjective factors, being subject to uncertain timing, and potentially leading to unexpected results.¹¹ For example, the proposed acquisition of Hummer from General Motors by a provincial SOE truck company was abandoned due to the buyer’s failure to obtain the requisite regulatory approvals, although the significance of this is uncertain since it appears from media sources that the buyer failed to submit the appropriate requests and/or supporting documentation rather than the transaction being rejected on its merits.¹² A prospective buyer’s ability to obtain all necessary government approvals on a timely basis is a transactional risk that may be perceived as greater in the case of a Chinese buyer than for buyers from many developed nations. As discussed below, the seller may seek to address this risk to protect itself.

United States Regulatory Approvals

Acquisitions in the United States by Chinese companies are subject to the same U.S. regulatory

⁹ BFCA, *supra* note 5.

¹⁰ *Id.* China also has made efforts to facilitate loans to SOEs for FDI, and private companies have been successful in obtaining funding to finance FDI. See also, Stratford Global Intelligence, *China: Reviving an Overseas Acquisition Strategy*, February 19, 2009.

¹¹ Luo, *supra* note 4; RSM McGladrey, *supra* note 3; UCLA, *supra* note 5.

¹² Norihiko Shirouzu, *Failure of Hummer Bid Highlights China’s Murky Regulatory Process*, *The Wall Street Journal*, February 25, 2010.

regime as acquisitions by any other non-U.S. buyer, although the impact of these regulations for Chinese acquirers may be more or less problematic, depending upon the particular regulations and the circumstances.

*Section 721 of the Defense Production Act of 1950, as amended (CFIUS).*¹³ The purpose of CFIUS and the regulations thereunder¹⁴ is to authorize the president to suspend or prohibit any acquisition, merger, or takeover when, in the president's judgment, there is credible evidence to believe that in such transaction the foreign person exercising control over a business engaged in interstate commerce *might* (emphasis added) take action that would threaten to impair national security.¹⁵ CFIUS and the regulations apply to "covered transactions," meaning any merger, acquisition, or takeover that is proposed or pending by or with any foreign person which *could* (emphasis added) result in foreign control of any person engaged in interstate commerce.¹⁶ CFIUS permits the parties to a covered transaction to make a notice filing (which requires extensive information and creates a legal liability for false information) with the Committee on Foreign Investment in the United States ("CFIUS" or the Committee), but does not legally obligate the parties to do so. If the parties do file a notice, then the Committee, acting for the president, has 30 days to review the transaction and decide whether to conduct a 45-day investigation to determine the effects of the transaction on U.S. national security. In addition, absent such notice, appropriate government personnel and bodies can require the Committee to conduct such a review under certain circumstances, and it must conduct an investigation if the acquirer is a foreign government-controlled entity. Alternatives available to the U.S. government are to take no action regarding the transaction, seek to suspend or prohibit it, negotiate an agreement intended to mitigate the transaction's consequences relative to national security or, for a period of three years after the transaction is completed

but subject to limited exceptions, to seek divestment.¹⁷ The principal advantage to the parties in giving notice under CFIUS is that, upon doing so and assuming the transaction is not blocked, the government cannot require divestment post-closing. In actuality, as shown by Appendix B, very few notices are filed and even fewer investigations are conducted.

Nevertheless, the potential impact of CFIUS and the potential adverse U.S. political reaction to an acquisition by a Chinese entity, especially a Chinese governmental body or an SOE, have already proven to be problematic in deals involving at least two Chinese buyers and may continue to be so in the future. One example is the attempt in 2005 by CNOOC LTD. to purchase UNOCAL, which was abandoned due to public resistance.¹⁸ More recently, an acquisition of a controlling stake of a U.S. gold mine company by a Chinese provincial SOE was abandoned when the Committee announced that it intended to recommend to the president that he block the transaction.¹⁹ The articulated basis for the national security concern was that the gold mine was located 50 miles from a U.S. military installation.²⁰ By contrast, there was only mixed public commentary concerning the attempted purchase by a Chinese provincial SOE of Hummer from General Motors. The decision whether to make a CFIUS filing, the resultant potential delays, and possible adverse outcomes, may involve more political sensitivities (especially if the buyer is not a private entity) than most covered transactions and, as discussed below, raise considerations and potential risks, which should be considered by the parties together with their advisors. It should be noted that CFIUS filings are not public and are not even obtainable via FOIA request.

¹³ Section 721 of the Defense Production Act of 1950, 50 App. U.S.C. 2170 (as amended by the Foreign Investment and National Security Act of 2007).

¹⁴ 31 CFR Part 800 *et seq.*

¹⁵ The full scope of sectors and matters that may be deemed to threaten to impair national security is uncertain. See Kenneth Y. Hui, *National Security Review of Foreign Mergers and Acquisitions of Domestic Companies in China and the United States*. This may include areas such as energy resources, raw materials, infrastructure, and critical technologies.

¹⁶ Control does not require a majority ownership position but can exist based on other factors. 31 CFR Part 800.203(b). See Hui, *supra* note 15.

¹⁷ In 1990, President Bush ordered the post-closing divestiture of MAMCO Manufacturing, a U.S. aircraft parts company, by China International Trust and Investment Corp. as to which a CFIUS notice had been filed by the buyer but the CFIUS review had not been completed at the time the deal closed.

¹⁸ UCLA, *supra* note 5; Chen Weihua, *Hard Journey for Chinese Investment in U.S.*, China Daily, December 4, 2009, reprinted from Financial Times Information.

¹⁹ Matthew L. Sullivan, *Mining for Meaning: Assessing CFIUS's Rejection of the Firstgold Acquisition*, Publicist Vol. 4, Spring 2010 (an online publication of the Berkeley Journal of International Law).

²⁰ *Id.* However, some commentators have questioned whether the real reason was concern regarding the loss of control of natural resources.

Hart-Scott-Rodino. An acquisition by a Chinese company of a U.S. business is subject to the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended²¹ (the HSR), on the same terms as any acquisition of a business engaged in interstate commerce by a foreign acquirer.²² Assuming at least the U.S. target is engaged in interstate commerce, an HSR filing must be made if the HSR size of the parties and size of the transaction tests are met, regardless of whether the buyer does business in the United States. Chinese acquirers must comply with the HSR obligation to file with the U.S. government authorities the required information, including disclosure of the buyer's ultimate parent entity, as defined for HSR purposes. The HSR filing also requires disclosure regarding the acquirer's business operations; however, this only pertains to its operations in the U.S. so a Chinese acquirer (or any other foreign acquirer) would not have to disclose its non-U.S. business operations. Some foreign buyers have been uncomfortable with the required HSR disclosures, and in light of Chinese sensitivities and perceptions of the U.S., especially in the case of government entities and SOEs, it is possible that some prospective Chinese buyers may consider whether or not to proceed with a transaction as a result of an HSR filing requirement. However, in light of the limited use of HSR information, which is kept confidential, in general such disclosure should not be a barrier to a transaction.

U.S. Securities Laws

United States securities laws and regulations pertain, *inter alia*, to acquisitions of companies registered thereunder (*i.e.*, public companies) in several respects, which can vary depending upon the terms and structure of the transaction.²³ By their terms, these laws and regulations apply no differently to a proposed acquisition by a Chinese buyer of a public company than to any similar acquisition by any other foreign buyer. However, the issue may be one of varying SEC sensitivities to a transaction. For example, at one end of

the spectrum, a friendly purchase for cash of all of the stock of a public company by a Chinese buyer may raise no special concerns. On the other hand, a hostile offer (generally a rare event), or a purchase proposed to be paid for partly in cash and partly in shares of a Chinese buyer that is not itself a public company in the U.S., or a purchase by a Chinese buyer of a controlling interest but not all of the shares of a public company, are each more likely to raise sensitivities and thus a more detailed SEC review of the filed documents. The use of shares of a foreign buyer of a U.S. public company would almost certainly involve a public offering, and thus the need to register under the federal securities laws and make all requisite filings. This would be much more burdensome than would be required in a cash deal. A purchase, even for cash, of a controlling stake, but not all the shares, of a public company may trigger enhanced SEC review, especially if the buyer is a Chinese government entity or an SOE. In those cases, among other matters, the SEC may question whether the motivations of the buyer in operating the company going forward will be purely financial considerations congruent with the financial interests of the remaining stockholders or may also involve political aspects. Accordingly, especially depending upon the nature of the Chinese buyer, it may be well-advised to give special consideration to the terms of any attempted acquisition of a U.S. public company. None of the Appendix A transactions, or attempted transactions, involved SEC registration.

Transactional Practices and Experience

Prevalent factors in foreign investments and acquisitions in China, especially in the early days of such transactions, have been differences between buyers and sellers in transactional practices, language, cultural expectations, and deal experience. Due to the early stage and limited number of China-to-U.S. inbound deals, such factors are now likely to be germane to acquisitions by Chinese buyers in the U.S. For example, as a general perception, as compared with their U.S. counterparts, Chinese businesses often engage in a slower deal process and prefer shorter, "looser," or less detailed agreements with disputes resolved by discussion and mediation. Litigation or binding arbitration is seen only as a last resort. However, these approaches generally will not best serve Chinese buyers in the U.S. market and could likely prove to be against their interests. In addition, many potential Chinese buyers do not have experienced international deal makers. Even those that do are unlikely, as a whole, to have comparable, if any, experience in making acquisitions in

²¹ 15 U.S.C. 18a.

²² While acquisitions by or from foreign government entities of assets located in that foreign country are exempt from the HSR filing requirements, HSR Rule 802.52, an acquisition by a foreign government entity of a business engaged in interstate commerce is not exempt.

²³ While these laws and regulations do not empower the SEC to approve or disapprove transactions, the SEC review process is often an effective means by the SEC of lengthening the time to effect a transaction, and thus potentially result in its abandonment.

the U.S.²⁴ Moreover, acquisitions primarily of raw materials and energy supply companies are not necessarily the optimal background for acquisitions of the types of businesses most likely to be acquired in the U.S., such as those involving significant intellectual property, research and development facilities, recognized brands, and distribution channels. This lack of experience with the U.S. market may disadvantage them in comparison not only with U.S. buyers, but also relative to many buyers from developed regions, such as Europeans with their established history of U.S. acquisitions. Accordingly, it is particularly important that while developing experience in the U.S. market, Chinese buyers have expert help in understanding upfront the U.S. deal-making process, including being advised as to what at any given time are customary business terms, such as the amount of a break-up fee. They will also need guidance in taking appropriate actions and obtaining appropriate protections. These include conducting due diligence and obtaining satisfactory contractual terms, such as adequate seller representations and warranties and, at least in the case of non-public targets, indemnities.

U.S. Public Perception

In many respects, acquisitions in the U.S. by Chinese buyers may prove to be as or even more politicized than the initial acquisitions in the U.S. by Japanese buyers. At the time such Japanese acquisitions first became prevalent, they raised significant concerns that U.S. major businesses and assets were being bought up by the Japanese. This xenophobia existed even though overall European acquisitions surpassed Japanese acquisitions. While Japan may have been viewed at that time as an economic rival, it was a political ally. China and the U.S. though are viewed by many in both countries as economic rivals and in certain respects political rivals. From a U.S. perspective, this perception may result in China acquisitions being more likely to be problematic under CFIUS and in the court of public opinion, especially if the buyer is a government entity or SOE.²⁵

For example, both union and non-union employees, as well as a seller's community, might be particularly concerned that a Chinese acquisition may result in the relocation of plants and jobs to China.²⁶ As a consequence, the parties may need to take steps to satisfy these constituencies, including perhaps adopting measures to preserve U.S. operations, at least for a period of time. If Chinese buyers are willing to establish themselves in the sellers' communities and retain operations, these issues should be of much less concern. Acquisitions by Chinese buyers are also potentially subject to adverse pressures as a result of the macro-political environment. Both the U.S. government and U.S. businesses have raised concerns and objections to various Chinese practices, including for example, allegations that China is artificially holding down the value of its currency and the on-going censorship dispute between China and Google. The result of this environment, especially in the case of larger deals or deals involving Chinese government buyers or SOEs, may be to increase opposition political pressure or heighten the risks under CFIUS. There is of course nothing that an individual buyer can do regarding the macro-political environment other than attempt to ameliorate its impact on a given transaction. For example, the buyer might announce (and perhaps contractually commit to) positive measures, and follow through on them, serving to evidence that the various constituencies should not have meaningful concerns regarding the transaction and post-closing activities.²⁷ Another oft held perception in the U.S. is that in China ownership of others' intellectual property is not adequately respected. While this is frequently cited in regard to pirated entertainment intellectual property, such as movies and music, if sellers are sufficiently concerned about protecting their intellectual property or other confidential information, this might adversely affect their willingness to disclose proprietary information in the due diligence process.

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Don Lee, *China Spends, U.S. Wins?*, McClatchy Tribune, March 7, 2010. Chinese perception of the U.S. might also impact Chinese government attitudes towards investments in the United States.

²⁶ Jia Lynn Yang, *Shanghaied in Florida*, Time Inc., March 6, 2006; Benjamin A. Shobert, *When China Comes to Iowa*, Asia Times Online, May 4, 2007.

²⁷ While not the focus of this article, joint ventures may not result in the same level of concern and political pressures. See Renewable Energy Group press release, *Joint Venture between Celo Wind Power LP and Shenyang Power Group for a total cost of approximately \$1.5 billion*, October, 29, 2009.

²⁴ Several of the buyers listed in Appendix A do have some experience with the U.S. financial markets by virtue of being foreign private issuers publicly traded in the United States or some experience with United States business practices generally by virtue of having first established their own operations in the U.S. prior to any acquisition.

²⁵ This was a possible concern relevant to President Bush's 1990 divestiture post-closing of the purchase of MAMCO Manufacturing, a U.S. aircraft parts company, by China International Trust and Investment Corp. and perhaps also affected the Firstgold deal in 2009. Weihua, *supra* note 18;

Forms of Chinese Acquiring Entities

As noted above, Chinese acquirers can either be government entities, such as CIC, SOEs (either national or provincial), or private companies. Although government entities have been active in acquisitions outside the U.S. and in FDI in the U.S., to date in the U.S. this has only been in the context of minority investments rather than in control transactions. In the event that a government entity was to seek an acquisition in the U.S., there is an enhanced likelihood that political pressures and scrutiny in the mandatory CFIUS investigation would be heightened. In the case of SOEs, they also face potential political pressures and mandatory investigation, although the pressure might not necessarily be as severe as in the case of a government entity. Note that the proposed acquirers of Firstgold Mine and Hummer were provincial SOEs (*see* Appendix A). As noted, the Firstgold deal was abandoned after the Committee announced it would recommend that the president block the transaction under CFIUS, and while the Hummer deal died due to the failure to obtain Chinese regulatory approval, at least some commentators believed that eventually it would have been blocked on the U.S. side. Accordingly, a party considering selling a U.S. business to a Chinese government entity or an SOE should consider the potential unique implications of such a deal, including whether to shy away from any such buyer or to seek special protections in the transaction. While some of the same concerns can be applicable, although certainly to a lesser extent, in the case of a buyer that is a Chinese private entity, in fact commentators are reporting a rise in U.S. acquisitions by Chinese private entities.²⁸

Post-Closing Activities and Regulation

In all cross-border acquisitions, the buyer must be prepared, at a minimum, to operate the acquired business in accordance with in-country legal requirements, if not “best practices.” While, for example, there are meaningful differences in various legal requirements between the U.S. and many European countries (for instance, labor laws are often more favorable to employees in European countries), there is generally understood to be a much greater disparity between the breadth and strictness of many U.S. domestic legal requirements (both federal and state) pertaining to business operations as compared with Chinese domestic legal requirements, as well as regarding the level of compliance with the respective requirements. Just a few examples are the WARN Act, OSHA, non-

discrimination laws, and environmental standards. As a result of this, Chinese managers of acquired businesses may face particular needs and challenges in this area, ranging from particular difficulty in explaining these U.S. legal requirements to superiors in China, the need for enhanced reliance on U.S. staff to identify, explain, and address these matters, and more use of outside experts to advise them regarding their obligations and options. These concerns may also affect the consummation or terms of a transaction, especially if the buyer accepts an earn-out or future compensation that is tied to the future successful operation of the business.

RISK ALLOCATION AND DEAL TERMS

As a direct result of the foregoing factors, for a proposed acquisition by a Chinese buyer of a U.S. business to be successful both the buyer and the seller must potentially address additional risks and considerations than they may have faced before and, in the case of a U.S. seller, additional to those they would face with a U.S. buyer or even a European buyer. These risks and considerations are likely to vary based on the specifics of each proposed transaction, but in each case it is important that the parties understand them and either accept them or agree upon deal terms that reduce or adequately address them.

One risk is the buyer’s possible failure to obtain on a timely basis all requisite Chinese regulatory approvals. In virtually all instances, it is to be expected that the buyer will have a better understanding of the true measure of this risk, *i.e.*, the particular approvals required and the likelihood of it obtaining them on a timely basis, as well as being the only party in a position to satisfactorily resolve this risk by obtaining such approvals. It will not be unexpected therefore that the seller will seek to place upon the buyer the contractual obligation to seek and obtain such approvals within a specified time frame and perhaps seek to enforce this by imposing a penalty or other adverse consequences upon the buyer if it is unsuccessful. The seller may seek to have the buyer obtain all necessary Chinese approvals as early in the process as possible, such as between the signing of a letter of intent and entering into a definitive agreement. If this cannot be done or if the definitive agreement is signed with a “buyer’s out” if it does not obtain the approvals, in either case the seller may take the position, as one possible approach, that it should receive a break-up fee.

CFIUS also can create particular risks for the parties: both the risk inherent in timing delays for a review and/or an investigation, and the risk of the government blocking or conditioning a deal, or arguably in the worst

²⁸ Luo, *supra* note 4.

case, seeking post-closing divestment. The level of risk will depend upon a variety of factors, including whether the buyer is a government entity, SOE, or private entity; whether the nature of the seller's business raises national security concerns; and as a practical matter, the level of attention the deal attracts. The parties will need to collectively decide whether to file a CFIUS notice since it is voluntary and either party can do so, although in the case of a government entity or SOE there are stronger reasons to file. One option is to file early in the course of the transaction so if there is an adverse ruling or proposed government conditions that cannot be satisfactorily resolved, the parties can abandon or seek to restructure the transaction at an early stage. Another option is to not file at all, although in the case of a government entity or SOE buyer, not filing is a riskier option since if the government becomes aware of the transaction it must conduct an investigation and would be commencing it at a later date. The parties may negotiate any pre-closing allocation of risks arising from CFIUS. However, especially in the case of a private buyer, in most cases it is possible that CFIUS should not prove to be a significant concern.

By contrast to CFIUS concerns, assuming that a Chinese buyer is willing to proceed with a transaction even though an HSR filing is required, once this decision is made, HSR does not appear to pose any unique risks or circumstances that need to be handled in a manner different from other deals.

In the event that a Chinese buyer is considering acquiring a public company, the form of the transaction and the type of buyer entity will impact the level of information required to be filed with the SEC and potentially the extent of SEC scrutiny of the filed materials. In some cases, this can have the effect of delaying a transaction, so these matters should be discussed in advance with U.S. securities counsel. In this regard, for example, clearly a private buyer acquisition of 100% of a public company for cash should not pose unique concerns.

Consummation of a cross-border deal generally requires an understanding by the parties of each other's expectations, needs, and cultural perspectives, as well as a mutual understanding of "how the deal should be done." Language barriers can exacerbate the difficulties of achieving such understandings. It is therefore important, especially if the business principals themselves are not fully familiar with these matters, that they retain advisers who can facilitate such understandings, seek to bridge the parties' perspectives,

and satisfy the parties' business objectives while providing necessary legal protections and appreciation of any accepted risks. Chinese buyers would do well to prepare themselves in this regard before seeking to undertake any particular transaction.

The consideration potentially posed by U.S. public perception and political agendas may argue for including in the transaction document covenants specifically addressing the operation of the acquired business for a negotiated period post-closing. Potential covenants might include preserving existing operations and maintaining the workforce, as well as limiting dividends and requiring reinvestment in the business. In the event of an earn-out or other arrangement by which payments to the seller are tied to future performance, the seller's desire for these and additional covenants would be enhanced.

While indemnity issues are generally perceived as more of a buyer's concern, at all stages of a deal a seller also faces the risks of improper actions by a buyer, such as the violation of confidentiality obligations in the due diligence process or a breach of covenants in the purchase agreement, including the failure to make payment when due of any contingent or deferred payments, indemnity, or damages claims. The seller needs a basis for adequately protecting itself against such risks. Even assuming that the transaction documents are governed by the laws of a U.S. state and that the parties contractually waive objections to venue and consent to U.S. jurisdiction, small and medium size sellers especially may be concerned about ultimately succeeding in enforcing their rights and collecting amounts due them. There is less experience in U.S.-based deals involving Chinese buyers, as compared with European buyers. Thus, U.S. sellers may be concerned as to how to satisfy themselves that a Chinese court will recognize a judgment or award issued in its favor in the U.S., that the Chinese legal system will enforce it, and, in a country as vast as China, that the seller will be able to attach the buyer's assets and ultimately collect all amounts due. Some of these points may be more of a concern in the case of a government entity or SOE, and the last point in particular may be more of a concern in the case of a private entity. Moreover, the seller may have substantial concerns about the time and expense of the foregoing. As a result, sellers may consider requiring special protective measures. These could include, for example, escrows or letters of credit to back up obligations in fixed amounts, such as break-up fees, purchase price installments, and even contingent

payments. Sellers may also seek other security located outside China. Possibilities include a pledge of the stock of the target company or a guarantee by the target itself, perhaps secured by all of its assets or by its key assets. These seller concerns, and potential means of addressing them, should not be viewed as mistrust of the particular Chinese party or a cultural divide; instead they should be recognized as pragmatic concerns based on the limited number of Chinese acquisitions in the United States, the limited experience of U.S. sellers generally in seeking to enforce those rights, uncertainties about the Chinese legal systems, and the potentially substantial related costs of collecting amounts due.

CONCLUSION

For many reasons Chinese control acquisitions in the United States are almost certain to increase, and do so dramatically in the near future. But acquisitions from China of U.S. businesses do have meaningful differentiating factors from other transactions, and therefore pose novel risks, as well as potentially requiring creative measures to address them. Nevertheless, as businesses consider these opportunities they should not shy away from them but, if the deal would otherwise make business sense, work together with their advisors to overcome these hurdles. ■

APPENDIX A

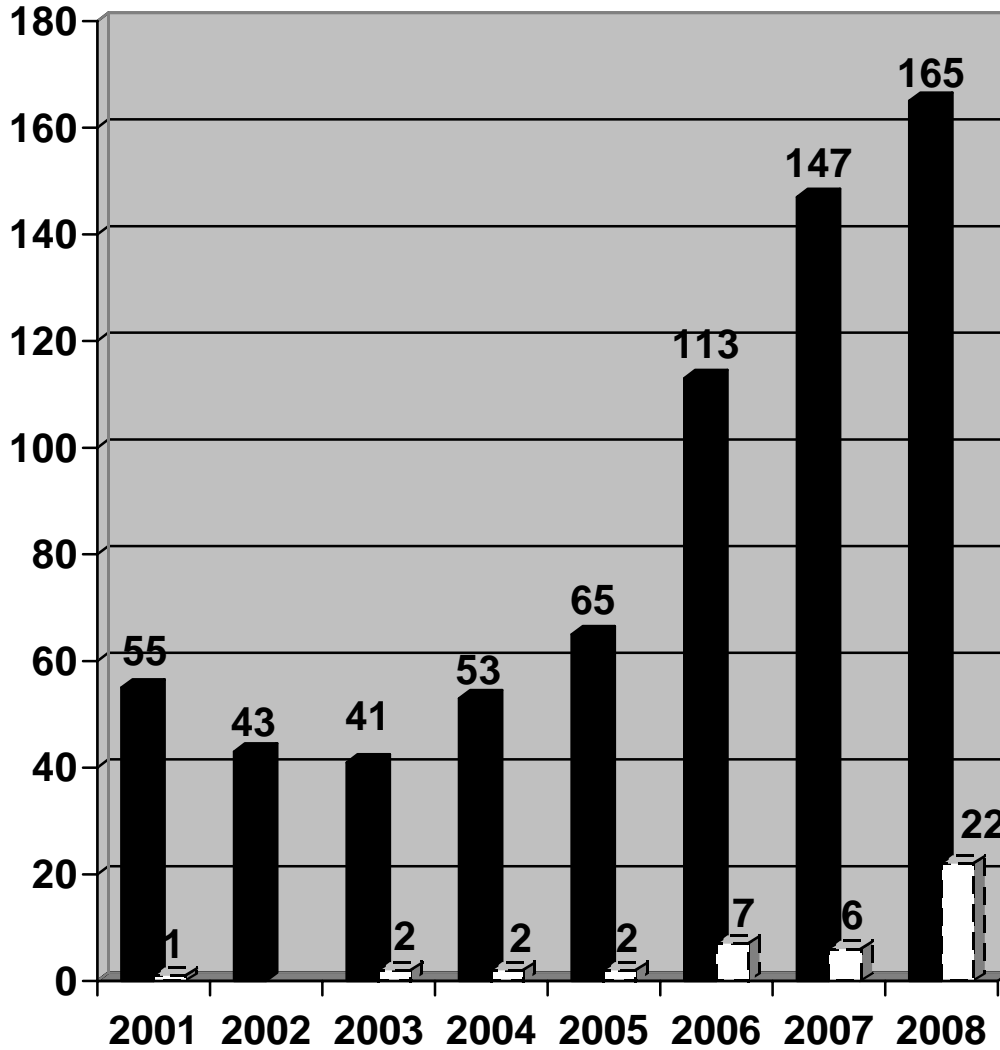
**CHINESE ACQUISITIONS OF UNITED STATES BUSINESSES
COMPLETED AND ABANDONED 2004 - 2009**

Acquirer	Target	Industry	Consideration	Status	Date
Lenovo	PC Hardware division of IBM	Computers	Cash \$1.75 Billion	Completed	2004
CNOOC (Chinese National Offshore Oil Corp.)	Unocal	Energy	Cash \$18.5 Billion	Abandoned/political CFIUS factors	2005
Haier	Maytag	Home Appliances	Cash \$1.3 Billion	Abandoned	2005
hiSoft Technology International Ltd.	Envisage Solutions Inc.	Enterprise Software	Undisclosed	Completed	03/07
Neapco, LLC, affiliate of Wanxiang Group Co. Ltd.	Automotive Components Holdings, controlled by Ford Motor Company	Automotive Components	Undisclosed Cash	Completed	Announced 4/07 Completed 01/08
Jiangxi Greatsource Display Tech. Co. Ltd.	I/Omagic Corporation	Computers – Peripheral Equipment	Cash \$95 Million for approx. 70%	Status unknown	Announced 05/07
Xinhua Sports & Entertainment (Xinhua Finance Media Ltd.)	Small World Television	Television	Cash and Stock Cash \$5 Million Stock 0.5462 M 70% stake	Completed	Announced 08/07 Completed 08/07
Coupled Products LLC (wholly-owned subsidiary of Wangxiang Group Co. Ltd.)	Dana Corp.	Auto/Trk Parts & Equipment	Undisclosed Cash	Completed	09/07
Universal Furniture (Division of Lacquer Craft Manufacturing)	Pennsylvania House (name only) and related assets of La-Z-Boy Inc. Pennsylvania House products will continue to be serviced by La-Z-Boy.	Home Furnishings	Cash \$1.65 Million	Completed	10/07
Spreadtrum Communications, Inc.	Quorum Systems, Inc.	Electronic Components-Semiconductor	Cash and Stock Cash \$55 Million Stock \$15 Million up to \$6 Million earnout	Completed	Announced 11/07 Completed 01/08
Jiangsu Jianghuai Engine Co., Ltd.	All-Power America LLC	Engines-Internal Combustion	Cash \$9.2982 Million	Completed	12/07
WuXi PharmaTech Inc.	AppTec Laboratory Services Inc.	Testing of biopharmaceuticals	Cash \$151 Million Assumption \$11.7 Million debt	Completed	Announced 01/08
iSoftStone Information Service Corporation	Akona Consulting	Software Tools	Undisclosed	Completed	Announced 02/08 Completed 02/08

Acquirer	Target	Industry	Consideration	Status	Date
Suntech Power Holdings Co., Ltd.	EI Solutions	Power Conv/Supply Equipment	Undisclosed	Completed	10/08
Mindray Medical International Limited	Data Scope's patient monitoring business	Medical Products	Cash \$240 Million	Completed	Announced 03/08 Completed 05/08
Anhui Zhongding Sealing Parts Co. Ltd.	Allied-Baltic Rubber Inc.	Chemicals-Fibers	Cash \$4.5 Million	Completed	Announced 06/08
VanceInfo Technologies Inc.	Wireless Info Tech Ltd.	Telecom Services	Cash \$1.08 Million Stock earnout	Completed	Announced 09/08
Markor International Furniture	Shnadig Furniture	Upholstery Manufacturer	Cash Est. \$8.94 Million	Completed	Announced 01/09
Lenovo Group Ltd.	Switchbox Labs Inc.	Computers	Undisclosed	Completed	01/09
HE-5 Resources Corp.	Trading Barter Bank	Diversified Financial Services	Undisclosed	Completed	03/09
Beijing West Heavy Industries Co. Ltd.	Brake and suspension parts business of Delphi Corporation	Automotive parts	Cash \$100 Million	Completed	03/09
Jiangsu Shunda Semiconductor	Solar EnerTech Corp.	Solar	Cash \$1.7 Million Joint Venture	Formed	Announced 04/09
Sichuan Tengzhong Heavy Industrial Machinery	Hummer brand of General Motors	Automotive	\$150 Million	Abandoned (Chinese regulatory approval issue)	Announced 6/09 Definitive Agreement 9/09 Abandoned 2/10
Shanghai Electric Group Corp.	Goss International Corp.	Printing-Commercial	Undisclosed	Investment Completed	Announced 09/09
Anhui Zhongding Sealing Parts Co. Ltd.	Subsidiaries of Myers Industries	Rubber products	Cash Approx. \$10 Million	Completed	Announced 09/09 Completed 11/09
Baoding Tianwei Group Co. Ltd.	Hoku Scientific Inc.	Energy-Alternate Sources	60% Investment	Completed	Announced 09/09 Completed 10/09
JV, having Shanghai Jin Jiang Int'l Hotels (Group) Company Limited as 50% member	Interstate Hotels & Resorts	Hotels & Motels	Cash \$307 Million	Completed	Announced 12/09 Completed 3/10
Northwest Non Ferrous International Investment Company Ltd.	Firstgold Corp.	Mining	Cash Approximately \$26 Million for majority share	Abandoned based on CFIUS statement	12/09
China Heaven Creation International Performing Arts Company	Theatre in Branson, Mo.	Theatre	Cash \$3.5 Million	Completed	12/09

APPENDIX B

CFIUS Filings and Investigations 2001 - 2008



Black – Filings
White - Investigations

Source: US Treasury Department
Reprinted from : Is the United States Ready for Foreign Direct Investment from Emerging Markets?
The Case of China, Karl P. Sauvart (forthcoming)

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