October 3, 2011

Comments of the Organization for International Investment on CFIUS Process

The Organization for International Investment (OFII) respectfully submits comments for consideration regarding ways to enhance the foreign investment review process administered by the Committee on Foreign Investment in the United States ("CFIUS"). The CFIUS process, while involving a relatively small percentage of total foreign investment in the United States, plays a major role in shaping international views of the openness and attractiveness of the U.S. economy. Therefore, OFII believes that increasing the timeliness and efficiency of the CFIUS process – without any changes to the Executive Order – can have a positive impact on the U.S. economy while still ensuring the prioritization of national security.

Background

OFII is the leading U.S. business association representing the unique interests of U.S. subsidiaries of foreign-headquartered companies. These companies come from a broad cross-section of the economy and employ more than five million Americans in such critical fields as high-skilled manufacturing, engineering, and innovative research and development. Our membership includes many of the companies that appear most frequently before CFIUS. Over the last decade OFII has been an active participant in various policy matters related to foreign investment and the CFIUS process, including the debate following the Dubai Ports World controversy and the ultimate statutory amendments enacted in the Foreign Investment and National Security Act of 2007 ("FINSA"). We believed then — and continue to believe — that the amendments to the CFIUS process that occurred in 2007 and 2008, as embodied in FINSA, the implementing Executive Order, and the implementing regulations, represented a net plus for the regulatory and political environment for foreign investment in the United States.

We commend the Obama Administration for its recent leadership on open investment matters. The President's Statement on the "Commitment of the United States to Open Investment Policy," in combination with the President's Executive Order establishing the SelectUSA Initiative and the Council of Economic Advisors' recent report on U.S. Inbound Foreign Direct Investment, was a strong and welcomed affirmation of the longstanding commitment of the U.S. to an open investment policy and recognition of the important role of foreign direct investment in strengthening the U.S. economy. Likewise, Deputy Secretary of the Treasury Neal Wolin's address to the Singapore Exchange in May was an important statement to investors regarding the role that CFIUS plays in preserving an open investment market while carefully — and very narrowly — focusing on controlling investments that affect national security.

The Administration's actions come as the U.S. is facing historic challenges to its position as the premier place for global investment. Though the U.S. remains the top worldwide recipient of foreign direct investment, it is experiencing sharp downward trends both in its share of global investment and in the number of Americans working for U.S. subsidiaries of global companies. As mergers and acquisitions comprise the majority of foreign direct investment in the United States (approximately 90%), attitudes on the CFIUS process have a direct effect on the level of such investment. OFII believes that modest changes to the interpretation of certain CFIUS protocols can have a positive impact on the attractiveness of doing business in the United States without compromising national security.

Importance of Quick Reviews and Transparency

Apart from the economics of a transaction, nothing matters more to transaction parties than knowing what approvals they must obtain, the rules related to those approvals, and when they can expect to receive the approvals. In turn, the longer that the average timeframes extend for the CFIUS review and the less transparency that exists within the CFIUS process and any reasons for delay, the more uncertainty is introduced to foreign investors.

We recognize that CFIUS has maintained a strong record in approving the overwhelming majority of transactions that it reviews within the 75-day statutory timeframe for a review and investigation. This record is important for foreign investors. At the same time, OFII believes the efficiency and transparency of the CFIUS process can be improved. According to the data published by CFIUS, 38.5 percent of its cases (25 out of 65) proceeded to the second-stage investigation in 2009, and 37.6 percent (35 out of 93) proceeded to a second-stage investigation in 2010. This is roughly equivalent to the **total** number of investigations in the first 20 years of the CFIUS process following the enactment of the Exon-Florio Amendment in 1988 — a total that includes 2008, the first year of CFIUS under the new statutory amendments. Indeed, the rate of investigations over the last two years (roughly 38 percent) is more than double the rate of investigations in 2008 (slightly less than 15 percent).

Even accounting for the new differences in the law (the statutory presumption of investigation for foreign government-controlled transactions and transactions involving critical infrastructure) and practice (fewer withdrawals to avoid the second-stage investigation), the much higher number of investigations is alarming. As explained below, the higher number of investigations also correlates to concerns over the transparency in the process. These factors heighten the risk for foreign-owned bidders that they may be discounted and discriminated against in a M&A auction process — which can include being forced to pay a premium because of the added regulatory burden.

Concerns Related to the Application of Executive Order 13456

We respectfully submit that CFIUS should be able to reduce the higher number of investigations and increase transparency to transaction parties through very modest changes in how CFIUS applies and interprets certain elements of Executive Order 13456. Specifically, we have concerns about the Committee's application of Section 6(a) of the Executive Order, which provides that "communication with the parties to a transaction shall occur through or in the presence of the lead agency, or the [Department of Treasury] if no lead agency has been designated."

We understand that this rule helps to define and organize the CFIUS process. However, as a practical matter, we have concerns that it is being applied to limit CFIUS's communications with the transaction parties, and also to reduce the transaction parties' ability to discuss issues with key agencies during the review process. It is not unusual, for example, for even a lead agency to defer question and communications to the Treasury Department (notwithstanding the language in the Executive Order), and parties have very limited, if any, ability to communicate with agencies that are not formally designated as the "lead," even if those agencies may have concerns or questions about the transaction.

From the perspective of transaction parties, this channeling of communications through the Treasury Department and the corresponding barrier to dealing with other member agencies of CFIUS can obfuscate the review process. It adds a layer between the transaction parties, which have the best understanding of the transaction and the business at issue, and those elements of the government that might have the greatest interest or greatest concerns about the transaction. In addition, as chair, the Treasury Department is naturally protective of the review process and the deliberations of the Committee. These are appropriate qualities for an administrator of an inter-agency process, and the Treasury Department deserves credit for its fidelity to its role as chair. But these very same qualities that make it an effective chair, when combined with the fact that the Treasury Department often does not have the substantive equities or expertise that may underlie a particular concern, mean that the Treasury Department may feel constrained in its communications to parties and those communications, in turn, will appear more equivocal and less insightful to transaction parties. This dynamic limits the ability of the transaction parties to address directly and clearly particular interests or concerns of the CFIUS member agencies.

There also is another important element of the Executive Order at play — Section 7(b), which requires the Committee to agree to and approve any risk mitigation measure before it is proposed and negotiated

with transaction parties. To be sure, there are sound policy reasons underlying this rule. Prior to FINSA and the implementing Executive Order, individual agency members of CFIUS often operated with a certain degree of independence in pursuing their particular interests in a transaction. That resulted in a proliferation of one-off mitigation agreements, many of which were only loosely, at most, related to national security. The Executive Order requirement for the Committee to form consensus around any mitigation proposal, therefore, is sensible and important to ensure that the CFIUS process remains narrowly tailored on true national security risk.

We recognize that the process of coming to consensus related to mitigation is a serious one that often requires robust discussion among the Committee members.[1] But we have concerns that the combination of this consensus requirement around mitigation, on the one hand, and an application of the Executive Order that limits communications channels with the parties, on the other, is contributing to review processes that are less transparent and more complex than necessary. This is having the unintended consequence of extending the formal timeframes for regulatory approval, as well as creating more pressure on transaction parties to engage individual agencies informally before starting the CFIUS process, since that is the only time that they can have direct, open communications with those agencies.

Recommendations

We are not advocating for any change to the Executive Order. Nor are we advocating for a return to the pre-FINSA system of free-for-all communications between individual agencies and transaction parties. Rather, our concern principally is how CFIUS is interpreting and applying Section 6(a) of the Executive Order, and, secondarily, how it is applying Section 6(a) in combination with the requirements of Section 7(b) for consensus on mitigation. We believe that those provisions can — and should — be interpreted and applied to provide a better balance between protecting information and exercising administrative discipline, on the one hand, and offering greater transparency to transaction parties during the review, on the other.

We offer the following recommendations to this end:

- The lead agency or agencies should be permitted — indeed, encouraged — to communicate directly with transaction parties, with the Treasury Department kept apprised of all communications. This should be part and parcel of assuming the function of being a lead agency.

- If more than one agency has equities in a transaction — for example, if more than one agency likely will be party to a mitigation agreement — that agency should preferably be designated as a "lead" agency or should be permitted to communicate directly with the transaction parties, as long as any other lead agency and the Treasury Department are kept apprised of the communications. For example, if the Department of Justice is the lead agency on a transaction, but the Department of Homeland Security also has interests in the transaction, there is no reason that the transaction parties should be shut off from communicating with DHS as long as there is transparency to DOJ and the Treasury Department.

- Parties and agencies should be free to communicate about potential concerns and mitigation considerations from the outset of a CFIUS review, provided they include the Treasury Department and any lead agency in the communications. In many cases that require mitigation,

[1] We also recognize that the robustness of the mitigation-related process inevitably will contribute to a minority of transactions (those that require mitigation or that are a close call) taking more time. But in view of the fact that only five percent of transactions have required mitigation over the last three years, it is hard to see how the requirements of Section 7 of the EO alone can fully explain or account for the overall longer timeframes.

the parties and the agencies know going into the process that mitigation may be likely. Allowing them to communicate about the potential issues and mitigation measures will create efficiencies without minimizing or undercutting the appropriate requirement that any mitigation be based on a consensus view of the Committee. Furthermore, if there is a concern about a transaction, allowing this direct communication earlier in the process — without prejudging any outcome and while still allowing CFIUS to form a consensus view informed by other inputs, such as the threat analysis provided by the Director of National Intelligence — will better enable the parties and CFIUS to address the concerns and avoid unnecessary crises and complexities as the statutory deadlines approach.

- To the extent that the Treasury Department or the lead agency forward questions from other agencies, they should, to the extent possible, identify the agency asking the question. Knowing who is asking a question can be fundamental to understanding exactly what is being asked and, in turn, to providing a direct answer. Thus, transparency related to the source of the question could facilitate the review by enabling the transaction parties to provide more focused, concrete responses.

We believe that these measures are fully allowed and supported by the Executive Order. They would create greater efficiencies in the CFIUS process. And, they would enable transaction parties to make informed decisions about fundamental aspects of the transaction, such as setting a closing date, timing the extension of offer letters to the seller's employees, and organizing for other post-transaction integration plans.

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OFII appreciates the opportunity to provide the foregoing observations and recommendations with respect to the CFIUS process. We believe that these are subtle, but important, changes that can help further establish the CFIUS process as a strong model upholding the openness of a market to foreign investment while still providing appropriate scrutiny to transactions that implicate legitimate national security interests.