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FEDERAL GOVERNMENT NIXES ACQUISITION OF 3COM BY CHINESE FIRM

The sale of 3Com Corp. to a group that includes a Chinese corporation with ties to the Chinese military has been put on indefinite hold, after the group this week withdrew its application for approval of the acquisition by CFIUS (the Committee on Foreign Investment in the United States). CFIUS, a federal government agency that reviews acquisitions of U.S. assets by foreign companies, apparently had raised a variety of national security objections to the acquisition.

The roadblock to acquisition was a victory for WLF, which in January had written to CFIUS, urging it not to approve the deal as currently structured. WLF argued that the proposed deal needed to be overhauled to ensure that sensitive military-related technology did not fall into enemy hands. WLF's letter said that the 3Com Corp. acquisition, as currently structured, "raises grave national security concerns."

3Com Corp. is a computer networking company based in Massachusetts. One of its divisions, TippingPoint, engages in highly sensitive national security work. In particular, TippingPoint provides the U.S. Department of Defense with intrusion prevention technology, designed to prevent intrusions into telecommunications systems maintained by DoD. Such intrusions raise vital national security concerns. Nor are such intrusions merely hypothetical; DoD believes that the Chinese military conducted a massive cyber-attack on its systems in June 2007, an attack that temporarily shut down DoD systems. The technology supplied by 3Com plays a vital role in efforts to prevent such attacks in the future.

In October 2007, 3Com agreed to be acquired by a group headed by Bain Capital Partners. Huawei Technologies, a major Chinese telecommunications company, was to have an initial stake of 16.5% of the acquiring entity, with the right to increase that share to 21.5%. Huawei's only apparent motive for joining the acquisition group was to gain access to 3Com's technology. "We concur with U.S. Rep. Thaddeus McCotter's assessment that CFIUS's refusal to approve the deal is a victory for America's cyber security and national security," said WLF Chief Counsel Richard Samp in response to this week's development.

WLF's letter to CFIUS last month stated that the acquisition deal, as currently structured, raised too great a risk that 3Com's intrusion prevention technology would fall into the hands of the Chinese military, a group whose hostile intentions toward the United States have already been demonstrated by its 2007 cyber attack. WLF urged CFIUS not to approve the acquisition unless Bain agrees to divest 3Com's TippingPoint division.

WLF's letter said that there is good reason to fear that Huawei would use its position as a minority owner to funnel sensitive 3Com technology to the Chinese army. WLF noted that the head of Huawei, Ren Zhengfei, is a former officer in the Chinese army. WLF said that there is considerable uncertainty surrounding Huawei's corporate status. Ren Zhengfei reportedly owns 1% of outstanding Huawei shares, and just who owns the remaining shares is far from clear. WLF charged that while Zhengfei contends that Huawei is 100% employee-owned, there is at least some basis for concern that the Chinese government and/or the People's Liberation Army either own or have significant control over Huawei. WLF noted that the Rand Corporation reports that Huawei has "deep ties" with the Chinese military. WLF also charged Huawei has had a history of sharing its technology with enemies of the United States. WLF noted that the CIA has reported that in 2000, Huawei -- in violation of a United Nations embargo -- sold fiber optics equipment to Iraq for the purpose of upgrading Iraq's military technology. Huawei also maintained business dealings with the Taliban regime in Afghanistan and the Chinese military.

The WLF letter urged CFIUS to block the 3Com acquisition in the absence of an agreement to divest TippingPoint. CFIUS in early January 2008 commenced a 45-day investigation of the proposed acquisition. Bain last week withdrew its request for CFIUS approval, apparently after receiving signals that CFIUS would not approve the deal as currently structured because of national security concerns. Bain has said that it may seek to negotiate a restructured acquisition agreement but indicated that the purchase price may be considerably reduced if it is forced to divest TippingPoint and other 3Com businesses that possess technology important to U.S. national security.

WLF is a public interest law and policy center with supporters in all 50 states. WLF strongly supports efforts to promote and protect U.S. national security. It also supports efforts to reduce barriers to the free flow of capital across international borders, and seeks to promote a proper balance between those sometimes conflicting goals.

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For further information, contact WLF Chief Counsel Richard Samp, (202) 588-0302. A copy of WLF's letter to CFIUS is available on its web site, www.wlf.org.