

KIRKLAND ALERT

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Dealmakers, Take Note: GAO to Study CFIUS at Congress' Urging

On October 3, 2016, the U.S. Government Accountability Office (“GAO”) announced that it would undertake an assessment of the Committee on Foreign Investment in the United States (“CFIUS”) review process to evaluate “*how the current statutory and administrative authorities of the Committee on Foreign Investment in the United States have kept pace with the growing scope of foreign acquisitions in important economic sectors in the United States.*” The GAO’s statement responds to a [September 15 letter](#) from 16 Members of Congress (the “September 15 Letter”) calling on the GAO to examine the advisability of identified enhancements to CFIUS’ authority and jurisdictional ambit in light of recent high-profile acquisitions by Chinese buyers of U.S. businesses in the telecommunications, media and agriculture sectors. GAO studies often are requested and then relied upon by lawmakers to advance legislative agendas and support bills for passage into law.

Notably, the September 15 Letter was signed by Members representing disparate political views, reflecting growing bipartisan concerns about perceived risks arising from foreign direct investment. Since February 2016, over 130 Members of Congress have signed letters to the Secretary of the Treasury, Chair of CFIUS, urging CFIUS to review potential foreign acquisitions of U.S. businesses in the financial, manufacturing, agriculture and transportation sectors.¹

Dealmakers can glean several takeaways from the developments that prompted the September 15 Letter and the GAO’s announcement.

- ***Transactions involving state-affiliated buyers garner greater regulatory and other scrutiny.*** A prospective buyer’s direct or indirect affiliation with a foreign government may not necessarily raise material CFIUS issues for a deal, but will likely spark CFIUS questions. Currently, transactions notified to CFIUS involving foreign government-controlled acquirers must undergo a 45-day investigation following the initial 30-day review, unless the Department of the Treasury grants a waiver. The September 15 Letter questions whether CFIUS should give “*special consideration*” to acquirers “*that may be under state control from designated countries, especially China and Russia*” and encourages the GAO to consider whether a filing should be mandatory for deals with Chinese state-owned and/or state-controlled acquirers. In a similar vein, Members of Congress have characterized the involvement of a state-affiliated entity in a deal as indicating that the deal warrants thorough scrutiny and, potentially, “mitigation” to reduce foreign control. A key focus of Congress is situations where acquirers are largely directed by foreign governments, though they may be structured as independent entities. As the CFIUS review process is primarily voluntarily initiated by the parties to a

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covered transaction, requiring certain transactions involving state-owned enterprises to be notified to CFIUS would significantly expand CFIUS' workload. U.S. law also may need to change to implement such an approach, as it currently requires that in addition to foreign control, the U.S. target business must implicate national security concerns for CFIUS to exercise jurisdiction.

In the current policy (and political) environment, no industry sector should be assumed to be a safe harbor from CFIUS review.

- ***Perceived risk increasingly attaches to deals in sectors that have not historically been considered risky for national security purposes.*** As discussed in our [Client Alert on the CFIUS annual report](#), the industry range of transactions notified to CFIUS has expanded rapidly in recent years. In addition to expressing more traditional unease regarding foreign takeovers of sensitive U.S. technology companies, the September 15 Letter links Chinese buyers' acquisitions of U.S. entertainment companies with "*serious security questions*" worthy of CFIUS' consideration. For example, the September 15 Letter expresses concern that foreign acquisitions in the telecommunications and media sectors could lead to foreign control of U.S. "*soft power*" institutions. This broad view of national security reflects the intent of the Foreign Investment and National Security Act of 2007 ("FINSA"), which codified the current CFIUS process and made clear that "national security" considerations could be relevant across diverse industries and commercial situations. In the current policy (and political) environment, no industry sector should be assumed to be a safe harbor from CFIUS review.
- ***U.S. companies' ability to compete in the marketplace against companies receiving foreign government support is a core national security policy concern.*** The September 15 Letter recommends that the GAO consider whether CFIUS' assessment of national security risk should include a "*net economic benefit*" test. Specifically, the September 15 Letter expressed concern about situations where foreign state-owned bidders may be benefiting from illegal subsidies to gain access to the U.S. market as part of a country's "*strategic plan*," and where foreign governments in those countries do not reciprocally allow foreign investment in their corresponding industry sectors. To the extent that acquisition of a U.S. company would significantly increase the amount of foreign ownership of multiple businesses operating in the same industry, a deal may be more likely to attract negative attention. This proposal would require parties to a proposed transaction in the United States to carefully consider a bidder's financial profile, as well as the political landscape for foreign investment in the foreign country's corresponding industry sector.

The GAO indicated that it will not commence its assessment for approximately four months, although there is not a firm deadline and it remains to be seen how long the study will take. When released, the study will likely provide key insights as to how the U.S. government views CFIUS' role in managing evolving national security risks and its findings and recommendations in turn could trigger Congressional action.

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The United States, the EU and other countries scrutinize or regulate international business activities to advance priority national security, foreign policy and other objectives. If not addressed effectively, such governmental scrutiny or regulation can adversely impact business strategy and investment decisions, lead to significant individual and corporate civil and criminal penalties, and may even result in imprisonment for responsible persons.

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¹ See, e.g., Letter from Members of U.S. Cong. to Hon. Marisa Lago, Assistant Sec'y, Comm. on Foreign Inv. in the U.S. (Feb. 16, 2016) (regarding the proposed acquisition of the Chicago Stock Exchange); Letter from Walter B. Jones, Member of Cong. to Hon. Jacob J. Lew, Sec'y, U.S. Dep't of Treasury (Feb. 24, 2016) (regarding the potential acquisition of Terex and Chinese foreign direct investment generally); Letter from U.S. Senators to Hon. Jacob J. Lew, Sec'y, U.S. Dep't of Treasury (Mar. 24, 2016) (regarding the proposed acquisition of Syngenta); Letter from U.S. Senators to Hon. Jacob J. Lew, Sec'y, U.S. Dep't of Treasury (Sept. 28, 2016) (regarding the proposed acquisition of Vertex Railcar Corporation).

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