

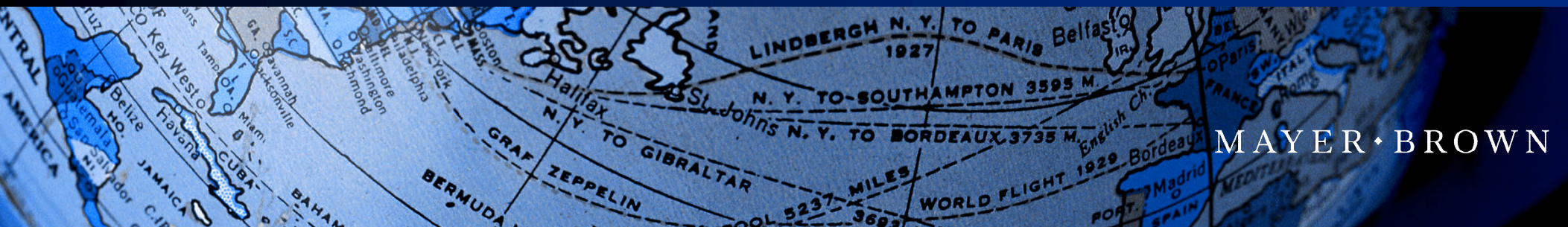
An Ocean Apart: The Regulatory Responses to Sovereign Wealth Funds by Europe and the United States

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Crans Montana Forum

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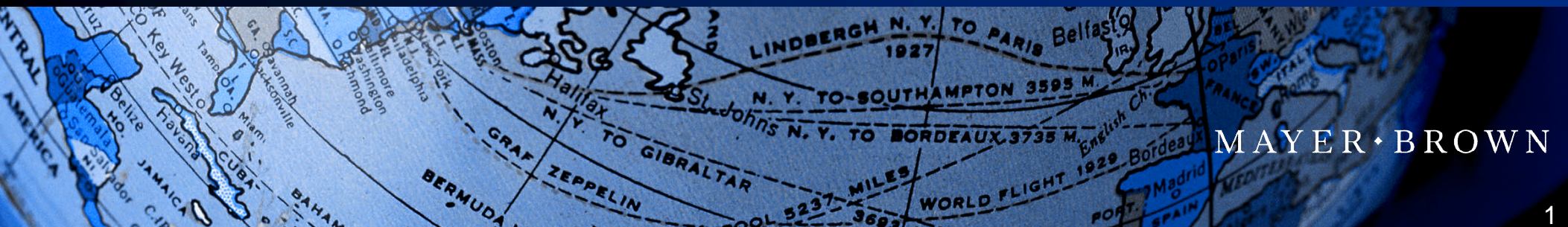
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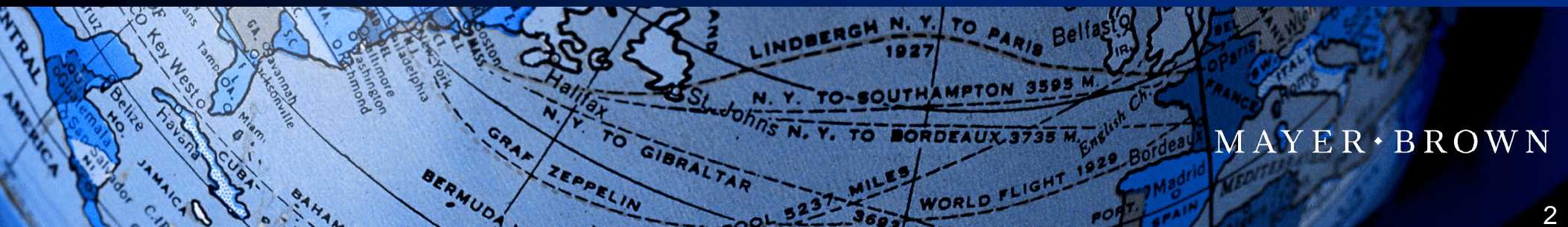
Introduction

- Growth in Number and Size of Sovereign Wealth Funds (SWFs) has Raised Concerns on Both Sides of Atlantic
- Threat of Market Distortion
- Threat to National Security
- Despite Similar Concerns, Regulatory Responses of Europe and the United States Have Been Strikingly Different



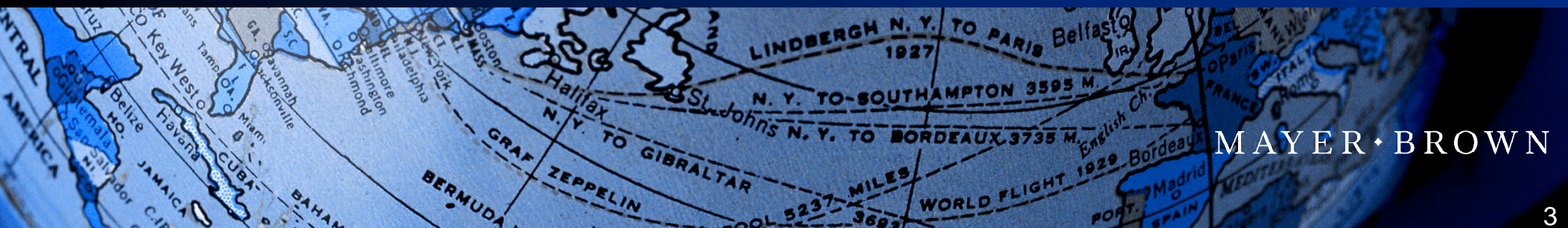
The Two Different Approaches

- The European Approach: Regulation that is Non-Mandatory but Targeted at SWFs
- The American Approach: Regulation that is Mandatory but Not Targeted at SWFs



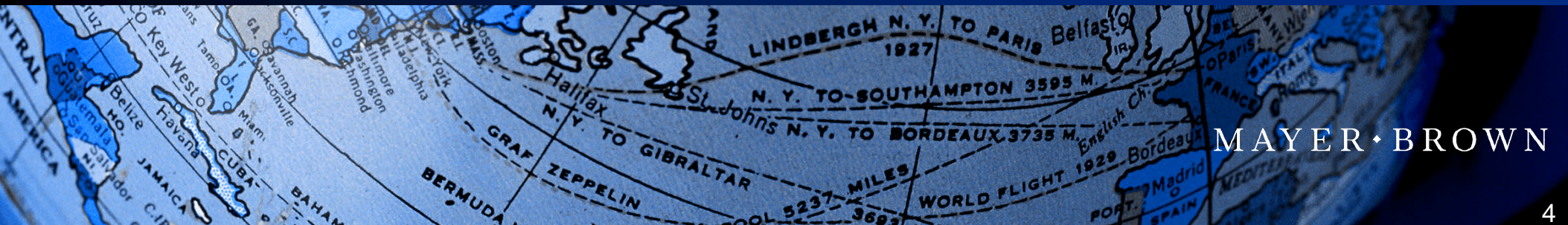
The European Approach : Premises

- SWFs are Different in Character from Other Foreign Government Instrumentalities
 - SWFs are Generally Less Transparent
 - Enhancing Transparency is Effective Antidote to Economic and Security Concerns
- Greater Transparency Should Be Encouraged, Not Mandated
 - Voluntary Regulation is Less Protectionist and Distortive of Capital Markets
 - SWFs, if Faced with Alternative of EU-Wide Voluntary Code or Prospect of Mandatory National Legislation, Will Opt for Code



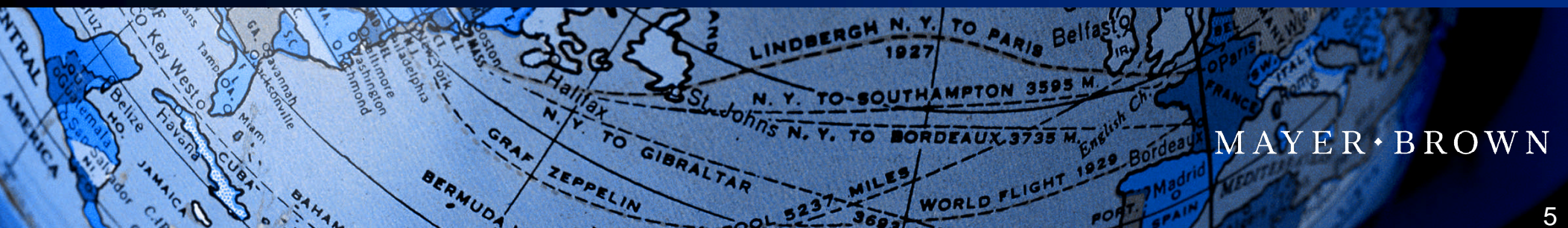
The European Approach : The Proposal

- Commission Proposal Seeks to Guide Routine Operations of SWFs Rather than Install Checkpoints for Investments
- Voluntary Code of Conduct Calls for Issuance of Policies and Disclosure of Information
- Policies to be Issued would Address Risk Management, Investment Objectives, Governance
- Information to be Disclosed would Address Investment Positions and Asset Allocation, Exercise of Ownership Rights, Use of Leverage, Composition of Assets by Currency, Size and Source of Resources, Home-Country Regulations and Oversight



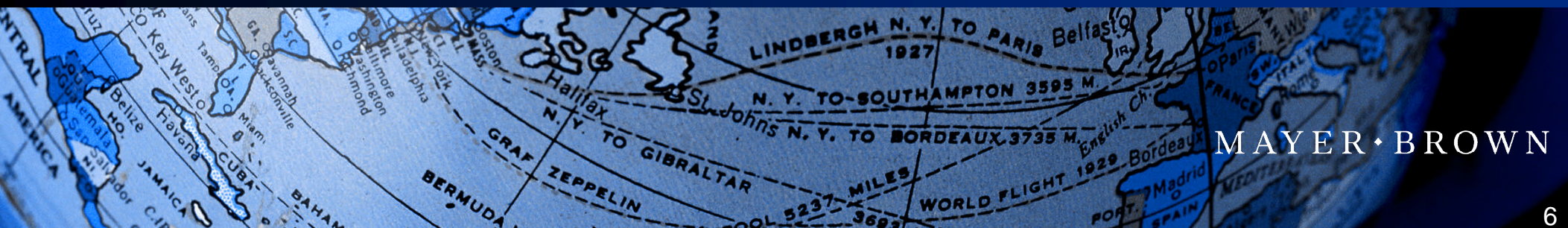
The American Approach: Premises

- Premises Underlying U.S. Approach are Opposite of Those Underlying European Approach
- SWFs are Not Materially Different in Character from Other Foreign Government Instrumentalities and Accordingly Do Not Call for Different Regulatory Response
 - Exon-Florio Amendment, Enacted in 1988, Already Authorizes President to Block Any Foreign Acquisition of a U.S. Business that Would Threaten to Impair the National Security
 - Exon-Florio Amendment Has No Provisions Specific to SWFs
 - Exon-Florio Amendment Makes No Distinctions Among SWFs Based on Their Transparency



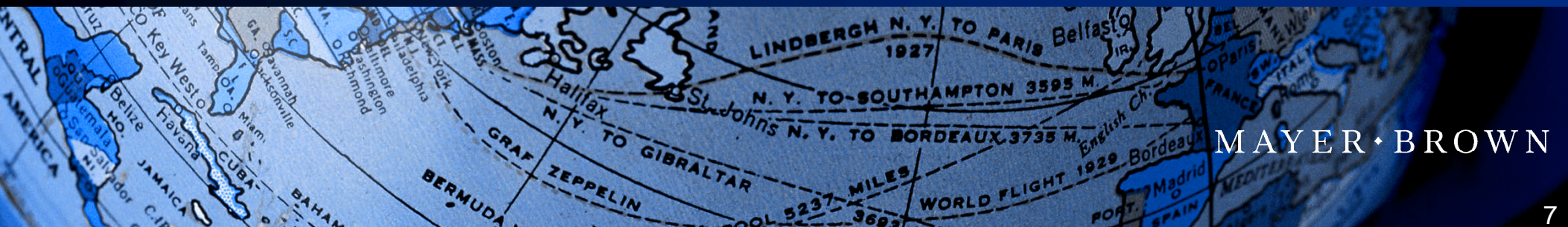
The American Approach: Premises (contd.)

- Mandatory, not Voluntary, Regulation Is Necessary
 - Dubai Ports World Controversy Strengthened U.S. Political Support for More Stringent Regulation of Foreign Government Investments
 - Exon-Florio Amendment was Substantially Revised in 2007 Specifically to Codify “Lessons Learned” from Dubai Ports World
 - Congress Having So Recently Legislated on Regulation of Foreign Government Investments, There is Less Appetite to Launch New Initiative on SWFs
 - No Political Support Exists for Supplanting Mandatory Exon-Florio Amendment with Voluntary Code



The American Approach in Practice

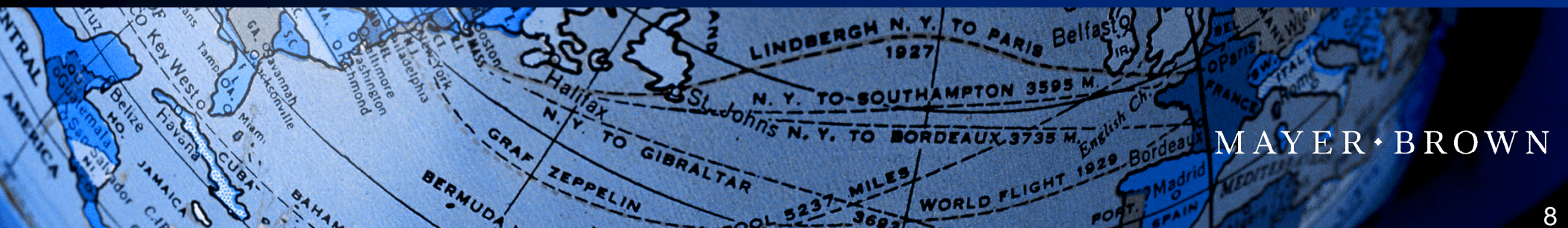
- Now Entering Third Phase in Two Decades of Application of Exon-Florio Amendment
- First Phase: Focus on Defense and Intelligence Sectors
- Second Phase (post-9/11): Scrutiny Extended to Critical Infrastructure, Telecommunications, Energy Sectors
- Third Phase (post-DPW): Greater Political Attention and Accountability
- Doubling of National Security Reviews of Foreign Acquisitions, 2005 to 2006
- Tripling of More Intense Investigations of Foreign Acquisitions, 2005 to 2006



The American Approach: Noteworthy Transactions

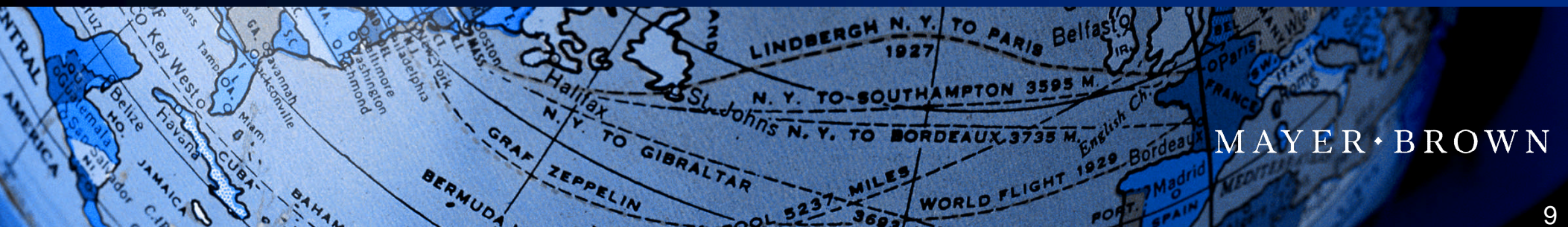
- 2006: Dubai Ports World/Peninsular and Oriental Steam Navigation Company.
 - DPW Forced to Sell U.S. Port Handling Business to U.S. Entity.
- 2005: China National Offshore Oil Corporation/Unocal.
 - Political and Popular Uproar Ended Deal before Parties Requested National Security Review.
- 2005: BAE/United Defense
 - British Acquisition Approved Pursuant to Longstanding Special Security Agreement.
- 2003: ST Telemedia/Global Crossing.
 - Singapore SWF Acquisition Approved, with Network Security Agreement Covering Physical, Logical, Information, and Personal Security, Overseen by a Board Security Committee.
- 2000: Nippon Telephone & Telegraph Company/Verio, Inc.
 - Approved, with Strict Ban on Japanese Government Involvement in Internet Service Provider Firm.
- 1990: China National Aero-Technology Import and Export Corporation/Mamco Manufacturing Company.
 - Only Transaction Ever Prohibited by the President on National Security Grounds.

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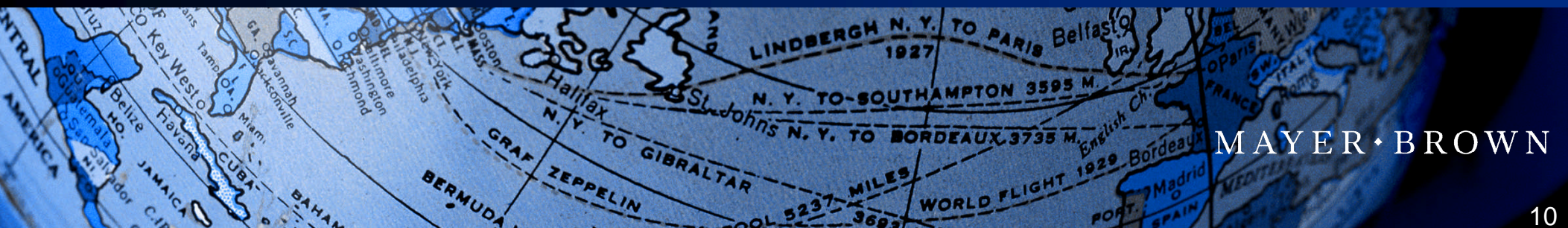
The American Approach: The Process

- The Test: Whether Acquisition of U.S. Business by Foreign Party “Threatens to Impair the National Security”
- Mandatory Notification If Foreign Government Ownership
- Confidential Consideration by Committee on Foreign Investment in the United States (CFIUS)
- 30/45/15-Day Stages of Review, Investigation, Presidential Decision
- Historically, Only Two Percent of Notifications Are Subject to Investigation Stage
- Frequent Manipulation of Deadlines Through Withdrawal and Resubmission of Notifications



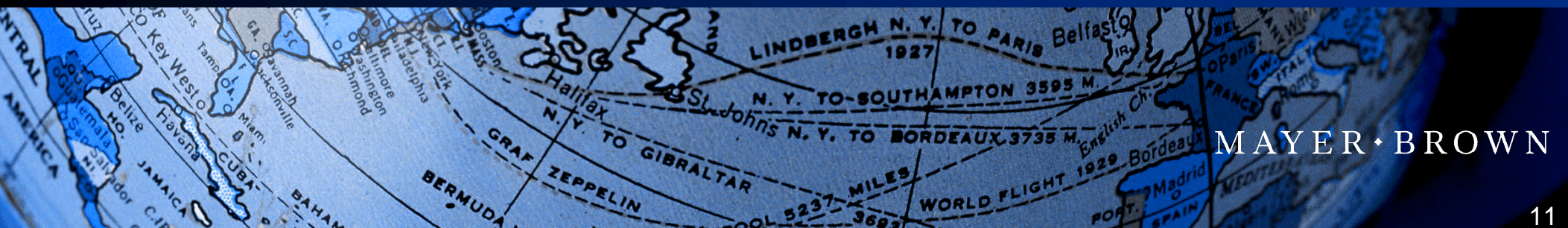
The American Approach: CFIUS Members

- Treasury (Chair)
- Defense
- State
- Commerce
- Justice
- Homeland Security
- Energy
- U.S. Trade Representative
- Office of Science and Technology Policy
- Non-Member Observers:
 - Office of Management and Budget
 - Council of Economic Advisers
 - Assistants to President for National Security, Economic Policy, Homeland Security



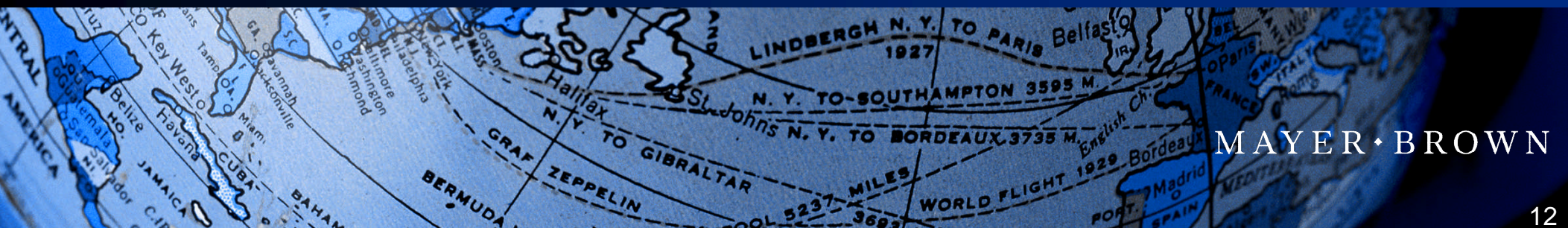
The American Approach, Phase 1: The Traditional National Security Criteria

- No Statutory Definition of “National Security”
- Statutory “Factors” That CFIUS “May” Consider Focus on Military Production and Preparedness
- CFIUS Regulations Focus on Whether U.S. Target Makes Goods and Technologies With Defense or Military End-Uses and Whether It Supplies the Defense Department or Military Branches
- CFIUS Regulations Also Focus on Whether Foreign Acquirer Plans to Move Production Offshore



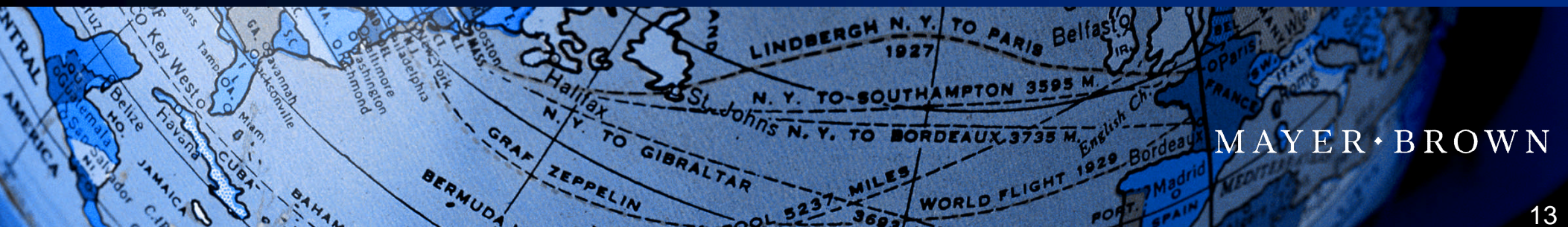
The American Approach, Phase 2: The New National Security Criteria

- Without Change in Statute or Regulations, CFIUS Expanded The Scope of Its National Security Scrutiny After 9/11
- Acquisitions in Industry Sectors Critical to Homeland Security — Telecommunications, Infrastructure, Energy — Are Now More Difficult
- National Security Credentials of Acquirer Are More Carefully Examined, Through Formal Threat Assessment by Director of National Intelligence



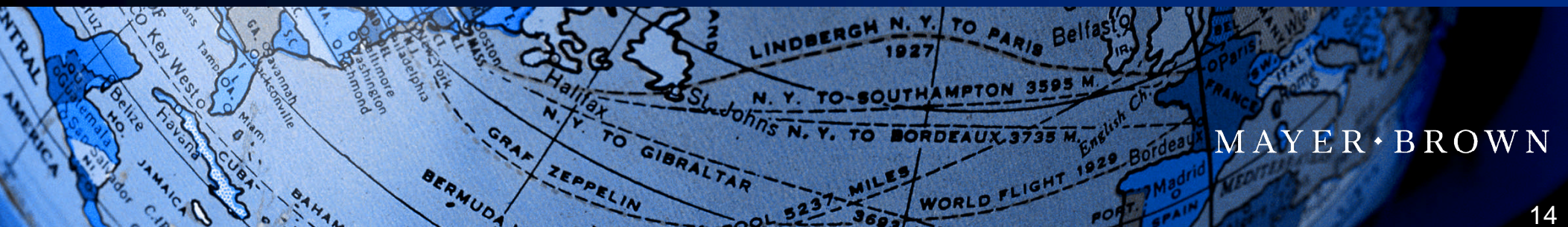
The American Approach, Phase 2: Borrowing Safeguards from NISP

- Increasingly, Safeguards That Had Been Required Only Under National Industrial Security Program (NISP) (for Targets with Classified Facilities) Are Being Demanded Generally in Acquisitions with National Security Implications
- Separate Boards of Directors Consisting of U.S. Citizens, Board Members and Management Approved by Department of Defense, Security Committees, and Special Security Agreements Are Among Structural Safeguards That Insulate Foreign Acquirer from Sensitive U.S. Operations



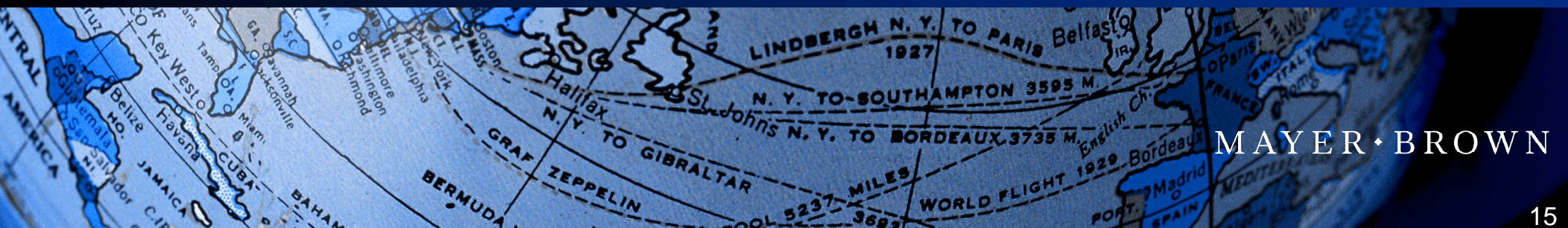
The American Approach, Phase 3: Legislative Response to Dubai Ports World

- Strengthen Political Accountability for National Security Screening of Foreign Acquisitions
- Codify Broader Criteria for Scrutiny
- Impose Mandatory Investigations Under Certain Circumstances
- Change the Structure of CFIUS
- Require CFIUS to Report More Fully and Frequently to Congress



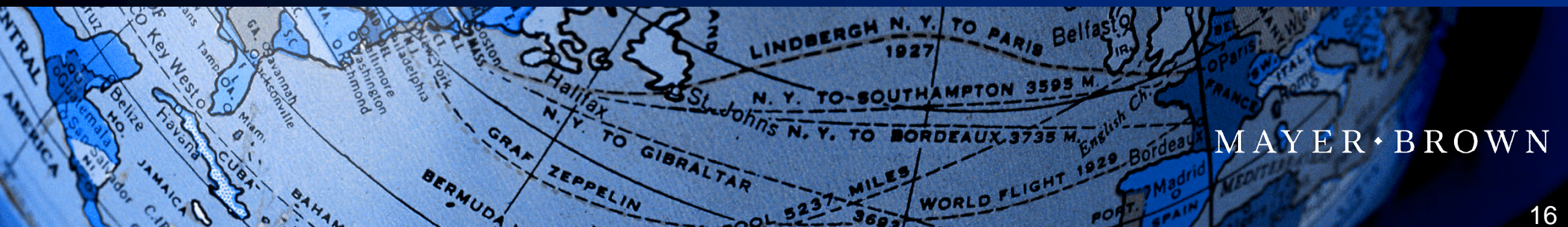
The American Approach, Phase 3: Extensive Amendments Enacted in 2007

- The Foreign Investment and National Security Act of 2007
- Lead Agency Must be Designated for Each Review to Take Charge of Mitigation Agreements and Compliance Monitoring
- 30-Day Review, With Approval at Assistant Secretary Level
- 45-Day Investigation Required If Transaction Involves Foreign Government or Threatens “Critical Infrastructure” or Threatens National Security or Lead Agency So Recommends
- Deputy Secretary of Treasury and Deputy Secretary of Lead Agency Can Jointly Decline Investigation Otherwise Required if No National Security Concerns



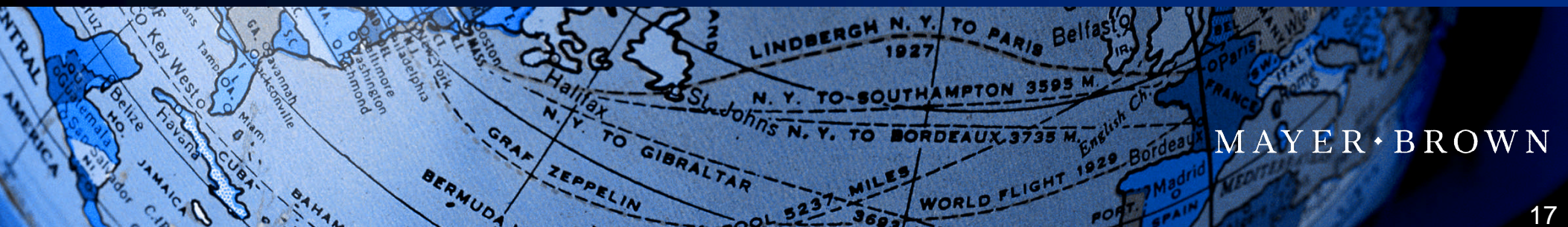
The American Approach, Phase 3: Extensive Amendments Enacted in 2007 (contd.)

- Assessment by Director of National Intelligence
- Required Consideration of Potential Impact on Energy Assets, Critical Technologies, Critical Infrastructure
- CFIUS Must Notify Congress Upon Conclusion of Each Review/Investigation
- Annual Reporting to Congress on CFIUS Activities
- Energy Department Added to CFIUS and Six Current CFIUS Members Removed – Fewer Pro-Business, Pro-Technology Agencies; USTR and OSTP Restored by Executive Order



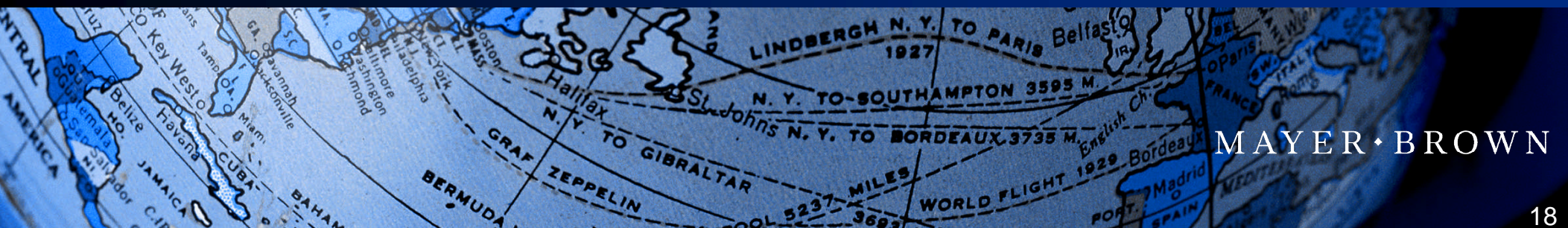
The American Approach, Phase 3: Impact of the New Amendments on SWFs

- Greater Political Oversight of National Security Reviews
- Less Dominance by Treasury Department
- More Frequent 45-Day Investigations
- Greater Scrutiny of Nationality and National Security Background of Foreign Acquirer
- Greater Scrutiny of Minority Interests by Governments
- More Common Reviews Beyond Defense Sector
- Greater CFIUS Sensitivity to Congressional Concerns
- More Frequent Imposition of Conditions on Acquisitions
- Heightened CFIUS Attention to National Security at Expense of Investment Promotion



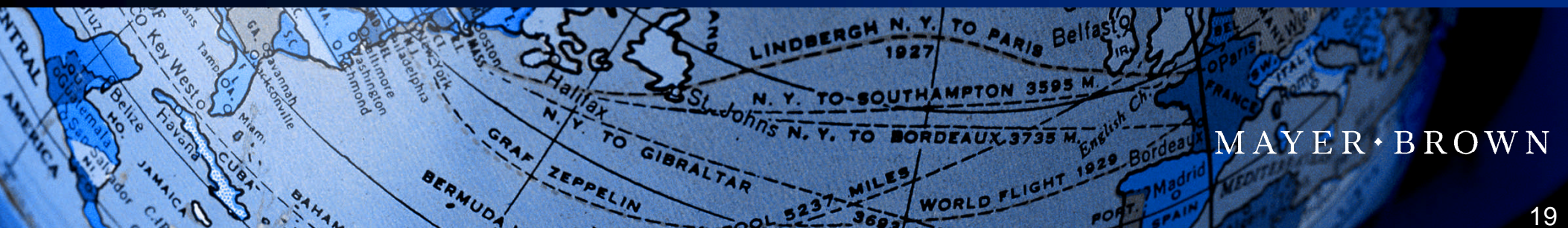
The American Approach, Phase 3: The Political Calculus

- Treasury: Business Case; Impact of Foreign Investment (Jobs)
- Defense: National Security; U.S. Industrial Base; Technology
- State: Non-Proliferation; Bilateral Relations
- Commerce: Export Controls; U.S. Industrial Base; Jobs
- Justice: Technology; Surveillance; Homeland Security



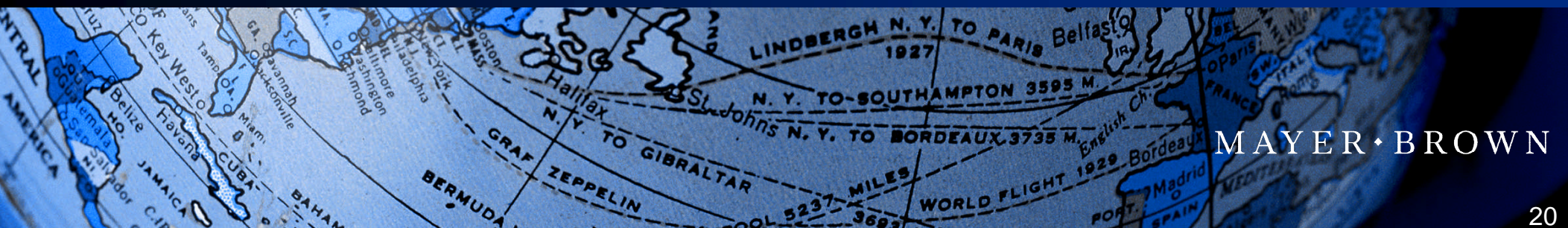
The American Approach, Phase 3: The Political Calculus (contd.)

- Homeland Security: Internal Security; Technology
- Energy: Energy Independence; Proliferation
- Congress: Economic Development In Home District or State; Political Sensitivity of Target or Acquirer
- White House: Impact on Relations with U.S. Allies, Congress; Impact on Presidential Priorities; Proximity to Next Election



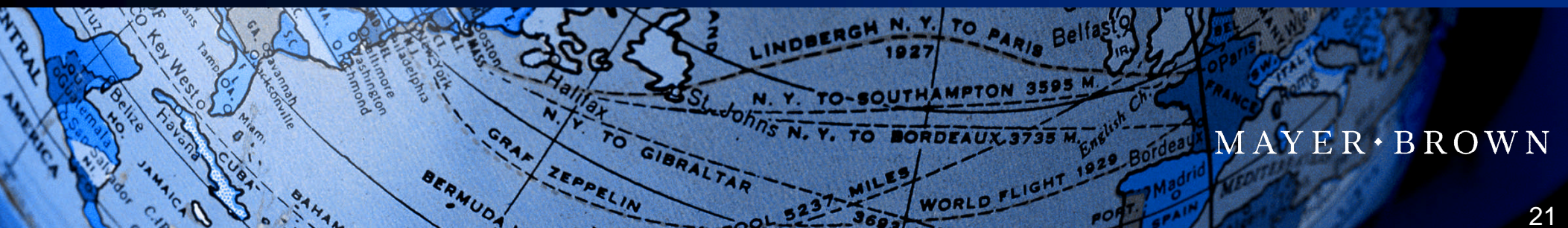
The American Approach: Mastering the New Environment for National Security Acquisitions

- Broader Consideration of the Appropriateness of Filing an Exon-Florio Notification
- Anticipation of More Searching and More Prolonged CFIUS Examinations
- Pre-Filing Consultations with CFIUS
- Earlier Introduction of Security Safeguards
- Anticipation of More Political Pressures



Prospects for Trans-Atlantic Convergence

- Although the Contrast between the European Approach and the American Approach is Stark, There is Some Evidence of Convergence
 - Denmark Has Stated that Voluntary Code Should be Prologue to Mandatory Regulation
 - EU Ambassador to United States Has Suggested that EU Create an Investment Review Body Like CFIUS
 - In the United States, Congress Has Held Hearings on SWFs and a Task Force Has been Formed to Consider Need for SWF-Specific Legislation
 - U.S. Treasury and SWFs of Abu Dhabi and Singapore Have Agreed to Voluntary Policy Principles
 - Both Europe and the United States Support the IMF Effort to Identify Best Practices for SWFs and the OECD Effort to Identify Best Practices for Recipient Countries



Prospects for Trans-Atlantic Convergence (contd.)

- Lessons to Be Learned on Both Sides of the Atlantic
 - In Refining Voluntary Principles for SWFs, EU May Take into Account that Opacity of CFIUS Process and Lack of Precise U.S. Definitions of “Control” and “National Security” Cause Market Distortion and Perceptions that Political Considerations Trump Economic Ones
 - New CFIUS Regulations, to be Proposed in Late April 2008, Present Early Opportunity for United States to Reflect on EU Articulation of Voluntary Code of Conduct

