



## UNITED STATES

Caroline Binham, senior reporter

The US is the undisputed biggest economy and legal market in the world, and politics is omnipresent.

Private equity is one sector that has had its fair share of political scrutiny recently, on both sides of the Atlantic. One of the sector's favourite tools has been bridge equity. But with a downturn looming, the

question is, for how much longer?

Politics, meanwhile, ultimately scuppered the 2005 Dubai Ports deal, arguably the pinnacle of US isolationism. But recent legislation suggests that the US is making it easier for overseas investors. This US Special Report examines just how easy.

Finally, the Food and Drugs Administration (FDA) is one of the US's most headline-generating agencies. Recent drugs trials have been mired in controversy and political imbroglios. But as this special report argues, the FDA could be nursed back to the robust health necessary for a respected regulator.

# Rational security

With new legislation, the US government hopes to make foreign investment more easily accessible and accountable – something it considers to be important for a safer and more prosperous future. By **David Marchick** and **David Fagan**

**O**n 26 July US President George Bush signed into law the Foreign Investment and National Security Act of 2007, which reforms the US national security review process administered by the Committee on Foreign Investment in the US (CFIUS).

In signing the law the White House explicitly linked the maintenance of “a climate conducive to foreign investment” to strengthening national security. The president's signing closes a chapter on the political storm over investment issues that was begun by controversy over the proposed Dubai Ports World investment in 2006.

The newly enacted legislation is a success for foreign investors and the US market because it codifies existing practice and timeframes, creates greater accountability for members of the CFIUS and should lead to regulations that create greater transparency and predictability for transactions. Moreover, by enabling Congress to return to a more dispassionate oversight role the legislation has two additional effects: first, it eases the political risk environment for transactions; and second, it provides executive agency decision-makers with important breathing room to conduct their reviews, based strictly on the merits of particular transactions, without having to worry about being hauled before a hostile congressional committee.

#### Statutory responsibility and membership

The law codifies the CFIUS's existing authority and practice to review and investigate acquisitions by foreign persons of US companies that are engaged in interstate commerce and have some connection to US national security. For the first time the law will specifically authorise the CFIUS to negotiate, impose and enforce conditions necessary to mitigate any threat to national security presented by a given transaction. The law confirms the secretary of the treasury as the chair of the committee, and lists six members (the secretaries of homeland security, commerce, defense, state and energy, and the attorney general), and two agencies in an ex officio capacity (the secretary of labour and the director of national intelligence). The Energy Department's role in the CFIUS is new. The law also preserves authority for the president to designate additional members, including the heads of White House agencies, as appropriate.

#### The evergreen provision

The law helpfully creates tight control on the use of what has become known as the ‘evergreen’ provision in mitigation agreements entered into by the CFIUS. The committee can reopen transactions previously reviewed or investigated if any party to the transaction submitted false or misleading material information to the CFIUS, or materially breaches a mitigation agreement. However, the law makes it clear that the CFIUS

can only reopen a transaction for a material breach if there is a finding of intentional breach by the lead agency and a finding by all of the CFIUS that no other remedies are available.

#### Timing

The new law maintains the timeframes that exist under current law. Specifically, reviews must be completed within 30 days after the CFIUS receives notice of a covered transaction or reopens a review pursuant to the evergreen provision (see below). Investigations must be completed within 45 days.

#### Investigation triggers

A transaction will be subject to investigation if, after a 30-day review, any of the following apply: the transaction threatens to impair the national security of the US and the threat has not been mitigated during review; the transaction is a foreign government-controlled transaction; the transaction would result in foreign control of any critical infrastructure and could impair national security, unless the impairment has been mitigated during the review period; or the lead agency and the CFIUS agree that an investigation should occur.

#### Transactions with national security implications

The law requires the CFIUS to issue guidance on the types of transactions that have been reviewed and that have raised national security considerations. The guidance will address specifically transactions that involve foreign control of critical infrastructure. The guidance is to be published within nine months of the president's signature.

#### Lead agencies

The law creates additional authority for agencies with the greatest equities in a transaction by adopting the concept of a lead agency, or agencies, for each transaction. Appointed by the Treasury Department, the lead agency will be responsible for negotiating mitigation agreements on behalf of the CFIUS and will be charged with monitoring and enforcing these agreements.

#### Senior-level involvement

The law requires the involvement of senior level officials, including with respect to certifications provided to Congress, in decisions not to investigate covered transactions involving foreign government ownership, or in certain transactions involving critical infrastructure and in decisions to reopen an investigation under the evergreen provision.

#### Foreign government-controlled transactions

The law creates a greater and higher level of scrutiny for transactions involving investment by state-owned entities (SOEs). However, second-stage investigation of such transactions are not

required if the secretary or deputy secretary of the treasury and an equivalent official at the lead agency determine that the proposed transaction will not impair national security. For acquisitions by SOEs that reach the investigation stage, the law requires an assessment of the foreign country's compliance with US and multilateral counter-terrorism, nonproliferation and export control regimes.

#### Transactions involving critical infrastructure

As noted, the legislation effectively codifies existing practice. Specifically transactions that would result in foreign control over critical infrastructure and could impair national security will go to a second stage investigation unless the impairment has been mitigated during the review period.

#### Expanded list of factors for national security consideration

The law expands the expressly enumerated factors that the CFIUS should consider in assessing the national security impact of a transaction. The expanded list essentially codifies factors that the CFIUS already considers, such as: the risk of technology transfer to a country that is a threat to the US; the impact of a transaction on critical infrastructure and critical technologies; foreign government ownership; and, when there is foreign government ownership and a transaction is subject to an investigation, it considers that government's cooperation on counter-terrorism, nonproliferation and export control matters.

#### Congress notification and oversight

Under the law, Congress will receive written notice at the conclusion of the CFIUS process for all reviews and investigations. The law also requires detailed annual reports to Congress on the activities of the CFIUS, including information on the transactions that have been reviewed or investigated within the previous 12 months.

#### Conclusion

The final law is not perfect and leaves some questions and details to be worked out when implementing the regulations. For example, the law states that a violation of the law includes violations of “any mitigation agreement entered into or conditions imposed” by the CFIUS. Still left unanswered are questions such as who will determine what constitutes a violation, whether there will be a materiality threshold and how the penalties will be administered.

Overall, however, the recent US legislation is a positive development for foreign investors and prospective US sellers. It will result in greater regulatory clarity and will cool political pressures on transactions – two outcomes that are a long way from last year's Dubai Ports World controversy and fallout. ■

*David Marchick is a partner and David Fagan is an associate at Covington & Burling*



PHOTOGRAPHY