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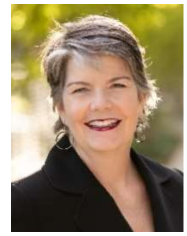
BPE Global Hot Topic – April 2023



Dear Due Diligence Team

You are clearly experts at finding potential acquisitions based on a target's impressive technological attributes and we certainly don't want to get in the way of your critical work. But there are a few more tips and tricks you might not be considering on how to ensure that your strategic purchase doesn't end up costing the company a lot more money on top of what you paid for the acquisition.

Today's growth strategies are all about buying emerging companies and leveraging their technology to gain market share, increase revenue or expand product offerings. But buyer beware, just because a target is mind-blowingly brilliant from a technical perspective, the technology itself may come with trade compliance red tape. When you are thinking about a target, you need to equip your team with the tools to understand the true cost of acquiring a business – not just what you have to pay their shareholders. The true cost of acquiring any business will include:

1. Cost of acquiring the money – if you are taking foreign investment, you must ensure that the funds don't trigger a Committee on Foreign Investment in the United States (CFIUS) review. CFIUS is an inter-agency committee that reviews the national security implications of foreign investments in U.S. companies. If the target designs, tests, manufactures, fabricates, or develops "critical technology" based on 31 CFR § 801.204 you may have a mandatory CFIUS filing requirement.
2. Cost of development – depending on the type of technology that you are acquiring – you may need to obtain deemed export licenses for certain foreign national employees and contractors to develop, produce or even support the technology. This will require you to develop and/or expand your export compliance program.
3. Cost of foreign customers – you may make something that is not in itself subject to National Security export controls, but the target may be selling to end users or for end uses such as military end use that require export licenses. An acquisition may require you to expand your export compliance program and manage orders in a way that you haven't in the past. You may have to implement more transactional processes, obtaining and managing export authorizations for individual shipments and meeting mandatory reporting requirements.
4. Cost of regulatory change – your acquisition may land the company smack dab in the middle of a tug-of-war between Washington and Beijing. Whether it's retaliatory tariffs or sanctions, there are ever-evolving regulatory changes where you can't predict whether new regulations will cut off your ability to make or sell your product.

These are all costs that you must factor in before you buy a company. And they all cost money and take time.

Your work does not stop once you own the target. Before the ink dries on the contract you need to conduct an internal assessment to determine if the target has any potential export or import violations

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and areas of high risk. And, although you probably have a good idea of the company's technology because of any CFIUS work that you undertook as part of the acquisition, you are now going to have to classify every one of their products and software as well as any technology that might have been missed. You're going to have to build out a product classification matrix that includes any export controls that apply and any tariffs that will be imposed. You'll want to know sooner rather than later if any of your imports are subject to antidumping or countervailing duties (think aluminum and steel). You are going to want to look at how the target determines the Country of Origin for their products. And if they were making any duty free, Buy American Act or Trade Agreements Act claims. And all of this is to simply understand what exposure the company has.

Then you should audit specific transactions. You should screen all of the target's customers – for demos as well as product purchases. Then you are going to want to get a list of all the target's sales, service and free of charge exports for the past five years. We recommend doing a targeted assessment, focusing on high-risk products, countries, end uses and end users. And then you need to follow the paper trail and assess whether the target was filing accurate declarations with the various government agencies that they interact with. And you are still not done! You are going to have to assess any systems that the target put in place to screen, classify or determine license requirements. You will also need to assess the personnel in charge of import and export compliance to ensure they are qualified and accountable.

We want to leave you with a word of caution… If you are saying to yourself that it is not worth the effort and that your diligence work was enough, the Department of Treasury just issued a settlement agreement with Wells Fargo in March of 2023 for apparent violations that occurred between 2010 and 2015. In addition to wiring $300,000 to the U.S. Department of Treasury, Wells Fargo spent countless hours to research and compose the disclosure. They undoubtedly paid many thousands of dollars to have legal counsel review and perfect the disclosure. They have committed internal resources and systems to terminate the cause of the conduct at issue. And they've been doing all of this for at least eight years. And this is all because Wells Fargo inherited Wachovia's trade insourcing relationships when Wells Fargo acquired Wachovia in 2008.

Now you have the tips and tricks on what to consider during and after an acquisition. And now it is your job to keep your company safe from unnecessary expense and exposure resulting from an acquisition.

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