Foreign Investment Review Gets Its Own Review

The House Financial Services Committee plans a hearing Feb. 7 on the need for changes in the U.S. program that reviews the national-security implications of foreign investments.

The hearing comes amid growing concern in the business community about the secretive government panel that examines the deals—the Committee on Foreign Investment in the U.S., or CFIUS. A study (see the PDF) released today by lawyer David Marchick, a partner at Covington & Burling, found the Bush administration tightened its scrutiny of foreign deals following the controversy last year over Dubai Ports World’s bid to manage several U.S. ports. The company is owned by the government of Dubai in the United Arab Emirates.

In his study, released by the National Foundation for American Policy, an Arlington, Va.-based think tank, Marchick says securing CFIUS approval “has grown more difficult for foreign investors, adding to uncertainty and increasing the regulatory risk” associated with such deals.

House Financial Services Chairman Barney Frank (D., Mass.) is one of several lawmakers backing legislation designed to improve disclosure and raise accountability within CFIUS. The legislation, among other things, would require CFIUS to conduct a 45-day investigation for all proposed investments involving foreign government-owned firms.

Critics have complained that CFIUS did not conduct a 45-day investigation before approving the DP World transaction last year. The company, owned by the government of Dubai, later decided to divest those assets amid outrage on Capitol Hill.

“This hearing will provide an important opportunity for the Committee to take a hard look at the CFIUS process and to discuss appropriate changes that are needed,” said Illinois Rep. Luis Gutierrez, a senior Democrat on the House Financial Services Committee. – Greg Hitt
WASHINGTON (AP) - Federal reviews of proposed foreign acquisitions of U.S. companies, which have become more common, more time-consuming and more intensive, threaten to slow outside investment in the United States, a new study concludes.

"The pendulum has swung too far and unless it shifts back toward the center, much-needed investment could be chilled and U.S. jobs and economic growth will be lost," says a study due out Thursday from the National Foundation for American Policy, a free-market think tank.

The scrutiny of foreign investment in so-called "critical infrastructure," which includes ports, power plants and telecommunications networks, intensified in the wake of the September 11 terrorist attacks, the study said.

Last year, the Bush administration cracked down on foreign investment after Congress reacted strongly to a proposed purchased of operating rights at five U.S. ports by a Dubai-based company.

The purchase by Dubai Ports World was initially approved by the Committee on Foreign Investment in the United States (CFIUS). An interagency group, CFIUS reviews can reject foreign acquisitions of U.S. companies over national security concerns. Its membership includes 12 federal agencies, including the Departments of Treasury, Justice, Defense, Homeland Security and Commerce.

Congressional opposition also helped thwart a 2005 effort by Chinese oil company CNOOC to purchase California-based Unocal.

Donald L. Evans, chief executive of the Financial Services Forum, said that companies want to know whether CFIUS is keeping to its mandate of "national security-related issues" or expanding to a "more protectionist kind of mentality."

The forum, one of several groups lobbying Congress for more clarity in the foreign investment review process, represents large banks and financial services companies, such as Citigroup Inc., Wachovia Corp. and American Express Co.

CFIUS reviews can be initiated by the companies involved in the deal or by CFIUS member agencies. CFIUS reviewed 113 transactions in 2006, up from 53 in 2004 and 65 in 2005, the study found. Seven of the reviews were extended beyond the standard 30-days into a 45-day investigation, up from 2 extensions in 2005.
In some cases, the reviews lasted longer, the report said. The purchase of Lucent Technologies Inc. by French telecom equipment maker Alcatel, for example, wasn't approved until seven-and-a-half months after the deal was announced.

CFIUS' additional conditions can reduce the value of a deal because of the expense and time involved, the report said. The Department of Homeland Security pushed for security-related changes to 15 transactions in 2006, more than in the previous three years combined, the study found. Such changes can require foreign buyers to sell parts of a U.S. company that does government contracting work or to appoint U.S. citizens to oversee the work.

The CFIUS process should be clarified, the report said, through legislation or by executive order.

Brookly McLaughlin, a Treasury Department spokeswoman, said she could not comment on the report because she had not seen it. But the Bush administration "firmly believes it's important to maintain an economic environment that is welcoming to international investment," she added.

That still seems to be the case. Gary C. Hufbauer, a senior fellow at the Peterson Institute for International Economics, said 2006 "was a good year for foreign investment in the U.S."

According to the Commerce Department, foreign direct investment -- or the purchase of companies, factories or other physical assets -- reached $134.9 billion in the first three quarters of 2006, above the $99.4 billion for all of 2005.

The study says that U.S. subsidiaries of foreign-owned companies employ more than 5 million Americans, the report says.

Some economists dispute the notion that foreign investment creates jobs. Robert E. Scott, senior international economist at the liberal-leaning Economic Policy Institute, said that foreign companies frequently buy U.S. firms to take advantage of brand and marketing power, while closing production facilities and laying off workers here.
WASHINGTON (Reuters) - The U.S. government reviewed 73 percent more foreign acquisitions of American assets in 2006 than in the previous year, raising concerns some foreign investors may soon prefer to go elsewhere, according to a think tank study released Thursday.

The jump is due in part to the Congressional backlash over state-owned Dubai Ports World's purchase of some U.S. operations one year ago, the report said. Dubai Ports World was later forced to sell the American assets after lawmakers said national security risks had not been fully considered.

"The pendulum has swung too far and unless it shifts back toward the center, much-needed investment could be chilled and flow to other countries," said the report by the National Foundation for American Policy, a free market think tank.

The Committee on Foreign Investment in the United States (CFIUS) a multi-agency panel chaired by Treasury Secretary Hank Paulson, reviews the national security implications of foreign acquisitions. It can also broker agreements to ensure safeguards are in place.

In 2006, CFIUS examined 113 deals worth more than $95 billion, a 73 percent rise over the previous year, the study said. Seven of the 2006 deals faced extended investigations and two required approval by President Bush.

Another result of the Dubai Ports World fallout is that companies with no direct links to national security -- which often triggers a CFIUS review -- are now filing for government review and clearance.

"There's certainly a growing body evidence that it has had a somewhat chilling effect on foreign capital coming into the United States, which hurts our U.S. economy," said Donald Evans, former U.S. Secretary of Commerce and now chief executive of the Financial Services Forum.

Other countries could retaliate by limiting investment in their markets if deals are rejected, he said.

The report, authored by David Marchick of the Covington & Burling law firm, also said new security agreements could hurt investment. It pointed to an agreement added to Alcatel's acquisition of Lucent Technologies that would permit the U.S. government to force the companies to unwind their deal if it was violated.
Congress failed in 2006 to overhaul the CFIUS process. Lawmakers this month offered new legislation to tighten the rules for foreign takeovers and to require longer reviews involving foreign state-owned companies.

Marchick, who has advised companies about CFIUS reviews, urged Bush to issue an executive order to clarify the government's view on how to protect critical infrastructure and how foreign ownership could affect national security. He also suggested setting guidance for security agreements and clarifying what issues should be included in CFIUS reviews.

"Congress and the executive branch need to find the right balance to meet the twin objectives of protecting national security and promoting investment in the United States," the report said.
WASHINGTON (Dow Jones)--The White House should clear up confusion over U.S. policies on foreign investment so overseas investors will know what to expect, a new study said Thursday. The U.S. government's Committee for Foreign Investment in the United States, known as CFIUS, has changed significantly since the Sept. 11, 2001, terrorist attacks, according to a new report from the National Foundation for American Policy written by Washington lawyer David Marchick. Congress also has weighed in on the issue, in a series of hearings last year that debated whether a Dubai-based ports company should operate U.S. ports. Companies need more explicit instructions on when to file with CFIUS for a review, along with what kind of timetable to expect, Marchick said in his report. Marchick's report calls for an executive order, possibly paired with congressional action. He endorsed last year's House of Representatives version of proposed legislation, rather than a more restrictive Senate bill. The House is poised to take up the issue again in 2007. On Thursday, the House Financial Services Committee announced a Feb. 7 hearing on CFIUS, the aftermath of the Dubai Ports World issue, and possible reforms. "After all the outrage surrounding the Dubai Ports fiasco, the public expects changes in the foreign investment vetting system," said U.S. Rep. Carolyn Maloney, D-N.Y., and a top Democrat on the panel, in a statement on the hearing plans. "We have the opportunity to get something smart and balanced done in the House again, and the prospects for getting something to the president's desk should be better in the new Congress," Maloney said. Marchick said U.S. officials ought to welcome foreign investment. Few transactions pose a big risk, he said, and in the case of big conglomerates, where a company is headquartered may not be that significant. For example, U.S. investors own big stakes in both U.S-based Exxon Mobil Corp. (XOM) and U.K.-based BP PLC (BP). But if they were making a potentially sensitive acquisition, only BP would need to check with CFIUS, he said. "My general view is that most foreign acquisitions don't create real national security issues," Marchick said during a conference call with reporters. Because of the current uncertainty, the number of filings has soared. The study cites 113 filings in 2006, a 73% increase over the prior year. These transactions were worth more than $100 billion, according to publicly available data, Marchick said. Former Commerce Secretary Don Evans, now chief executive of the Financial Services Forum, said the U.S. needs to clear up its regulations so the process will work better. He said the U.S. economy suffers when foreigners are discouraged from U.S. investments. -By Rebecca Christie, Dow Jones Newswires; 202-862-9243; rebecca.christie@dowjones.com [01-25-07 1534ET]
Study of CFIUS Finds Increase in Filings Following Dubai Ports World Controversy

The federal government's panel reviewing the national security implications of foreign acquisitions of businesses in the United States is getting more applications and taking longer to conduct reviews than it did prior to the controversy over Dubai Ports World's plans to purchase the rights to operate six U.S. ports, according to a study released Jan. 24 by the National Foundation for American Policy.

Moreover, the Committee on Foreign Investment in the United States (CFIUS) is asking far more companies to make changes to their purchase plans, including divesting some parts of the businesses, than they did before the Dubai Ports World acquisition of United Kingdom-based Peninsular & Oriental Steam Navigation Co. raised alarms in Congress.

CFIUS, an interagency committee chaired by the Treasury Department, approved DP World's acquisition plans in January 2006, but later bowed to Congressional pressure to reopen the review. The firm eventually volunteered to sell the rights to the U.S. port operations that it had gained in its purchase of P&O Steam Navigation.

David Marchick, a partner at law firm Covington & Burling and the author of the National Foundation for American Policy's study, said the controversy about the Dubai Ports World deal has had a chilling effect on foreign investment in the United States and has created significantly more uncertainty for businesses interested in investing in U.S. operations.

As evidence of the growing concerns, Marchick said applications to CFIUS rose 73 percent in 2006 to 113 filings and the number of transactions that required more detailed investigations jumped 250 percent. The more stringent approach being taken also resulted in more withdrawals of applications for review, up 150 percent, as firms decided the deal would not be worth the concessions that would have to be made to get U.S. approval, the study said.

While the official process is still for an initial 30-day review of an application and a second 45-day investigation, if needed, some reviews have taken longer to get approval. For instance, Marchick's report said it took 7 1/2 months to get President Bush's approval for the Lucent Technologies-Alcatel merger.

Scaring Away Investment?

"If the pattern of longer time periods for CFIUS reviews continues, foreign investors will either be less interested in investing in the United States or U.S. companies will simply refuse to sell to foreign investors because of the risk of lengthy closing times for deals," the study said.

Marchick added that the stakes of not responding to investors' concerns are high, noting that the value of the transactions submitted to CFIUS for review exceeded $95.5 billion.
For the firms that do ultimately get approval, the number of deals that required a "mitigation agreement" as a condition for approval surged to 15 in 2006, compared to just 13 over the entire 2003-2005 period. Investors in the information technology sector in particular are facing a greater likelihood of being compelled to enter into a mitigation or national security agreement in order to get approval from CFIUS, the study said.

Moreover, signing such agreements has typically been seen as a form of insurance against a future divestment order from the president, but recent CFIUS actions have taken away such legal "safe harbors," adding more uncertainty for foreign investors.

In the case of the Alcatel-Lucent merger, CFIUS required the parties to agree that the CFIUS review could be reopened and divestment potentially could be ordered if the "parties materially fail to comply with any of" the terms of a negotiated security agreement.

But the study said some of the other changes that have taken place in the CFIUS process over the past year have been beneficial. The committee is now communicating more with Congress and agencies contributing to the CFIUS process are devoting more resources to the reviews.

Unfortunately, businesses completing transactions are also filing more applications with CFIUS even if there is only a tenuous relationship to national security.

"Unless there is a change in the environment, even more transactions will be filed without a real nexus to national security, potentially changing CFIUS from a national security review process to more of an investment review process," Marchick warned. "The increase in filings is also problematic as it could stretch the agencies' abilities to focus on the cases that actually might pose a threat to national security."

The study concluded that President Bush should issue an executive order that would implement many of the proposals made by Congress in 2006, including a regulatory guidance on what mitigation agreements should include and how they should be enforced.

**House to Hold Hearing**

If Congress chooses to enact legislation, the study said it should use the House bill passed in 2006 (H.R. 5337) as a starting point. A similar bill (H.R. 556) was introduced in the House on Jan. 19 and will be the basis for a House Financial Services Committee hearing announced for Feb. 7.

"After all the outrage surrounding the Dubai Ports fiasco, the public expects changes in the foreign investment vetting system, which is why it's so important that this issue is coming before the committee so quickly," said Rep. Carolyn Maloney (D-N.Y.), a sponsor of the bill. "I believe the bill we reintroduced this year reflects a smart and balanced approach that will accomplish the most important goals: better security, while encouraging safe foreign investment."

A Treasury Department spokeswoman declined to comment on the study, but said the administration "firmly believes it's important to maintain an economic environment that is welcoming to international investment."

She also declined to endorse any particular legislation, but she said the administration intends to work with Congress to reform CFIUS.