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CFIUS Issues Proposed Regulations

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On April 21, 2008, the Committee on Foreign Investment in the United States (“CFIUS”) issued proposed regulations governing national security reviews of foreign investments in U.S. businesses. These new regulations were issued to implement amendments adopted by the Foreign Investment and National Security Act of 2007 (“FINSAs”) to the Exon-Florio Amendment to the Defense Production Act of 1950. FINSAs became effective on October 24, 2007, and the proposed regulations address changes to the law legislated by FINSAs and codify certain existing CFIUS administrative practices.

FINSAs permits the President of the United States to block acquisitions, mergers, or takeovers of U.S. companies or assets by foreign-owned or foreign-controlled entities when, in the President’s view, such transactions threaten the national security of the United States. Parties to a transaction subject to FINSAs (referred to in the proposed regulations as a “covered transaction”) may voluntarily file a notification with CFIUS to give the U.S. Government an opportunity to review the transaction and address any potential national security concerns. CFIUS is an interagency committee chaired by the Secretary of the Treasury and composed of various representatives of the executive branch of the U.S. Government, including the Attorney General and the Secretaries of Homeland Security, Commerce, Defense, State, and Energy. The Director of National Intelligence and the Secretary of Labor serve as *ex officio* members of CFIUS.

FINSAs provides for a 30-day CFIUS review of a covered transaction to determine the effect of the transaction on national security, and to address any threat posed by such transaction. CFIUS designates a “lead agency” to conduct the review (however, each CFIUS member is involved). The CFIUS review can be extended into an additional 45-day investigation in cases where the transaction:

- threatens to impair national security and that threat has not been mitigated prior to the conclusion of the initial 30-day CFIUS review;
- involves a foreign government-controlled acquiring entity; or
- could result in foreign control over critical infrastructure.

In addition, an extended investigation can be undertaken at the recommendation of the lead agency and with the concurrence of the other CFIUS members.

To address congressional concern over appropriate accountability for CFIUS decisions, FINSAs requires that a high-level official of the Department of the Treasury and the lead agency certify to Congress that there are no unresolved national security issues. For example, for transactions involving foreign government ownership or critical infrastructure, the Deputy Secretaries of the Treasury and the lead agency must certify that the transaction does not threaten national security in order for the transaction to be cleared within the initial 30-day review. If a 45-day investigation is initiated and any national security concerns remain unresolved at the end of such investigation, the transaction must be referred to the President, who then must make a determination within 15 days on whether to approve or block the transaction.

The proposed regulations (which will be set forth at 31 C.F.R. Part 800 and replace the existing regulations) deal primarily with the administrative aspects of CFIUS reviews and investigations. For example:

- the proposed regulations make explicit the current practice of encouraging parties to a covered transaction to consult with CFIUS prior to making a formal submission;
- the specific information required in a CFIUS notice has been expanded to include information CFIUS now routinely requests in any event, such as personal identifier information for the directors and senior managers of the foreign acquiring entity and an organizational chart showing the relationship between the foreign acquiring entity and its parent and affiliated entities;
- the notice must include a discussion of “critical infrastructure” involved in the transaction, which is defined to cover any asset or system that if destroyed or incapacitated would have a “debilitating effect on national security” and a discussion of “critical technology” that includes items subject to U.S. export control restrictions; and
- the notifying parties must submit appropriate certificates as to the accuracy and completeness of the information provided in the notice and, prior to the conclusion of the review or investigation, a bring down certificate with respect to any additional information provided to CFIUS.

Although submitting false information to a governmental authority has always been subject to penalties, the proposed regulations provide for civil penalties of up to \$250,000 for (a) submission of a material misstatement or omission in a notice to CFIUS or making a false certification and (b) each violation of a material agreement entered into with CFIUS or specific conditions imposed on the parties. In addition, the proposed regulations make it clear that mitigation agreements can provide for liquidated damages.

The proposed regulations retain many of the key provisions of the current regulations, while clarifying certain concepts, and include numerous examples to further clarify the scope and applicability of key concepts. For example, “control” continues to be defined as the power (either affirmatively or negatively) to influence important matters affecting a business and not in terms of specific percentages of shares or board seats held. Rather, CFIUS would examine all relevant factors that might give the acquiring party influence over important business matters. Thus, an acquisition of 10% or less of the voting interests of an entity made “solely for the purpose of investment” (as defined in the proposed regulations) would not involve an acquisition of control and would not be subject to FINSAs. However, CFIUS may view an acquisition of a 9% voting interest coupled with a board seat as conferring control. Significantly, the definition of “control” now includes a list of minority shareholder protective rights (such as the power to prevent the sale of the assets of an entity, prohibitions on changes to the organizational documents of an entity, and anti-dilution protection) that shall not be deemed to confer control.

The proposed regulations are subject to a 45-day comment period, and CFIUS has scheduled a public meeting on May 2 to discuss issues associated with the proposed regulations. While the final form of the regulations may contain further clarifications and revisions, we do not expect the final regulations to be materially different from those proposed, and CFIUS is likely to conduct its reviews and investigations in the meantime in accordance with the provisions of the proposed regulations.