# CLIENT UPDATE

# CFIUS REVIEW REQUIRES DUE PROCESS

NEW YORK
Mark W. Friedman
mwfriedman@debevoise.com

Maurizio Levi-Minzi
mleviminzi@debevoise.com

Bruce E. Yannett
beyannett@debevoise.com

Steven S. Michaels
ssmichaels@debevoise.com

WASHINGTON, D.C.
Jeffrey P. Cunard
jpcunard@debevoise.com

LONDON
Geoffrey P. Burgess
gpburgess@debevoise.com

MOSCOW
Alan V. Kartashkin
avkartashkin@debevoise.com

HONG KONG
E. Drew Dutton
eddutton@debevoise.com

Andrew M. Ostrognai
amostrognai@debevoise.com

Stuart J. Valentine
sjvalentine@debevoise.com

The U.S. Court of Appeals for the D.C. Circuit recently held that, in certain situations, the Committee on Foreign Investment in the United States ("CFIUS") is required to afford due process to persons submitting notices for CFIUS review after the closing of a transaction. Under the Exon-Florio amendment to the Defense Production Act of 1950 (the "DPA"), CFIUS reviews transactions where the acquisition of a U.S. business by a foreign person may raise national security concerns.[1] The Court of Appeals reviewed an order by which President Obama, after CFIUS review, had directed Ralls Corporation ("Ralls"), a Delaware corporation owned by two Chinese nationals, to unwind an acquisition and "divest itself" of its interests in four Oregon wind farm companies which were sited near a U.S. naval bombing range.[2]

The government has until August 29 to seek rehearing or rehearing *en banc* and, if it chooses not to seek such review, it must seek review in the Supreme Court of the United States by October 13.

The *Ralls* case arose in circumstances that are somewhat unusual for CFIUS. Typically, parties to a transaction that may be subject to

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1 50 U.S.C. app. § 2170(a)(3).

2 *Ralls Corp. v. Committee on Foreign Investment in the United States*, No. 13-5315, 2014 U.S. App. LEXIS 13389 (D.C. Cir. July 15, 2014). In addition to divesting itself of the assets, Ralls was required to undertake additional measures regarding installations undertaken during its ownership at the wind farm locations. *See* Slip op. at 8-11, 2014 U.S. App. LEXIS 13389 at *10-*12.

review by CFIUS submit a notice upon the signing of a letter of intent or a purchase agreement and the transaction is often subject to a closing condition that CFIUS approval be obtained. In *Ralls*, by contrast, the transaction had been consummated and notice was submitted to the Committee after the fact.

In this situation, held the Court of Appeals, Ralls already had acquired a state law-recognized property interest in the property that the President ordered to be divested and, accordingly, Ralls was entitled to due process in the CFIUS review. Specifically, in overturning the President's order, the court held that Ralls was denied its right to be notified of the non-classified evidence on which the Executive Branch sought to rely to deny approval for the transaction, and to have a fair opportunity to respond to that evidence.[3] The Court of Appeals rejected the government's contentions that (1) the DPA barred judicial review of the due process argument; (2) the risk of a presidential veto of the Ralls transaction meant Ralls had no protectable property interest; and (3) in any case, Ralls received the "process due" as Ralls had the opportunities to pre-clear the transaction before it was closed and to make a presentation to CFIUS before a final decision by the Executive Branch.[4] The court instructed CFIUS to provide Ralls with the process it was due, leaving the President on remand with only a limited defense to further disclosure based on the doctrine of Executive Privilege.[5]

Parties involved in a CFIUS review often perceive that process as a one-way flow of information to the government: they may meet with staff and then submit a draft notice, to be followed with a formal notice, after which they are required to respond to questions from CFIUS staff, though more informal meetings and exchanges may be possible. The decision-making process may seem less than fully transparent. The *Ralls* decision might encourage greater transparency and enhanced give-and-take with the government, to enable the parties to address any national security concerns implicated by foreign control of a business.

Nevertheless, the direct effect of the holding in *Ralls* is not clear, at least for most transactions notified to CFIUS. First, unlike in *Ralls*, parties generally submit notices to CFIUS before closing, where their property interests are contingent and, under the Court of Appeals' analysis, due process considerations may not apply. The court noted that, unlike circumstances where property interests are fully-vested, due process protections might not attach where the law providing the property right itself contains contingencies

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3 *Id*. at 47, 2014 U.S. App. LEXIS 13389 at *51.

4 *Id.* at 14-38, 2014 U.S. App. LEXIS 13389 at *20-*43.

5 *Id.* at 38, 47, 2014 U.S. App. LEXIS 13389 at *60, *74.

(as, more than 30 years ago, in the case of attachments of Iranian assets that originated as conditional federal licenses).[6]

Second, that parties may have new due process-mandated opportunities to interact with the government may not prove to be all that significant for most CFIUS reviews. The majority of the reviews result in CFIUS clearing transactions within the initial 30-day review period. Many of the rest are cleared within the subsequent 45-day investigation phase. Thus, the number of covered transactions where the government would have substantive security-related concerns, where the parties are unable or unwilling to agree to appropriate mitigation measures and where their having added transparency as to those concerns would provide a meaningful benefit may be relatively small.

*Ralls* may have significance to the larger field of property and investor rights, as well as constitutional, statutory and bilateral investment treaty protections for those rights. By recognizing that the existence of, and risks imposed by, CFIUS review are not contingencies that defeat investment-backed expectations or property rights conveyed by state law, the decision may strengthen the hand of investors vis-à-vis the government. Although the existence of property, at least for purposes of procedural due process, does not automatically mean that just compensation lies for its deprivation (or define the circumstances in which a taking occurs), the decision suggests that the government's interest in regulating private property, even to further national security, has limits.

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Please do not hesitate to contact us with any questions.

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[6] Slip op. at 31, 2014 U.S. App. LEXIS 13389 at *47 (citing *Dames & Moore v. Regan*, 453 U.S. 654 (1981)).