Buying a U.S. Business – Key Legal and Commercial Considerations for Non-U.S. Buyers
Agenda

- Main issues for foreign buyers
- Target identity and attributes
- Corporate legal barriers
- Regulatory restrictions and filing requirements
- Transaction structure
- Financing and choice of consideration
- Employee considerations
- Majority equity investments
- Purchase agreement considerations
- Special risks
- Impact of acquisition on foreign parent and ex-U.S. business
- U.S. export controls
- U.S. tax considerations
What are main issues in acquisition of U.S. business by non-U.S. company?

- Who and where is target?
  - If target is a company, is it private or public, listed or unlisted?
  - U.S. law requires a formal offer procedure to be followed if target company is publicly held
- How does a foreign buyer structure a purchase of a U.S. business?
- What U.S. corporate legal barriers may restrict an acquisition?
  - Special charter clauses (shareholder approvals/rights of first refusal)
  - Change of control provisions in important contracts
- What U.S. governmental approvals will be required?
- How can a foreign buyer finance an acquisition and what consideration may be paid?
- How does a foreign buyer deal with target’s U.S. employees?
- What special U.S. risks should foreign parent corporation be aware of?
- What precautions should be taken to avoid subjecting foreign operations and affiliates to U.S. regulation?
Identity of U.S. Target

- U.S. companies are formed under state law (50 variations but Delaware most common)
- Two forms of U.S. companies
  - Private companies
    - Corporations
    - Limited liability companies
    - Partnerships
      - Limited partnerships
      - Limited liability partnerships
      - General partnerships
  - Public companies (SEC reporting)
    - NYSE/NASDAQ listed
    - “Voluntary” filers (public debt)
- Formal offer procedure is
  - Required for acquisition of U.S. public companies under U.S. federal securities law
  - Occasionally followed to acquire private company with large number of stockholders
U.S. Corporate Legal Barriers

- Sale of U.S. company may be subject to restrictions in target company’s charter documents (certificate of incorporation/bylaws) or shareholders’ agreement
- Common restrictions include
  - Shareholder approval (e.g. minimum vote hurdles or blocking votes)
  - Rights of first refusal
  - Tag-along/drag along (forced sale) rights
- U.S. family-owned and venture-backed companies have greater complexity
- If less than 100% of equity is acquired
  - Buyer may need agreement with remaining U.S. stockholders
  - U.S. law provides important protection for minority shareholders to assure that “squeeze-out” and “sell-out” rights are at “fair” price
- Important U.S. contracts may have clauses causing termination on sale or change in control
U.S. Regulatory Restrictions - General

- General absence of exchange controls or government regulation or licensing of foreign investment or foreign acquisitions in U.S.
- No restrictions on repatriation of U.S. profits or U.S. exchange control rules for foreign companies, although withholding taxes may apply depending on the nature of the U.S. business
- No general restrictions on foreign ownership of U.S. shares or assets
- Foreign owned enterprises generally have equal access to federal and state investment incentives and benefits*

* Many cities and states offer significant tax and other incentives to induce foreign manufacturers to establish facilities and create jobs.
U.S. Regulatory Restrictions – Antitrust

- U.S. antitrust authorities can investigate any U.S. merger or acquisition as “anti-competitive”
- But only transactions meeting minimum value tests of Hart-Scott-Rodino (“HSR”) Act require prior notification to Federal Trade Commission (FTC) and Antitrust Division of U.S. Department of Justice (DOJ) and expiration of waiting periods
- Notification required if following criteria are met
  - Aggregate transaction value above US$70.9 million
  - If transaction is between US$70.9 million and US$283.6 million, size of parties satisfies certain threshold requirements*
- Pre-merger notification is mandatory unless exemption applies
- Initial waiting period is 30 calendar days (all-cash tender offers and insolvency transactions is 15 calendar days)

* Annual net sales or total assets in excess of $141.8 million on one side, and annual net sales or total assets in excess of $14.2 million on the other side.
U.S. Regulatory Restrictions – Antitrust (cont.)

- Parties can request early termination of HSR waiting period, which allows agencies to exercise discretion to terminate waiting period before it expires.
- FTC or DOJ can extend initial waiting period by making “second request” for additional information from person filing notification:
  - Deals with second requests often take up to six months or more to be resolved
  - Expense of second request can exceed $1 million
  - Important to assess U.S. antitrust risk ahead of negotiations
- Prior to closing, U.S. business must be operated independent of buyer ("gun-jumping restrictions")
U.S. Regulatory Restrictions – Exon-Florio/CFIUS*

- Special filing and approval requirements for acquisitions by foreign buyer of U.S. businesses raising “national security” or “homeland security” concerns
- No authoritative list of sectors. See appendix for factors considered.
- Special scrutiny on industries considered to be U.S. “critical infrastructure” (defined very broadly)

- Agriculture, Food and Water
- Aerospace
- Banking and Finance
- Chemicals and Hazardous Materials
- Emergency Services
- Encryption or Other Information Security
- Energy Infrastructure and Resources
- Defense Industrial Base and other Defense and Intelligence Contracts
- Fiber Optics
- Government Contractors
- Information Technology
- Military-use Information, Technologies and Products
- Mining and Minerals
- Natural Resources
- Postal and Shipping
- Public Health
- Semiconductors
- Radar
- Telecommunications
- Transportation Infrastructure
- Weapons
- Other Critical Infrastructure or Technologies

* Committee on Foreign Investment in the United States (administers Exon-Florio).
U.S. Regulatory Restrictions – Exon-Florio/CFIUS (cont.)

- 30-day review, and if no decision is made in initial review, CFIUS starts 45-day second-stage investigation
- 45-day investigation of deals involving critical infrastructure or investments by entity controlled by foreign government
- CFIUS can either
  - Determine that transaction does not pose national security threat
  - Present recommendation to President to block or unwind transaction (President has 15 days in which to make his decision)
- In practice, parties to transaction either enter into mitigation agreement to enable transaction to proceed, or voluntarily withdraw CFIUS notice and terminate deal
U.S. Regulatory Restrictions – Other Sensitive and Regulated Sectors

- Agricultural land
- Aviation
- Banking / financial services
- Communications/broadcast licenses (TV, cable, radio)
- Defense
- Gaming
- Healthcare
- Insurance
- Maritime shipping
- Minerals
- Public utilities
- Wireless satellite networks
U.S. Regulatory Restrictions - Reporting

- Periodic, direct investment reports to U.S. Department of Commerce pursuant to International Investment and Trade in Services Survey Act, if foreign enterprise acquires
  - Real estate or
  - 10% or more of a substantial enterprise
- Non-U.S. investment in U.S. real estate exceeding certain thresholds triggers reporting under Foreign Investment in Real Property Tax Act and requires withholding of sales proceeds upon sale of property unless certain exemptions apply
- Acquisition of U.S. farming, ranching, timber or forestry land exceeding certain sizes reportable to U.S. Department of Agriculture
- Real estate acquisitions may also give rise to other state and local reporting obligations
U.S. Regulatory Restrictions – Agricultural Land

- As of August 2013, at least eight states (Iowa, Minnesota, Missouri, Nebraska, North Dakota, Oklahoma, South Dakota and Wisconsin) restrict the ownership of agricultural land by foreign entities and/or individuals.
- State exceptions vary based on use, ownership of foreign entity, size, location and other factors. For example, the restriction is not applicable to land acquired for use other than farming in Iowa, and in Missouri the restriction only applies to land larger than five acres which is capable of supporting agricultural enterprise.
- Legislation is currently being discussed within the states that may alter some of the current restrictions.
Transaction Structure

- U.S. mergers and acquisitions can take number of different forms
  - Public target (clearly regulated) vs. private target
  - Consensual transactions
    - Stock acquisitions (private or open market purchases)
      - 100%
      - Partial equity stake
    - Asset acquisitions
  - Mergers (one-step)
  - Tender offer (two-step)
  - Unsolicited/hostile transactions
    - Tender offers
    - Proxy contests

- Consideration paid by acquiror may consist of stock, cash and/or debt securities or combination
- Choice of structure and consideration paid by acquiror will determine which rules are applicable
Transaction Structure – Stock Purchases

- Simplest form of U.S. acquisition, especially if there are few shareholders and all are willing to sell

- Advantages
  - U.S. company retains all assets, including licenses, permits, and franchises (can be difficult to transfer because of need to obtain consents from issuing government agencies)
    - Important contracts and leases may be unaffected by transfer
    - Must investigate, however, to make certain that change of control of target will not bring about termination of permits or contracts
  - Few transfer documents required
  - Acquisition may be completed fairly quickly
  - Transfer taxes may be limited or avoided, although such taxes are relatively low in most states (exception is real estate in some states)
  - Net operating losses can be used post-acquisition (subject to certain restrictions)
## Transaction Structure – Stock Purchases (cont.)

- **Disadvantages**
  - U.S. company will retain all tax and other contingent liabilities, whether disclosed or undisclosed, although seller will typically indemnify buyer against certain undisclosed liabilities of U.S. target (subject to limits on indemnification)
  - Purchase price for U.S. business may not be reflected in tax basis of U.S. corporation’s assets after acquisition, unless seller consents to certain elections (usually disadvantageous to seller)
  - Cumbersome if buyer does not wish to purchase U.S. business in its entirety
    - May be possible for target to rid itself of unwanted business or assets prior to share acquisition
    - Legal and tax aspects of demerger (or corporate split) can be complicated in United States
Transaction Structure – Asset Acquisitions

- Advantages
  - Buyer’s tax basis in U.S. assets increased to reflect purchase price
  - Not all assets of U.S. company need be purchased
    - If interested in only one line of business or one division of seller, asset purchase is best
  - Not all liabilities need be acquired
  - Certain liabilities may pass to acquirer in any case
    - Certain state property taxes will constitute lien on assets acquired
    - Environmental liabilities may become responsibility of any subsequent owner of U.S. real estate
    - Known employment-related (e.g. wage/hour violation) liabilities may pass to buyer under Federal law
    - U.S. pension liabilities may pass to purchaser under some circumstances
    - Some states impose responsibility on acquiring company for product liability claims even for products sold prior to acquisition
  - Seller will usually indemnify buyer against any such liabilities in acquisition agreement, which may be sufficient if seller is financially sound
  - If selling company is insolvent, special procedures should be followed to avoid any charge of “fraudulent conveyance” (actionable by company’s creditors post-transaction)
### Transaction Structure – Asset Acquisitions (cont.)

**Disadvantages**

- Favorable tax attributes of U.S. corporation normally lost in asset acquisition
- More complex than share acquisition because all U.S. assets must be transferred
- Consents to transfer of certain valuable assets, such as licenses, permits, or contracts, may not be obtainable or may be obtainable only at significant price

**But being foreign buyer usually not barrier to obtaining consents from U.S. public or private parties**
Transaction Structure – Mergers

- Creature of U.S. state corporation statutes
- Two entities are joined by operation of law
- All assets and liabilities become property of surviving entity (or new entity) solely by filing with State Secretary of State
- One entity disappears and other continues as successor to both lines of business
- Requires consent of board of directors and shareholders (in corporation) or members (in limited liability company)
- Equity interests in target convert to cash, to equity interests in acquiring entity, or to equity interests in another entity (parent)
- Target entity may be survivor (reverse merger)
- Structure of choice in acquisition of U.S. public company or company with numerous or uncooperative shareholders
Transaction Structure – Mergers (cont.)

➢ Advantages
  • Exchange of U.S. target shares are automatic (no separate transfer documents required)
  • Shareholders of target have no option to retain their shares if bidder acquires over a certain percentage of shares (generally over 50% but may be as high as 66-80% depending on the company)
  • Shareholders may have right to recover appraised value in lieu of amount offered to them in merger but (absent fraud) may not block acquisition
  • Transfer taxes normally do not apply in merger
  • Valuable permits and contracts may be easier to transfer in merger than asset sale

➢ Disadvantages
  • May be time consuming because of need to hold shareholder meeting and provide necessary disclosures to shareholders
  • Contractual indemnification and escrow needs to be addressed separately since shareholders are often not parties to merger agreement
U.S. Financing and Choice of Consideration

- Main forms of consideration that can be offered in U.S. acquisition are cash, shares or notes/debentures (debt instruments)
- If buyer does not have sufficient funds to finance acquisition, main options are to borrow cash or issue shares (either as consideration or equity finance)
- Common to finance acquisition with U.S. target’s assets or future profits (leveraged buyout)
  - U.S. assets of target may be pledged to bank or other financial institution, or buyer may issue high interest, subordinated debt instruments, normally referred to as high-yield bonds
  - Bonds constitute securities and must be registered with SEC unless exemption from registration is available
  - Unlike under many European corporate laws, use of target’s U.S. assets to finance acquisition is not illegal or present personal liability risks for managers
- Non-U.S. buyers may use parent company/shareholder loans to finance acquisition, especially if they have borrowed in their own countries
- No legal requirement to have firm or committed funding before announcing U.S. transaction or signing acquisition agreement
Choice of consideration

- No special restrictions on form of consideration that foreign buyers can offer sellers
- In selecting consideration to be paid, analysis focuses on
  - Buyer’s financial resources
  - Expected dilution to Buyer’s outstanding shares (and potential effect on their market price) if securities are issued
  - Preference of U.S. target’s shareholders as to form of consideration

Disadvantages of offering securities as consideration

- Delay and expense resulting from registering securities with U.S. Securities and Exchange Commission (unless exemption applies)
- Possible intrusive/extensive disclosure obligations under U.S. securities laws that accompany having securities registered under U.S. Exchange Act
- Parent company liability under antifraud provisions of U.S. securities laws
- Possible illiquidity in U.S. trading market for buyer’s securities
U.S. Employee Considerations

- No legal requirements for target’s Board or buyer to inform or consult U.S. employees about sale
  - Sellers may have legal obligation to provide notice and bargain with labor representatives of target’s employees regarding effects of sale (if employees are organized)
  - Buyer may have legal obligation to recognize and bargain with labor representatives of target’s employees upon closing of sale

- Stock purchase transaction ordinarily requires buyer to retain employees and assume all labor agreements and employment liabilities of target

- Employees do not automatically become employees of buyer in U.S. asset purchase
  - No legal obligation to
    - Hire/retain all employees of target
    - Assume labor agreements covering employees of target
  - Asset purchaser can ordinarily change terms and conditions of employment
  - Buyer may have successor liability for ongoing legal violations affecting target’s employees
  - Federal law violations known to buyer will be buyer’s responsibility
U.S. Employee Considerations (cont.)

- Collective bargaining/union agreements may require buyer to assume existing agreements or impose other restrictions on transaction
  - May limit buyer’s ability to change wage rates, hours of work and other employment terms
  - May require assumption of
    - Defined benefit/pension plan liabilities
    - Multi-employer pension or welfare fund obligations, including withdrawal liability
    - Post-retirement medical benefit obligations
- U.S. law has employment “at will” concept
  - Terminations ordinarily permitted without severance or notice, subject to laws prohibiting employment discrimination
  - May be modified by severance plan, labor agreement or individual employment agreement
Federal law (WARN Act) and some state laws, as well as collective bargaining agreements, require advance notice when certain sites are closed or mass layoffs occur:

- Typically, notice does not apply where less than 50 full-time employees are impacted.
- 60-day notice must be provided to labor representatives, employees and governmental entities.
- Foreign parent company may be liable for failure to provide notice depending on degree of parent/subsidiary interdependence.

Federal law (COBRA) requires that terminated U.S. employees be allowed to continue any employer-sponsored health program for period of time but at cost of employee (certain states may impose this cost on employer).
U.S. Employee Considerations - Pension and Other Benefits

- If target has maintained any employee benefit programs, including pension plans, responsibility for continued adequate funding of these obligations may pass to buyer, even in asset acquisition.

- Buyer of U.S. business may incur significant obligations created prior to acquisition, including making up any underfunding of pension plan.

- Retirement benefit plans are subject to extensive U.S. federal regulation.

- In any U.S. acquisition, target corporation’s pension and retirement plans should be examined in detail by experts (lawyers and actuaries) hired by buyer to avoid assuming substantial unexpected liabilities.

- Buyer’s foreign parent company may also have liability for underfunded pension plan under U.S. law (PBGC v. Asahi Tec Corp.)
U.S. Employee Considerations – Executive Compensation Arrangements

- “Golden parachute” agreements
  - Pay executive between 1 and 3 times annual compensation upon termination after change in control
  - “Excess” payments are subject to a tax penalty (20% excise tax) and are not deductible by company
  - Executives are often grossed-up to protect against the tax
  - Increases cost to 2.5x original amount
- Retirement plans subject to enhancement
- Non-compete covenants sometimes trigger on termination
  - Not always enforceable for term or under scope contained in contract
  - Can be supported by future severance payments
U.S. Employee Considerations – Stock-Based Compensation and Incentive Awards

- Stock options and restricted stock issues to employees under vesting conditions (time/performance)
- Transaction may accelerate vesting and receipt of shares
- Key issue: can buyer eliminate future right to buy equity under stock plan?
  - Cash-out options
  - Conversion to parent options
- Some plans require consent of holders in order to eliminate options/derivatives
- Performance-based plans need to be reviewed to determine how transaction would affect unearned portion
U.S. Considerations – Target Directors

- At closing, U.S. directors will tender resignations from the Board
  - No payment owing
  - Standard US. practice
  - Obtain written resignations as a closing delivery
- Directors may also be removed without “cause” by sole stockholder after closing
# Majority Equity Investments

- Partial share purchase leaves buyer with minority shareholders in U.S. target
- Buyer can use second-step merger to cash out remaining U.S. minority shareholders
- If minority holders remain investors
  - Buyer must deal with U.S. target on arm’s-length basis to avoid controlling shareholder liability for self-dealing
    - Need stockholders agreement to address governance and buy–out issues
- In some states, statutory freeze-out laws require buyers that surpass certain ownership threshold in company (usually between 10% and 20%) to wait specified period of time before gaining control of company or entering into any transactions with company
  - Prior approval of U.S. Board generally avoids restriction
  - Usually limited to listed companies
**Purchase Agreement Considerations**

- Foreign buyer should avoid proposing terms that deviate substantially from those viewed as “U.S. style” or are dramatically contrary to U.S. practices
- Foreign regulatory approvals and export of foreign currency generally not suitable conditions to U.S. closing
- Transaction agreements should be governed by U.S. law
  - State of incorporation
  - State in which U.S. company resides
  - Another commercially-acceptable law, such as New York or Delaware
- Disputes will be resolved in U.S.
  - Consider arbitration vs. court proceeding for resolution of disputes
  - Waiver of jury trial recommended
Special Risks* – Usually Able to Diligence

* For more detail on risk mitigation strategies, see presentation entitled “Strategies to Mitigate M&A Deal Risk – What Post-Closing Disputes Teach Us About Structuring Our Deals”, by E. Kitslaar and A. Schaeffer.
U.S. “legacy” (discontinued business) risks (can be impossible or expensive to diligence)

- What are they?
  - Sold businesses
  - Closed facilities
  - Discontinued product lines
  - Environmental/off-site disposal
  - Legacy employment/health & safety

- Solution: negotiate structural/carve-out indemnity
Impact of Acquisition on Foreign Parent and Ex-U.S. Business

- Assuming transaction is structured properly and acquired operations are operated properly post-transaction, U.S. law should not impact buyer’s business materially or at all outside U.S., or require significant disclosure with U.S. government regarding non-U.S. activities of foreign buyer.

- So long as appropriate corporate procedures and other practices are observed, foreign parent company should not be liable under U.S. law for liabilities of its acquired U.S. subsidiary*

- Exception for certain liabilities (i.e., environmental) when parent actively participates in and exercises control over operations of subsidiary’s facility**

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* U.S. legal principles under which parent corporation may be held liable for activities of its subsidiaries are generally known as “piercing corporate veil” and “alter ego” liability. In brief, key preventive measures to avoid such liability include observance of subsidiaries’ corporate formalities (for example, decision-making by subsidiaries’ own officers and board of directors), different compositions of boards and officers of parent and subsidiary, adequate capitalization of U.S. entity and subsidiary maintaining separate adequate books and records. “Alter ego” theories focus on whether persons acting on behalf of subsidiary are its own officers and employees, or those of its parent. These factors also are relevant to determining if the foreign parent will be subject to jurisdiction of U.S. courts and governmental agencies under the “minimum contacts” test. See separate Jones Day memoranda for summary of key concepts.

** Parent “must manage, direct, or conduct operations specifically related to pollution, that is, operations have to do with leakage or disposal of hazardous wastes or decisions about compliance with environmental regulations” in order to be held liable.
U.S. Foreign Corrupt Practices Act – Applicability to Foreign Buyers

- U.S. Foreign Corrupt Practices Act (“FCPA”) generally prohibits certain types of payments to government officials and certain other persons by U.S. companies and related parties to influence acts or decisions of foreign official to assist in obtaining or retaining business for U.S. company
- U.S. company does not cease to be subject to FCPA if it is acquired by foreign company
- Non-U.S. activities conducted by foreign buyer unrelated to its U.S. subsidiary do not, however, become subject to FCPA due to ownership of U.S. subsidiary
- But foreign parent or stockholder of U.S. company would be liable under FCPA if it engaged in prohibited activities for benefit of its U.S. subsidiary
U.S. Export Controls – Applicability to Transactions with Foreign Buyer

➢ U.S. export control laws restrict U.S. person’s business activities with certain foreign persons
➢ Intra-company transactions between U.S. target/subsidiary and foreign parent (and non-U.S. affiliates) are subject to these regulations
➢ Export control laws regulate
  • With whom you can trade
    – No/restricted trade with specified countries and an ever-growing directory of individuals and companies (U.S. Treasury Department embargoes - Office of Foreign Assets Control (OFAC))
    – No assistance with export transaction involving parties determined to have violated U.S. export control laws (U.S. Commerce Department Denied Persons List)
    – No exports and (some) imports by “debarred” parties of munitions and technologies that are specifically designed or modified for military use (U.S. State Department debarred parties)
    – No technology export to certain entities (including individuals) engaged in proliferation of weapons of mass destruction, missile technology, biological and chemical weapons (U.S. Commerce Department “Entity List”)
U.S. Export Controls – Applicability to Transactions with Foreign Buyer

• What can be sold
  – Most exports/re-exports of commercial or “dual-use” items do not require a license to many destinations, but high-end technology and related items fall into controlled categories and are more restricted, often requiring export licenses (U.S. Commerce Department Bureau of Industry and Security)
  – Restricts exports and (some) imports of “munitions” (U.S. State Department)
  – Controlled export of technology used in certain aspects of nuclear power generation (U.S. Department of Energy – Nuclear Regulatory Commission (NRC))

• Conditions of sale/anti-boycott regulations – prohibits furthering or supporting another country’s boycott that the U.S. does not sanction (e.g. Arab League boycott of Israel)
Exports Can Occur in Various Indirect Ways Through Disclosure

- Ability to access computer drives
- Telephone
- Email
- Fax
- Computer data disclosure
- Face-to-face conversations
- Training sessions
- Site tours
“Facilitation” Explained

- **Description:** Approving, facilitating, or guaranteeing a transaction that would be prohibited if performed by a U.S. person or from the United States
- Facilitation has been described as a “difficult” and “elusive” concept
- **Examples:**
  - Referring prohibited “business opportunities” to non-U.S. companies
  - Changing operating practices and procedures of parent or affiliate to avoid prohibitions
  - Giving approvals for prohibited transactions
  - Providing support for prohibited transactions

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**Sudan Example**

31 C.F.R. § 538.407

- (b) To avoid potential liability for U.S. persons under this part, a U.S. parent corporation must ensure that its foreign subsidiaries act independently of any U.S. person with respect to all transactions and activities relating to the exportation or reexportation of goods, technology, or services between Sudan and any other location including but not limited to business and legal planning; decision making; designing, ordering or transporting goods; and financial, insurance, and other risks. See §538.505 with respect to exports of, *inter alia*, certain legal services benefitting Sudan.

- (c) No U.S. person may change its policies or operating procedures, or those of a foreign affiliate or subsidiary, in order to enable a foreign entity owned or controlled by U.S. persons to enter into a transaction that could not be entered into directly by a U.S. person or from the United States pursuant to this part.

- (d) No U.S. person may refer to a foreign person purchase orders, requests for bids, or similar business opportunities involving Sudan or the Government of Sudan to which the United States person could not directly respond as a result of the prohibitions contained in this part.

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**§538.407 Facilitation by a United States person.**

(a) The prohibition contained in §538.206 against facilitation by a United States person of the exportation or reexportation of goods, technology, or services between Sudan and any destination (including the United States) bars any unlicensed action by a U.S. person that assists or supports trading activity with Sudan by any person. Facilitation of a trade or financial transaction that could be engaged in directly by a U.S. person or from the United States consistent with the prohibitions, general licenses and exemptions contained in this part is not prohibited. Activity of a purely clerical or reporting nature that does not further trade or financial transactions with Sudan or the Government of Sudan is not considered prohibited facilitation. For example, reporting on the results of a subsidiary’s trade with Sudan is not prohibited, while financing or insuring that trade or warranting the quality of goods sold by a subsidiary to the Government of Sudan constitutes prohibited facilitation.
U.S. Federal Income Tax Considerations for Foreign Buyers - General

- U.S. tax structuring is complex and must be considered as one of the first items when acquiring a U.S. business
- Basic U.S. tax framework for foreign buyers owning US businesses
  - Foreign buyers without separate US taxable presence not taxed in US on capital gain income from sale of stock in a US corporation
  - Exception - foreign buyers taxed on capital gains from stock in corporations with US real estate assets (broadly defined) >50% of assets
  - Foreign buyers taxed in US on share of US-sourced active business income - effectively connected income or “ECI” and have to file U.S. tax returns
  - Foreign buyers are taxed at the rate of 30% (or lower rate as established by an applicable treaty) on their share of dividends paid by U.S. corporations and of certain types of interest income received from U.S. corporations
- ECI structuring issues
  - Foreign buyer’s investment in a U.S. partnership or LLC carrying on active US business will create ECI
  - U.S. partnership or LLC owned by a foreign buyer generally have duty to withhold tax on foreign LP’s share of ECI
U.S. Tax Filing, Payment and Reporting by U.S. Subsidiary and Foreign Buyer

- **U.S. subsidiary**
  - U.S. subsidiary will continue to file U.S. federal, state and local tax returns and pay taxes
  - U.S. subsidiary will have to file information returns to report transactions with its foreign parent and other related parties
    - Identity of the foreign buyer will be disclosed on information returns, but no other information about the foreign buyer will be disclosed to the IRS

- **Foreign buyer**
  - No obligation to file U.S. tax returns or pay U.S. taxes (unless ECI)
  - Dividends paid by U.S. subsidiary to the foreign buyer are subject to withholding at 30% rate, unless reduced by a tax treaty

- **Transactions between foreign buyer and U.S. subsidiary**
  - Capitalization of U.S. subsidiary: use of loans can be advantageous, but restrictions on deductibility in U.S. for related party debt and other limitations
  - Transfer pricing: transactions between foreign parent and U.S. subsidiary must be at “arm’s length,” otherwise IRS has a right to adjust prices charged
  - Employee tax issues: may want to “second” employees from foreign parent to U.S. sub—tax deduction at U.S. subsidiary level for salary paid
New Tax Withholding Obligations – FATCA

- To make it more difficult for U.S. citizens and residents to avoid U.S. tax by holding U.S. assets offshore, tax legislation enacted in 2010 (FATCA) imposes a 30% withholding tax on payments to certain non-U.S. entities unless those entities disclose to the IRS information about U.S. account holders.
- Payments of U.S. source interest, dividends and disposition of securities made to a foreign financial institution (such as a foreign buyer that is an investment fund) will be subject to the FATCA withholding tax unless an agreement is in place with the IRS.
- Effective date of FATCA is delayed to apply to payments made after July 1, 2014.
- IRS announced that foreign financial institutions (including non-U.S. funds) need to enter into an agreement with the IRS by January 1, 2014 to meet the deadlines.
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<th>CFIUS National Security Factors</th>
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<td>• FINSA* enumerates the following factors that may be considered:</td>
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<td>• Domestic production needed for projected national defense requirements;</td>
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<td>• The capability and capacity of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services;</td>
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<td>• The control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the United States to meet national security requirements;</td>
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<td>• The potential effects of the proposed or pending transaction on sales of military goods, equipment, or technology to any country identified under applicable law as (1) supporting terrorism, (2) a potential regional military threat to the interests of the United States, or (3) a country of concern for missile proliferation or the proliferation of chemical and biological weapons;</td>
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<td>• The potential effects of the proposed or pending transaction on U.S. international technological leadership in areas affecting national security;</td>
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<td>• The potential national security-related effects on United States critical infrastructure, including major energy assets;</td>
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<td>• The potential national-security related effects on United States critical technologies;</td>
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<tr>
<td>• Whether the buyer is, is controlled by, or is acting on behalf of a foreign government;</td>
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<tr>
<td>• The country’s adherence to non-proliferation regimes, record of providing assistance with counter-terrorism efforts, and the potential for theft of technologies with military applications;</td>
</tr>
<tr>
<td>• The long-term projection of US requirements for sources of energy and other critical resources and material; and</td>
</tr>
<tr>
<td>• Any other factors that the President or CFIUS may determine to be appropriate.</td>
</tr>
</tbody>
</table>
