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This article uses SEC filings, public reports, cases, and press reports to examine how companies involved in transactions for control approach review by the Committee on Foreign Investment in the United States (CFIUS). Due to the case-by-case nature of CFIUS review and the evolving and politicized nature of the review process, it can be difficult to assess how to approach interactions with CFIUS. In addition to examining how companies allocate risks related to CFIUS review, this article attempts to provide a short primer on how target boards might assess and analyze the CFIUS process.

I. INTRODUCTION

During a four-week period in early 2016, action by the Committee on Foreign Investment in the United States ("CFIUS" or "the Committee") resulted in the termination or rejection of three cross-border deal proposals. All three involved investments from Chinese companies into the United States. In the first situation, CFIUS blocked an investment in Philips Lumileds, a U.S. subsidiary of Philips.[1] In the second case, out of fear of CFIUS action, U.S.-based Fairchild Semiconductor rejected a consortium's acquisition proposal and accepted a lower bid from an American company.[2] In the third instance, a Chinese firm

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[1] Toby Sterling, *U.S. Blocks Philips' $3.3 Billion Sale of Lumileds to Asian Buyers*, REUTERS (Jan. 22, 2016, 1:59 PM), http://www.reuters.com/article/us-philips-lumileds-sale-idUSKCN0V02D4.

[2] *See* Press Release, Fairchild Semiconductor, Fairchild Board of Directors Determines the Acquisition Proposal from China Resources and Hua Capital is Not a Superior Proposal, (Feb.

terminated its investment plan in a U.S. company after CFIUS began an investigation.[3] These cases are but a snapshot of the Committee's key role in cross-border mergers and acquisitions.

This article considers the impact of CFIUS review from the perspective of a U.S. corporate board involved in a transaction for control.[4] This article begins with a brief introduction into CFIUS, including its mechanisms for control and brief history. Next, the article addresses CFIUS concerns during the offer stage — how a target board should approach a hostile offer from a foreign acquirer or how a board might prepare itself for a friendly deal. Third, it looks at key deal terms, such as the price and deal protection measures a board should take to protect shareholders from the costs of a blocked deal. As might be expected from a committee focused on national security, CFIUS provides relatively little in the way of public disclosure. This article

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16, 2016), https://www.fairchildsemi.com/about/press-releases/Press-Release.html?id=20160216-fairchild-board-of-directors; Keith Bradsher & Paul Mozur, *Political Backlash Grows in Washington to Chinese Takeovers*, N.Y. TIMES (Feb. 16, 2016), http://www.nytimes.com/2016/02/18/business/dealbook/china-fairchild-semiconductor-bid-rejected.html.

[3] Arash Massoudi & James Fontanella-Khan, *Tsinghua kills $3.8bn investment plan in Western Digital*, FINANCIAL TIMES (Feb. 23, 2016). Tsinghua sought an approximately 15% stake in Western Digital and requested a board seat. *Id.*

[4] The threshold at which a transaction may result in "control" of the corporation is dependent on the specific situation. For example, while shareholdings below 50% are not generally considered controlling, a plaintiff can demonstrate actual control through domination of corporate conduct by a minority shareholder. *See* Kahn v. Lynch Commc'n Sys., Inc., 638 A.2d 1110, 1114 (Del. 1994) (holding a 43.3% minority shareholder to have had control over business decisions). CFIUS, of course, is not bound by state corporation law definitions of control and may look beyond these shareholding thresholds. *See* 31 C.F.R. § 800.301(a) (2016) (delineating which transactions are covered transactions). CFIUS regulations are explicit that the "actual arrangements for control" are not important; what matters is whether the deal "results or could result in control of a U.S. business by a foreign person." Thus, some deals which do not involve traditional "control" shareholding thresholds still trigger review.

relies on SEC filings, corporate releases, cases, and press reports to understand how boards have addressed CFIUS-related challenges.

II. THE COMMITTEE'S EVOLVING ROLE

CFIUS is a U.S.-based, interagency committee comprised of key executive branch officials.[5] A transaction is covered by CFIUS if it "results or could result in control of a U.S. business by a foreign person."[6] Notification is voluntarily, but if parties fail to notify the Committee, it may still take action, even after a deal is closed.[7] In general, CFIUS raises three concerns for parties to a potentially covered transaction. First, the review process takes a good deal of time, which can delay an agreement: thirty days for the initial review and forty-five days for the investigation, should one be necessary.[8] Regarding lengthy investigations, it is likely a covered transaction will be investigated – during the six-year period from 2009 to 2014, CFIUS reported it conducted investigations in nearly 40% of cases.[9] Second, the Committee may indicate that certain mitigation measures are necessary. [10] The Committee may also recommend that an approved deal be unwound due to failures to comply with mitigation requirements.[11] Third, the Committee can recommend that the President block or

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[5] *SEE* JAMES K. JACKSON, CONG. RESEARCH SERV., RL33388, THE COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES (CFIUS) 1–7 (2016), https://www.fas.org/sgp/crs/natsec/RL33388.pdf.

[6] 31 C.F.R § 800.301(a).

[7] 31 C.F.R § 800.401(a), (b) (2016).

[8] 31 C.F.R. § 800.501–506 (2016). For example, in the Waldorf deal, CFIUS's review lasted from October 2014 to February 2015. *China's Anbang Insurance Gets U.S. Go-aheadfor $1.95 bln Waldorf Astoria Buy*, REUTERS (Feb. 1, 2015, 8:48 PM), http://www.reuters.com/article/anbang-waldorf-idUSB9N0TO01420150202.

[9] JACKSON, *supra* note 5, at 25.

[10] 31 C.F.R. § 800.501–506.

[11] *E.g.*, JACKSON, *supra* note 5, at 6.

suspend a transaction.[12] While it is extraordinarily rare for the President to block a deal, the threat of such sanction forces companies to submit to "voluntary review;" if they do not, CFIUS may recommend divestiture, even post- closing.[13]

A history of CFIUS is beyond the scope of this article; however, it is worth noting CFIUS has often been a lightning rod for those concerned about the influence or threat posed by particular foreign countries. The first major expansion of CFIUS's power, through the 1988 Exon-Florio provision, was a reaction to concerns over Japanese takeovers of U.S. firms.[14] In 2007, concerns about Middle Eastern investors led to the Foreign Investment and Security Act, which expanded the Committee's authority to include "critical infrastructure" and homeland security concerns.[15]

Over the past decade, observers conclude CFIUS has begun to focus more on Chinese investments.[16] One innocuous explanation is China is also the largest source of

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[12] 31 C.F.R. § 800.506(b).

[13] *E.g.*, MEREDITH M. BROWN, RALPH C. FERRARA & PAUL S. BIRD, TAKEOVERS: A STRATEGIC GUIDE TO MERGERS AND ACQUISITIONS SUPPLEMENT 1–16 (2010) (describing the Polaris Financial divestiture of IdenTrust and the Ralls case).

[14] One deal of note involved a potential sale of Fairchild Semiconductor to Fujitsu, which fell through in the face of political opposition. JACKSON, *supra* note 5, at 3–4. *See also* Margaret L. Merrill, *Overcoming CFIUS Jitters: A Practical Guide for Understanding the Committee on Foreign Investment in the United States*, 30 QUINNIPIAC L. REV. 1, 19 (2011). As described in the introduction, Fairchild recently rejected an offer partially out of concerns over CFIUS approval — perhaps due to experiencing deja vu.

[15] Foreign Investment and National Security Act of 2007, Pub. L. No. 110–49, § 4, 121 Stat. 246, 253–54 (2007).

[16] *See* Shawn Donnan, *US Reviews of Investments Made by China Increase*, FINANCIAL TIMES (Feb. 19, 2016), http://www.ft.com/intl/cms/s/0/6ef4ffdc-d75b-11e5-969e-9d801cf5e15b.html#axzz45OCDI376; *see also* Minxin Pei, *Washington Is Giving the Cold Shoulder to Chinese Investment*, FORTUNE (Feb. 23, 2016, 10:43 AM), http://fortune.com/2016/02/23/chinese-company-acquisitions-us-companies/.

covered transactions, comprising nearly 20% of the total covered transactions over the three-year period from 2012 through 2014. [17] However, members of Congress have raised explicit concerns about Chinese investment, including recommending publicly that CFIUS review specific deals. [18] Coupled with its record of investigation into Chinese acquisitions, it is reasonable to conclude CFIUS is particularly concerned about Chinese investment. It has scrutinized a Chinese company's acquisition of the Waldorf Astoria [19] and SAP's acquisition of an HR software company.[20]

The Committee will consider a range of threats in its review. [21] Of particular importance is the relationship between the target business and the acquiring country; for example, it is hard to imagine a U.K. acquirer facing the same in-depth investigation and public opposition as the Chinese firm Shuanghui International when it acquired Smithfield Foods.[22] Critics of the deal specifically focused

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[17] JACKSON, *supra* note 5, at 19.

[18] *See* Rebecca Spalding, *Affymetrix Bid's China Ties Spark National Security Talk*, BLOOMBERG (Mar. 21, 2016, 6:57 PM), http://www.bloomberg.com/news/articles/2016-03-21/affymetrix-bid-s-china-ties-must-be-examined-congresswoman-says; *see also* David Mclaughlin, *Chinese Bid for Chicago Exchange Draws Congressional Concern*, BLOOMBERG (Feb. 17, 2016, 12:34 PM), http://www.bloomberg.com/news/articles/2016-02-17/chinese-bid-for-chicago-exchange-draws-congressional-concern.

[19] *China's Anbang Insurance Gets U.S. Go-ahead for $1.95 bln Waldorf Astoria Buy*, *supra* note 8.

[20] SuccessFactors, Inc., Tender Offer Statement Amend. 7 (Schedule TO/A) (Dec. 16, 2011), https://www.sec.gov/Archives/edgar/data/1402305/000119312512019895/d268167dsctota.htm (last visited Oct. 28, 2016).

[21] *See generally* THEODORE H. MORAN, THREE THREATS: AN ANALYTICAL FRAMEWORK FOR THE CFIUS PROCESS (2009) (categorizing CFIUS threats into three groups: The first threat is the foreign acquisition of key resources, such that the U.S. might become reliant on a foreign power for essential goods or services. The second threat involves the potential for transfer of technology or expertise to a foreign power. The third threat involves the risk of espionage or infiltration through acquisition of key assets.).

[22] *See* Michael J. de la Merced, *U.S. Security Panel Clears a Chinese Takeover of Smithfield Foods*, N.Y. TIMES (Sept. 6, 2013,

on concerns about Chinese food safety practices,[23] which might not have been relevant for an acquirer based in another country.

III. CFIUS CONSIDERATIONS IN THE OFFER STAGE

When a U.S. board receives an offer from a foreign acquirer, it should include CFIUS considerations in planning its response. Whether or not the offer is solicited by the target, the uncertainties created by the CFIUS process create both opportunities and problems for target boards of directors.

A. HOSTILE OFFERS

For boards facing a hostile offer, the prospect of CFIUS review can help a target board resist the proposal. "Since 1990, nearly half of the transactions CFIUS investigated were terminated by the firms involved."[24] Although this percentage has dropped to approximately 20% over the past six years,[25] it is still quite high. A target board could, therefore, argue that such transactions do not warrant

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6:25 PM), http://dealbook.nytimes.com/2013/09/06/national-security-panel-approves-smithfield-sale-to-chinese-company/.

[23] Press Release, Debbie Stabenow, Bipartisan Group of Senators Urge Appropriate Oversight of Proposed Smithfield Purchase (June 20, 2013), http://www.stabenow.senate.gov/news/bipartisan-group-of-senators-urge-appropriate-oversight-of-proposed-smithfield-purchase (last visited Oct. 28, 2016); Letter from Senators Max Baucus and Orrin Hatch, U.S. Sen. Comm. on Fin., to the Hon. Michael Froman, U.S. Trade Rep., and the Hon. Jacob Lew, U.S. Sec. of the Treasury (June 21, 2013), http://www.finance.senate.gov/imo/media/doc/062113%20Smithfield%20Letter.pdf.

[24] JACKSON, *supra* note 5, at 9.

[25] *Id.* at 6. Note the percentage of withdrawn notices per year fluctuates significantly — in 2012, it was close to 44%, but in 2014, it was only 18%.

serious consideration without a prohibitive premium and onerous deal protection measures.

In the antitrust context, it is well established that an informed board can decline an offer that is higher in nominal terms but that creates real regulatory risk.[26] Given these cases, it seems likely that a board which informs itself about the risks involved with CFIUS review — mandatory divestitures, delays, or even a blocked deal — would be protected by the business judgment rule.[27] Indeed, this is what Fairchild Semiconductor recently concluded when it found a nominally higher offer from a Chinese consortium did not constitute a "superior proposal" compared to its agreement with an American company.[28] The board did not change its recommendation, even after it secured a "hell-or- high-water commitment" from the consortium, since it felt that there was still a "non-negligible risk" of CFIUS blocking a deal.[29]

Courts are also likely to draw a parallel with antitrust case law regarding a board's willingness to consider potential mitigation measures in evaluating an offer. In *In*

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[26] *See* In re BJ's Wholesale Club, Inc. S'holders Litig., No. CIV.A. 6623- VCN, 2013 WL 396202 at *9 (Del. Ch. Jan. 31, 2013) (informed and legitimate concerns about antitrust risk are sufficient to presume the board's good-faith business judgment); In re Cogent, Inc. S'holder Litig., 7 A.3d 487, 512 (Del. Ch. 2010) ("potential regulatory approvals relating to antitrust considerations presents a legitimate risk factor for the Board to consider "); In re J.P. Stevens & Co., Inc. S'holders Litig., 542 A.2d 770, 781 n.6 (Del. Ch.1988) ("the Special Committee was entirely justified in considering any legitimate threat that the antitrust laws posed to the consummation of any West Point proposal.").

[27] The business judgment rule is the presumption that "in making a business decision the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company." In re the Walt Disney Co. Derivative Litig., 906 A.2d 27, 52 (Del. 2006) (citing Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984)).

[28] Fairchild Semiconductor Int'l, Recommendation Statement (Schedule 14D-9A) (Feb. 4, 2016), https://www.sec.gov/Archives/edgar/data/1036960/000119312516463934/d22910dsc14d9a.htm at 5.

[29] *Id.*

re BJ's Wholesale Club, Inc., the court refused to find an implication of bad faith when the plaintiff asserted the board could have done more to mitigate the antitrust concerns in a rejected offer.[30] Therefore, a board could, for example, reasonably conclude selling off a lucrative government contracting business in order to permit the sale of other assets to a foreign investor would be too risky.

However, targets of hostile offers can use political pressure to wear down a hostile bidder. The board may even be able to rely on a preferred-domestic acquirer to carry out the dirty work of lobbying for CFIUS scrutiny. In its battle with the Chinese company China National Offshore Oil Corporation (CNOOC) over Unocal, Chevron issued a statement pointing to CNOOC's ties to the Chinese government [31] and also lobbied politicians, resulting in members of Congress urging a CFIUS investigation into the competing offer. [32] CNOOC also hired lobbyists [33] and invited review by CFIUS, but it was ultimately unsuccessful in its attempts to fight back.[34]

B. BOARDS SEEKING FRIENDLY DEALS

A board seeking a friendly deal with a foreign investor will need to plan ahead to increase the probability of CFIUS approval. As a preliminary step, the company should identify any ways in which its own business might trigger

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30 In re BJ's Wholesale Club Inc. S'holders Litig., No. CIV.A. 6623-VCN, 2013 WL 396202 at *9.

31 Press Release, Chevron Corp., Chevron Corporation Statement on Unocal Transaction (June 22, 2005), https://www.sec.gov/Archives/edgar/data/93410/000095014905000441/f10205ae425.htm.

32 Matt Pottinger, Russell Gold, et al., *Cnooc Drops Offer for Unocal, Exposing U.S.-Chinese Tensions*, WALL ST. J. (Aug. 3, 2005), http://www.wsj.com/articles/SB112295744495102393.

33 *Id.*

34 Justin Blum, *CNOOC Requests U.S. Security Scrutiny*, WASH. POST (June 28, 2005), http://www.washingtonpost.com/wp-dyn/content/article/2005/06/27/AR2005062701501.html.

CFIUS review. This has become harder to predict, and it should encompass not only obvious triggers such as government contracts but also particular assets such as potentially sensitive real estate.[35]

After reviewing its own business, the target board should evaluate its potential acquirers. [36] As much as possible, the target should seek out information on the acquiring company, such as its sources of financing and connections to foreign governments. [37] Some foreign companies, such as sovereign wealth funds or companies known to have close ties to foreign governments, appear to be more likely to trigger U.S. scrutiny. For example, the House Intelligence Committee recommended the Obama administration block acquisitions by the Chinese companies Huawei and ZTE.[38]

Additionally, transparency is a major concern for both CFIUS and Congress. In Chongquing Casin Enterprise Group's ongoing efforts to acquire the Chicago Stock Exchange, opponents of the deal cited the lack of transparency in the acquirer's ownership structure and relationship to the Chinese government.[39] Even the CEO of the exchange has stated that he does not know who owns the company and that it is unclear whether the Chinese government has a minority stake.[40] A target board seeking a

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[35] *See* Press Release, The White House Office of the Press Secretary, Order Signed by the President Regarding the Acquisition of Four U.S. Wind Farm Project Companies by Ralls Corporation (Sept. 28, 2012) (wind farms were located near U.S. naval facilities).

[36] *See, e.g.*, JACKSON, *supra* note 5, at 27–28 (listing risk-mitigating factors that CFIUS considers during investigation of transactions).

[37] *See, e.g.*, *id.*

[38] *Id.*

[39] Letter from 47 Members of Congress to the Hon. Marisa Lao, Assistant Secretary, Dep't of the Treasury (Feb. 16, 2016), https://lynnjenkins.house.gov/uploads/Letter%20To%20CFIUS%20Re%20Chicago%20Stock%20Exchange%20Purchase.pdf.

[40] Josh Rogin, *Congress Wary of National Security Implications of Chinese Deal for Chicago Stock Exchange*, CHI. TRIB. (Feb. 17, 2016, 8:29 AM),

foreign investor should therefore encourage a potential acquirer to disclose this sort of information, rather than permitting opponents to create costly regulatory hurdles due to a lack of disclosure.[41]

The target should also consider how to structure its sale to best avoid CFIUS scrutiny.[42] A target may make itself more attractive to foreign suitors by preemptively selling any CFIUS-triggering aspect of the business, then selling the remaining portion of the business to a foreign buyer.[43] To maximize sale value, the parties will want to choreograph the acquisition process carefully so the companies' additions remain separate.[44] In the bankruptcy auction for A123 Systems, for example, the bankers running the auction contacted a U.S. company to bid for sensitive security assets, while a Chinese company bid on the larger remainder.[45] Pairing these bids enabled the deal to proceed without scrutiny.[46]

IV. DURING THE DEAL

A. DEAL PRICE

Once a deal is in process, a target board should work to ensure that its shareholders are adequately compensated for the regulatory risks posed by a foreign acquisition. This

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http://www.chicagotribune.com/business/ct-congress-chicago-stock-exchange-sale-20160217-story.html.

41 *See* Merrill, *supra* note 14, at 36-40.

42 *See, e.g.*, Julie Wernau, *Navitas Key to Sale of A123 to Chinese Firm*, CHI. TRIB. (Jan. 30, 2013), http://articles.chicagotribune.com/2013-01-30/business/ct-biz-0130-navitas-20130130_1_navitas-systems-wanxiang-group-microsun-technologies.

43 *Id.*

44 *Id.*

45 *Id.*

46 *Id.*

may require a significant premium: Unocal's board concluded that CNOOC's offer was not "sufficient to compensate [] stockholders for the higher risk"[47] despite an approximately $1.5 billion premium over Chevron's offer.[48] Even Institutional Shareholder Services, a leading advisory firm, supported the Chevron bid, agreeing that CNOOC's offer did not adequately compensate for the regulatory risk.[49] Fairchild's board recently made a similar decision, as described above.[50]

Chinese buyers use cash as consideration more than half of the time, which may be attractive to stockholders.[51] However, a target board should inquire about the origin of the acquirer's financing. In the Chevron-CNOOC battle, Chevron claimed CNOOC's access to low-interest loans gave it an unfair advantage, a claim echoed by political opponents of the CNOOC bid.[52] In another recent case, the

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[47] Shareholder Presentation, Unocal Corp., Unocal and Chevron (Rule 425 Filing) (Aug. 3, 2005), https://www.sec.gov/Archives/edgar/data/93410/000095014905000521/f10205ce425.htm.

[48] David Barboza & Andrew Ross Sorkin, *Chinese Oil Giant in Takeover Bid for U.S. Corporation*, N.Y. TIMES (June 23, 2005) http://www.nytimes.com/2005/06/23/business/worldbusiness/chinese-oil-giant-in-takeover-bid-for-us-corporation.html.

[49] Press Release, Unocal Corp., Unocal Wins ISS Support for Merger with Chevron (Aug. 1, 2005), https://www.sec.gov/Archives/edgar/containers/fix014/716039/000089882205000892/aug1pr.txt.

[50] Fairchild Semiconductor Int'l, *supra* note 28.

[51] *See* Nisha Gopalan & Christopher Langner, *Deal or No Deal?*, BLOOMBERG (Apr. 1, 2016, 2:11 AM), http://www.bloomberg.com/gadfly/articles/2016-04-01/deal-or-no-deal (noting 62% of Chinese buyers were to pay cash in failed or withdrawn deals); *see also* Alfred Rappaport & Mark L. Sirower, *Stock or Cash? The Trade-Offs for Buyers and Sellers in Mergers and Acquisitions*, HARV. BUS. REV. (Nov.-Dec. 1999), https://hbr.org/1999/11/stock-or-cash-the-trade-offs-for-buyers-and-sellers-in-mergers-and-acquisitions (stating shareholders of acquiring companies fare worse in stock transactions than they do in cash transactions).

[52] *See* Allen Sloan, *Parent's Help Puts Cnooc Bid in Different Light,* WASH. POST (July 26, 2005) (stating that Chevron

fact that the foreign offeror, Origin Technology Corporation, was a shell entity with unclear financing, was a reason for the U.S. target, Affymetrix Incorporated, to choose a domestic acquirer, notwithstanding a nominally higher bid.[53]

B. Termination Fees and CFIUS-Related Covenants

Aside from the pricing negotiation, the parties will need to determine how to address the CFIUS process in the merger agreement. There are three related decisions: the choice of whether to notify the Committee, the value of any CFIUS-related reverse termination fee, and the standard to which the parties will be held in addressing the Committee's concerns — the "efforts" covenant.

1. Notification

In most cases, parties who think they may fall within the Committee's purview should include a covenant binding

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has raised doubts about CNOOC's bid and that it would receive $4.5 billion from its parent company as a 30-year loan carrying a 3.5% interest rate); *see also* Press Release, Richard Pombo, Pombo Statement on CNOOC Bid Withdrawal (Aug. 2, 2005), https://votesmart.org/public-statement/119861/pombo-statement-on-cnooc-bid-withdrawal#.VwWjIxMrLeQ (arguing CNOOC's bid withdrawal is good news for the free market); *but see* Kate Linebaugh, *How Favorable Is Oil Bid's Financing?*, WALL ST. J. (June 30, 2005, 12:01 AM), https://www.wsj.com/articles/SB112007688254773231 (arguing the loans terms were not significantly advantageous to CNOOC).

53 *See* Kevin Miller & Megan Durisin, *Affymetrix Rejects $1.5 Billion Origin Bid, Favors Thermo*, BLOOMBERG (Mar. 20, 2016, 5:31 PM), http://www.bloomberg.com/news/articles/2016-03-20/affymetrix-rejects-1-5-bid-billion-origin-bid-favors-fisher (stating Affymetrix rejected Origin's offer of $16.10 per share and instead continues to recommend Thermo Fisher for its planned merger who offers $14 per share).

them to work together in notifying CFIUS.[54] On the other hand, the parties may not want to work together because they want to communicate confidence that the deal does not raise any CFIUS issues. As described in greater detail below, there is some evidence of such a signaling effect in the antitrust context. In the ongoing Tianjin-Ingram Micro deal, for example, the parties publicly decided not to notify, based on the parties' belief that they would not be blocked by the Committee.[55] A few months later, however, they reversed course "after consultation" with CFIUS. [56] In general, parties involved in most of the major deals discussed in this article did notify the Committee. Furthermore, many of those parties had joint covenants, which required them to work together on the CFIUS notification.

2. TERMINATION FEES & EFFORTS CLAUSES

A target board involved in a transaction likely to trigger CFIUS scrutiny should require inclusion of a reverse

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54 *See* Merrill, *supra* note 14, at 37-38 (explaining the Committee has required joint-filings).

55 *See generally* Press Release, Ingram Micro Inc., Ingram Micro Deal FAQs (Feb. 17, 2016), http://phx.corporate-ir.net/phoenix.zhtml?c=98566&p=hnagroup (such a move is risky; some commenters have suggested part of the reason the 3Com bid failed was that the acquirers did not voluntarily notify until the Committee was already interested in the transaction); Merrill, *supra* note 14, at 39 n.228. *See* Vipal Monga, *Ingram Micro To Submit $6 Billion Tianjin Tianhai Deal for CFIUS Review*, WALL ST. J. (July 21, 2016, 5:19 PM), http://blogs.wsj.com/cfo/2016/07/21/ingram-micro-to-submit-6-billion-tianjin-tianhai-deal-for-cfius-review/ (stating the company had previously indicated it did not expect to go before CFIUS but then reversed course).

56 Monga, *supra* note 55.

termination fee provision in the agreement. This fee will be enforceable after a blocked deal, even if the target later finds another acquirer,[57] and compensates shareholders for the costs of delays or a busted deal. Related to any fee provision will be the efforts covenant: requiring the acquirer to reach some standard of effort in complying with a CFIUS regulatory requirement for closing.[58]

A survey of merger agreements shows a spectrum of CFIUS-related termination fees and efforts clauses. In Huawei and Bain's withdrawn bid for 3Com, the acquirers offered a 3% termination fee in the event their bid failed to get regulatory approval, along with a "reasonable best efforts" clause that included a commitment to making necessary divestitures.[59] The ambiguity of the termination fee clause, and in particular its relationship to CFIUS action, resulted in litigation.[60] Target boards should thus take heed and make such clauses explicit. In 2014, Siemens agreed to a 5% reverse termination fee in the event CFIUS rejected its planned acquisition of Dresser-Rand, as well as a wide-ranging "best efforts" clause that included divestiture obligations.[61] In contrast, in SAP's 2011 acquisition of SuccessFactors, the parties required reasonable best efforts but also included an explicit limitation on obligations to

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[57] In re Chateaugay Corp., 198 B.R. 848, 861 (S.D.N.Y. 1996).

[58] *See, e.g.*, Dale Collins, *Sample Antitrust-Related Provisions in M&A Agreements*, ANTITRUST UNPACKED: ANTITRUST LAW BLOG 17 (Apr. 27, 2013), http://www.antitrustunpacked.com/siteFiles/BlogPosts/antitrust_risk_shifting4_27_2013.pdf.

[59] Agreement and Plan of Merger by and among Diamond II Holdings, Inc., Diamond II Acquisition Corp., and 3Com Corp., filed as Exhibit 2.1 to Form 8-K/A by 3Com, Inc. (Sept. 28, 2007). The "best efforts" clause is at §6.1(b); the termination fee is at §8.3(c)(iii).

[60] 3Com Corporation v. Diamond II Holdings, Inc., C.A. No. 3933-VCN, 2010 WL 2280734 (May 31, 2010) (case relating to discovery dispute over certain communications relating to the purpose of the termination fee).

[61] Siemens Energy Inc., Dynamo Acquisition Corp. & Dresser-Rand Group, Inc., Agreement and Plan for Merger 35 (Sept. 21, 2014). The "best efforts" clause is contained in § 5.6(b).

make divestitures.[62] In the Shanghui-Smithfield transaction described above, the parties explicitly excluded CFIUS risk from the reverse termination fee.[63] On the other hand, they included a best efforts clause for regulatory compliance, as well as a "hell or high water" divestiture requirement.[64]

More recently in the Fairchild deal, the board rejected a 4.3% reverse termination fee as insufficient, even though the foreign consortium had also offered a hell or high water CFIUS covenant.[65] In its ongoing acquisition of Ingram Micro, Tianjin offered a 6.7% reverse termination fee if the deal was rejected by CFIUS, despite the initial choice not to notify CFIUS.[66] This suggests some tension between the parties with regard to the best approach: a high termination fee implies Ingram saw a need for protection against regulatory action, while the public decision not to seek CFIUS review suggested that Tianjin was initially confident CFIUS would not be interested in the deal. The recent decision to seek review validates Ingram's concerns.

It is hard to discern a pattern in these agreements; perhaps because the parties are allocating not only the risks of their particular deal but also risks due to unpredictable, shifting political tensions. It appears from this small sample that higher reverse termination fees are correlated with a greater likelihood of success, thus suggesting confidence on the part of the acquirer.

Quantifying the value of a strong efforts clause is made more difficult by the lack of strong case law on what various

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[62] SAP America, Inc., Saturn Expansion Corp., & SuccessFactors, Inc., Agreement and Plan of Merger 51,53 (Dec. 3, 2011). The "reasonable best efforts" clause is contained within § 5.5(a) and the explicit non-divestiture clauses within § 5.5(h).

[63] *See* Smithfield Foods, Inc., Preliminary Proxy Statement (Schedule 14A) 154, § 8.03(e) (May 28, 2013).

[64] *Id.* at 139–40. "Hell or high water" requirements are those that require the party to take any and all actions necessary to accomplish the objective. *See*, *e.g.*, Hexion Specialty Chems., Inc. v. Huntsman Corp., 965 A.2d 715, 756 (Del. Ch. 2008).

[65] Fairchild Semiconductor Int'l, *supra* note 28.

[66] Ingram Micro Inc., Current Report: Entry into a Material Definitive Agreement (Form 8-K) 3 (Feb. 17, 2016).

efforts such standards require.[67] For this reason, targets are likely to require a significant and robust reverse termination fee. The Fairchild board's proxy amendment is a recent example of a board explaining why a mid-range (4.3%) fee plus a strong efforts clause is insufficient, even with a pricing premium to the domestic alternative.[68]

Are there risks associated with strong efforts clauses and termination fees? In the antitrust context, one study suggests there is evidence for both "signaling" and "bargaining" effects from hell or high water clauses: the antitrust authorities are more likely to take notice of an agreement with such a clause (the signaling effect), and the parties will have less negotiating leverage with the government if they are bound to undertake divestitures or other major actions (the bargaining effect).[69]

While similar effects may exist in the CFIUS context, the Committee has greater freedom than the antitrust authorities to investigate and require mitigation. Thus, while a foreign acquirer may be signaling CFIUS and lowering its bargaining power through voluntary notification and efforts clauses, it is still probably wise to work with the authorities to assuage their concerns.

C. Mitigation

A strong efforts clause is important because CFIUS approval may be conditioned on a variety of mitigation measures. At first blush, mitigation appears to be required

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[67] Delaware cases suggest the "reasonable best efforts" standard has not been clearly defined but may be met through good-faith affirmative efforts, which are still subordinate to the party's business judgment. Hexion Specialty Chems., Inc., 965 A.2d at 755 (finding violation of an efforts clause when there was bad faith conduct).

[68] *See* Fairchild Semiconductor, Press Release, *supra* note 2.

[69] See John D. Harkrider, *Risk-Shifting Provisions and Antitrust Risk: An Empirical Examination*, 20 ANTITRUST 52, 56 (2005).

relatively rarely; CFIUS reports only 8% of cases from 2012 to 2014 required mitigation.[70] This statistic is somewhat misleading, however, because it is based on *all* covered transactions, and the definition of a covered transaction is quite broad; a more useful data point is nearly 22% of all *investigated* transactions required mitigation measures in 2013.[71] CFIUS can require a variety of mitigation measures ranging from passive ownership through proxy boards staffed only by U.S. citizens, to active ownership with information-sharing restrictions between the parent and the domestic corporation.[72]

CFIUS does not disclose specific mitigation requirements in approved deals, but a review of several recent deals gives a sense of the spectrum of what can be required. In 2007, as the financial crisis gained steam, Abu Dhabi's sovereign wealth fund invested in Citibank. To allay any fears over the investment — hardly a trivial concern given the furor over the Dubai Ports World deal a year earlier — the fund confirmed that it would not be involved in the management or operation of Citibank.[73]

Similarly, CNOOC succeeded in winning CFIUS's approval for its acquisition of Nexen Inc. in 2013, [74] contingent on compliance with mitigation requirements. According to a leaked e-mail, the mitigation measures apparently included ceding "operator" or decision-making authority on Gulf Coast oil projects.[75] In contrast to the

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[70] JACKSON, *supra* note 5, at 23.

[71] *Id.* at 3, 23–27 (Table I-2 noting there were 48 investigations in 2013, and page 27 noting 11 negotiations resulted in mitigation measures to arrive at 22%).

[72] *See id.* at 23.

[73] *See* Heather Timmons & Julia Werdigier, *For Abu Dhabi and Citi, Credit Crisis Drove Deal*, N.Y. TIMES (Nov. 28, 2007), www.nytimes.com/2007/11/28/business/worldbusiness/28invest.html.

[74] Rebecca Penty, *Cnooc Wins Final Approval for $15.1 Billion Nexen Buy*, BLOOMBERG (Feb. 12, 2013, 10:36 PM), http://www.bloomberg.com/news/articles/2013-02-12/cnooc-wins-final-approval-for-15-1-billion-nexen-buy.

[75] *See* Rebecca Penty & Sara Forden, *Cnooc Said to Cede Control of Nexen's U.S. Gulf Assets*, BLOOMBERG (Mar. 1, 2013,

Citibank deal, CNOOC would still be able to have a partial role in the operation of the company.[76]

Foreign investors acquiring particularly sensitive assets may also use Proxy Agreements and Special Security Arrangements (SSA).[77] The Italian company Finmeccanica's acquisition of DRS Technologies, Inc., a U.S. defense contractor, illustrates these alternatives.[78] A subsidiary with a proxy board arrangement is used to address the most serious, top-secret contracts.[79] The parent can only review financial information and generally takes a passive role.[80] For those operations involving secret level clearances (and below), Finmeccanica set up a U.S. subsidiary with an SSA: a board comprised of three outside directors (all U.S. citizens) and two inside directors (one of whom was a U.S. citizen).[81] There are additional information security requirements and both subsidiaries are expected to be financially independent.[82]

The specific mitigation measures required appears to be based on the type of threat CFIUS may perceive.[83] Boards of companies involved in sensitive national security or critical infrastructure businesses may want to consider proposing proxy or SSA arrangements proactively, as

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7:43 PM), http://www.bloomberg.com/news/articles/2013-03-01/cnooc-said-to-cede-control-of-nexen-s-u-s-gulf-assets.

[76] *See id.*

[77] *See e.g.*, Office of the Deputy Under Secretary of Defense for Policy Support, INT'L PROGRAMS SECURITY HANDBOOK 126 (2009), http://www.iscs.dsca.mil/documents/ips/Chapter12_062009.pdf.

[78] *Finmeccanica to Acquire DRS for US $5.2 billion*, PRNEWSWIRE.COM (May 12, 2008 1:00 PM), http://www.prnewswire.com/news-releases/finmeccanica-to-acquire-drs-for-us52-billion-euro-34-billion-57237712.html.

[79] *FOCI FAQs*, U.S. DEP'T OF DEF., DEF. SEC. SERV. (Feb. 2008), http://www.dss.mil/isp/foci/foci_faqs.html.

[80] MORAN, *supra* note 21, at 30–31.

[81] *Id.*

[82] *Id.*

[83] Spalding, *supra* note 18 (suggesting Theodore Moran's threat framework may be a useful guide here. SSAs and proxy arrangements appear to be most appropriate for the second and third types of threats in his taxonomy).

opposed to passively or retroactively, in their notice to CFIUS to show their goodwill. Even if the parties do not propose such measures, they may be forced to accept them.[84] For exchange offers in which shareholders will continue to own a stake in the merged company, the target board should carefully evaluate how ongoing compliance with these intrusive governance requirements might impact the value of the company going forward.

V. CONCLUSION

While foreign investors grow increasingly concerned with the Committee's activism, members of Congress hope to expand its role to address concerns over the state of the United States' critical infrastructure, technological competitiveness, and susceptibility to espionage.[85] As the deals discussed in this article show, boards of American companies should watch this debate carefully because it will influence not only the willingness of foreign investors to make acquisition proposals but also the tactics with which these domestic boards respond.

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[84] Alan C. Myers & Ann Beth Stebbins, *2013 Insights: Global M&A* 123 (Jan. 2013), https://www.skadden.com/sites/default/files/publications/Skadden_2013_Insights_Global_M-A.pdf (finding proxy arrangements are becoming more frequent).

[85] James R. Clapper, Dir. of Nat'l Intelligence, *Worldwide Threat Assessment of the US Intelligence Community*, (Feb. 9, 2016) https://www.armed-services.senate.gov/imo/media/doc/Clapper_02-09-16.pdf.