

Social Enterprise Associates
Tip Sheet #8

Co-authored with the
International Transactions Clinic
University of Michigan Law School

Tip sheets #5-8 are a series of 4 annotated commentaries to assist entrepreneurs interested in creating and operating ventures in the United States by providing easy-to-understand explanations for common legal documents.

Tip Sheet #8

Biggest Concerns for Foreign Investment in the United States

Understanding major concerns & pitfalls that foreign investors might encounter when investing in U.S. businesses

Introduction

Taking an idea from conceptualization to inception and finally to market is filled with many challenges. Legal documents in particular are hard for entrepreneurs to understand, so many gloss over them. However, they carry immense importance, as bad or wrong documents can cost a lot of money.

Social Enterprise Associates (SEA) and the International Transactions Clinic (ITC) at the University of Michigan Law School collaborated to produce four annotated commentaries (Social Enterprise Associates Tip Sheets #5-8) to assist entrepreneurs interested in creating and operating ventures in the United States by providing clear and easy-to-understand language that deciphers common business legal documents. These four documents are:

- Tip Sheet #5 – Articles of Incorporation
- Tip Sheet #6 – Articles of Organization (LLC)
- Tip Sheet #7 – Commercial Loan Agreement
- Tip Sheet #8 – Biggest Concerns for Foreign Investment in the U.S.

The Biggest Concerns for Foreign Investment in the U.S.

This document briefly outlines major concerns and pitfalls that foreign investors (i.e., you) might encounter when investing in U.S. businesses. The items below are divided into two categories: (1) Compliance and Internal Controls; and (2) Commercial Concerns and Business Decisions. The logic behind this division is this: you cannot ignore the first category without risking civil and/or criminal liability, while the second category primarily addresses business decisions. Obviously, any issue—even compliance and criminal liability—can be reduced to some form of business risk, but this outline aims to help you prioritize these issues.

I. Compliance & Internal Controls

The following items deal with compliance issues—things you must do to remain within the laws of the host-country, or face possible liability. These issues are contained in statutes and regulations.

1. Bribery – *The Foreign Corrupt Practices Act*

- a. What is it?
 - i. The FCPA is a U.S. Federal law that makes it illegal to bribe or offer any sort of payment to a foreign official, political party, or other government official in order to influence the person in violation of their official duty or to secure an improper advantage in an attempt to obtain or retain business. In short, it makes bribing foreign official illegal. The FCPA applies to US businesses and individuals as well as anyone “making use of interstate commerce corruptly.” This means the Act would apply to a foreign entity securing financing in the U.S. if a part of that financing was used to bribe a foreign official. Currently, the United Kingdom is the only other country that has a similar anti-bribery provision.
- b. Why do I care?
 - i. The reality of the situation is that one man’s bribe is another man’s way of doing business. In many countries, particularly in the developing world, bribes and kickbacks to government officials are a practical necessity for an individual or entity trying to do business. In many places the bribes and kickback schemes are essentially codified and constitute an important part of underpaid government officials’ salaries. This means that foreign entities that receive US financing have to be particularly careful not to run afoul of this unique provision.
- c. What if I want to know more?
 - i. The Department of Justice provides more information [here](#).

2. Foreign Account Tax Compliance Act (“FATCA”)

- a. What is it?
 - i. The FATCA is a new provision to US law that will take effect in 2013. It requires that a non-US commercial entity that receives certain types of payments from U.S. sources be subject to a 30% withholding tax unless certain exemptions apply. The law applies broadly to any foreign business, professional service firm, and many other non-U.S. entities receiving, directly or indirectly, payments from U.S. sources.
- b. Why do I care?
 - i. The short answer is that you probably don’t. If you are just borrowing money from the U.S. this law does not apply to you at all. However, should your relationship with the US lending institution evolves to the point where you are receiving dividends, interest, royalties, payments for legal settlements, rents on real property in the US or other such payments, you will be subject to FATCA.
- c. What if I want to know more?
 - i. The IRS has authored a number of reports and letters to clarify and explain FATCA.
 - ii. <http://www.irs.gov/businesses/corporations/article/0,,id=236667,00.html>

3. Anti-Money Laundering

- a. The Anti-Money Laundering Act and “Know-Your-Customer” requirements.
- b. What are they?
 - i. Anti-Money Laundering (AML) is a component of the Bank Secrecy Act, which establishes the requirements banks must meet before lending.
 - ii. Put simply, banks need to accurately identify their borrowers, to ensure that funds are not flowing to terrorists, money launderers, etc.
 - iii. These components are embodied in the “due diligence requirements” (*i.e.*, homework and background checks) known as “Know Your Customer” checks.
- c. Why do I care?
 - i. These are primarily procedural hurdles—compliance is easy, but if you are accessing U.S. debt, you will likely encounter these procedures.
- d. What if I want to know more?
 - i. [The Bank Secrecy Act](#)
 - ii. [The US PATRIOT ACT](#)

4. Securities Regulations

- a. The Securities Act of 1933 & The Exchange Act of 1934
 - i. If you want to sound “in the know”: the '33 Act and the '34 Act.
- b. What are they?
 - i. The statutes that create the foundation for securities regulation in U.S. law.
- c. Why do I care?
 - i. You're trying to participate (*i.e.*, buy shares) in companies that are located in the U.S. Chances are you have some sort of exit strategy (*i.e.*, selling your shares at a later date). Unfortunately, under U.S. law your shares in the company are “restricted”—you cannot simply sell them in the open market. To sell on the open market, the shares must be registered with the Securities and Exchange Commission (the SEC), or qualify for an exemption from the registration requirement.
- d. But do I *really* care?
 - i. The good news is that given the likely structure of your investment, these shares—although technically *restricted*—will fall within a number of exceptions. The advice of a seasoned securities lawyer is invaluable in these situations.
- e. What if I want to know more?
 - i. Wikipedia actually provides a good primer on the 33 Act [here](#), and the 34 Act [here](#).
 - ii. Also check out the [SEC's website](#), as it provides many useful tools.

II. Commercial Concerns & Business Decisions

The following list describes certain elements of US law, the knowledge of which may help you to make more informed business decisions, allocate risk, and more fully understand potential pitfalls. These are probably not as crucial as the items in the previous section, but knowledge of them will certainly help you navigate investments in the U.S.

1. Filing Law Suits Against Foreign Countries

- a. The Foreign Sovereign Immunities Act
- b. What is it?
 - i. A U.S. law that restricts foreign sovereigns (e.g., the country of France) from being sued in U.S. courts.
- c. Why do I care?
 - i. This may have little practical effect on you, but if you have a venture in the U.S., that corporate entity may be prohibited from suing, say, your native country in U.S. courts.
- d. What if I want to learn more?
 - i. The Legal Information Institute (LII) at Cornell Law School provides the text of the act in an easy-to-use way [here](#).

2. Intellectual Property

- a. The Copyright Act, The Lanham Act, The Patent Act, the Berne Convention, and TRIPS
- b. What are they?
 - i. The Copyright, Lanham, and Patent Acts are the three statutes that comprise the majority of U.S. Intellectual Property Law.
 - ii. The Berne Convention is an international convention for the protection of literary and artistic works.
 - iii. The TRIPS Agreement (or the Agreement on Trade-Related Aspects of Intellectual Property Rights) administered by the World Trade Organization (WTO) as part of the General Agreement on Tariffs and Trade (GATT). It sets minimum standards for copyright, trademark, and patent protection for member countries.
- c. Why do I care?
 - i. You might not care too much about the Berne Convention, because there is a good chance it doesn't implicate the kinds of works involved in your venture.
 - ii. You probably care about TRIPS, because if you come from a non-member country, the U.S. (as a member) will likely have higher IP standards than those in your native country.
 - iii. Chances are, if you're investing in a company, that company is creating *something*. There will usually be some intellectual property component in any output, and it is worthwhile to know how that intellectual property is treated in the host country. IP laws vary considerably from country to country, so you cannot assume that something "ownable" in one country is "ownable" in another.
 - iv. As an example, many European countries believe in "moral rights"—the idea that an artist or author has a say in the treatment of works even after signing away ownership to those rights. Conversely, the U.S. recognizes moral rights only in limited circumstances.
- d. What if I want to learn more?
 - i. Copyrights are handled by the U.S. Copyright Office. The Office provides very useful and easy to understand circulars [here](#).

- ii. Patents and Trademarks go through the U.S. Patent and Trademark Office. Like the Copyright Office, the USPTO provides very clear explanations of basic trademark and patent issues [here](#).

3. International Bankruptcy

- a. The Model Law of Cross-Border Insolvency
- b. What is it?
 - i. As part of a major overhaul of the US bankruptcy code in 2005, a new Chapter was added to govern instances of foreign entities with debts in the U.S.
 - ii. Chapter 15 is the United States' version of the United Nations Model Law on Cross-Border Insolvency.
- c. Why do I care?
 - i. In the event that you are caught up in a bankruptcy proceeding in your home country or some other foreign country, Chapter 15 will govern how proceedings will take place if you need to access U.S. courts. Chapter 15 is designed to help coordinate cross-border bankruptcy and insolvency proceedings and as such should be the first place you look if you have borrowed
- d. What if I want to learn more?
 - i. An overview of Chapter 15 is provided [here](#).
 - ii. An overview of the Model Law in general is provided [here](#).

4. Expropriation and Disposal Clauses

- a. What are they?
 - i. In simple terms, the host country decides to nationalize your assets (*i.e., say your stuff belongs to them*).
- b. Why do I care?
 - i. Banks will consider this an event of default. So, not only are you bummed that your investment is gone, but also the bank is probably going to accelerate your loan (*i.e., it's all due now*).
 - ii. You probably don't care, because the U.S. will probably never do this – but expropriation is always a possibility.

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