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NEWS

# GOING TO EL NORTE

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**Slowing economic growth in their home jurisdictions is leading increasing numbers of Latin America investors to look for opportunities in developed economies. Debevoise & Plimpton LLP partners Maurizio Levi-Minzi and Peter Furci consider the issues and challenges facing Latin American investors in the US**

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Latin American investors heeding recent warnings from the World Bank that the region is facing years of slower economic growth are increasingly looking for investments in developed countries, such as the United States. Many may find inspiration in the words of English author Lewis Carroll, who wrote in a different context: "it takes all the running you can do, to keep in the same place. If you want to get somewhere else, you must run at least twice as fast as that!"

A combination of chronic deficits, high inflation, lower commodities prices, weak productivity growth and unsuccessful economic policies have brought about a structural slowdown in many countries throughout Latin America and new challenges for the powerful and dynamic family groups that have emerged in recent years as the champions of the continent. As a result, the imperatives of diversification and globalisation are powering a drive by Latin American investors to establish a presence in the North, but doing so involves navigating issues and processes that may not be familiar to them. Below, we provide a brief introduction of some of the key differences when doing deals "en el Norte".

## Same game, different rules

Several of the Latin American investors looking for investments in the United States are family-controlled businesses or investment vehicles. Many grew and matured in domestic markets where they competed successfully with other family-controlled businesses with similar internal dynamics, found ways to cooperate with powerful government institutions and learned to leverage their relations with foreign investors and foreign lenders.

While most of these investors are very sophisticated global players who have dealt with international parties in their own respective markets, they are increasingly recognising that the rules of engagement when playing away from home are not the same. Initially, Latin American investors expected that their general familiarity with US business culture and M&A practices would facilitate their forays into the country. And to some extent that has proven true. But, in other significant respects, Latin American investors are discovering that partnering with US counterparties abroad is not the same as partnering with US companies at home.

First, the good news. Latin American investors are very pleased to discover how easy it is to carry out some corporate actions in the United States. For instance, the fact that a company can be formed in Delaware in less than a day puts broad smiles on their faces. On the other hand, many investors are often puzzled by the formalities involved in getting a deal approved by their counterparties if the deal involves minority shareholders or a public company. Adapting to the more robust states' laws of fiduciary duties, which runs from a controlling shareholder to the minority investors, and from the board of directors to the shareholders, can be a challenge for investors that enjoy more independence and fewer restrictions at home.

The duties imposed on a fiduciary will vary based on the context of any given transaction. Generally speaking, fiduciary duties require the board to act in the best interest of the company's shareholders and are heightened in the context of a sale. However, these duties can often be satisfied by a rigorous sales process. Fiduciary duties may also require a board to consider multiple aspects of a transaction, such as whether the target is more valuable to the shareholders as an independent entity pursuing its own corporate objectives, or whether there are any unique risks involved with a particular buyer, such as regulatory or closing risks. Therefore, even presenting the highest bid price does not necessarily guarantee an investor will be selected by the board as a winning bidder. Against this backdrop, US targets are often subject to an auction or other rigorous sales process before locking up with any one buyer. In some cases, an agreement to sell a company that would restrict the board from considering competing proposals from other potential buyers would constitute a violation of the board's fiduciary duties. US targets are focused on complying with applicable fiduciary duties in an effort to minimise the risk of shareholder litigation, which is relatively common in the US and almost a certainty if the target is a public company.

This legal framework surprises Latin American investors who truly believe they are making very strong offers for US targets. To succeed in the pursuit of these targets, it is necessary to accept the fact that the board's observation of the process does not necessarily imply a disagreement with the value proposition and modulate your strategy accordingly.

### Adopting a new risk profile

Taking calculated risks is how many Latin American investors built the fortunes that they are now seeking to invest in a diversified portfolio that includes US assets. But investing in US assets involves identifying and pricing risks in a very different context. In the United States, pending or threatened litigations or environmental exposure can impact targets in a manner that is much more devastating than similar matters on the Latin American investor's home turf. The risks and potential damages need to be weighed carefully and investigated thoroughly. Adjusting to the different context and the potential magnitude of these risks is critically important to the success of the investment.

Similarly, a great deal of attention needs to be paid to compliance matters generally. Compliance programmes that might seem robust to Latin American investors may actually be inadequate in view of the far stricter legal requirements in the United States. Assessing these issues properly is critical to avoiding surprises down the road and, to that end, Latin American investors should consider involving their advisers earlier in the process than they might have otherwise considered doing when pursuing deals on their home turf.

Another aspect of US investing which Latin American investors need to be aware of is the complex US tax system, which can impose high tax burdens and filing requirements on non-US investors in the absence of careful planning and structuring. Latin American investors often expect that so long as they invest from an offshore vehicle, taxes should be minimal. However, this is often not the case. In the case of corporate investments, the US generally does not tax capital gains of non-US investors, but does impose a withholding tax of 30 per cent on dividends. This rate can be reduced by tax treaties, but the US tax treaty network with Latin American countries is less extensive than one might expect given the ties to the region. In the case of investments in partnerships and limited liability companies engaged in operating businesses in the United States, and for investments in US real estate, Latin American investors are often surprised to learn that their investing entity may be subject to direct tax payment and filing obligations at the federal, state and local level, at combined rates that can exceed 60 per cent. The importance of careful and customised tax structuring for US opportunities is, therefore, of the essence.

### A safe harbour

Latin American investors making an investment in a US target will also need to carefully consider whether the transaction will warrant submitting a voluntary notification to the Committee on Foreign Investment in the United States (CFIUS). This is an inter-agency committee of the federal government, including the US Departments of Treasury, Defence, Homeland Security, State and Commerce, charged with determining whether control by a foreign person over a US business may impair the national security of the United States. Although submitting a CFIUS notice is voluntary, in an appropriate transaction, parties to a transaction seek clearance from CFIUS post-signing to obtain a safe harbour from actions by the US government, which could include blocking the transaction or, in the rarest of cases, a forced divestiture of the US business post-closing. CFIUS jurisdiction only applies to controlling investments, but for these purposes, control is defined broadly.

To the surprise of many Latin American investors, national security is deemed to extend well beyond investments in the weapons or defence industry. CFIUS filings are made with respect to the telecommunications, software, mining, oil and gas, manufacturing, technology and consulting industries. National security includes infrastructure and the energy sector, including the power generation industry, whether upstream or downstream, and can be implicated where the US businesses have facilities located in close proximity to US government facilities, such as military bases. The process for obtaining CFIUS review is, by statute, intended to be fast. Once the parties submit a notice, CFIUS must complete its review within 30 days, subject to an additional 45 day investigation period if CFIUS determines a more detailed investigation is required.

None of these issues are showstoppers for the well-prepared and well-advised Latin American investor. We should expect the wave of Latin American investments in the United States and other emerged economies to continue. Ultimately, perhaps the most significant benefit to Latin American groups will be the lessons that they are learning in the North. Lessons on which they can also capitalise at home.

Debevoise & Plimpton LLP partner Jeffrey Cunard and associate Vincent Bianco also contributed to this article.