Cfius review needs greater transparency - opinion

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The fate of two of this year's blockbuster transactions – the proposed merger between EADS and BAE Systems and CNOOC Ltd's acquisition of Canadian oil and gas company Nexen Inc. – may be decided in a little-known office in the US Department of the Treasury. The Committee on Foreign Investment in the US, known as Cfius, will be called upon to determine whether either transaction poses a risk to US national security.

Cfius review is becoming a more frequent hurdle to investments and acquisitions by foreign parties. While Cfius challenges to proposed transactions are infrequently reported, the lack of public guidance from the Agency and the complete secrecy that surrounds its deliberations are increasingly frustrating for investors and acquirers. These parties must determine whether the voluntary filing is warranted and whether a particular transaction is likely to raise Cfius concerns.

Exemplifying such frustration, for the first time in its history, Cfius was sued in court by Ralls Corp, a Chinese company, regarding one of its decisions, which was President Obama upheld on September 28. With the increasing importance of Cfius, it is time for changes to enable more transparency regarding the bases for the Agency's decisions.

In 2007, the Foreign Investment and National Security Act expanded Cfius' scope and powers. The law mandated that the Agency consider the impact of proposed transactions on so-called critical infrastructure – including energy assets and information technology. It is also those industries – telecommunications, computer software, and energy assets – that have been the focus of foreign investment recently.

Cfius' prominence and workload has increased considerably since 2007. Today, virtually any non-U.S. entity contemplating a significant investment in the U.S. must consider whether a Cfius filing is warranted.

Bucking the trend

The current US administration has encouraged increased transparency in government through the introduction of its Open Government Initiative and in the healthcare reform law. Cfius, however, has remained immune to this trend.

A major reason for this resistance to transparency is the national security focus of its review. As Cfius increasingly becomes a gatekeeper of international investments and transactions, continued secrecy and opaqueness can be expected to cause controversy, further judicial challenges, and potential retaliation by other governments. There may also be reductions in foreign investment into the US.

Cfius could greatly reduce the uncertainty regarding its review process, and by extension the frustration surrounding its decisions, by providing brief general summaries of the bases for its determinations with respect to proposed transactions.

At present, the only public indication of the Agency's activities is the annual report that Cfius is required to provide to the US Congress. This describes the number of notices submitted,

investigations initiated as a result of those notices, the industries involved in the proposed transactions, and the nationalities for non-US parties to the transactions. Cfius does not publish any transaction-specific information or decisions.

In contrast, numerous US regulatory and enforcement agencies, including the Department of Justice Antitrust Division and the Food and Drug Administration, commonly provide public statements describing their decisions, while accommodating confidentiality concerns. Any similar brief summaries of Cfius' parameters of decision would necessarily be circumspect, in view of security concerns and the need to protect the Agency's deliberative process.

Nonetheless, it is difficult to conclude that US government, foreign government, foreign investors and acquirers, and indeed Cfius itself, would not be better served by a short statement of the parties to the transaction, the industry involved, and the Agency's general rationale for its determination. Such transparency, which would require an amendment of the Agency's statute, would enhance the predictability and likely the legitimacy of Cfius' decisions, enabling both US sellers and foreign investors and acquirers to better gauge Cfius' probable concerns and more efficiently undertake investments in US businesses.

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See here for IFLR's coverage of Cfius' impact on the Cnooc/Nexen deal

And here for tips on how to close China/US mergers