

## Traton/Navistar: Legal Experts Expect U.S. Truckmaker Buyout to Face CFIUS Review

Navistar International (NAV), the U.S. truckmaker undergoing a \$3.7 billion buyout by Volkswagen (ETR: VOW) subsidiary Traton (ETR: 8TRA), has said that the merging parties “do not intend to file a CFIUS notice in connection with the transactions.”

But that assertion may prove premature in light of VW’s foreign ownership and Navistar’s minority stake in Navistar Defense, which features a lineup of armored vehicles and holds a number of U.S. defense contracts, said legal experts familiar with the Committee on Foreign Investment in the United States, which screens deals for national security threats.

Instead, the panel will likely ask both Navistar and Traton to submit a joint CFIUS filing, experts said.

“Given the current CFIUS enforcement environment, any investment in a U.S. defense contractor has a reasonable likelihood of receiving CFIUS scrutiny,” said Christopher Swift, a partner and national security lawyer at Foley & Lardner.

The Defense Department, which sits on the panel, may be concerned about its vendors’ contractual commitments, Swift said. CFIUS might also want to review Navistar’s leading role in the development of driverless vehicles, experts said.

After spurning two previous takeover offers, Navistar reached a definitive agreement this month to sell itself to Traton, which manufactures heavy truck brands including Scania and MAN and already owns 16.7% of Navistar. Wolfsburg, Germany-based VW, in turn, owns almost 90% of Traton.

That foreign ownership may well raise concerns at CFIUS. Although the panel is known for its scrutiny of deals involving firms with Chinese ties, the committee also vets deals from investors in friendly countries. In this case, the German state of Lower Saxony is VW’s second-largest shareholder, with 20% of the voting rights, while Qatar’s sovereign-wealth fund is the third-biggest, with 17%.

To be sure, there are mitigating factors operating in Traton’s favor. Most importantly, Navistar in 2018 sold a 70% stake in Navistar Defense to Cerberus Capital Management, a New York-based private equity firm. Traton’s acquisition of Navistar’s 30% stake in its former defense subsidiary, then, would still leave Cerberus firmly in control of the business.

President Donald Trump has in recent years viewed top Cerberus executives as trusted advisers on national security matters. In 2018, for example, the president chose Cerberus co-founder Stephen Feinberg to lead the Intelligence Advisory Board. And just this May, Trump nominated Cerberus Managing Director Louis Bremer, a former Navy SEAL, to become an assistant secretary of defense.

These close ties could have direct bearing on a CFIUS review because the Navistar deal might land at the panel before Trump leaves the White House, and while he still holds sway over national security matters.

The companies have [said](#) they expect to close the deal in mid-2021. Spokespeople for VW and Traton declined to comment. Navistar and CFIUS representatives didn't respond to requests for comment.

**Export regulations.** Traton's buyout of Navistar could be subject to a mandatory filing with CFIUS because the target produces export-controlled equipment.

Though the Lisle, Illinois-based company is best known for its commercial trucks and buses, Navistar Defense also produces armored trucks and fighting vehicles.

And although Cerberus now holds a majority of that company's equity, Navistar as part of the purchase deal inked a long-term agreement to supply military and commercial parts and chassis to its former defense subsidiary.

Just last month, Navistar Defense won a \$44 million U.S. Army contract to provide technical services for mine-resistant, ambush-protected MaxxPro vehicles.

Under new CFIUS [rules](#) that went into effect on October 15, merger partners must conduct a detailed analysis to determine whether any goods that they produce are subject to the International Traffic in Arms Regulations (ITAR) and Export Administration Regulations (EAR), two laws regulating exports of military technology, commercial technology and intellectual property.

The new CFIUS rules require a filing if a U.S. merger target needs government approval to export, re-export or transfer products or technology. Making that determination can be a highly complex process, experts said. Prior to October 15, parties to transactions instead had to determine whether the technology involved was used in or designed for one of 27 sensitive industries listed in the old CFIUS regulation. That made the process of deciding whether companies must file with CFIUS a much easier task, the experts said.

To grasp the complexity, consider Navistar’s work on driverless vehicles, which deploy artificial intelligence, navigation equipment, security cameras and sensor technology including radar and laser radar. EAR’s Commerce Control List (CCL), a main point of reference for dealmakers, includes at least four categories related to autonomous-driving technology. Category 3 in the list, for instance, covers semiconductors and integrated circuits used in driverless vehicles. Category 5 includes security items such as the encryption needed to protect a vehicle from hackers. Cameras and sensors are covered under Category 6, while navigation equipment falls under Category 7.

Some Navistar products also require licensing under ITAR, which regulates the export and transfer of defense technology as well as “dual-use” products, which have both military and civil uses.

“Normally, a U.S. company that has ITAR-controlled technology or technology on the commerce list would be a high priority for CFIUS to review, even if investors are from friendly countries,” said Swift. The U.S. government is adamant about ensuring that certain controlled items don’t fall into the wrong hands, he said.

Friendly countries remain a concern because they may take advantage of their access to the U.S. to “collect sensitive military and civilian technologies and to acquire know-how in priority sectors,” said a 2018 [report](#) from the National Counterintelligence and Security Center.

**To file or not to file?** Although Navistar’s remarks about CFIUS may seem “a little overconfident,” the merger partners might still be seeking to resolve national security issues surrounding the deal, said another expert, who requested anonymity because they’ve worked with one of the firms in the past.

“The fact that Bremer is close to the administration could also play a part” in their calculations, the expert said. The Cerberus director’s experience with the Defense Department is likely to be viewed positively within CFIUS, some experts added.

The danger in not filing a deal with CFIUS is that the committee “always has the authority to claw back a deal,” said Harry G. Broadman, who served on CFIUS and now chairs the Emerging Markets and CFIUS practices at Berkeley Research Group.

The clawback provision allows CFIUS to retroactively review mergers and acquisitions that the companies didn’t initially submit for approval. The panel can then restrict the deals by imposing mitigations or even unwinding them altogether.

“Parties need to determine the present value of filing at the outset versus the risk of having a deal being clawed back down the road,” Broadman said. After a new foreign-investment law went into

full effect this year, proactive filing with CFIUS became the new normal for dealmakers, experts said.

**Qatari ownership.** The presence of two Qatari representatives on VW's 20-member supervisory board could also attract CFIUS questions, the experts said.

“Qatar sovereign funds invest heavily in the technology and energy sectors,” said one international trade lawyer who has in the past facilitated deals involving buyers from the Middle East. CFIUS tends to take Qatari investments very seriously because most Qatari funds operating in the U.S. are government-controlled, the lawyer said.

That said, CFIUS has approved a number of deals involving the country's sovereign funds. In 2019, for example, the Qatar Investment Authority (QIA) paid \$550 million to acquire a significant stake in privately held Oryx Midstream Services, a midstream crude operator based in the Permian Basin.

CFIUS ultimately approved the purchase but is said to have subjected it to mitigations, which remain classified. That same year, QIA committed to investing \$45 billion in the U.S. economy, according to the State Department.

Because Germany is a close NATO ally, the committee will be less concerned about two VW board seats reserved for Lower Saxony. U.S. security experts do worry that Germany suffers from loose investment controls and dependence on Russian gas. But CFIUS will walk a fine line here, knowing that any questions it raises about German board members could be seen as unwarranted meddling in the country's “codetermination” laws, which give labor leaders half the seats on supervisory boards.

**State Department review.** The Navistar buyout will also need approval from the Directorate of Defense Trade Controls (DDTC), a powerful but often overlooked agency within the U.S. State Department. Companies that manufacture, export or broker defense products and services must register with the DDTC.

The agency mainly reviews risks related to ITAR-controlled products and services, notably the risk of a foreign investor gaining access to defense and dual-use technology.

“Any time there is foreign investment in a company that is registered with DDTC, they will run their own national security investigation,” said Swift.

Foreign buyers seeking control over a U.S. defense contractor must notify the DDTC 60 days before the deal closes, even if the target doesn't export its products. The DDTC typically takes up to 60

days to review whether certain licenses held by a domestic business can be transferred to a foreign buyer.

DDTC and CFIUS run parallel investigations but share information. In fact, when a buyer submits an application to the DDTC, the State Department agency asks whether a voluntary application will be submitted to CFIUS.