

July 27, 2007

Predictable Rules Once Again Govern Foreign Investment into the United States: President Bush Signs CFIUS Reform into Law

Yesterday, President Bush signed the Foreign Investment and National Security Act of 2007 (“the Act”) into law. The Act amends and modernizes Section 721 of the Defense Production Act of 1950, also known as the Exon-Florio provision. Exon-Florio established the procedures for reviewing proposed foreign investments into the United States by an interagency body known as the Committee of Foreign Investment in the United States (“CFIUS”). Exon-Florio permits the President to prevent or undo acquisitions, mergers, or takeovers of U.S. companies or assets by foreign-owned or foreign-controlled entities when, in the view of the President, such transactions threaten the national security of the United States.

As discussed below, the Act reforms the CFIUS review process by expanding the scope of coverage, incorporating an “evergreen” provision, tightening formal review procedures, particularly for foreign government owned or controlled entities, and increasing congressional reporting requirements. The Act becomes effective in ninety (90) days.

Background

The CFIUS process is voluntary. Parties to a transaction that may potentially affect national security may voluntarily file a notification to CFIUS. This notification begins a ninety (90) day process during which the U.S. government has an opportunity to review the proposed transaction and address any potential national security concerns. Companies submit to this process to ensure that, once vetted, any approved transaction cannot later be prohibited or altered, unless a material misstatement or omission is discovered. Parties that do not submit to CFIUS review do not receive this “safe harbor” protection.

The CFIUS review process became an international news flash when CFIUS approved the sale of a company that operated six major U.S. ports to Dubai Ports World International. In the wake of the ensuing uproar, legislation was proposed in the Senate that would have lengthened and intensified CFIUS review, but the measure was scuttled due to strong opposition from the business community. Nevertheless, some tightening of CFIUS procedures has been a foregone conclusion since the Dubai Ports World imbroglio. The passage of the Act ends eighteen months of uncertainty.

The Foreign Investment and National Security Act of 2007

The Act makes certain significant changes to the CFIUS review process, such as:

- Heightening the scrutiny of any transaction where a foreign government or an entity controlled by a foreign government is a party, or whenever a transaction would result in the foreign control of “critical infrastructure.”

- Defining “critical infrastructure” broadly to include “systems or assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems or assets would have a debilitating impact on national security.” This definition expands the types of transactions subject to CFIUS review to include energy generation and transportation.
- Including an “evergreen” provision. Under the new law, if the investigation of a transaction results in a mitigation agreement, and at some later date, a party to the mitigation agreement intentionally commits a material breach of the agreement, either CFIUS or the President may re-open the review if “there are no other remedies or enforcement tools available to address such breach.” A re-opened review can result in additional mitigation agreements or even the unwinding of the transaction. Previously, CFIUS could re-open a review only when it discovered a material omission or misstatement by one or more of the parties to the transaction made during the initial review period.
- Designating a lead agency, depending on subject matter expertise, to review each transaction. The lead agency is granted the authority to negotiate, monitor, modify, and enforce mitigation agreements.
- Requiring a full forty-five (45) day review for transactions by companies owned or controlled by foreign governments unless the Treasury secretary or deputy and the head of the lead agency determine that the transaction will not impair national security.
- Increasing the role of congressional oversight by requiring CFIUS to provide an annual report to Congress as well as a certified notice to Congress specifying its determinations, decision-making rationales, and actions taken.
- Appointing the Director of National Intelligence as an *ex officio* member of CFIUS. The Director must perform a national security threat analysis for all proposed transactions.

The Expected Impact of the Act on U.S. and Foreign Business

Foreign businesses seeking to acquire U.S. assets, and U.S. companies courting foreign investment, will find that the Act makes significant changes to the CFIUS process, most notably by the expanded scope of reviewable transactions. The Act greatly increases the number of transactions that will be subject to review, from toll roads to energy generation to ports. The new law also adds a new risk factor with the new “evergreen” provision. Under the old regulation, only a material omission or misstatement could result in a re-opened review; now, an intentional breach of a mitigation agreement can trigger a review. How these changes will play out is uncertain. What is not uncertain is that whatever the outcome of a CFIUS review, it is not reviewable by the courts – both the old regulations and the new law expressly state that CFIUS review and the President’s determinations are not judicially reviewable.

In view of the expanded provisions for congressional review and oversight, there likely will be fewer surprises and hence a reduced likelihood of the type of political outcry that followed the attempted Dubai Ports World acquisition. Most important, with the threat of inappropriate congressional meddling laid to rest by the passage of the Act and with the rules once again being fixed, a stable climate for foreign investment into the United States has been restored.

The Financial Services Forum, the Business Roundtable, the Organization for International Investment and the U.S. Chamber of Commerce issued a joint statement endorsing the Act on July 11, stating “We applaud the... passage of the Foreign Investment and National Security Act of 2007. This action... will protect our national security while keeping America open for business and restore predictability and certainty to the CFIUS process.”

* * * * *

Haynes and Boone’s International Compliance and Trade Practice Group represents leading U.S., foreign and global industrial, energy (oilfield services and exploration), technology, aerospace and defense industry corporations in Exon-Florio reviews, U.S. export control, sanctions, anti-boycott and Foreign Corrupt Practices Act compliance investigations, transactional planning, governmental licensing, civil and criminal enforcement proceedings and import relief actions. The Practice Group includes former in-house counsel, U.S. prosecutors, Justice Department lawyers, and International Trade Commission officials with decades of experience advising global companies on compliance with U.S. and foreign trade and investment laws, and protecting them in civil and criminal investigations if they do not.

Haynes and Boone, LLP, is an international corporate law firm, with offices in Texas, Washington, D.C., Mexico City, Moscow and New York, providing a full spectrum of legal services. With more than 450 attorneys, Haynes and Boone is ranked among the largest law firms in the nation by National Law Journal. The firm has been recognized by Vault.com as one of the “20 Best Law Firms to Work For,” by Corporate Board Member Magazine as one of the “Best Corporate Law Firms in America,” and has received the Minority Corporate Counsel Association’s Thomas L. Sager Award for commitment to diversity.

For additional information, please contact:

Kenneth B. Reisenfeld
202-654-4511 (Washington, DC)
Ken.Reisenfeld@haynesboone.com

Edward M. Lebow
202-654-4514 (Washington, DC)
Ed.Lebow@haynesboone.com