

DEAL TRAFFIC CONTROL

Navigating a deal safely home means avoiding political turbulence

BY MICHELE DAVIS
AND SU-LIN CHENG NICHOLS,
BRUNSWICK, WASHINGTON, DC

It is one of the most intense times for a company: making a significant acquisition means following a strict due diligence program to deal with all the financial and regulatory hurdles. However, companies are increasingly finding that they must also consider the myriad political obstacles that can disrupt their plans.

When it comes to acquisitions, politics is best thought of in its broadest sense. Dealmakers would do well to consider the full panoply of actors who might be motivated to disrupt their deal. A potentially disruptive force, for example, could be a competitor creating political obstacles to a deal for purely commercial reasons.

As Stephanie Kirchgassner, Washington correspondent for the *Financial Times*, says, “I have gotten pitched by parties that are opposed to a deal – often for competitive reasons – and are trying to drum up opposition on the Hill on national security grounds. I have a high degree of skepticism about pursuing such stories, but whether I do or not, these pitches do catch my attention.”

Activist groups, similarly, might care little about a specific transaction but could see it as an opportunity to stoke a policy debate or to lobby for investment and jobs. It can be easy to become ensnared in a broader debate – and once that happens, it becomes far more difficult to control your own destiny.

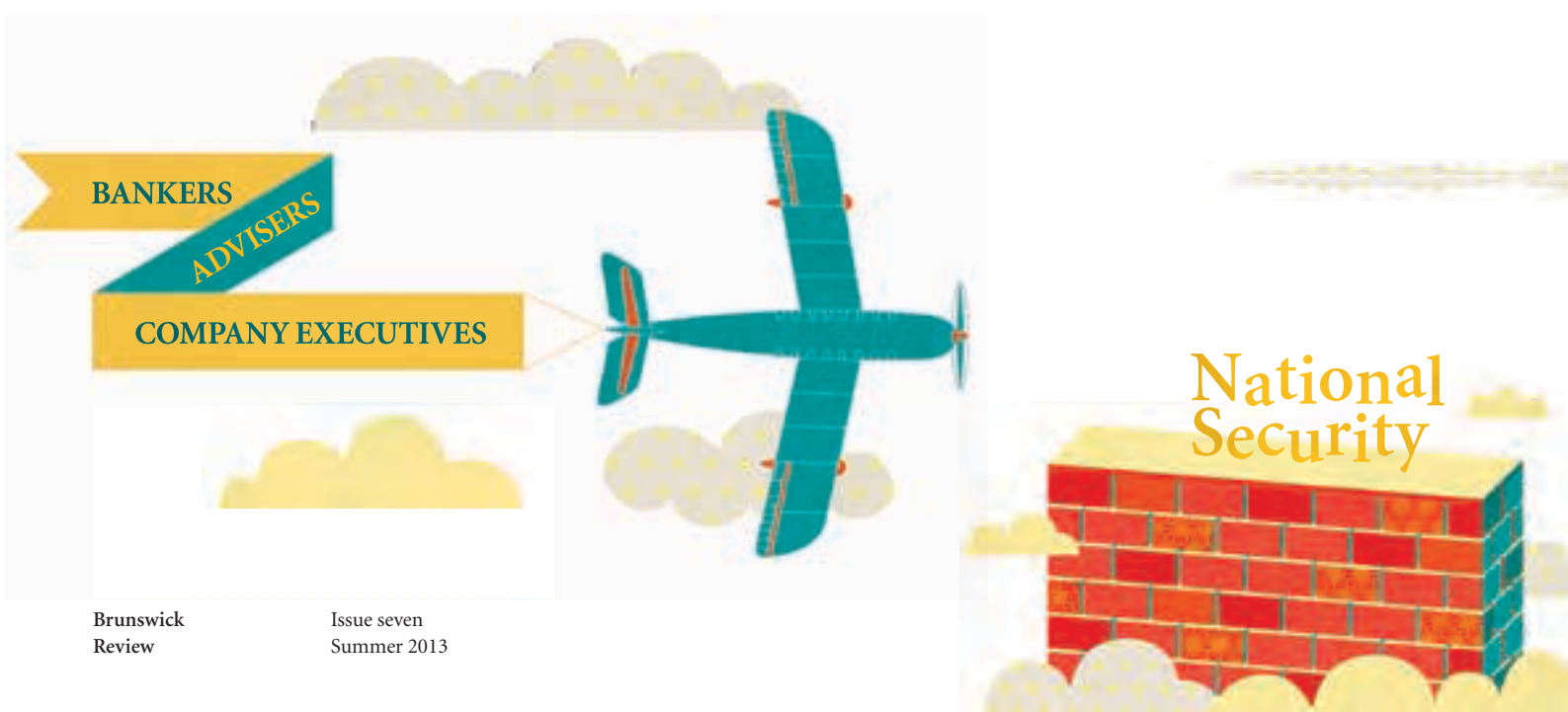
Governments around the world have been putting foreign acquiring companies under greater scrutiny, especially if there is a question of national security involved.

In Washington, DC, this is governed by the Committee on Foreign Investment in the United States (CFIUS), a collection of federal agencies led by the Treasury Department, which can deny permission for a foreign investment that the committee judges would represent a significant risk to national security.

Cases that are candidates for CFIUS scrutiny often garner press interest too. “There are certain companies and countries and sectors that pique my interest because I know they also attract the interest of CFIUS and could be controversial,” says Kirchgassner. “A company’s preparedness or lack of preparedness for the CFIUS process is also something I look out for as it can be a good sign of how the review is likely to go. I try to glean as much information as possible for our readers about this very secretive and opaque process.”

Indeed, the language of CFIUS can be vague – deliberately so – in order to give the government and its agencies (which include Homeland Security and Defense) plenty of scope to determine what types of deals might pose a threat to national security. This can run from fairly obvious, off-limits transactions in the defense sector, to assessments more difficult to predict, such as those that might impact on “critical infrastructure.”

Earlier this year, a highly publicized CFIUS intervention derailed a Chinese company’s deal that, on the face of it, seemed to involve fairly innocuous wind farms in the Pacific Northwest, but turned out to be a challenging transaction. ➤



Ralls Corporation, a Delaware-incorporated company owned by Chinese nationals who are also senior executives in Sany Group, a Chinese wind turbine maker, purchased interests in four wind farm projects in Oregon in spring 2012. The plan was to build Sany wind turbine generators on the sites in order to demonstrate their reliability.

However, the sites overlapped restricted airspace used by the US Naval Air Station at Whidbey Island and neither Ralls nor the seller, a unit of Terna Energy, which is a division of a Greece-based group, had sought CFIUS clearance prior to the deal. An application for CFIUS approval was filed only after it was requested.

As John Villasenor wrote in *Forbes* magazine, companies that have obtained CFIUS clearance before a transaction are usually safe from future actions because of a “safe harbor” provision, but “when foreign buyers decline to seek pre-transaction approval, things can get far more complicated.”

Ralls had all of the legal documentation and permits in place to build turbines and connect them to the power grid, and proceeded to do so after the purchase was completed. However, the Navy had previously written to the Oregon Public Utility Commission about potential “negative security implications” of the sites’ locations, and having been requested after the fact to file notice of the transaction, Ralls was then ordered by CFIUS to halt production. Attempts to sell the wind farms were blocked, and in September 2012 Ralls

was ordered to divest the assets within 90 days.

Ralls then took the unprecedented step of challenging the Presidential Order in court, which decided to hear the case on the grounds of Ralls’ claim that it was denied property without due process. It proved futile, as the court found that the law allows the President to exercise wide powers without explanation because of the classified nature of national security decisions.

The risk associated with foreign investment in the US is often linked with China. However, transactions covered by CFIUS have been overwhelmingly European. The UK, traditionally the largest foreign investor in the US, accounted for 26 percent of transactions covered in the 2009-11 period, according to CFIUS (see chart).

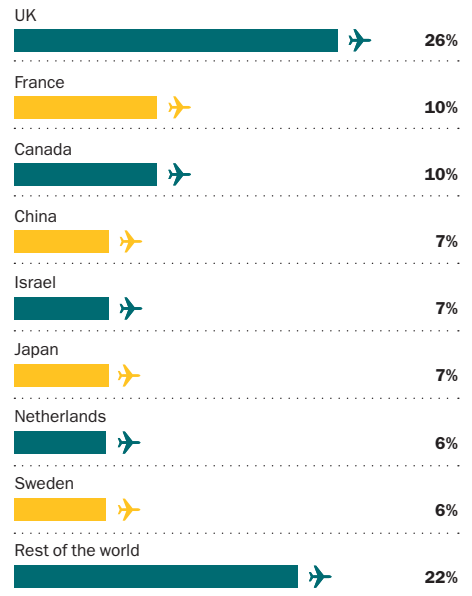
In 2011, the French defense company Safran won approval for its purchase of US company L-1 only after agreeing to establish a three-person proxy board to manage sensitive US contracts, which make up roughly 80 percent of L-1’s business.

Clearly, the national security implications of a deal are essential considerations in a broader public affairs strategy, and too often a foreign acquirer without a pre-deal public affairs plan is caught off guard, having expected to stay out of the public eye and avoid questions until a deal is done.

A disrupter of a deal can often get Members of Congress to repeat and amplify their concerns, which then spawns more media coverage, and escalates into a

Headwinds

Deals covered by CFIUS, 2009-11 by country



Source: CFIUS Annual Report, December 2012
Percentages do not total 100 because of rounding



negative media cycle, potentially undermining the deal.

This can be avoided. A good illustration of best practice, for example, was the recent approval of the purchase by BGI-Senzhen, a Chinese genomics firm, of California-based Complete Genomics. Before announcing the transaction – believed to be the first successful acquisition of a publicly-traded US company by a Chinese company – BGI had established strong partnerships in the US and a reputation for doing work that advanced medical knowledge, including with the Children’s Hospital of Philadelphia to research pediatric brain tumors, and with advocacy organization Autism Speaks to create a sequenced genome library.

Still, BGI was not widely known in the US and a competitor, Illumina – like Complete, based in California – stepped forward to try to purchase Complete itself, and attempted to raise national security concerns about BGI in an appeal to shareholders.

BGI tackled the national security issue head on. The company’s Chief Operating Officer, Ye Yin, wrote to Complete CEO Clifford Reid (a letter filed with the Securities and Exchange Commission), stating, “Illumina knows quite well from its business relationship with BGI that there are no national security issues implicated ... Illumina has been a strong supporter of BGI’s business and has repeatedly praised BGI as a business partner.” He went on to detail the business relationship and the benefits of BGI’s acquisition of Complete.

BGI was transparent and responsive, and the accusations did not gain traction. Almost no one in Washington took the bait and no Member of Congress ever publicly voiced concern.

“In a first-of-its-kind international transaction, we knew we needed to complement our legal strategy with a forward-leaning strategy of telling the company’s story to the media and to other stakeholders,” said Arthur B. Culvahouse Jr of O’Melveny & Myers, BGI’s legal counsel on the deal, and a former White House counsel.

So what is the best plan for success? A robust public affairs plan will not overcome true national security risks. But where there is a gray area that could be easily politicized, an acquirer needs a proactive strategy to inform all stakeholders of the benefits of the transaction and to address potential political arguments. A full analysis of (and preparation for) any risks must anticipate and head off critics – and this includes any left-field attempts to portray a well-intentioned deal as a threat to the nation’s security. 😊

.....
Michele Davis is a Partner in Brunswick’s Washington, DC office, and former Assistant Secretary for Public Affairs at the US Treasury Department. She advises on cross-border M&A communications, crises and public affairs.

Su-Lin Cheng Nichols is a Director in Brunswick’s Washington, DC office and has advised on a number of cross-border transactions. She specializes in public affairs, media relations and corporate reputation.

12345

Five questions to ask your deal team

1. What broader political and policy dynamics could this deal potentially stir up?
2. Which stakeholders, if they mount opposition, pose the greatest threat to the deal?
3. Which third parties can be enlisted to help?
4. What are the reputational assets and liabilities of the parties to the deal?
5. How will you shape your messages to be more effective, given the political environment?



Stakeholders

