MQR Associati

United States Market Entry for Foreign Enterprises

Foreign Direct Investment into the United States

We have organized this Blog Series from the perspective of the risk as well as reward which each market entry modality presents to the Foreign enterprise. Accordingly, we have begun our Series with lowest level of risk posed by the simple opening of a Representative or Branch Office in the U.S. From there, US market penetration usually encompasses the establishment of U.S. sales channel which can be either direct or indirect. Again, a U.S. sales channel presents a relative low level of risk as they can be dismantled should they prove unproductive.

We next discussed the technology-centric modalities such as VAR's and production or manufacturing licensing which involved the onshoring of intellectual property in some manner or form ("IP"). Here, the commensurate level of risk is elevated significantly as third parties now exercise control of the Foreign enterprise's IP pursuant to applicable licensing regimes. This enhanced risk level however also brings the prospect of higher returns due to the intrinsic value of the IP subject to license.

In this post, we now progress to the highest level of risk as well as reward, the permanent investment of capital upon U.S. soil.

A foreign direct investment project carries enormous significance for the Foreign enterprise as it entails the investment of permanent capital upon foreign soil. Unlike deploying a sales channel in the United States which can easily be disbanded if sales do not materialize, a direct investment of capital into the U.S. signifies a long-term commitment of capital which can only be returned thru profit distributions, liquidation or sale of the entity. With high risk of course comes high reward as the untaxed appreciation of investment capital deployed is the indisputable form of wealth creation.

For Foreign enterprises contemplating an acquisition of or merger with an existing US business, the process begins with the search for a qualified acquisition target or candidate. In many instances, the Foreign acquiror may already have a target or several in consideration through its existing sales channels in the US of thru competition in the

marketplace. In other cases, the services of an Investment Banker with specialization in the chosen field of interest will also present an array of possible acquisition targets. Initial contacts with the target can be made thru various channels, such as direct contact by the Foreign suitor within the target organization at a high level, or thru a third-party intermediary such as the Foreign enterprise's counsel, accountant or investment banker if employed.[1]

The initial discussions remain of course at a high level wherein the Foreign suitor will explain its business and interest in expanding its operations in the US thru a strategic alliance with the target. Should the target want to explore an alliance further, the next step would entail the disclosure by the target of certain proprietary information, commonly expressed by a written Nondisclosure Agreement ("NDA"). Where the NDA covers only the protection of target's proprietary information, the NDA is unliteral in nature whereas often times, the Foreign suitor will also disclose confidential information to the Target, thus the need for a mutual NDA.

Regardless of whether the NDA is unilateral or mutual in form, the target is very concerned with the nature of the information first disclosed to the Foreign suitor. In many instances, the information disclosed is closely curated by the target with often key financial or technological information only superficially disclosed. Only later in the acquisition process where a definitive term sheet or MOU is agreed upon does more fulsome proprietary information begin to be divulged.

Moreover, NDA's within the acquisition process demand careful attention and scrutiny as disputes and litigation can arise particularly where the Foreign suitor decides not to follow thru with the

[1] An Foreign suitor may also be invited to participate in an auction of the target where the Board of the target has decided to market the sale of the target thru an auction process. In this instance, the sale process is governed by strict rules often promulgated by an Investment Banker managing the sale process. Foreign companies competing in an auction process will be discussed later in a separate post.

acquisition after having the benefit of the target's confidential information. This is particularly in play where the Foreign suitor and target are competitors in the marketplace where an inartful NDA may be grounds for claims of wrongful use of the target's confidential information in the marketplace by the ex-suitor

Also, where the target is a public company with shares traded upon a US stock exchange, there is a standard methodology and practice which has evolved with respect to NDA's, particularly where the target has decided to sell itself via an auction process.[2]

No matter the context of the manner in which NDA comes into play, whether in a private or public setting, the key feature for Foreign suitor which an NDA grants is the right to conduct due diligence of the target within defined time limits. Thus, the NDA is the gateway to whether a commitment of permanent investment capital by the Foreign suitor is warranted. Moreover, the NDA should provide sufficient confidential information to allow the Foreign suitor to decide whether to proceed with offering a term sheet outlining the basis economic and legal terms of a prospective acquisition or merger with the Target.

Term Sheets and MOUs will be explored in the next post.

[2] See Footnote 1.

