

Alternative Regulatory Regimes for FOCD/FOCI

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FOCD Framework under AEA

- Section 103d of Atomic Energy Act imposes two prohibitions
 1. No license to entity “owned, controlled, or dominated by an alien, foreign corporation, or foreign government”
 - Direct foreign ownership prohibited
 - 100% indirect ownership prohibited
 - NRC has never approved greater than 50% indirect ownership
 - Possible to “negate” FOCD with NAP (unless direct/100% indirect ownership)
 2. No license if “inimical to the common defenses and security or to the health and safety of the public”

FOCD Framework under AEA (cont'd)

- **FOCD analysis is country-neutral**
 - No deference for countries with good U.S. relations
 - No special scrutiny for countries with bad U.S. relations
- **Inimicality test not country-neutral**
 - Provides backstop to catch potentially problematic applications
 - Also applies to purely U.S. entities

U.S. Policy under CFIUS

- U.S. “Open Investment Policy” welcomes foreign direct investment
 - U.S. number one recipient of FDI in world
- General presumption that foreign investments treated same as domestic
 - Sector-specific exceptions – e.g., nuclear, aviation, communications, classified defense facilities
 - Committee on Foreign Investment in the United States (“CFIUS”) establishes catch-all review mechanism for virtually any industry

Evaluating FOCD/FOCI Regimes

- Efficacy of FOCD/FOCI regime depends on risks against which it protects

Examples of Risks

Sabotage

Espionage

Unauthorized access to U.S. IP

Export control violations

Diminished supply of product in U.S. market

Foreign control of critical product/industry

CFIUS Mitigation

- Common solution in CFIUS is “mitigation”
 - Security conditions placed on transactions
- Allows clearance of transactions that would otherwise pose unacceptable risks
- Mitigation concept somewhat similar to NRC’s Negation Action Plan (“NAP”)

Regulation under CFIUS

- CFIUS charged with reviewing transactions that implicate national security
 - Default is that foreign investment is good
 - Mitigation is preferable to blocking a deal
- Authority is more flexible
 - Applies to all industries
 - CFIUS must defer to other industry-specific provisions of law, *e.g.*, AEA, also EAA, DOD FOCI rules

Regulation under CFIUS (cont'd)

- Examples of industries that may trigger CFIUS scrutiny:
 - Defense companies
 - Transportation infrastructure
 - Chemical facilities
 - Bio-technology
 - Nuclear technology
 - Energy companies
 - Telecom products/services
 - Computer hardware/software
 - Businesses located near defense facilities

Scope of CFIUS' Jurisdiction

- CFIUS covers even 10% foreign ownership
 - Covered transaction = transaction that can result in control of a U.S. business (broadly defined)
 - 10% ownership (or even less) may constitute control
 - But CFIUS estimates it reviews only 10% of covered foreign investment per year
 - And only 10% of those end up with mitigation agreements

CFIUS Risk Analysis

- Threat
 - Intent and capability of acquirer
 - Not country-neutral
- Vulnerability
 - Assets being acquired
- Consequence
 - Adverse effects of exploitation

CFIUS Risk Analysis (cont'd)

- No formal distinction between direct/indirect ownership
- No *per se* limits on foreign ownership
- No safe harbor
 - Only if $\geq 10\%$ percent and purely passive investment
 - Limits gamesmanship/creative lawyering

Timing of Review

- CFIUS must complete review within statutory timeframe
 - Initial review = 30 days
 - CFIUS may (and too often does) extend additional 45 days by commencing “investigation”
 - Combination of voluntary notification and capped review period allows investors to achieve finality before closing

CFIUS Authority

- After review/investigation, three options:
 - Clear transaction (85-90%)
 - Clear with “Mitigation Agreement” (5-15%)
 - Decline to clear (0-5%)
 - Parties can withdraw, or CFIUS can recommend to President that he block/divest

CFIUS Mitigation Agreements

- CFIUS has broad authority to negotiate Mitigation Agreements as condition to clearing transaction
 - Foreign Investment and National Security Act of 2007 (“FINSA”) codified practice
 - Mitigation Agreements similar to NAPs, but less focused on formal ownership

CFIUS Mitigation Agreements (cont'd)

- CFIUS uses different mitigation tools depending on particular concerns
 - Typical concerns include sabotage/espionage, foreign control/influence, export controls, or USG products
 - Will not require mitigation solely on basis of foreign ownership
- Flexibility gives CFIUS leverage
 - Companies make substantial concessions because usually not commercially material
 - Companies unwilling to accept mitigation will not invest in the first place

Common CFIUS Mitigation Terms

- Security plan with security officer and periodic USG meetings
- U.S. citizens in key positions
- Screening of key personnel
- Functions and locations limited to U.S. citizens and/or USG-approved personnel
- Segregated networks
- Visitation/access restrictions
- Limitations on location (*e.g.*, certain facilities must be maintained inside US)
- Guidelines and terms for handling USG contracts
- Protecting customer information/other sensitive information
- Regular compliance certifications
- USG audit rights

Another regime: DSS/FOCI

- Applied by DSS if cleared U.S. company comes under foreign ownership, control, or influence (“FOCI”)
- FOCI mitigation driven by templates
 - Different mitigation instruments depending on level of FOCI
 - Templates pre-approved; ability to deviate restricted
 - Template approach works because of narrow focus

Conclusions

- Depending on goals, FOCD regime may be too restrictive/not restrictive enough
- CFIUS review less-defined, more flexible
- Possible solution is to deny application only if FOCD could have adverse effect
 - Adverse effect defined based on regulatory goals