

Uber, Tesla, and Slack show how Saudi cash is flowing into Silicon Valley. Here are 5 questions every US tech startup founder needs to ask before taking money from a foreign investor.

Becky Peterson May 18, 2019, 8:45 AM



Doreen Edelman, head of Lowenstein Sandler's Global Trade & Policy Group. Lowenstein Sandler

- From Japan's SoftBank to the Australian sovereign wealth fund, foreign money is pouring into Silicon Valley startups.
- While it may be tempting for founders to take large checks from generous investors, attorney Doreen Edelman said that US companies need to consider the risks they take when accepting foreign investments.
- Companies in industries like artificial intelligence, the Internet of Things, and robotics may see their foreign investments rejected by the US government on the grounds of national security.

- **While it's possible to get some investments through, Edelman said, the more access and control an investor has, the more time, paperwork and money it will take to get approved.**
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Uber took a \$3.5 billion investment from the Saudi Public Investment Fund in 2016, and gave a board seat to its managing director.

Databricks took \$33.24 million in 2015 in a round with participation from Future Fund, the Australian sovereign wealth fund.

And Zumper took \$45.65 million in a 2018 round led by Axel Springer, the German publishing giant (which also happens to own Business Insider).

Yes, the early days of Silicon Valley were so geographically constricted that many of the most high-profile investments were made by people who worked near each other on the legendary Sand Hill Road. But today, the startup investment ecosystem is global, with large checks being written by foreign allies and adversaries alike.

While investors are eager to open their wallets, taking a foreign investment isn't as simple as cashing a check, said Doreen Edelman, head of Lowenstein Sandler's Global Trade & Policy Group.

As US startup founders consider to whom they want to sell equity, they must also consider a host of legal issues that could come up with foreign investors, she said.

Depending on the circumstances, investments from foreign investors could create delays, extra paperwork, and result in costly fees. In the most extreme cases, the investment may be blocked entirely. Even if the investment has been completed, though, the US government may force a divestiture afterwards.

Sanctions and tariffs can also create problems for companies down the road.

Before any of that happens, these are the five questions Edelman says every tech founder needs to ask themselves when considering a foreign investment.

What's the industry?



Robotics company Boston Dynamics was acquired by SoftBank, a Japanese company.
Boston Dynamics

If you're a tech company working on artificial intelligence, robotics, the Internet of Things, or personal data, your foreign investment could be blocked on grounds of national security, Edelman said.

There are 27 different industries under the Department of the Treasury's [Foreign Investment Risk Review Modernization Act of 2018](#), known as the FIRRMA pilot program, which are required to file with CFIUS ahead of a foreign investment.

Companies outside of those industries can voluntarily file with CFIUS as well just to make sure everything is in good standing.

In theory, regulations against foreign investments are designed to prevent foreign governments from getting access to technology or intellectual property that could harm US national security. You probably don't want a foreign government to have access to the software used by the National Security Agency, for example.

But the definition of "national security" is up to a continuous, fluctuating interpretation.

Traditionally such laws only impacted technologies in the defense sector. But today the US government takes a broader scope, Edelman said.

"It could be anything, if you look at it through the lens of, what could an anti-US government or group do with it?" she said.

Could that change in the future?



IBM CEO Ginni Rometty may have a strong grip on government contracts, but founders who might want to compete with IBM should think through foreign investments. [IBM](#)

Whether or not a technology is used by the defense sector today, Edelman said, it's important that founders consider whether they could eventually grow into the niche.

"Could you be in the defense sector? Be aware of what that will mean going forward," she said. "To some companies, it just means we have to plan ahead, just like any other government filings. We may have to make additional filings. And that just takes time and money."

Under certain circumstance, she said, the government could force the foreign investor to divest from the startup, or the company may be forced to avoid certain natural growth opportunities involving their product development, so as to not rock the boat.

"If Chinese money is going to invest in a potential defense product, even a commercial product that may work in the defense sector in the future, you need to be prepared that it's going to affect what you can do down the road," Edelman said, adding that the same concern applies to investors from other countries.

"You're going to be limited because the US government is not going to allow you to have that technology or those patents or that software that can be contracted away to the Chinese, or just for the Chinese to have access to that technology," she said.

Who is the investor?



Sorry, Prime Minister Justin Trudeau, even Canadian investors could face scrutiny from the US government. MARTIN OUELLET-DIOTTE/AFP/Getty Images

While CFIUS has more-or-less put a pause on all acquisitions and investments between the US and China, founders need to pay attention to foreign investors whether they are based in a country that is a friend or a foe to the US.

"It can be Canada. It can be Israel. It can be Germany," said Edelman.

Ultimately, whether or not an investment is an issue will come down to the specifics of the investment, Edelman added.

If Mubadala, a state-owned investment firm in the United Arab Emirates, was a limited partner in a funding round without any control over the company, it would most likely not cause a stir.

"If it's truly an LP just investing for money," she said, "it can invest in whatever it wants."

That said, founders will want to be mindful of the shifting geopolitical landscape since the Trump Administration mixes politics and trade differently than in the past, she said.

"This president is using the tools in his tool box differently," Edelman said.

A Japanese company that does business with North Korea or Iran will be viewed differently than a Japanese company that doesn't, for example.

"It's very possible that the political situation would allow this administration to use these trade tools to either punish or enforce the political positions that the president is taking. That's why 'national security' is flexible in how the government defines these terms," said Edelman.

Will they have access to the "secret sauce?"



Steve Mnuchin, secretary of the U.S. Treasury, may have more concerns about a foreign investment if that investor has access to the technology as part of the deal.
Yuri Gripas/Reuters

Another question founders should ask before taking a foreign investment is how much information they would be required to share with the investor.

Foreign access to "any control technology or the secret sauce or the IP or personal data" could all create issues for the company, Edelman said.

Early stage investors are often deeply involved in the business process, and access intellectual property and customer data as part of day-to-day business. The US government sometimes requires permits to share technology between countries.

Companies in industries highlighted by FIRMA are required to file with CFIUS if investors will have access to their technology.

Founders must also consider whether there are any export controls on their product.

While a tech company may not necessarily export products via ships at sea, some cloud based software is still controlled for export and may face restrictions on who can use it or buy it abroad.

"A tech company that doesn't export but is going to take foreign investment needs to understand if any of its product is controlled for export," Edelman said.

Will they have a board seat?



Rajeev Misra, the head of SoftBank's Vision Fund, makes a lot of investments in the US but the investment fund still faces pushback from the government. [Reuters / Mike Blake](#)

Giving up a board seat to a foreign investor further complicates the process.

Japan's SoftBank has made tons of investments in US tech startups, but even it failed to get approval for two seats on Uber's board.

"If you want to give them the board seat, you need to know that would require you to go through the CIFIUS process," Edelman said regarding companies under the FIRRMA pilot program guidelines.

Even companies which are not mandated to file may be inclined to file because of the board seat, she said.

Disclosure: Axel Springer is Business Insider's parent company.