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ALERTS

# Mergers & Acquisitions: Trade Compliance, Successor Liability & Due Diligence

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The concept of “purchasing” the seller’s liability (i.e., “successor liability”) is old news to anyone involved in mergers and acquisitions (M&A). Yet, parties to M&A deals continue to overlook the potential for successor liability associated with violations of U.S. export/import laws. Indeed, the current maximum civil penalty for violations of U.S. export control laws exceed $1 million per violation, and penalties for customs/import violations can reach as high as the domestic value of the imported merchandise. Because U.S. courts have and likely will continue to recognize the U.S. government’s ability to pursue claims for unpaid duties and/or monetary penalties under a successor liability theory, even where the deal is strictly an asset purchase, purchasers should invest in necessary due diligence efforts focusing on seller’s compliance with U.S. import/export laws. Discussed below are some issues and questions that commonly arise when conducting such due diligence.(1) In addition to due diligence, parties involved in a transaction that could result in control of a U.S. business by a foreign person should assess the risk associated with reviews by the Committee on Foreign Investment in the U.S. (CFIUS) and potential divestiture mandated by the President of the United States.

## Export Controls and Sanctions

Sellers often say that the export classification of their products and/or technology is “EAR99” and that no license is required for export, when in fact the product should have been classified under either the U.S. Munitions List (USML) or Commerce Control List (CCL), in which case a license may have been required from either the State or Commerce Department prior to export. Also, does the seller know where, to whom, and for what purpose its product is being exported? Does it have procedures for screening vendors and customers against the various U.S. sanctions and denied parties lists? These are all basic elements of an export compliance program, and purchasers often find out only later that the seller could have prevented violations had it invested in implementing these basic procedures.

Additionally, if any party to the deal is registered with the State Department’s Directorate of Defense Trade Controls (DDTC) as a manufacturer, exporter or broker of defense articles or services that party is required to notify DDTC *at least 60 days prior* to closing of any intended sale or transfer to a foreign person of ownership or control of the registered company or any entity thereof.

## II. Foreign Investment in the U.S.

When a transaction could result in control of a U.S. business by a foreign person (*i.e.,* a “covered transaction”), parties to the transaction should consider whether to file a voluntary notice of the transaction to CFIUS,

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which is an inter-agency committee that reviews the national security implications of foreign investments in U.S. companies or operations. It is important to note that CFIUS takes a broad view of potential national security risks, which includes infrastructure, energy and close proximity to a sensitive U.S. installation. Although CFIUS filings are voluntary, CFIUS has the authority to require review of covered transactions and may prohibit, suspend or impose mitigation measures on the transaction. And in cases where a transaction has been completed, CFIUS may require divestiture of the foreign ownership or control. Assessment of the CFIUS risk should be considered at the outset of a proposed transaction.

## III. Customs and Import

Sellers often say they rely on freight forwarders, customs brokers, or foreign vendors to declare the correct tariff classification (HTS code) for the sellers' imported goods, and that all of their goods are eligible for duty-free treatment. Either response should serve as a red flag and should trigger additional diligence to ensure duty free entry was justified. Other important issues include whether seller imported goods subject to antidumping and countervailing duty, declared the correct value of the goods (particularly when importing goods from related companies) or correctly claimed preferential duty treatment under free trade agreements or other preferential trade programs.

(1)Note: the issues and questions discussed here is not an exhaustive or complete list for due diligence. Due diligence questions should always be customized to each specific transaction.