

US Appellate Court Clarifies Due Process Rights for Parties Subject to CFIUS Review of Foreign Investments

The US Court of Appeals for the DC Circuit has reversed a lower court's ruling and held that companies undergoing review by the Committee on Foreign Investment in the United States (CFIUS or the Committee) have a due process right to notice of unclassified evidence and an opportunity to rebut that evidence. If the July 15 decision stands, it could significantly change the relationship between CFIUS, on the one hand, and the foreign investors and US businesses that seek its approval of acquisitions affecting US national security, on the other.

CFIUS is an Executive Branch committee chaired by the Treasury Secretary. It reviews transactions that could result in "foreign control" of US businesses, where such foreign control could threaten to impair the national security. In *Ralls Corp. v. CFIUS*, No. 13-5315, a US corporation owned by Chinese nationals (Ralls) challenged orders by CFIUS and the President blocking Ralls's acquisition of four US companies for the purpose of developing wind farms in Oregon.

Background

Following a notification submitted to CFIUS by the parties to the transaction, CFIUS determined that Ralls's acquisition of the companies threatened national security, so the Committee issued a temporary mitigation order (CFIUS Order) restricting Ralls's access to and ongoing construction at the windfarm sites, which are located in and around US Navy restricted

airspace and a bombing zone. In accordance with the Defense Production Act of 1950, the matter was then submitted to the President, who also determined that the transaction constituted a threat to national security. The President revoked the CFIUS Order and issued a permanent order (Presidential Order) prohibiting the transaction and requiring Ralls to divest itself of the companies. Neither the CFIUS Order nor the Presidential Order described the evidence upon which the national security threat findings were based.

Ralls challenged both the CFIUS Order and the Presidential Order in district court, alleging that the orders violated Ralls's rights under the Due Process Clause of the Fifth Amendment to the US Constitution. Specifically, Ralls claimed that neither CFIUS nor the President had provided it with the opportunity to review and rebut the evidence upon which the determination was based. Ralls also alleged that the CFIUS Order violated various requirements of the Administrative Procedure Act (APA).

The district court dismissed Ralls's claims regarding the CFIUS Order as moot because that order was revoked and replaced by the Presidential Order. It also dismissed Ralls's due process claims regarding the Presidential Order, concluding that Ralls had received all the process that it was constitutionally due. For additional background on the CFIUS review of Ralls's acquisitions and on Ralls's claims before

the district court, see our Legal Update of October 5, 2012.¹

The DC Circuit Opinion

Ralls appealed the district court's decision, and the DC Circuit reversed. First, despite language in the statute that expressly limits judicial review in the CFIUS context, the appellate court concluded that the relevant statute and related legislative history do not provide clear and convincing evidence that Congress's intent was to prevent judicial review of a due process challenge to the Presidential Order.

The text of the statute provides that "actions of the President under paragraph (1) of subsection (d) ... of this section shall not be subject to judicial review."² The "actions" referred to are "such action[s] for such time as the President considers appropriate to suspend or prohibit any covered transaction that threatens to impair the national security of the United States."³ While the final action (i.e., the order restricting the Ralls transaction) would be immune from judicial review under this provision, the court held that the provision did not limit the reviewability of a constitutional claim challenging the *process* preceding such presidential action.

Second, the appellate court rejected the government's argument that Ralls's due process challenge constitutes a non-justiciable political question (i.e., a matter of political discretion that by definition cannot be adjudicated by the courts). It held that Ralls's due process claim did not require the courts to review the *outcome* of the President's determination (i.e., the political question). Rather, it required the court to look at the *process* preceding that determination and to decide whether Ralls should have been given notice of, and access to, the non-classified evidence used to make the determination. The court found that such an analysis does not encroach upon the political discretion of the Executive Branch. It then turned to the merits of the claim.

The appellate court found that Ralls had a constitutionally protected property interest in the companies that it acquired under Oregon state law. The government had argued that Ralls's state-law property interests were not constitutionally protected because they were known to be "contingent" upon CFIUS review, pursuant to federal law. In rejecting this argument, the court noted that Ralls's property interests fully vested upon completion of the transaction, whereupon the due process protections of the US Constitution attached. The court also noted that Ralls did not waive this protection by failing to seek CFIUS's approval of the transaction before closing.

After finding that Ralls had a property interest that was protected by the Due Process Clause, the court turned to the question of what process is owed in such a case. It concluded that Ralls had a due process right to: (i) notice of the government's intended action; (ii) notice of the *unclassified* information upon which the government relied; and (iii) an opportunity to rebut that information. However, the court made clear that due process does *not* require the disclosure of *classified* information that supports official action.

The fact that Ralls was afforded the chance to present evidence to CFIUS and interact with CFIUS was deemed insufficient process because Ralls was not given the opportunity to craft its submissions to CFIUS to address its national security concerns or refute the factual basis underlying these concerns. The court suggested that adequate process at the CFIUS stage would also fulfill the due process obligations of the President.

On the question of access to unclassified information, the government, for the first time at oral argument, raised the possibility of invoking executive privilege on remand to shield the disclosure of certain unclassified information. The DC Circuit did not consider this question because it was not raised in the

government's brief. Rather, it left the question to be decided by the district court on remand.

Finally, the DC Circuit reversed the district court's holding that, because the Presidential Order revoked the CFIUS order, Ralls's claims regarding the CFIUS Order were moot. Instead, the DC Circuit held that Ralls's CFIUS Order claims fell under the "capable of repetition yet evading review" exception to mootness. First, the DC Circuit examined whether the CFIUS Order would "evade review" because it was too short in duration to be fully litigated in the US Supreme Court before it expired. The court noted that, as a general matter, Committee actions that are in effect less than two years cannot be fully litigated, and that, therefore, the CFIUS Order, which was in effect for only 57 days, would "evade review." Next, the court considered whether there was a reasonable expectation that Ralls would be subjected to the same action by CFIUS again. It concluded that such a reasonable expectation exists because Ralls intends to pursue other windfarm development projects in the United States.

Based on the foregoing findings, the DC Circuit remanded the case to the district court with instructions that Ralls be afforded the process outlined in its decision, including access to the unclassified evidence relied upon by the President and a chance to respond to such evidence. Moreover, because the district court had dismissed Ralls's claims on the CFIUS Order as moot, the DC Circuit directed the district court to consider the merits of these claims.

Next Steps

The government still has several options. First, it can request the DC Circuit to review *en banc* the three-judge panel's decision. Alternatively, or in addition (i.e., after failing to obtain relief from the *en banc* DC Circuit), the government can seek Supreme Court review of the panel's decision. Finally, the government can accept the remand to the district court and try to invoke

executive privilege as a shield against disclosing unclassified information to Ralls.

If the DC Circuit's decision (or portions of it) stands, the Ralls case will have important implications for any company subject to CFIUS review.

The remand of the merits of Ralls's claims on the CFIUS Order may have dramatic consequences for other companies undergoing CFIUS review. More companies undergo review at the Committee level than at the presidential level. Presidents have issued blocking orders only twice in the history of the CFIUS statute. Orders issued at the Committee level are now subject to judicial review regardless of whether there is subsequent presidential review. Perhaps more importantly, because CFIUS and not the President is subject to the APA, a wider range of legal claims can be brought against CFIUS orders than against presidential orders, such as alleged violations of APA requirements for reasoned decision-making and adequate evidence. Should the lower court on remand find that this CFIUS Order violates the APA, its decision could have a significant effect on the CFIUS process for all companies.

In addition, full implementation of the DC Circuit's requirements would insert significant new steps into the CFIUS review process. First, CFIUS would have to segregate non-classified information from the classified information upon which it relied to make decisions in each case, and provide the non-classified information to the parties to the transaction. Second, the parties would be able to respond to this information, either by rebutting particular facts or by tailoring the transaction to attempt to meet CFIUS concerns. Given that the Defense Production Act requires CFIUS to act on strict deadlines—an initial 30-day review, then a 45-day investigation, and finally a 15-day presidential review—adding these new steps to the process creates the risk of a backlog. Because CFIUS cannot change the statutory deadlines, the most likely point of delay would be the time

it takes CFIUS to deem a filing “complete,” which starts the statutory timelines.

These changes will likely benefit parties to transactions that raise significant security concerns with CFIUS, affording them insights into the government’s thinking not previously required to be shared, and also another opportunity to make their case. However, such additional procedural rights do not mean that CFIUS will come to a different substantive conclusion. In addition, the potential delays caused by such changes may harm parties to time-sensitive transactions.

All of these repercussions could be nullified, of course, if the DC Circuit’s decision is vacated or reversed.

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Endnotes

- 1 Available at <http://www.mayerbrown.com/President-Obama-Orders-Divestiture-of-Chinese-Investment-in-US-Wind-Farms-Investor-Mounts-Unprecedented-Legal-Challenge-10-04-2012/>.
- 2 50 U.S.C. app. § 2170(e).
- 3 Id. § 2170(d)(1).

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