WHEN THE TEMPEST SUBSIDES: INVESTMENT IN THE U.S. MARITIME SECTOR

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The economic crisis is far from over. But heartening signs have recently begun to appear, including indications of positive growth in some European nations, a healthier stock market in the United States, and heightened interest in new investments by some sovereign wealth funds. These hopeful trends may signal renewed interest in investing in the U.S. maritime industry. When evaluating a potential investment in the industry, the first issue investors usually consider is that of U.S. citizen ownership and control requirements. It is also important, however, to analyze the impact of other U.S. laws on the potential investment. This article reviews some new developments relating to foreign investment, as well as some existing restrictions relating to economic sanctions, that should be on everyone's radar screen.

For more than 20 years, the federal-level Committee on Foreign Investment in the United States (CFIUS) has reviewed foreign investment transactions involving foreign control for possible effects on U.S. national security. In late 2008, CFIUS issued new regulations[1] implementing changes to its prior procedures and practices required by the Foreign Investment and National Security Act of 2007 (FINSA). FINSA was adopted following several high-profile transactions that would have resulted in foreign control of various firms in the U.S. One of the most controversial of these was Dubai Ports World's acquisition in 2006 of Peninsular & Oriental Steam Navigation Company, a British firm that managed several important U.S. ports. Public debate surrounding this and other transactions indicated a certain level of wariness in Congress and the U.S. public concerning some investments by foreign firms, especially those linked to foreign governments.

The final regulations implementing FINSA expand greatly upon the earlier rules governing CFIUS reviews of transactions, describing in more detail both the CFIUS process and the voluminous information requested of parties notifying transactions to CFIUS. They also reflect FINSA's enhanced scrutiny of transactions that involve foreign government control or that relate to U.S. "critical infrastructure" (defined very broadly as systems or assets so vital to the U.S. that their incapacity or destruction would have a debilitating impact on national security).

Notwithstanding the many changes, the essentials of the prior CFIUS process were retained. First and foremost, CFIUS's jurisdiction continues to reach only those transactions involving a foreign person's acquisition of control of a U.S. business where the acquisition raises U.S. national security concerns. CFIUS's broad approach to control was also retained – and CFIUS is not necessarily bound by rules of other agencies as to what constitutes control. Although CFIUS typically gives considerable deference to the views of relevant regulatory agencies, CFIUS has found control in cases where foreign ownership was considerably less than 25 percent. Therefore, it is conceivable that CFIUS could find foreign control in cases that would not be deemed to constitute foreign control under maritime laws.

Other existing features remain intact: (1) notification by parties of transactions for CFIUS review continues to be voluntary; 2) CFIUS reviews are constrained by strict time limits (30 days for transactions that raise no issues and up to a total of 90 days for others); (3) CFIUS's focus remains on national security concerns rather than on broader economic or non-security interests; and (4) the President is the only person who can take action to suspend or prohibit a transaction, and only for national security reasons.

The new regulations set forth several general factors of interest to the maritime industry. First, the regulations make clear that loan transactions are not subject to CFIUS review except where, as a result of the loan, a foreign firm acquires rights in a U.S. business that are characteristic of an equity investment. In addition, investments considered to be start-up or "greenfield" transactions are not covered. Also, a safe harbor from CFIUS's expansive approach to control exists for transactions in which the foreign investor is acquiring less than 10 percent of voting interests and the transaction is solely for the purpose of passive investment. Various sovereign wealth funds ("SWFs") that took positions in U.S. financial institutions prior to the economic crisis reportedly made investments that would qualify for this passive investment exception. This could well be a favored approach for SWFs seeking future U.S. investments in various sectors, particularly in light of the greater post-FINSA scrutiny of transactions involving foreign government control.

A few examples illustrate some issues of particular relevance to the maritime sector. Going forward, any prudent foreign investor acquiring control of port management or port operations in the U.S. will want to give careful consideration to seeking CFIUS review. This is not only because of the Dubai Ports World matter or the emphasis in FINSA on critical infrastructure. It is also based on the important guidance that CFIUS issued in December 2008 concerning the types of transactions that have presented national security considerations in prior CFIUS reviews. The guidance stated that numerous businesses involved in transportation had been the subject of past reviews, and maritime shipping and port terminal operations were specifically cited as examples in the transportation sector. The CFIUS guidance also noted that a major source of prior reviews was transactions involving federal government contractors. Not every firm involved in transportation, of course, will present issues for CFIUS. A company that owns or builds ships used solely for fishing or hauling refrigerated food, for example, is less likely to present national security concerns. On the other hand, the acquisition of a U.S. shipping company that is a contractor to the U.S. military could easily implicate national security.

In addition to possible questions regarding initial acquisitions of U.S. firms, foreign companies operating in the United States – or considering doing so – must observe current U.S. economic sanctions enforced by the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC). These apply not only to U.S. individuals, wherever located, but also to any individual or company located in the U.S., regardless of how the company was acquired (e.g., by merger or as a start-up) or whether it is domestically or foreign controlled.

OFAC's current economic sanctions programs divide broadly into two categories: those focused on particular countries, including Cuba, Iran, North Korea, and Sudan; and those focused on designated organizations or individuals, who have been singled out because of their association with such activities as terrorism, narcotics trafficking, or the proliferation of weapons of mass destruction.

While all OFAC programs significantly affect dealings with the named countries, individuals, or firms, OFAC's robust Cuba sanctions and its vestigial North Korea program have specific prohibitions focused on the maritime industry.

The long-standing U.S. sanctions on dealings with Cuba affect vessels of all nationalities, if those vessels call at U.S. ports after touching in Cuba. Vessels that enter a Cuban port to trade goods or purchase services may not enter a U.S. port to load or unload freight for a period of 180 days following departure from Cuba. Also, vessels carrying goods or passengers to or from Cuba may not enter a U.S. port with those goods or passengers on board. Note that the well-publicized relaxation of Cuba sanctions announced by the U.S. in 2009 will ease restrictions on family travel, gifts, and remittances, and offers greater opportunities for telecommunications links between the U.S. and Cuba. They do not, however, involve any easing of the vessel restrictions.

The sanctions with respect to North Korea have been significantly reduced in recent years, but U.S. individuals and U.S.-located firms still are not permitted to register a vessel in North Korea or to own, lease, operate, or insure any vessel flagged by North Korea.

With respect to Iran and Sudan, OFAC's comprehensive sanctions programs contain specific provisions targeting the petroleum industry in each country (plus the petrochemical industry in Sudan). As a result, transportation of petroleum to and from those countries is of concern to OFAC. In 2008 OFAC – for reasons relating to Iran's proliferation activities -- prohibited U.S. persons generally from dealings with Iran's national maritime carrier, the Islamic Republic of Iran Shipping Lines (IRISL), and other affiliated entities.

Foreign companies as well as U.S. companies can be affected by these sanctions. For example, because the OFAC restrictions apply to all U.S. individuals, wherever located, a U.S. citizen employee of a foreign shipping company, even if residing outside the U.S., may not be substantively involved in the charter of one of the company's ships to carry oil to an embargoed country such as Cuba. Moreover, persons within the U.S., including U.S.-located offices of foreign firms, may not engage in any unauthorized facilitation outside the U.S. of economic dealings with the embargoed countries, such as brokering shipping services between a third country and Sudan.

The examples above demonstrate how two different but significant areas of U.S. law can affect investment in the maritime sector. Although the recent amendments to the CFIUS regulations are extensive, foreign firms – and their U.S. partners -- are unlikely to find that the changes will pose significant additional barriers to foreign investment. In the case of economic sanctions, both domestic and foreign investors need to remain as alert as ever to the requirements imposed by this favored instrument of U.S. foreign policy.

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[1] *73 Fed. Reg. 70702 (Nov. 21, 2008).*