

ALERT



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Treasury Department Issues Proposed Regulations Implementing Foreign Investment and National Security Act of 2007

On July 26, 2007, President Bush signed into law the Foreign Investment and National Security Act of 2007, Pub. L. 110-49, 121 Stat. 246 (“FINSA”), which amended Section 721 of the Defense Production Act of 1950, 50 U.S.C. App. § 2170 *et seq.* (the so-called “Exon-Florio Amendment”). The Exon-Florio Amendment authorized the President to review mergers, acquisitions, and takeovers by any foreign person that could result in foreign control of a U.S. business to determine the effects of such transactions on the national security of the United States. Generally, FINSA codified certain aspects of the structure, role, process, and responsibilities of the Committee on Foreign Investment in the United States (“CFIUS”), the interagency committee that conducts national security reviews under the Exon-Florio Amendment. FINSA took effect on October 24, 2007.

On April 23, 2008, the Treasury Department published proposed regulations implementing FINSA. *See* 73 Fed. Reg. 21,861 (Apr. 23, 2008). The following summarizes the key aspects of FINSA and the proposed regulations, including describing each possible stage of the reformed CFIUS process.

I. CFIUS Membership

FINSA formally established CFIUS, which previously had been created by Executive Order No. 11858 (May 7, 1975). Through FINSA, Congress appointed seven cabinet secretaries, or their designees, to CFIUS: Treasury (Chairperson); Homeland Security; Commerce; Defense; State; Justice; and Energy. In addition, Congress designated the Secretary of Labor and the Director of National Intelligence (“DNI”) as non-voting, *ex officio* members and authorized the President to include the heads of any other executive department, agency or office, as the President deems appropriate. Under FINSA, the DNI is to provide independent analyses of any national security threats posed by foreign investment transactions and is to have no other policy role. Under the proposed regulations, the Secretary of Labor is required to identify for CFIUS any risk mitigation provisions proposed to or by CFIUS that would violate United States labor laws.

Pursuant to executive Order No. 13456 (Jan. 23, 2008), the President also included the United States Trade Representative and the Director of the Office of Science and Technology Policy as members of CFIUS. In addition, the President granted observer status to the Director of the Office of Management and Budget, the Chairman of the Council on Economic Advisers, the

Assistant to the President for National Security Affairs, the Assistant to the President for Economic Policy, and the Assistant to the President for Homeland Security and Counterterrorism.

II. CFIUS Review and Investigation Process and Procedures

A. Mechanisms for Initiating CFIUS Review

A CFIUS review of the possible national security implications of a foreign investment in the United States may be initiated unilaterally by CFIUS, but more commonly is initiated upon acceptance by CFIUS of a joint voluntary notice submitted by the parties to a “covered transaction.” The proposed regulations explicitly encourage such parties to contact CFIUS before formally filing and recommend that the parties file a substantially complete draft notice. Indeed, prudence often dictates that the parties to a proposed transaction consult with CFIUS, as well as key Members of Congress and officials of the CFIUS member agencies relevant to a proposed transaction, even in advance of a pre-filing.

B. Contents of Joint Voluntary Notice

Joint voluntary notices submitted to CFIUS for review historically have been required to include detailed information relating to the proposed transaction, as well as the parties to such transaction. The proposed regulations, however, greatly expand the scope of the information required to be included in a joint voluntary notice. The proposed new information requirements, which, in some instances, CFIUS already has been asking of notifying parties, include:

- the transaction value;
- the names of any and all financial institutions involved in the transaction (*e.g.*, advisers, underwriters, etc.) or sources of financing;
- with respect to the U.S. business being acquired, market share information for primary product or service lines, including an explanation of how that estimate was derived, and a list of direct competitors for those primary product or service lines;
- with respect to the U.S. business being acquired, information pertaining to contracts with any agency of the United States Government¹;
- with respect to the U.S. business being acquired, information pertaining to the production and trade of “critical technologies,” including those subject to United States export controls;

- biographical information for members of the board of directors, senior management, and each ultimate beneficial owner of five percent or more of the outstanding securities of the foreign acquirer and its intermediate and ultimate parents;
- certain “personal identifier information” to be set forth in a separate document for the members of the board of directors and senior executives of the foreign acquirer and its ultimate parent, and any other entities in the same chain of ownership that could exercise control over the U.S. business being acquired;
- certain “business identifier information” for parents of the foreign acquirer, including the ultimate parent, and any other entities in the same chain of ownership that could exercise control over the U.S. business being acquired;
- an organizational chart illustrating all of the entities or individuals above the foreign person that is a party to the transaction up to the person or persons having ultimate control of that person, including the percentage shares held by each; and
- information as to whether any party to the currently proposed transaction was ever a party to a transaction previously notified to CFIUS or is, or was ever, a party to a mitigation agreement entered into or a condition imposed under the Exon-Florio Amendment.

Under FINSA, each party also is required to certify the accuracy and completeness of the joint voluntary notice and any follow-up information provided by CFIUS.² CFIUS expects that the need to request follow-up information will be reduced in light of the additional requirements for filing a joint voluntary notice. When information is requested by CFIUS during the course of a review, however, the proposed regulations require that the party to whom the request is directed submit the requested information within two business days or else request an extension of time in writing.

C. Conduct and Possible Outcomes of CFIUS Review/Investigation

As noted above, CFIUS typically commences its review of a “covered transaction” upon acceptance of a joint voluntary notice.³ Such reviews are required to be completed no later than the 30th day after the date of commencement after which, as detailed below, CFIUS may initiate an additional 45-day investigation. During the course of its review, CFIUS will evaluate the national security impact of the proposed transaction. Under FINSA, CFIUS specifically will examine the potential national security-related effects on United States “critical infrastructure,” including major energy assets,⁴ and U.S. “critical technologies.” In addition, in cases involving

acquisitions by foreign government-controlled entities, CFIUS will consider whether the acquiring entity's national government adheres to arms control, non-proliferation, and disarmament regimes, its cooperation with the United States with respect to counter-terrorism efforts, and the potential for transshipment or diversion of technologies with military applications, including an analysis of the subject country's export control laws and regulations.

Where a "covered transaction" presents national security concerns, FINSA provides statutory authority for CFIUS, or a lead agency acting on behalf of CFIUS, to enter into mitigation agreements with the parties to the transaction or impose conditions on the transaction to address such concerns.⁵ If there are no unresolved national security concerns, including as a result of a mitigation agreement or the imposition of conditions, the transaction will be "cleared" by CFIUS at the conclusion of the 30-day review period.

However, if CFIUS or a member agency determines that the transaction threatens to impair U.S. national security and such threat has not been mitigated prior to or during the 30-day review, CFIUS must initiate an additional 45-day investigation. In addition, unless the Treasury Secretary and the head of any lead agency certify that the transaction will not impair the national security of the United States, FINSA and the proposed regulations direct that CFIUS undertake a full 45-day investigation to determine the effects on national security of any "covered transaction" that (i) is a "foreign government-controlled transaction"; or (ii) would result in the control by a foreign person of "critical infrastructure" of or within the United States, if CFIUS determines that the transaction could impair the national security and such impairment has not been mitigated.

If CFIUS initiates a 45-day investigation and determines that there are no unresolved national security concerns, the transaction will be "cleared" by CFIUS at the conclusion of the 45-day investigation period.⁶ However, under the following circumstances, the ultimate decision regarding the national security implications of the proposed transaction, will reside with the President, who is required to act within 15 days: (i) CFIUS recommends that the President suspend or prohibit the transaction; (ii) the CFIUS member agencies are unable to reach a decision on whether to recommend that the President suspend or prohibit a transaction; or (iii) CFIUS requests that the President make a determination with regard to the transaction. Thus, under FINSA, the President retains the sole authority to block a transaction.⁷

¹ The current regulations require only the identification of contracts with agencies of the United States Government that have national defense responsibilities.

² The proposed regulations provide for civil penalties not to exceed \$250,000 per violation for the intentional or grossly negligent submission of a material misstatement or omission in a notice or for making a false certification. In addition, if a party to a transaction submits false or misleading material information or omits material information, under the proposed regulations CFIUS may reopen an already-concluded review and revise any recommendations made to the President.

³ Joint voluntary notices may be withdrawn at any time prior to any action being taken by CFIUS. However, the proposed regulations direct that CFIUS establish (i) interim protections to address specific national security concerns with the transaction identified during the review or investigation of the transaction; and (ii) a process for tracking actions that may be taken by any party to a covered transaction before notice is filed.

⁴ CFIUS also will examine the potential effects of the transaction on the long-term projections of U.S. requirements for sources of energy and other critical resources and material.

⁵ The proposed regulations provide for the inclusion of liquidated or actual damages provisions for breaches of such agreements and provides for civil penalties not to exceed \$250,000 per violation for the intentional or grossly negligent violation of a material agreement or condition entered into with the United States. In addition, if there are no other remedies available to address the breach, FINSA authorizes CFIUS to reopen its review. We note, however, that the proposed regulations do not speak directly to this issue.

⁶ For transactions on which CFIUS has completed a 30-day review or a 45-day investigation, FINSA requires certification to Congress by a high-level Treasury Department official and an official at any lead agency that there are no unresolved national security concerns. In addition, FINSA requires that CFIUS submit an annual report to Congress that includes a listing of transactions reviewed or investigated during the preceding 12-month period, an analysis related to foreign direct investment and critical technologies, and a report on foreign direct investment from certain countries.

⁷ In the absence of a determination by CFIUS that a proposed transaction is not a covered transaction, "clearance" by CFIUS of a proposed transaction after a 30-day review or 45-day investigation, or a decision by the President not to exercise his authority under the Exon-Florio Amendment, all authority available to the President or CFIUS under the Exon-Florio Amendment, including divestment authority, shall remain available at the discretion of the President.

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