Insight

CFIUS: A Primer

MEGHAN MILLOY, JACQUELINE VARAS | APRIL 13, 2018

Executive Summary

- The Committee on Foreign Investment in the United States, or CFIUS, is an interagency committee created in 1975 that reviews certain mergers, acquisitions, or other foreign investments in the United States to determine whether they may threaten national security.
- While CFIUS has broad authority to review transactions and request modifications that would mitigate national security threats, the ultimate decision to approve or deny a transaction lies with the president.
- Eight of the last 10 transaction denials by CFIUS have involved Chinese companies. These denials correspond with a rise in Chinese investment in the United States and growing concern over transactions between U.S. and Chinese companies.

Introduction

The Committee on Foreign Investment in the United States (CFIUS) is an interagency committee chaired by the Secretary of the Treasury that has the power to review mergers, acquisitions, and other foreign investments in the United States. If it determines that an investment poses a threat to national security, CFIUS can block the transaction. Most recently, CFIUS has been in the spotlight for its actions to bar the takeover of U.S. chip manufacturer Qualcomm by Singapore-based tech giant Broadcom. Simultaneously, some are seeking to reform CFIUS and its processes. As the debate heats up over whether and how to reform CFIUS, it's important to understand what CFIUS is, what it does, and what beneficial reform might look like.

What is CFIUS?

Created in 1975 by Executive Order 11858 from President Gerald Ford, CFIUS was tasked with "support[ing] unequivocally such [international] investment, consistent with the protection of national security." Originally, CFIUS consisted of the United States Trade Representative, the Director of the Office of Science and Technology Policy, and "the heads of any other executive department, agency, or office, as the President or the Secretary of the Treasury determines appropriate, on a case-by-case basis." The Director of the Office of Management and Budget (OMB), the Chairman of the Council of 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 were to observe and participate as appropriate, as well as report to the president on CFIUS's activities.

Today, members of CFIUS include the Secretary of the Treasury, the Attorney General, the Secretary of Homeland Security, the Secretary of Commerce, the Secretary of Defense, the Secretary of State, the Secretary of Energy, the U.S. Trade Representative, and the Director of the Office of Science and Technology Policy. OMB, the Council of Economic Advisers, the National Security Council, the National Economic Council, and the Homeland Security council are invited to send a representative to observe and, as appropriate, participate.

Congress gave CFIUS the authority to bar a transaction in the interest of national security by amending the

Defense Production Act of 1950 with a change to section 721 in 1988, commonly referred to as the Exon-Florio Amendment. This amendment allows CFIUS to investigate investments meeting certain requirements, called covered transactions, and take necessary actions to protect the national security of the United States.

The definition of a covered transaction is "any merger, acquisition, or takeover that is proposed or pending after August 23, 1988, by or with any foreign person which could result in foreign control of any person engaged in interstate commerce in the United States." By having such a broad definition of what transactions may be subject to CFIUS review, the law gives great discretion to the administration in how to exercise its power to block or substantially impede certain foreign transactions in the United States.

What Does CFIUS Do?

Submitting transactions to CFIUS for review is completely voluntary. It nevertheless is often in the interest of U.S. companies to undergo this process in order to avoid a mandatory CFIUS review years later, when any resulting changes would likely be more burdensome. This incentive is especially strong for companies that participate in transactions covered within the CFIUS jurisdiction (i.e. that result in foreign ownership) and that involve nations with higher national security risks. Once a transaction is approved by CFIUS, it will most likely not be scrutinized again.

If investments are determined to be covered transactions, the parties will then complete responses to a set of questions from 31 CFR 800.402. The questions require a great amount of detail, ranging from basic information about the owners and shareholders of the acquiring parent company to questions about the types of products and services it provides.

As the parties prepare their responses to the questions, they jointly submit their pre-filing notification to alert CFIUS of the transaction. CFIUS will then review the parties' drafts and advise as to whether or not the parties should add or amend their responses before submitting their final notice. Once the parties submit their final notice, CFIUS begins its 30-day review of the transaction, in which it may ask for additional information. The process doesn't always take the full 30 days, and when transactions are less complicated, it can be much shorter.

Assuming CFIUS approves the transaction, it will issue a no-action letter effectively giving the green light to the transaction and providing a safe harbor for the parties against future actions that might unwind the transaction. Parties may also choose to withdraw their notice at any point during the review. CFIUS must approve the withdrawal and may add conditions, including requiring updates on the status of the transaction and any intent to refile in the future.

If a transaction is more complicated or has potential implications for national security, the process is less streamlined and with multiple outcome possibilities. The process begins the same way, with both parties to a covered transaction submitting a pre-filing notice and then their final notice to CFIUS. CFIUS then conducts its 30-day review and determines whether or not a formal investigation is required, with the Director for National Intelligence giving CFIUS a full analysis of any effects the transaction may have on national security. If CFIUS determines that an investigation is not required, then the parties receive their no-action letter, as described above.

If CFIUS determines that an investigation is required, the review moves into a 45-day investigation period. During this time, CFIUS meets with all member agencies as well as the parties to the transaction to discuss the transaction itself, its implications on national security, and options for modifying the transaction to mitigate national security concerns. CFIUS will then decide whether to recommend to the president that the transaction

be blocked. At this point, the parties can choose to withdraw their filing with CFIUS's consent and agree to refile at a later date with modifications. Nearly half of the transactions investigated by CFIUS since 1990 have been prematurely terminated by the firms involved to avoid a negative ruling. On the other hand, if the parties agree to take the appropriate steps to mitigate national security concerns, CFIUS may approve the transaction.

If the transactions are not modified or voluntarily terminated, the president has the authority to block them. This has only happened four times before: twice by President Obama and twice by President Trump.

Altogether, the CFIUS process can take anywhere from as little as 30 days to as much as four months.

Issues with the CFIUS Process

CFIUS, and especially the Treasury Department as the group's chairing department, has an incredible amount of leeway with what it can and cannot do with companies, and there is little recourse for companies that have their transactions blocked. Even if CFIUS decides to unwind a transaction fully, its decision is not subject to review by a court. As a result, CFIUS has the ability to act under the cover of national-security concerns with little recourse for affected companies.

At the heart of the concerns with the CFIUS review process is its lack of transparency, both with the parties of covered transactions and with the public and taxpayers who all, to some extent, have an interest in whether or not these transactions go through. One proposal for reform is to update CFIUS's ability to employ current technology in determining national security threats. There are also suggestions to make the review process more open and transparent (insofar as national security issues allow) both during and after the decision-making process, not unlike the Financial Stability Oversight Council's designation process. This added transparency could ensure that the companies and the public know why a particular decision has been made.

Another potential motivation for reform involves the increasing presence of China as an investor in the United States. Inbound Chinese investment more than tripled to $53.7 billion from 2015 to 2016, although dropped to its second-highest level in 2017. Concerns about this rapid rise, coupled with concerns about Chinese industrial policy, intellectual-property theft, and U.S. involvement with Chinese state-owned enterprises, have resulted in calls for CFIUS to scrutinize more closely transactions involving Chinese companies.

Proposals for CFIUS Reform

Some reforms have been made to CFIUS since its creation, but nothing sweeping has been done to the commission's structure or process since the Foreign Investment and National Security Act of 2007, which significantly expanded CFIUS's mandate. Most recently, the Foreign Investment Risk Review Modernization Act was introduced by John Cornyn in the Senate and Robert Pittenger in the House of Representatives to "modernize and strengthen the process by which…CFIUS…reviews acquisitions, mergers, and other foreign investments in the United States for national security risks." Specifically, FIRRMA would:

- Expand CFIUS's jurisdiction to include certain joint ventures, minority position investments, and real estate transactions near military bases or other sensitive national security facilities;
- Update the Committee's definition of "critical technologies" to include emerging technologies that could be essential for maintaining the U.S. technological advantage over countries that pose national security threats, such as China;
- Allow foreign investors so submit "light filings" to CFIUS for certain types of transactions;

- Add new national security factors for CFIUS to consider in its analyses; and
- Authorize CFIUS to exempt certain otherwise-covered transactions if all foreign investors are from a country that meets certain criteria, such as being a U.S. treaty ally and having a mutual investment security arrangement.

Proponents of this legislation argue that the reforms above would strengthen U.S. national security and protect against rising threats such as intellectual property theft. Others suggest that it goes too far in expanding CFIUS's jurisdiction and will discourage foreign investment as a result.

Conclusion

CFIUS is an important tool in the United States' defense against foreign threats to our national security. It should remain focused on its mission of protecting against threats to national security. Yet it should also seek a transparent and streamlined process for reviewing covered transactions to ensure that nonthreatening, legitimate investment in the United States can gain approval without excessive burden.