

WebMemo



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New CFIUS Regulations Support U.S. National and Economic Security Concerns

Daniella Markheim

On November 14, the U.S. Treasury Department released the Final Regulations implementing the Foreign Investment and National Security Act of 2007 (FINSAs) which expands the authority, scope, and size of the Committee on Foreign Investments in the United States (CFIUS) and requires increased congressional oversight of CFIUS decisions.

The regulations cater to the spirit of the Bush Administration's policy to support international investment that promotes economic growth, productivity, competitiveness, and job creation while stressing that such investment must be consistent with the protection of the national security. While regulations will likely have a net positive impact on the U.S. investment regime, only time and practice will reveal the actual effectiveness of the new regulations in carrying out FINSAs legislation while preserving the open investment climate upon which the U.S. economy relies. Whether CFIUS gets that time will depend on President-elect Barack Obama's foreign investment policy.

Implementing FINSAs Reforms. The United States generally welcomes foreign investors and provides them nondiscriminatory access to investment opportunities. While the bulk of foreign investment in America generates no threat to national security, the Exon-Florio provision was implemented in 1988 to ensure that foreign direct investment remains benign.¹ The provision was designed "to suspend or prohibit any foreign acquisition, merger or takeover of a U.S. corporation that is determined to threaten the national security of the United States." Per Executive Order 11858, Exon-Florio is carried out by

CFIUS, an inter-agency committee chaired by the U.S. Treasury and composed of representatives from the 12 federal agencies and departments that monitor foreign investment. In order to reduce the economic cost of delaying investment, CFIUS conducts its reviews in as timely a manner as possible.

The practice of foreign investors voluntarily notifying CFIUS of acquisitions that may need review will continue. The incentive for firms to notify the CFIUS process voluntarily is strong; firms that should notify CFIUS of an acquisition but do not remain subject indefinitely to divestment or other negative actions by the President. Under the new rules, CFIUS may also initiate reviews and investigations and may enter into preliminary consultations with foreign investors to identify any problems before an official review is started. Because the amount of information required to initiate a filing has been expanded, CFIUS will need to guard against data requirements forming an unnecessary barrier to foreign investment.

Under FINSAs and the new implementing regulations, CFIUS will continue the 30-day reviews of planned foreign acquisitions, followed by additional 45-day evaluations for exceptional cases. At the end of an extended review, a report is provided

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to the President, who then has up to 15 days to announce whether the investment is approved. Importantly, FINSA increases the extent of CFIUS reporting to Congress in a way that should ensure that vital national interests are looked after without politicizing the foreign investment vetting process.

Flexible Regulations. With FINSA reform, the secretary of energy joins the attorney general and the secretaries of commerce, defense, homeland security, and state as CFIUS agencies. Additionally, the director of national intelligence is mandated to provide CFIUS independent analysis of the potential national security implications of transactions, and the secretary of labor will advise CFIUS on U.S. labor laws. The President may add additional members as needed. The Treasury will continue to chair CFIUS and will assign appropriate agencies to lead responsibility for investigations.

FINSA expands the range of investment transactions falling under CFIUS review and mandates additional CFIUS scrutiny of transactions where a foreign government—or an entity controlled by a foreign government—seeks to acquire and control a U.S. asset. Additionally, FINSA increases the scope of CFIUS review to consider transactions involving critical U.S. infrastructure essential to national security. Mandatory investigations may be avoided if senior officials in Treasury and lead agencies grant an exception or if investors conclude mitigation agreements to address national security concerns associated with foreign control of a U.S. asset.

CFIUS needs this flexibility to differentiate the level of investigation required for each case. A foreign government-owned company headquartered in an ally country that competes fairly should not automatically face a more stringent investment approval process.

Importantly, implementing regulations narrows the scope of transactions covered by CFIUS/FINSA legislation, clearly defines foreign “control” of an asset, and indicates what may constitute “critical infrastructure” on a case-by-case basis. Covered transactions are those mergers, acquisitions, or takeovers that could result in foreign control of a U.S. asset. “Control” represents the ability to exercise “power, direct or indirect, whether or not exer-

cised...to determine, direct, or decide important matters concerning an entity.” With this approach, generally, only non-passive investors in covered transactions will be considered by CFIUS—regardless of the size of their ownership stake.

FINSA codifies CFIUS’s authority to re-open approved transactions and impose civil penalties on any party that has submitted false or misleading material information or intentionally and materially breaches a national security agreement aimed at mitigating the risk of the transaction. CFIUS is also mandated to conduct post-approval monitoring of mitigation agreements to ensure the foreign agent’s compliance.

Better Security for Investors and Investments. FINSA expanded the scope of CFIUS and strengthened the committee’s mandate to evaluate and monitor the national security implications of foreign control of U.S. businesses. However, newly released implementing regulations preserve important flexibilities in defining what transactions are covered by CFIUS, when potential foreign ownership of a domestic asset may represent a threat, and what may be classified as “critical infrastructure.” Rather than automatic reviews of specific categories of transactions, CFIUS can review proposed investments based on the individual characteristics of the transaction. While these regulations may result in CFIUS reviewing more transactions than necessary, they reduce the chance that a harmful investment will slip through without proper consideration.

In general, the new rules over FINSA implementation increase the transparency of the CFIUS process and should reduce the level of uncertainty that foreign investors face. Similarly, requirements for additional communication between CFIUS and Congress over CFIUS investigations should help to reduce Congress’ uncertainty over the safety of foreign acquisitions. The new implementing regulations may need to be fine-tuned over time, but they are likely to result in a sound balance between America’s national and economic security concerns.

—Daniella Markheim is Jay Van Andel Senior Trade Policy Analyst in the Center for International Trade and Economics at The Heritage Foundation.

1. Exon-Florio Amendment, 50 U.S.C. app. § 2170 (1988).