

April 23, 2018

TO: Members, Subcommittee on Digital Commerce and Consumer Protection

FROM: Committee Majority Staff

RE: Hearing entitled “Perspectives on Reform of the CFIUS Review Process”

I. INTRODUCTION

The Subcommittee on Digital Commerce and Consumer Protection will hold a hearing on Thursday, April 26, 2018, at 10:15 a.m. in 2322 Rayburn House Office Building. The hearing is entitled “Perspectives on Reform of the CFIUS Review Process.”

II. WITNESSES

Panel I

- The Honorable Heath P. Tarbert, Assistant Secretary, International Markets and Investment Policy, U.S. Department of the Treasury; and
- The Honorable Richard E. Ashooh, Assistant Secretary, Export Administration, U.S. Department of Commerce.

Panel II

- The Honorable Clay Lowery, Managing Director, Rock Creek Global Advisors, and former Assistant Secretary for International Affairs, U.S. Department of the Treasury;
- Dr. Derek Scissors, Resident Scholar, the American Enterprise Institute; and
- The Honorable Kevin J. Wolf, Partner, Akin Gump Strauss Hauer and Feld, LLP and former Assistant Secretary for Export Administration in the Bureau of Industry and Security (BIS), U.S. Department of Commerce
- Ms. Celeste Drake, Trade and Globalization Policy Specialist, AFL-CIO

III. BACKGROUND

The United States government utilizes various mechanisms to control risks to national security arising from transactions with foreign entities. Primary among these are the Committee on Foreign Investment in the United States (CFIUS), which reviews investments in U.S.

businesses; and export controls, which include various authorities lead by the Department of Commerce to restrict the sale of U.S. goods and products to non-U.S. persons.

A. The History of CFIUS

CFIUS Origins.

CFIUS is a multi-agency U.S. governmental body tasked with reviewing investments in United States businesses by non-U.S. persons, where such investment could result in control of the U.S. business by the non-U.S. person, and where such control would raise national security concerns.

CFIUS is authorized pursuant to the Defense Production Act of 1950 and is granted authority to review “any merger, acquisition, or takeover . . . by or with any foreign person which could result in foreign control of any person engaged in interstate commerce in the United States” in order to “determine the effects of the transaction on the national security of the United States.”¹ CFIUS was first created by Executive Order of President Ford in 1975. Per that order, CFIUS was to have “primary continuing responsibility within the Executive Branch for monitoring the impact of foreign investment in the United States, both direct and portfolio, and for coordinating the implementation of United States policy on such investment.”² In 1988, Congress gave the President the authority to block proposed foreign purchases that threatened national security.

In 2007, after the attempt by Dubai Ports World to purchase port management companies that oversaw six U.S. ports,³ Congress passed the Foreign Investment and National Security Act (FINSA).⁴ This law established CFIUS as a statutorily-created entity headed by the Secretary of the U.S. Treasury, as well as the heads of the Departments of Justice, Homeland Security, Commerce, Defense, State, and Energy, and the Offices of the U.S. Trade Representative and Science and Technology Policy.⁵

Energy and Commerce Committee Jurisdiction.

The Energy and Commerce Committee has long played a role in CFIUS related measures; the Committee has jurisdiction over foreign investment in the U.S. The 1988 Exon-Florio provision that marked Congress’ first substantive legislative effort on the subject was included as Section 5021 of the Omnibus Trade and Competitiveness Act of 1988.⁶ The provision originated

¹ Section 721 of the Defense Production Act of 1950 (50 U.S. Code § 4565)

² Executive Order 11858 of May 7, 1975, 40 FR 20263

³ For background, *see generally* Stephen E. Flynn, *The DP World Controversy and the Ongoing Vulnerability of U.S. Seaports*, Testimony Before the House Committee on Armed Services (March 2, 2006) <https://www.cfr.org/report/dp-world-controversy-and-ongoing-vulnerability-us-seaports-prepared-remarks>

⁴ P.L. 110-49 (July 26, 2007)

⁵ The following offices also observe and, as appropriate, participate in CFIUS’s activities: the Office of Management & Budget, the Council of Economic Advisors, the National Security Council, the National Economic Council, and the Homeland Security Council.

⁶ P.L. 100-148 (August 23, 1988)

in bills reported by the Commerce Committee in the Senate and the Energy and Commerce Committee in the House.⁷

In 2006, in light of the Dubai Ports proposal discussed above, then-Rep. Roy Blunt introduced H.R. 5337, the National Security Foreign Investment Reform and Strengthened Transparency Act of 2006,⁸ which was primarily referred to the Financial Services Committee and additionally to the Energy and Commerce Committee and International Relations Committee. Under the leadership of Energy and Commerce Chairman Joe Barton, the Committee marked up the legislation with substantial amendment. The measure subsequently passed the House, but stalled in the Senate. The next session of Congress, Rep. Carolyn Maloney introduced substantially similar legislation, which received the same referral; that measure eventually became law.⁹

B. The CFIUS Review Process Under Current Law

FINSA provides that a CFIUS review may be initiated by either the President, acting through the Committee,¹⁰ or upon a notice submitted by a party to the transaction.¹¹ If CFIUS determines that a proposed transaction would result in control of the U.S. corporation by a foreign government (including a corporation owned or controlled by a foreign government), CFIUS is statutorily obligated to conduct a review.

In practice, parties to a transaction often submit a request for review to avoid uncertainty around a potential deal. After formally accepting a filing, CFIUS has 30 calendar days to “review” the transaction and decide whether to clear it or commence an “investigation” (essentially, an extension or continuation of the initial review) instead. That investigation can last up to an additional 45 days, although the process can be terminated early, at any point during the 45-day investigation period. If CFIUS still has not resolved any potential national security concerns at the end of the 45-day investigation period, CFIUS is responsible for making a formal recommendation to the President as to whether to clear or block the transaction. The President then has up to 15 additional days to decide whether to suspend, prohibit, or impose conditions on the deal.¹²

If CFIUS determines that a transaction entails national security risks that are not adequately addressed by other provisions of U.S. law, it may impose conditions on parties to mitigate such risks, or it may refer the case to the President for action.¹³ Actions to mitigate risks to national security may include requiring that only U.S. citizens have access to certain information, facilities, or functions; establishing guidelines for contracts with the U.S.

⁷ Jackson, James K., *The Committee on Foreign Investment in the United States (CFIUS)*, Congressional Research Service, March 13, 2018. <https://fas.org/sgp/crs/natsec/RL33388.pdf>

⁸ Available at <https://www.congress.gov/bill/109th-congress/house-bill/533>

⁹ Foreign Investment and National Security Act of 2007, P.L. 110-49

¹⁰ Section 721 of the Defense Production Act of 1950 (50 U.S.C. 4565(b)(1)(D))

¹¹ *Id.* at 4565(b)(1)(C)

¹² See Process Overview, U.S. Department of the Treasury, International (retrieved April 12, 2018) <https://www.treasury.gov/resource-center/international/foreign-investment/Pages/cfius-overview.aspx>

¹³ *Id.*

government; allowing the U.S. government to review and block future corporate actions; requiring the company to undergo periodic audits or other measures designed to mitigate the effects on national security.¹⁴

Persons subject to CFIUS review face civil penalties for making material misstatements, omitting information, or violating the terms of a mitigation agreement. These are subject in each instance to civil penalties of \$250,000 per violation and are in addition to any other penalties that may attach under other provisions of civil or criminal law.¹⁵

There have been five transactions blocked by the President after CFIUS review; four of these have occurred during the last two Administrations. In 2012, President Obama blocked Ralls Corporation, a U.S. company owned by Chinese nationals, from acquiring a U.S. wind farm energy firm located near a Defense Department facility. In 2016, President Obama blocked a Chinese investment firm from acquiring a German company, Aixtron, that had U.S. based assets.¹⁶ In 2017, President Trump blocked a Chinese company from purchasing Lattice Semiconductor, and in March, the President Trump blocked a Singapore-based company, Broadcom Limited, from completing a hostile takeover of Qualcomm.¹⁷

C. Export Controls

Whereas under current law the CFIUS review process concerns foreign investment in U.S. companies, other federal laws exist to address the export of security-sensitive U.S. technology and equipment.¹⁸ These laws and associated regulations are primarily directed at preventing the export of defense-related and dual-use technology and goods. Under the current U.S. export control system, the Departments of Commerce, State, and Treasury have authority to issue different types of export licenses and maintain lists of both items that are prohibited for export, as well as parties to whom it is illegal to export.¹⁹ Additionally, the Departments of Commerce, State, Homeland Security, Justice, and Defense, as well as the Nuclear Regulatory Commission and the Federal Bureau of Investigation, all play a role in enforcing U.S. export controls.²⁰

¹⁴ *Overview of the CFIUS Process*, Latham & Watkins (retrieved April 12, 2018) <https://www.lw.com/thoughtLeadership/overview-CFIUS-process>

¹⁵ 31 CFR 800.801

¹⁶ Jackson, *The Committee on Foreign Investment in the United States (CFIUS)*.

¹⁷ Cecilia Kang and Alan Rappaport, *Trump Blocks Broadcom's Bid for Qualcomm*, New York Times (March 12, 2018) <https://www.nytimes.com/2018/03/12/technology/trump-broadcom-qualcomm-merger.html>

¹⁸ See e.g. The Arms Export Control Act (22 U.S.C. Ch.39); the Export Administration Act of 1979 (50 U.S.C. App. 2401 *et. seq.*)

¹⁹ “Exports of dual-use goods and technologies—as well as some military items—are licensed by the Department of Commerce, munitions are licensed by the Department of State, and restrictions on exports based on U.S. sanctions are administered by the U.S. Department of the Treasury.” Ian Ferguson and Paul Kerr, *The U.S. Export Control System and the Export Control Reform Initiative* CRS Report (March 15, 2018) <https://fas.org/sgp/crs/natsec/R41916.pdf>

²⁰ *Id.*

The Bureau of Industry and Security (BIS) in the Department of Commerce administers export licensing and enforcement of prohibitions on exports of dual-use technologies through regulations²¹ enacted pursuant to the Export Administration Act (EEA). This includes the Commerce Control List (CCL)²² which contains the specific items subject to controls. The BIS also maintains lists of persons and entities, as well as embargoed nations, without a specific license.

The Nuclear Regulatory Commission administers a subset of the EEA related to military and dual-use technology of a nuclear nature, as well as through powers granted by the Atomic Energy Act of 1954.²³ Additionally, the Department of Energy authorizes the export nuclear technology, and the State Department's Directorate of Defense Trade Controls (DDTC) has licensing authority with respect to nuclear items with a military purpose.²⁴

The State Department administers the International Traffic in Arms Regulations (ITAR),²⁵ which require that any person engaged in the manufacture, export, or brokering of arms or defense services must register with the U.S. government. The ITAR sets out the requirements for licenses or other authorizations for specific exports of defense articles and services as well as the U.S. Munitions List (USL), which describe the articles and services subject to regulation.²⁶

The U.S. Treasury administers programs designed to enforce economic and trade sanctions against targeted foreign governments, individuals, and entities through the Office of Foreign Assets Control (OFAC).²⁷ According to the Department of Treasury, "OFAC acts under Presidential national emergency powers, as well as authority granted by specific legislation, to impose controls on transactions and freeze assets under US jurisdiction."²⁸ These authorities include specific U.S. sanctions legislation²⁹ as well as more general authorities authorizing the President to impose sanctions on foreign persons and governments granted by the International Emergency Economic Powers Act,³⁰ the National Emergencies Act,³¹ and other laws.

Owing to the disbursed nature of managing export controls, in 2009, President Obama announced the Export Control Reform Initiative.³² Under that proposal, the President directed the relevant agencies to implement reforms to reconcile various definitions, regulations, and policies for export controls with the ultimate goal of creating a single control list, single licensing

²¹ 15 C.F.R. 730 et seq.

²² The list is available at <https://www.bis.doc.gov/index.php/regulations/export-administration-regulations-ear>

²³ P.L. 83-703

²⁴ Ferguson and Kerr, *The U.S. Export Control System and the Export Control Reform Initiative*.

²⁵ 22 CFR 120-130

²⁶ The USML can be found here https://www.ecfr.gov/cgi-bin/text/idx?SID=86008bdf41fb2e79cc5df41a180750a&node=22:1.0.1.13.58&rgn=div5#se22.1.121_11

²⁷ See <https://www.treasury.gov/about/organizational-structure/offices/Pages/Office-of-Foreign-Assets-Control.aspx>

²⁸ *Id.*

²⁹ See e.g. the Countering America's Adversaries Through Sanctions Act (P.L. 115-44)

³⁰ 50 U.S.C. 1701 et seq.

³¹ 50 U.S.C. 1601 et seq.

³² See Press Release, *President Obama Lays the Foundation for a New Export Control System To Strengthen National Security and the Competitiveness of Key U.S. Manufacturing and Technology Sectors*, THE WHITE HOUSE, OFFICE OF THE PRESS SEC'Y (Aug. 30, 2010), <http://1.usa.gov/14uULyw>

agency, unified information technology system, and enforcement coordination center.³³ While progress has been made—for instance, State, Commerce, and Treasury now maintain a searchable “Consolidated Screening List”³⁴ and the State Department has transferred 15 categories from the USML to the CCL—these efforts are ongoing.³⁵

IV. LEGISLATION

H.R. 4311, Foreign Investment Risk Review Modernization Act of 2017.

The Foreign Investment Risk Review Modernization Act of 2017, H.R. 4311, (and a companion measure sponsored by Senators Cornyn and Feinstein in the Senate³⁶) would add new authorities and review factors to existing law.³⁷ As introduced, the bill expands the scope of transactions potentially reviewable by CFIUS, including certain non-passive, non-controlling investments in U.S. critical technology or critical infrastructure companies, real estate purchases near sensitive military installations, and transactions structured to evade CFIUS review. The legislation would also allow CFIUS review of any transaction whereby a U.S. critical technology company would lend intellectual property and associated support to any foreign person, such as in the case of a joint venture.

The bill would require parties to a transaction to submit a notice to CFIUS if the transaction would allow a foreign person in which a foreign government owns a voting interest of 25 percent or more, to obtain a voting interest of 25 percent or more in a U.S. corporation (25/25 review), and additionally, in such other circumstances as the Committee determines by rule. The legislation also would add a host of new matters to the list of national security concerns CFIUS is to consider, such as the effect of the transaction on cybersecurity, whether the transaction is likely to expose sensitive data about U.S. citizens to foreign persons or governments (e.g. ID numbers or genomic information), and whether the transaction could facilitate fraudulent or criminal activity affecting U.S. security.

The legislation would allow CFIUS to exclude reviews of certain transactions, such as those where other authorities, such as export control requirements, are deemed adequate to address national security concerns. The bill would also allow CFIUS to exempt transactions involving U.S. allies. The legislation also would establish a fund at the U.S. Treasury to pay for CFIUS, authorize appropriations for such fund, and allow CFIUS to charge user fees to companies in the proposed transaction equal to the lesser of \$300,000 or 1 percent of the transaction’s value. On April 12, 2018, the Committee on Financial Services held a legislative hearing on H.R. 4311.³⁸

³³ *About Export Control Reform*, Export.gov (retrieved April 18, 2018) <https://2016.export.gov/ecr/>

³⁴ Available at https://2016.export.gov/ecr/eg_main_023148.asp

³⁵ Jackson at 14.

³⁶ S. 2098, available at <https://www.congress.gov/bill/115th-congress/senate-bill/2098/text?q=%7B%22search%22%3A%22committee+foreign+investment%22%7D&r=1>

³⁷ Available at <https://www.congress.gov/bill/115th-congress/house-bill/4311/text>

³⁸ *Subcommittee Examines Proposed CFIUS Changes*, Committee on Financial Services, United States House of Representatives (April 12, 2018) <https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=403315>

H.R. 5040, Export Control Reform Act of 2018.

House Foreign Affairs Committee Chairman Edward Royce and Rep. Eliot Engel introduced H.R. 5040, the Export Control Reform Act of 2018, which would substantially update U.S. export control authorities.³⁹ The legislation would establish a permanent statutory basis for the control of commercial and some military items licensed by the Department of Commerce, while repealing the Export Administration Act of 1979 (EAA). The legislation would require the President to establish controls over the export of certain dual-use and military items. The administration of those controls would be delegated to the Secretary of Commerce, Secretary of Defense, Secretary of State, the Director of National Intelligences, and other appropriate Federal agencies. The Department of Commerce would be given authority to issue licenses and other authorization for exports. The legislation was passed out of the House Foreign Affairs Committee on April 17, 2018.

V. ISSUES

The following issues may be examined at the hearing:

- Do strategic and national security concerns implicate deficiencies in the current CFIUS review process?
- What are the implications for international and interstate commerce from enhancing the review process for foreign acquisitions of U.S. assets?
- How has the investment environment changed for foreign direct investment in the United States changed since 2007?

VI. STAFF CONTACTS

If you have any questions regarding this hearing, please contact Melissa Froelich or Gregory Zerzan of the Committee staff at (202) 225-2927.

³⁹ H.R. 5040, available at <https://www.congress.gov/bill/115th-congress/house-bill/5040/text>