

President Obama Blocks Chinese Acquisition of Aixtron SE

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CFIUS

Acting on the recommendation of the Committee on Foreign Investment in the United States (“CFIUS”), President Barack Obama issued an [Executive Order](#) on Friday, December 2, prohibiting the acquisition of the U.S. business of Aixtron SE (“Aixtron”) by a company ultimately owned by investors in China. This is the first time that a President formally has utilized the authority of the CFIUS statute to block a foreign acquisition prior to consummation of the transaction.

The Administration did not offer a detailed account of the national security concerns underlying its decision to prohibit the transaction. However, in [a statement](#), the Department of the Treasury—which chairs CFIUS—noted that “the national security risk posed by the transaction relates, among other things, to the military applications of the overall technical body of knowledge and experience of Aixtron, a producer and innovator of semiconductor manufacturing equipment and technology.” The statement observed that Aixtron “manufactures equipment for the global semiconductor industry, including Metal-Organic Chemical Vapor Deposition (“MOCVD”) systems used to build compound semiconductor materials,” and that the putative buyer, Grand Chip Investment GmbH, is “ultimately owned by investors in China, some of whom have Chinese government ownership.” The statement also noted that the proposed acquisition would have been funded in part by an industrial investment fund supported by the Chinese government.

Aixtron and the buyer had submitted a voluntary notice of the transaction to CFIUS. Following a national security review, CFIUS declined to approve the transaction and instead recommended that the President prohibit it. The statute governing the CFIUS process—Section 721 of the Defense Production Act of 1950, as amended—authorizes the President “to suspend or prohibit any covered transaction that threatens to impair the national security of the United States” if the threat cannot be adequately addressed by other means.

We see the following key takeaways from this development:

1. **First Presidential Block.** Never before has the President prohibited a proposed but un consummated transaction on the recommendation of CFIUS, although the President has twice intervened after a transaction has closed. In 2012, President Obama [ordered](#) Ralls Corp., a U.S. company owned by two Chinese nationals, to divest certain project companies that owned wind farms located in proximity to restricted airspace associated with a U.S. Navy facility. And in 1990, President George H.W. Bush [ordered](#) that a Chinese government-affiliated entity divest its interest in MAMCO Manufacturing, a producer of airplane parts. In a number of other cases, potential acquirers have abandoned proposed acquisitions after CFIUS raised concerns, but did so voluntarily

and without triggering a formal prohibition by the President. The result in this case presumably reflects the willingness of the parties to force the White House to make a formal determination, rather than abandon the transaction in response to CFIUS's objections.

President Obama's action follows an unusual series of events, which saw the German Federal Ministry of Economic Affairs and Energy issue a clearance certificate for the transaction pursuant to the provisions of the German Foreign Trade Act and the German Foreign Trade Ordinance on September 8 to China's Fujian Grand Chip Investment Fund LP—the indirect shareholder of Grand Chip Investment GmbH—only then to reverse course and withdraw the certificate in late October. The German government itself made no formal statement in connection with the withdrawal at the time, although Deputy Economy Minister Matthias Machnig told German newspaper *Die Welt* that “the federal government has received previously unknown security-related information.” Subsequent press reports suggested that U.S. intelligence officials had expressed concern to their German counterparts regarding the proposed transaction.

- 2. Particular Sensitivities of Investment in the Semiconductor Sector, Especially from China.** The Executive Order is a vivid reminder that CFIUS is carefully scrutinizing foreign investments in sensitive U.S. industries, including the semiconductor sector, and especially when the transaction involves investment from China. The statement from the Treasury Department indicating that the national security concerns related to “the overall technical body of knowledge and experience of Aixtron” is the first time that CFIUS has publicly indicated that national security concerns can be grounded in the underlying know-how of individuals in a business—although this factor previously has arisen as an issue in other transactions involving advanced technologies, particularly in the semiconductor industry. This is not, however, the first time that CFIUS has indicated publicly that there can be particular sensitivities with businesses engaged in the design and production of equipment related to semiconductor manufacturing. In fact, in listing the types of transactions that have raised national security concerns, the last several [annual reports](#) published by CFIUS specifically [referenced](#) businesses that “[p]roduce certain types of advanced technologies that may be useful in defending, or in seeking to impair, U.S. national security, which may include businesses engaged in the design and production of semiconductors and other equipment or components that have both commercial and military applications.” The annual report also indicated that the U.S. intelligence community “judges that foreign governments are extremely likely to continue to use a range of collection methods to obtain critical U.S. technologies.”

These factors—the sensitivity of certain types of design and production know-how related to semiconductors and the belief that certain governments are utilizing all available collection sources, including mergers and acquisitions, to obtain critical technologies—are front and center in CFIUS's review of every transaction in the semiconductor sector, and particularly those from China. To this end, the U.S. government has observed, and is acutely aware of, China's robust efforts to develop its domestic semiconductor industry. Commerce Department Secretary Pritzker took the unusual step of making a major policy address last month focused specifically on the semiconductor industry and China, noting the Chinese government's announced objective of spending \$150 billion to increase China's self-supply of integrated circuits to 70 percent by 2025. While Secretary Pritzker was very clear to address the issue in trade rather than in investment terms, her public remarks—focused on one sector and

one country—clearly reflect the intensity of attention at the highest levels of the U.S. government on this issue.

This subject is particularly challenging for the U.S. government more broadly, as well as for CFIUS (more narrowly), in the context of particular transactions for several reasons. First, semiconductors and related technologies are foundational for a strong, consumer-based economy as well as for advanced military capabilities. Thus, a developing country such as China will have legitimate economic and national security reasons for pursuing the development of its semiconductor sector. Second, as the world's second-largest economy—and on the path to being the largest economy—China is an important and attractive market to companies in the semiconductor industry. The vast majority, if not all, leading semiconductor companies are nearly compelled to have a strategy to develop business in China simply as a matter of prudent planning for the future. This likely would be true even without the Chinese government injecting significant capital into the market, but it is certainly true when considering the Chinese government already has established funds of at least \$20 billion to support acquisition activity. Third, given where China is starting on the technology curve, the Chinese cannot accomplish the government's stated goals of growing their domestic semiconductor sector without pursuing acquisitions abroad—meaning that it is inevitable that there will be (as there already has been) an abundance of outbound transactions and acquisitions that are purely commercial in nature, and others that risk touching on national security sensitivities.

In this context, there are two points that are salient with respect to the Aixtron transaction: First, for every transaction in the semiconductor sector that involves China (and even some that do not involve China directly, but where there could be Chinese interests, such as if there are Chinese operations or customers of the existing U.S. business), CFIUS is conducting a very thorough risk-based analysis regardless of how benign the transaction may appear. These analyses are informing the U.S. government's views of how to respond to the challenging policy issues created by the rise of China in the semiconductor industry. Second, the Aixtron transaction touched a particular nerve because (i) the MOCVD machines made by Aixtron are key tools in manufacturing for both commercial and military purposes; (ii) the know-how reflected in that process appears to have been targeted by the Chinese government (or so the U.S. government believes); and (iii) there was Chinese government funding for the transaction.

- 3. CFIUS Will Interpret Its Jurisdiction Broadly Where It Has National Security Concerns.** CFIUS jurisdiction extends to transactions that will result in control by a foreign person over a “U.S. business,” which is defined to mean “any entity, irrespective of the nationality of the persons that control it, *engaged in interstate commerce in the United States, but only to the extent of its activities in interstate commerce.*” (emphasis added) While this definition is potentially broad—in concept, it can cover business components outside the United States that result in activities in U.S. interstate commerce—it also signals an intent to limit jurisdiction only to businesses that actually are resident in the United States. To this end, the CFIUS regulations specifically provide examples indicating that merely selling goods or services into the United States is insufficient to create CFIUS jurisdiction.

In this regard, it is notable that the scope of the Executive Order is defined by reference to “the U.S. business of Aixtron,” which is defined as “AIXTRON, Inc., a California corporation, the equity interests of AIXTRON, Inc., and *any asset of Aixtron or*

AIXTRON, Inc. *used in, or owned for the use in or benefit of, the activities in interstate commerce in the United States of AIXTRON, Inc.*, including without limitation any interest in any patents issued by, and any interest in any patent applications pending with, the United States Patent and Trademark Office (collectively, Aixtron US).” (emphasis added) Thus, while the Executive Order carefully focuses on the U.S. business of Aixtron, its scope potentially could encompass assets of Aixtron *outside* the U.S., to the extent those assets are “used in, or owned for the use in or benefit of” Aixtron, Inc.’s activities in the United States.

Neither the Executive Order nor the Treasury Department’s press release on this matter state precisely how far such a definition of “U.S. business” extends as it relates to Aixtron’s assets—and in particular whether, in fact, the Executive Order would cover assets outside the United States. Nevertheless, this seems to be a clear implication of the wording in the Executive Order. In turn, if there were to be any legal challenge of the Executive Order—and, in general, the President’s national security determination in a CFIUS matter is not subject to judicial review—we expect that it could focus on whether this definition exceeds the scope of CFIUS’s authorities. The only decision by a U.S. federal appeals court on the CFIUS process (which arose from the Ralls case described above) focused on the sufficiency of the process leading to CFIUS’s determinations, and did not address the scope of CFIUS’s jurisdiction with respect to the definition of what constitutes a “U.S. business” under the statute.

4. **The Aixtron Case Does Not Signal a Sea Change in the CFIUS Process, or that the U.S. Is Closed to Investment, Including Chinese Investment in the Semiconductor Industry.** Notwithstanding the foregoing, we do not believe that CFIUS’s and the President’s actions signal a broader retrenchment on the part of CFIUS or the U.S. government more generally, including in the semiconductor sector. CFIUS has approved recently, and we expect the Committee will continue to approve, Chinese acquisitions in the semiconductor sector that do not involve know-how or other assets with potentially sensitive applications. Rather, the Aixtron Executive Order—like the Ralls and MAMCO orders before it—is best understood as the product of an unusual confluence of circumstances focused on the perceived sensitivity of Aixtron’s know-how and products, and the U.S. government’s judgment regarding China’s intended use of those assets.
5. **Future Transactions Like Aixtron Are Inevitable.** In a sense, the Aixtron case is an inevitable outgrowth of the emergence of cross-border merger activity with China. So long as the U.S. and China remain two of the world’s largest economies, while also being significant military and political rivals, there almost certainly will be merger and acquisition activity that triggers concerns within CFIUS. In turn, we expect CFIUS to remain increasingly vigilant in matters involving investments in critical technology areas, such as semiconductors, and transactions generally involving investment from China. This is especially true in light of the [upcoming change in Administration](#), as President Obama’s appointees at the CFIUS agencies are succeeded by those of President-elect Trump. As we stated in our alert examining the CFIUS process under the incoming Trump Administration, this dynamic places even greater importance on transaction parties carefully planning with respect to matters that may involve U.S. government national security interests and CFIUS reviews.

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We hope that you find this analysis useful. Please do not hesitate to contact the following members of our CFIUS Practice Group if you would like to discuss any aspect of the foregoing in further detail:

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