INTRUDER ALERT! RUNNING THE REGULATORY GAUNTLET TO PURCHASE, OWN, AND OPERATE AMERICAN ENERGY AND MINERAL ASSETS BY FOREIGN ENTITIES

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I. INTRODUCTION

When should national security take preference over free market ideology? What may appear as two distinct topics—national security and an open investment policy—actually have been wedded together by terrorism, international corporate espionage, and "no holds barred" economic competition. In September 2012, the Foreign Investment and National Security Act of 2007 (FINSA)—a law packing a powerful and unreviewable presidential veto over specific purchases made by foreigners of domestic assets deemed "critical" and a law about which many Americans were completely unaware—made one of its rare, Godzilla-like appearances.[1] In this case, FINSA waded in to unravel a completed transaction involving a foreign entity investing along Oregon's shore in what became known as the "Ralls Decision."[2] Only twice in United States history has a President used FINSA to block a foreign investment entity for national security purposes.[3] National news coverage of both instances was instant and pervasive.[4]

Knowledge regarding this event rippled through the financial and legal communities, particularly among those who remembered the first such unraveling in the early 1990s, when President George H.W. Bush stopped a transaction involving military aircraft, reawakening memories of several "close calls."[5] For example, those in the oil and gas industry may have remembered a Dubai company's purchase of interests in United States ports that set off such

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1. Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246 (codified as amended at 5 U.S.C. § 5315 (2012), *amended by* Consolidated Appropriations Act of 2014, Pub. L. No. 113-76, 128 Stat. 5; 31 U.S.C. § 301 (2006); 50 U.S.C. app. §§ 2061 (2006 & Supp. 2011), 2170 (2006 & Supp. 2011)); *see infra* Part II.F.
2. *See infra* Part II.F.
3. *See infra* Part II.E, G.
4. *See infra* Part II.E, G.
5. *See infra* Part II.E, F.

clamoring that the Dubai company sold the assets to stave off the bad press and threat of future scrutiny.[6] Such incidents in the oil and gas field resonate even louder now with the continued advances in offshore oil and gas development in the Gulf of Mexico, the advent of shale hydrocarbons onshore, the rise in prices of precious metals, and a renewed interest in re-entering established fields with enhanced recovery techniques. Investors from outside the United States are not only looking with keen interest at American mineral resources, but also with puzzlement and worry at the laws and regulations that govern the purchase of the same.

While perhaps the single biggest barrier to foreign investment, FINSA is certainly not the only regulatory hurdle facing international investors looking to purchase, own, or operate American oil and gas interests.[7] Such investors must be careful, as both the federal government and individual state authorities have developed a myriad of constitutions, treaties, laws, and regulations that will affect—and in some cases prevent—foreign investment in American oil, gas, and mineral wealth.

Another concern for foreign investors is the different levels of the American government: a trifurcation of federal, state, and even local laws that can all affect, constrain, and even prevent foreign investment. Because the United States organizes its laws as a federalist system of state and federal laws, each of the fifty states has laws that vary according to regional priorities, and in some cases, according to legal influences prior to the territory joining the United States as a state.[8] Most relevant are differences among laws relating to hydrocarbons and mineral exploration, which in states with concentrations of such resources, can be directly contrary to traditional property laws that exist in other states (and even in mineral-rich states before such minerals' discovery). State laws regulate and, in some cases, restrict ownership of real property located in that state by non-residents, noncitizens, or companies organized outside the state.[9] Mineral rights such as oil and gas leases and permits, mining leases, and wind leases in the majority of states are derived from the mineral fee—a real property interest.[10]

Federal laws and treaties override state law if a conflict exists between the two. For example, even if a particular state's law provides for equal rights between a registered alien investor in a mineral right and a similar investor who

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6. David E. Sanger & Eric Lipton, *Bush Threatens to Veto Any Bill to Stop Port Takeover*, N.Y. TIMES (Feb. 21, 2006), http://www.nytimes.com/2006/02/21/politics/21cnd-port.html?_r=2&; *see infra* Part II.G.

7. *See generally* Frank B. Cross, *The Folly of Federalism*, 24 CARDOZO L. REV. 1 (2002) (discussing the federalist system's structure as it functions in the United States).

8. *See* John E. Kolb, *Foreign Investment in United States Oil and Gas Ventures*, 9 HOUS. J. INT'L L. 243, 245–52 (1987).

9. *See id.* at 246–48.

10. M. Craig Haase, *Mining Claim and Oil and Gas Leasehold Titles—Surface Inspection Requirements*, 26 ROCKY MTN. MIN. L. INST. 915, 922–49 (1980); Christianson Hartman, Comment, *Is the Wind Mine to Give Away? Guidance for Testators Wishing to Transfer a Wind Interest*, 1 EST. PLAN. & COMMUNITY PROP. L.J. 399, 407–11 (2009); Harold Hoffman, Comment, *Determination of Whether an Instrument Is a Lease or an Absolute Conveyance of Oil and Gas*, 25 TEX. L. REV. 157, 158 (1946).

is a United States citizen, a federal law that subjects only the alien investor to certain restrictions or scrutiny will preempt state law, effectively nullifying the promise of equality the state law attempted to provide. Different legal standards and procedures will apply under federal law depending on the type, location, and amount of assets sought, as well as the alien's home country and the laws therein.

This Article will examine the promulgation of statutory restrictions against foreign entity-controlled investments in the United States, as well as the two instances involving presidential denial of such transactions and their implications for the future of United States oil and gas development.[11] In some cases, purchasing United States oil, gas, and mineral real property has developed into an expensive endurance race that punishes ignorance.[12] The author's goal is to provide descriptions and analysis of federal and state laws that affect the purchase and ownership of oil, gas, and minerals in the United States to potential foreign investors and their domestic counsel.[13]

First, the general history and procedure of mineral exploration in the United States is covered with a discussion of the major federal acts that shape mineral development domestically.[14] Next, turning towards federal scrutiny of foreign investment in United States minerals, the history and development of the Committee on Foreign Investment in the United States and its weapon, FINSA, is discussed, along with an examination of some divestitures, sellouts, and related mitigations.[15] Subsequently, considering what happens after purchase, the International Investment Survey Act of 1976 is examined, as it delineates the nature of continued federal oversight of foreign entities and individuals owning domestic mineral real property and the responsibilities of those foreign owners.[16] Subsequently, several mineral-specific restrictions on foreign ownership at both the federal and state levels are described, followed by a review of the necessary technical levels and bonding requirements for foreign investors.[17] This Article concludes with brief reviews of the Territorial Land Act of 1887, the Trading with the Enemy Act, and the Foreign Investment in Real Property Tax Act of 1980.[18]

Several sections within this Article reference "alien corporations" and "foreign corporations." Alien corporations are entities incorporated or organized by laws other than state or federal laws of the United States. Foreign corporations are those entities incorporated or organized in one state and that are attempting to do business or own real property interests (which typically include mineral rights) in another state. On the federal level, this difference is

11. *See infra* Part II.A–G.
12. *See infra* Part II.C.
13. *See infra* Part II.
14. *See infra* text accompanying notes 22–65.
15. *See infra* Part II.A–G.
16. *See infra* Part II.H.1.
17. *See infra* Parts II.H.2–3.
18. *See infra* Parts II.H.2.a.i–ii, II.H.4.

important because a number of federal laws specifically target alien corporations. State laws are less likely to distinguish between alien corporations and foreign corporations. Generally, states simply require both kinds of entities to register to do business in the state.

In the United States, this federalist bifurcation broadly splits general categories of jurisprudence between state laws and federal laws, with each level being the primary source of coverage.[19] For example, despite continued federal encroachment, property law, criminal law, and enforcement of those laws are still generally within the realm of state law, while federal law typically covers relationships and transactions with international companies and persons. Because some states with long histories of oil, gas, or mineral development are leaders in mineral development and energy jurisprudence, this Article concentrates on the state laws of a few representative states instead of tracking the laws in all fifty states.[20] These states include New Mexico, Texas, Oklahoma, and Louisiana. The laws, regulations, and constitutions of these states are a focus of this Article.[21]

II. EXPLORING FOR MINERALS IN THE UNITED STATES—GENERALLY

In order to explore for minerals in the United States, one is generally required to acquire some kind of mineral right, lease, or other permit from the mineral owner. The United States is unlike most other countries in that states, private citizens, and corporations may own minerals, and indeed, currently own approximately 71% of the mineral acreage in the United States.[22] As stated, states may own minerals. Currently, the Texas General Land Office manages thirteen million acres of State-owned minerals.[23] Tribal nations of American Indians own minerals, often communally.[24] Foreign investors must be aware of the bifurcation between public and private mineral ownership in many parts of the United States.

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19. *See infra* Part II.H.2.a–b.

20. *See infra* Part II.H.2.b; *see also* Constitution Soc'y, *U.S. State Constitutions and Web Sites*, CONSTITUTION.ORG, http://www.constitution.org/cons/usstcons.htm (last updated Oct. 31, 2013) (providing the constitutions of the fifty states).

21. *See infra* Part II.H.2.b.

22. Dep't of the Interior, Bureau of Land Mgmt., *Public Land Statistics*, BUREAU OF LAND MGMT. (2012), *available at* http://www.blm.gov/public_land_statistics/pls12/pls2012.pdf. Federal public lands comprise almost 655 million acres, or about 29% of the total land area of the fifty states. *Id.* In addition, the United States has reserved 700 million acres of federal minerals, including reserved oil and gas rights to over 37 million acres of patented lands. *Id.*

23. TEX. GEN. LAND OFFICE, http://www.glo.texas.gov/what-we-do/state-lands/ (last visited Mar. 25, 2014).

24. *See Tribal Law*, INTERMOUNTAIN OIL & GAS BMP PROJECT, http://www.oildandgasbmps.org/laws/tribal (last visited Mar. 25, 2014).

Different public or private parties may own different types of minerals.[25] For example, the United States government may have reserved the coal when it patented (and initially granted) the land to private citizens. Then the patentee or its successor may have sold the oil rights to one party and the natural gas rights to another. In such a case, four different parties, public and private, separately own the coal, oil, natural gas, and all the other minerals. Minerals may be sold by depth, with the result that one party may own all the minerals above a certain depth while another party owns all the minerals below that depth, or the mineral tract may be subject to multiple horizontal severances.[26] Finally, given the fee title system that the United States inherited from Great Britain, one party may presently own the minerals while, upon the occurrence of a future event, another party may assume ownership or ownership may revert to earlier owners.[27] Needless to say, determining mineral ownership is sometimes a difficult, expensive, and time-consuming process.

Exploration for minerals without the necessary mineral rights given by the owner of the minerals in return for cash or royalties is considered trespass and subjects the interloper to civil action by the owner of the minerals.[28] Also, criminal liability may be a possibility, prosecuted by either the state where development took place (if the State or a private citizen or company owned the minerals) or the federal government (if federally owned minerals were involved).[29]

Actual production of the minerals exposes the trespasser to several theories of liability, such as actions for conversion and confiscation of production equipment.[30] Development of minerals owned by a state or the

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25. *See* F. Larry Leistritz & Stanley W. Voelker, *Coal Resource Ownership: Patterns, Problems, and Suggested Solutions*, 15 NAT. RESOURCES J. 643, 650 (1975).

26. *See* Timothy Fitzgerald, *Oil and Gas Leasing*, 5 MONTGUIDE, Oct. 2012, *available at* http://msuextension.org/publications/OutdoorsEnvironmentandWildlife/MT201209HR.pdf.

27. *See* T. P. Gallanis, *The Future of Future Interests*, 60 WASH. & LEE L. REV. 513, 514 (2003).

28. *See Subsurface Rights and Trespass Concerns a Frequent Issue in Texas Oil and Gas Industry*, LAW OFFS. OF GREGORY D. JORDAN, http://www.theaustintriallawyer.com/2011/10/subsurface-rights-and-trespass-concerns-a-frequent-issue-in-texas-oil-and-gas-industry/ (last visited Mar. 25, 2014).

29. *Id.* Most states, including Texas, recognize the difference between a "good faith" trespasser and a "bad faith" trespasser. *See id.* A good faith trespasser is one who has an honest and reasonable belief that he has the right to develop the minerals, but is mistaken. *See id.* An example is a developer who takes the mineral interest or lease from the wrong party after a reasonable (though erroneous) determination of the rightful owner. *See id.* A good faith trespasser is liable for the value of the minerals produced from the land but will be credited with any costs incurred from production, provided those costs conferred a benefit on the rightful owners of the mineral interest. *See id.* For example, the good faith trespasser will have to account to the mineral owner for all the money made from the sale of minerals but can first deduct from this amount the cost of drilling and production. *See id.* A bad faith trespasser is liable for the gross value of the production from the tract, without any deduction for costs. *See* Prize Energy Res., L.P. v. Cliff Hoskins, Inc., 345 S.W.3d 537, 557 (Tex. App.—San Antonio 2011, no pet.). A trespasser typically bears the burden of proving good faith. *See id.* Punitive damages can also be awarded against a bad faith trespasser. *See* Muehlstedt v. City of Lino Lakes, 473 N.W.2d 892, 898 (Minn. Ct. App. 1991). Questions of good faith or bad faith trespass on state or private lands are typically a matter of state case law. *See, e.g.*, *id.*

30. *See Subsurface Rights and Trespass Concerns a Frequent Issue in Texas Oil and Gas Industry*, *supra* note 28.

federal government without a mineral right may also subject the developer to various fines in addition to recovery by the authorities of the proceeds previously realized by the trespasser.[31]

A drilling permit of some kind is necessary in all states and on all federal lands for any significant drilling operation, including drilling for oil and gas or for disposing of contaminants.[32] Drilling and development without a drilling permit will subject the developer to fines and potentially the loss of any underlying mineral right.[33] All federal and state jurisdictions require some kind of drilling permit; on federal lands, the drilling permit is called an Application for a Permit to Drill.[34] The Federal Bureau of Land Management (BLM) is charged with examining applications and issuing permits for drilling.[35] Most filings are completed online.[36]

In the case of privately owned land, unless surveying activities included actions that would require a permit under any circumstances (such as the drilling of a test well for a check-shot survey or rock core samples or some other action that would require a State-issued permit), an oil and gas lease executed with the private landowner, when drafted with care, will contain all the necessary authority for the lessee to conduct reasonable surveys before drilling.[37]

On federal lands, the General Mining Law of 1872 (1872 Act) and the Mineral Leasing Act of 1920 (General Leasing Act) divide their coverage between "hardrock" minerals and coal and hydrocarbons.[38] The 1872 Act sets the rules for prospecting and mining hardrock minerals such as gold, silver, and copper on federal onshore lands, mainly in the American West.[39] The General

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31. *See id.*

32. *See*, *e.g.*, 16 TEX. ADMIN. CODE § 3.5 (2014) (Tex. R.R. Comm'n, Application to Drill, Deepen, Reenter, or Plug Back). Some states with significant oil and gas drilling activity possess more online resources than others. For example, in Texas, the Railroad Commission is charged with issuing drilling permits and maintains a clearinghouse of forms. *RRC Online System to File Forms*, RAILROAD COMMISSION OF TEX., http://www.rrc.state.tx.us/onlinefilings/rrconline.php (last visited Mar. 25, 2014) (requiring an application for password). The Railroad Commission also has an online manual for drilling permits and other operational concepts. *Drilling Permits: Online Filing User's Guide*, RAILROAD COMMISSION OF TEX. (May 28, 2008), *available at* http://www.rrc.state.tx.us/forms/publications/dp manual.pdf.

33. *See, e.g.*, 225 ILL. COMP. STAT. 725/8a (2007).

34. *See Oil and Gas Statistics*, BUREAU OF LAND MGMT., http://www.blm.gov/wo/st/en/prog/energy/oil_and_gas/statistics.html (last visited Mar. 25, 2014).

35. *Id.*

36. Federal applications for drilling permits are available on the United States Government Printing Office's Website. *See Electronic Code of Federal Regulations*, U.S. GOV'T PRINTING OFF., http://efcr.gov/cgi-bivtext-idx?SID=97822ac2b6060dd06948f9cc4652f4e&nodc=43:2.1.1.3.49&rgn=div5 (last visited Mar. 25, 2014).

37. *See, e.g.*, *Leasing for Oil & Gas in Ohio*, OHIO DEPARTMENT OF NAT. RESOURCES DIVISION OF OIL & GAS RESOURCES, http://oilandgas.ohiodnr.gov/citizens/leasing-information (last visited Mar. 25, 2014).

38. *See* Timothy Fitzgerald, *Understanding Mineral Rights*, 1 MONTGUIDE, Oct. 2012, *available at* http://msuextension.org/publications/OutdoorsEnvironmentandWildlife/MT 201207HR.pdf.

39. Act of May 10, 1872, ch. 152, 17 Stat. 91 (codified as amended at 30 U.S.C. §§ 29–30 (2012)); *see also The 1872 Mining Law*, GOLD PLACER, http://www.goldplacer.com/1872MiningLaw.htm (last visited Mar. 25, 2014) (providing the original text of the General Mining Law of 1872).

Leasing Act covers leasing of public lands for developing deposits of coal, petroleum, oil, natural gas, phosphates, and sodium on onshore and, as amended, offshore federal lands.[40] The federal government does not typically sell minerals.[41] Neither law applies to American Indian lands.[42]

The 1872 Act is used only for prospecting claims on federal onshore lands for gold, silver, copper, platinum, lead, zinc, molybdenum, uranium, and other placer minerals.[43] It is a leftover from the days of widespread individual prospecting and continues to this day.[44] The 1872 Act allows such prospectors to enter federal lands (except those federal lands that were purchased by federal authorities instead of being conquered) that have never been set aside for any other specific use and to claim lodes or placer deposits by claim staking their finds.[45] Generally, these minerals are "locatable" in that prospectors can go anywhere on federal lands where the 1872 Act is applicable, locate these minerals, and begin development operations if the law is followed.[46]

Surveying and prospecting is different under the 1872 Act and the Mineral Leasing Act.[47] The 1872 Act originally pertained to a wide range of minerals, including oil and natural gas, granted free access to people to develop such minerals in public domain lands, and established a claim–patent system.[48] The 1872 Act covers a range of hard rock minerals such as gold, silver, and copper, which can be prospected for, and claims laid upon, without any lease or permit first being issued.[49] The Mineral Leasing Act, however, set new regulations on oil, natural gas, oil shale, and coal, which resulted in removal of such materials and issues from the realm of the 1872 Act.[50] The Mineral Leasing Act provides notice and leasing rules for exploration and development of coal, oil, natural gas, and some other materials from federally owned lands.[51] Leases are secured by secret competitive bids.[52] Generally, these minerals are "leasable" in that a lease is required to explore for and develop them, and such exploration may

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40. Act of Feb. 25, 1920, ch. 1, 41 Stat. 437 (codified as amended at 30 U.S.C. § 181 et seq. (2012)).

41. 30 U.S.C. §§ 201 (2012), 226 (2012) (providing processes to govern acquisition of mineral leases on public lands).

42. William M. Foster, *Minerals and Allied Substances Available for Leasing or Similar Disposal*, 1B ROCKY MTN. MIN. L. FOUND. SPEC. INST. 1, 1 (1971).

43. 30 U.S.C. §§ 23 (2012), 35 (2012).

44. *See* Marc Stimpert, *Counterpoint: Opportunities Lost and Opportunities Gained: Separating Truth from Myth in the Western Ranching Debate*, 36 ENVTL. L. 481, 488 (2006).

45. *See* 30 U.S.C. §§ 22 (2012), 23, 35.

46. *See* 30 U.S.C. § 23 (listing minerals covered by the 1872 Act); Joel A. Ferre, Note, *Forest Service Regulations Governing Mining: Ecosystem Preservation Versus Economically Feasible Mining in the Natural Forests*, 15 J. ENERGY NAT. RESOURCES & ENVTL. L. 351, 354 n.12 (1955).

47. *See* source cited *infra* notes 48–57.

48. *See* 30 U.S.C. §§ 23, 35; Nev. Sierra Oil Co. v. Miller, 97 F. 681, 688–89 (C.C.S.D. Cal. 1899) (noting that the prior discovery rules of the 1872 Act apply to oil discoveries).

49. 30 U.S.C. §§ 22–23.

50. *See* 30 U.S.C. § 181 (2012) (listing oil as one of the minerals covered by the Mineral Leasing Act).

51. *See* 30 U.S.C. §§ 201 (a)–(b) (2012), 223 (2012) (providing rules that govern how to discover coal, oil, and gas).

52. *See* 30 U.S.C. §§ 201 (a)(1), 226(b)(1)(A) (2012) (setting out bidding procedures for coal, oil, and gas).

take place only on the lands covered by a lease or in a unit comprised of lands covered by several leases that have been approved by the federal government.[53] Surveying for "minerals" such as oil and gas and other materials covered by the Mineral Leasing Act requires either a lease to survey and develop or a formal notice, such as the Notice of Intent to Conduct Oil and Gas Exploration Operations.[54]

Meanwhile, with regards to BLM lands onshore, federal regulation allows a permittee to explore with geophysical surveys.[55] It does not apply to lands in the prospective coastal areas of the Arctic National Wildlife Refuge (ANWR-1002 lands) or to federal mineral estates where the overlying surface is privately owned.[56] Activities that are allowed include, but are not limited to, geophysical operations, geological surficial mapping, construction of roads and trails, and travel of vehicles over permitted lands.[57] The federal regulation "does not include core drilling for subsurface geologic information or drilling for oil and gas; these activities shall be authorized only by the issuance of an oil and gas lease" and a permit to drill.[58]

Airborne surveys such as those conducted for gravity and magnetic data, which do not interfere with surface operations and do not violate regulations of the Federal Aviation Administration, typically require no special permitting from the government.[59] Except for those surveys conducted for scientific purposes (which are covered under a separate permit), seafloor or surface surveys in the Outer Continental Shelf (OCS) require a commercial permit.[60] Notably, however, such commercial surveys may be conducted on federal OCS acreage that has already been leased to other parties.[61] Permits are also required for activities that include the use of explosives, such as seismic charges, drilling wells for core or check shot surveys, or "[d]eveloping data and information for proprietary use or sale."[62] Notices for the survey must be filed with the appropriate office of the Bureau of Ocean Energy Management (BOEM) and contain the required information.[63] While the survey is underway, the rules and

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53. *See* 30 U.S.C. §§ 181, 184(a)–(d) (2012) (setting out the minerals that can be leased and the limitations on leases under the Mineral Leasing Act).

54. *See* 30 U.S.C. § 223, 226; 43 C.F.R. § 3151.1 (2012).

55. 43 C.F.R. § 3150.0-1 (2012). The BLM's forms are typically promulgated by each of the several state and multi-state offices of the BLM; therefore, each BLM office may have its own online database. *See Utah: Forms, Regulations and Records*, BUREAU OF LAND MGMT., http://www.blm.gov/ut/st/en/prog/energy/oil_and_gas/forms_regulations.html (last visited Mar. 26, 2014).

56. *See* 43 C.F.R. § 3150.0-1(b)–(c).

57. *See* 43 C.F.R. § 3150.0-5 (2012).

58. *Id.* Drilling shot holes for seismic surveys is allowed. *Id.*

59. *See* 43 C.F.R. § 3150.0-1.

60. *See* 30 C.F.R. § 251.3 (2011). An online repository of forms for leasing and geological or geophysical surveys is available on the websites of the BOEM and the Bureau of Safety and Environmental Enforcement (BSEE). *See* BUREAU OF OCEAN ENERGY MGMT., http://www.boem.gov (last visited Mar. 26, 2014); BUREAU OF SAFETY & ENVTL. ENFORCEMENT, http://www.bsee.gov (last visited Mar. 26, 2014).

61. *See* 30 C.F.R. § 251.3.

62. 30 C.F.R. § 580.11 (2013).

63. 30 C.F.R. § 251.7(b) (2011).

protocols described in 30 C.F.R. § 251.6–.7 are in effect.[64] Drilling test wells requires a bond to be posted with the BOEM.[65]

Each state has its own rules about the permitting necessary for scientific or exploratory surveying on state lands or waters. For example, in Texas, the General Land Office will issue permits lasting ninety days, which can be extended in thirty-day increments. Such permitting attracts attention, however, so remember that while these surveys are underway, issuance of leases or permits within the permitted area will also continue. Therefore, when people discover that a geological and geophysical survey is being permitted and conducted, they may hurry to acquire leases or permits in the area.

A. CFIUS & FINSA

1. Committee on Foreign Investment in the United States (CFIUS)

The creation of the Committee on Foreign Investment in the United States (CFIUS) set the stage for the Ralls imbroglio. Established by President Gerald Ford's executive order in 1975, CFIUS is an interagency committee chaired by the Department of the Treasury within the Executive Branch.[66] It was initially formed to monitor the impact of foreign investment and control in the United States, review legislation related to foreign investment and control, review any investments that may impact United States national security, and coordinate the implementation of United States policy regarding foreign investment.[67] The committee consists of twelve members chaired by the Secretary of the Treasury.[68] The law requires a mandatory investigation of any transaction involving an entity "controlled by or acting on behalf of a foreign government."[69] Initially, CFIUS lacked its present authority to prevent or suspend foreign investment transactions in the United States.[70] Thus, CFIUS was initially an administrative agency that lacked regulatory power.[71]

Due to this lack of regulatory power, for over a decade CFIUS was mostly used as a watchdog group to "alert the government of potential problems with certain transactions."[72] Amid fears in Congress that the economy would suffer

64. *See id.*
65. *See id.*
66. Exec. Order No. 11858, 40 Fed. Reg. 20,263 (May 7, 1975).
67. *See id.* §1(b).
68. *See id.*
69. 31 C.F.R. § 800.214 (2012).
70. *Id.*
71. Kristy E. Young, Comment, *The Committee on Foreign Investment in the United States and the Foreign Investment and National Securities Act of 2007: A Delicate Balancing Act That Needs Revision*, 15 U.C. DAVIS J. INT'L L. & POL'Y 43, 46 (2008).
72. Maira Goes de Moraes Gavioli, *National Security or Xenophobia: The Impact of the Foreign Investment and National Security Act ("FINSA") in Foreign Investment in the U.S.*, 2 WM. MITCHELL L. RAZA J. 1, 6 (2011), *available at* http://www.web.wmitchell.edu/lawraza/wp-content/uploads/2011/03/FINAL-FINSA-for-Publication.pdf.

due to rising foreign investment, changes were initiated in 1988 with the passage of the Exon-Florio Amendment to the Defense Production Act of 1950.[73] Especially concerned with the threat of investment by foreign governments or entities controlling the defense industry contracts, Exon-Florio gave the President the right to suspend or prohibit mergers, acquisitions, or takeovers affecting national security that would result in "foreign control of persons engaged in interstate commerce."[74] Such actions must be based on "credible evidence that leads the President to believe that the foreign interest exercising control" could threaten national security and that other laws, in the President's opinion, do not adequately provide the President the ability to protect national security.[75] Also, "Congress sought to 'strengthen the President's power' while limiting that of Congress, thus emphasizing that 'the commercial nature of investment transactions should be free from political considerations.'"[76]

The Byrd Amendment to the Defense Production Act in 1993 further strengthened CFIUS.[77] This amendment mandated an automatic investigation by CFIUS when transactions involve "an acquirer that is controlled by or acting on behalf of a foreign government, if such acquisitions could affect [United States] national security."[78] Yet the Byrd Amendment did not grant CFIUS the authority to be a "gatekeeper" and demand notification of proposed transactions.[79] CFIUS still had to depend on the parties to a proposed transaction to voluntarily notify CFIUS for approval.[80]

This loophole caused some transactions that should have been subject to scrutiny to be missed because the transaction was not disclosed to CFIUS.[81] Companies were, therefore, encouraged to voluntarily report proposed transactions because of the "safe harbor" extended to transactions reviewed by

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73. Act of Sept. 8, 1950, ch. 932, 64 Stat. 798 (codified as amended at 50 U.S.C. app. §§ 2071–2172 (2006)). Section 2170 provides the Exon-Florio Amendment to the Defense Production Act of 1950. 50 U.S.C. app. § 2170 (2006 & Supp. 2011); *see* Ryan Peterson, Note, *Regulating the Global Marketplace: Why the U.S. Government Must Revise the Current Rules on Contracting with Foreign-Controlled U.S. Businesses*, 40 PUB. CONT. L.J. 1061, 1067 (2011).

74. Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418, § 5021, 102 Stat. 1107; *see* Deborah M. Mostaghel, *Dubai Ports World Under Exon-Florio: A Threat to National Security or a Tempest in a Seaport?*, 70 ALB. L. REV. 583, 601 (2007).

75. David N. Fagan, *The U.S. Regulatory and Institutional Framework for FDI*, 2 INVESTING IN THE U.S.: A REFERENCE SERIES FOR CHINESE INVESTORS 1, 10 (2008), *available at* http://www.vcc.columbia.edu/pubs/documents/FaganFinalEnglish_001.pdf (quoting 50 U.S.C. app. § 2170(d)(4)(A)) (internal quotation marks omitted).

76. Peterson, *supra* note 73, at 1068 (quoting JAMES K. JACKSON, CONG. RESEARCH SERVICE, RL 33388, THE COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES (CFIUS) 5 (2008), *available at* http://www.fas.org/sgp/crs/natsec/RL33388.pdf (updated Mar. 6, 2014)).

77. National Defense Authorization Act for Fiscal Year 1993, Pub. L. No. 102-484, § 837, 106 Stat. 2315, 2463–65 (1992) (amending 50 U.S.C. app. § 2170 (1988)).

78. Warren G. Lavey & Ivan A. Schlager, *U.S. Foreign Investment Act: Impact on Asian Companies*, ASIALAW (Sept. 2007), *available at* http://www.law.yale.edu/documents/pdf/cbl/US_Foreign_Invest _Act.pdf.

79. *Id.*

80. *Id.*

81. Mostaghel, *supra* note 74, at 602.

CFIUS.[82] Once CFIUS conclusively determined that a transaction did not threaten national security, it was subsequently shielded from further national security review by the Executive Branch.[83] Intended to be broad enough to allow the President flexibility to react to differing circumstances in each instance, the powers granted to the President by Exon-Florio include "broad injunctive and equitable relief, such as a prohibition on further stock purchases, the court-ordered divestiture of all or part of the acquired stock, imposition of civil penalties, and forfeiture of profits if needed to implement and enforce the statute."[84]

Before roughly 2007, energy transactions involving foreign-owned or foreign-controlled entities were both more routine[85] and not likely to be targeted for heightened CFIUS scrutiny.[86] Unless the energy transaction involved assets directly associated with the military or a market-controlling interest in a particular energy resource or source, it was typical that no submission for CFIUS review was made, as no national security concerns were commonly thought to exist.[87] In addition, if a submission were made, it generally passed review by CFIUS within the first thirty-day review phase.[88]

As the United States is the recipient of the largest amount of direct foreign investment in the world, purchase of strategic interests by foreigners has increasingly come into conflict with America's renewed sense of "national security" after the terrorist attacks on September 11, 2001.[89] In particular, the energy, water, and critical technologies sectors are some of the eighteen "critical infrastructures" that CFIUS aims to protect because of their essential function "to the minimal operations of the economy and government."[90] Also, because CFIUS was (and remains) ultimately under the direction of the

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82. National Defense Authorization Act for Fiscal Year 1993 § 837; Young, *supra* note 71, at 48–49.

83. *See* 50 U.S.C. app. § 2170(b)(1)(D) (2006 & Supp. 2011); U.S. GEN. ACCOUNTING OFFICE, GAO-NSIAD-96-12, NAT'L SEC. & INT'L AFFAIRS DIV., FOREIGN INVESTMENT: IMPLEMENTATION OF EXON-FLORIO AND RELATED AMENDMENTS 3 (1995), *available at* http://www.gao.gov/assets/230/221994.pdf.

84. S. REP. NO. 80, at 26–27 (1987).

85. *See generally* Leon B. Greenfield & Perry Lange, *The CFIUS Process: A Primer*, 6 THRESHOLD, no. 1, Winter 2005/2006, *available at* http://www.wilmerhale.com/files/Publication/98f0d23b-0510-47ef-a1a1-24f9dcb3752d/Presentation/PublicationAttachment/dc942fa3-988d-4959-b945-2b769eb99b7d/Greenfield_Lange_CFIUS_Process.pdf (providing an excellent examination of the CFIUS process just prior to the enactment of FINSA in 2007).

86. Joshua C. Zive, *Unreasonable Delays: CFIUS Reviews of Energy Transactions*, 3 HARV. BUS. L. REV. ONLINE 169 (2013), *available at* http://www.hblr.org/2013/04/unreasonable-delays-cfius-reviews-of-energy-transactions/.

87. *Id.* at 172.

88. *Id.* In fact, most submissions of any kind were passed over for "full" (i.e., longer than thirty days) CFIUS review from 1988 to 2005—the Congressional Research Service reported that of 1,500 transactions reviewed by CFIUS, only twenty-five underwent a "full" review. *Id.*

89. JAMES K. JACKSON, CONG. RESEARCH SERVICE, RL22863, FOREIGN INVESTMENT, CFIUS, AND HOMELAND SECURITY: AN OVERVIEW 1, 4 (2011), *available at* http://www.fas.org/sgp/crs/homesec/RS22863.pdf. "Direct foreign investor" means that an individual or corporation itself directly owns or invests in a foreign entity, in contrast to indirect investments that are obtained through mutual funds. *See id.* The United States is also the largest direct foreign investor. *Id.*

90. *Id.* (quoting 6 U.S.C. § 101(10) (2012)) (internal quotation marks omitted).

President, it was (and technically remains) limited in the investigation of covered transactions by the "guiding hand" of the President.[91] As described below, this power by the President may also unravel a deal with one fell stroke once CFIUS is on the case, and such Presidential invocation *may* coincide with elections or otherwise be shaded by politics.[92]

B. Foreign Investment and National Security Act (FINSA)

1. Coverage of Review

The most significant change to CFIUS came in 2007 with the passage of FINSA.[93] Acquisition by an alien entity of control over strategically important domestic assets such as oil and gas may also trigger FINSA.[94] The Exon-Florio provision, first implemented in 1988, gives the President the power to "suspend or prohibit any covered transaction," which is defined as "any acquisition, merger, or takeover" of a person engaged in interstate commerce by an alien entity if the President determines that the acquisition will threaten the national security of the United States.[95]

Under FINSA, the CFIUS review process has been codified and made much more rigorous.[96] It is important to note that FINSA's pre-notification provisions remain voluntary—the parties to a transaction are not required to obtain pre-acquisition clearance from any federal agency.[97] Although there is still no actual requirement that an alien entity seek CFIUS approval for a proposed transaction before it occurs, CFIUS monitors the media channels. If CFIUS gets wind of a transaction that it has not heard about that triggers its concern, CFIUS will ask the parties involved to submit an application and, if rebuffed, will likely start its own investigation.[98] CFIUS may suspend or even unwind any transaction after closing if it determines that the transaction represents a threat to "critical infrastructure"—which includes energy assets—by an alien party gaining "control" of the same.[99]

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91. *Id.*

92. *See infra* Part H.

93. Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246 (codified as amended at 5 U.S.C. § 5315 (2012), *amended by* Consolidated Appropriations Act of 2014, Pub. L. No. 113-76, 128 Stat. 5; 31 U.S.C. § 301 (2006)). FINSA became law in October 2007, and was followed by regulations published in April 2008. *See* 31 C.F.R. §§ 800.101–.801 (2013).

94. 50 U.S.C. app. § 2170 (2006 & Supp. 2011); *see* Edward L. Rubinoff & Tatman Ryder Savio, *CFIUS Implements FINSA Amendments to Exon-Florio Foreign Investment Law*, METROPOLITAN CORP. COUNS. 1, 33 (2008), *available at* http://metrocorpcounsel.com/pdf/2008/May/33.pdf.

95. 50 U.S.C. app. § 2170(a)(d). Specifically, in the rare occurrence CFIUS requests the President to rule on a proposed transaction, a report from CFIUS is sent, along with its recommendation of whether to allow or block the proposed transaction, and the President has fifteen days to act on the proposed transaction. *Id.* § 2170(b)–(d).

96. *Id.* § 2170(b)–(d).

97. *Id.* § 2170(b)(1)(C).

98. 31 C.F.R. § 800.401(b)–(c) (2013).

99. 50 U.S.C. app. § 2170(b)(2)(B)(i)(III).

Once an application is made to CFIUS, or if CFIUS instigates its own review, FINSA requires the parties to the transaction to address several concerns when seeking approval of an acquisition or merger.[100] First and most importantly, the foreign entity must address the extent to which the transaction will affect control of the nation's critical infrastructure in national security.[101] Based on the extent to which the transaction will impact this critical infrastructure, government regulators may impose a "mitigation agreement" on the parties seeking CFIUS approval for the transaction.[102] Before CFIUS is brought in, two threshold questions should be considered:

(1) Does the transaction give an alien entity control over a United States firm?

(2) Does the acquisition implicate interests that could be characterized as important for national defense?[103]

Considering the first question, what does "control" mean? When determining whether an entity is under foreign control, the applicable meaning of control appears to be that which CFIUS decides is appropriate.[104] First, no specific quantum of ownership exists to find a foreign investor in control.[105] In the Code of Federal Regulations, control does not rely on a majority stake in the business, but rather, is based on substantial shareholder approval rights or other influences.[106] The regulations promulgated under the Exon-Florio provision define control as the power to direct key matters affecting that firm—the power to sell off the corporation's assets, dissolve the firm, close its facilities, and terminate its contracts.[107] In addition, it is important to remember that seemingly benign relationships could trigger the law.[108] For example, a United States branch office or subsidiary of a foreign company may be deemed a United States person, and therefore, the statute could be applied if a different foreign entity acquires the domestic subsidiary.

While FINSA generally codified the Treasury Department's existing CFIUS regulations, it also better defined the review process of covered transactions and mergers.[109] A covered transaction is defined as any transaction by or with any foreign person that could possibly result in foreign control of a

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100. *Id.* § 2170(b)(2).

101. *Id.*

102. *Id.* § 2170(l)(1).

103. *Id.* § 2170(b)(2)(B).

104. 31 C.F.R. § 800.204 (2013); *see* Christopher M. Weimar, *Foreign Direct Investment and National Security Post-FINSA 2007*, 87 TEX. L. REV. 663, 673 (2009).

105. *See* 50 U.S.C. app. § 2170(a)(2); Rubinoff & Savio, *supra* note 94, at 33 (discussing FINSA amendments).

106. 31 C.F.R. §§ 800.204, .302 (2013); *see* Lavey & Schlager, *supra* note 78, at 67.

107. 31 C.F.R. § 800.204.

108. *See, e.g.*, 31 C.F.R. §§ 800.221 (2013), 800.226 (2013).

109. *See* Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246 (codified as amended at 5 U.S.C. § 5315 (2012), *amended by* Consolidated Appropriations Act of 2014, Pub. L. No. 113-76, 128 Stat. 5; 31 U.S.C. § 301 (2006)).

United States company.[110] FINSA now requires CFIUS to review all applications for foreign covered transactions and to investigate any foreign covered transactions that subsequently come to its attention through other means and raise initial concerns. CFIUS is required to determine whether the transaction threatens national security, a party to the transaction is a foreign entity, or the transaction could lead to foreign "control of any 'critical infrastructure that could impair the national security.'"[111]

Types of transactions ineligible for review by CFIUS, as designated by FINSA, include transactions made solely for the purpose of investment, such as real estate ventures or passive investments by foreigners.[112] Passive investments in the oil and gas context, while not described in FINSA, arguably include those types of assets and activities excluded from triggering the need to domesticate in the state where the assets or activity are located or take place. Examples could include the purchase and ownership of royalty interests in oil and gas leases, but would exclude non-operated leasehold working interests as nonpassive.[113]

By leaving certain terms undefined—such as "national security" and "control"—in the Exon-Florio Provision or FINSA legislation, Congress allowed CFIUS to have the power to allow definitions to be "interpreted broadly without limitation to a particular industry."[114] As guidance for CFIUS, however, Exon-Florio originally included factors that CFIUS should consider in determining whether a transaction involved a national security risk.[115] These include:

> (1) The domestic production needed for projected national-defense requirements;
> (2) the capability and capacity of domestic industries to meet national-defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services;
> (3) the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the U.S. to meet the requirements of national security;
> (4) the potential effects of the transaction on the sales of military goods, equipment or technology to a country that supports terrorism or

110. 50 U.S.C app. § 2170(a)(3).
111. JAMES K. JACKSON, CONG. RESEARCH SERVICE, RL33312, THE EXON-FLORIO NATIONAL SECURITY TEST FOR FOREIGN INVESTMENT 1, 11 (2013) [hereinafter JACKSON, EXON-FLORIO].
112. *Id.*
113. *Cf. id.*
114. Joshua W. Casselman, Note, *China's Latest 'Threat' to the United States: The Failed CNOOC-UNOCAL Merger and Its Implications for Exon-Florio and CFIUS*, 17 IND. INT'L & COMP. L. REV. 155, 157 (2007) (quoting JAMES K. JACKSON, CONG. RESEARCH SERVICE, RS22197, THE EXON-FLORIO NATIONAL SECURITY TEST FOR FOREIGN INVESTMENT 2 (2005) (updated Feb. 23, 2006)) (internal quotation marks omitted).
115. Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418, § 5021, 102 Stat. 1425.

proliferates missile technology or chemical and biological weapons; and

(5) the potential effects of the transaction on U.S. technological leadership in areas affecting U.S. national security.[116]

Following the passage of FINSA, Congress added six new factors to guide CFIUS in formal investigations.[117] An incident that heightened congressional awareness was the "proposed acquisition of U.S. port terminals by a Dubai-based company," described below, which passed through CFIUS without investigation.[118] The new factors include the following:

[1] the potential national-security related effects on United States critical infrastructure, *including major energy assets*;
[2] the potential national-security related effects on U.S. critical technologies;
[3] whether the covered transaction is a foreign government-controlled transaction;
[4] the subject country's adherence to nonproliferation control regimes and its relationship with the United States, specifically its record on cooperating in counter-terrorism efforts (as appropriate);
[5] the long-term projection of U.S. requirements for sources of energy and other critical resources and material; and
[6] other factors the President or the Committee may determine to be appropriate.[119]

"Critical infrastructure" is now defined to include "systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems or assets would have a debilitating impact on national security."[120] FINSA's expansion to include these six factors has made CFIUS scrutiny considerably more robust. In particular, however, the addition of the words "including major energy assets" has placed the energy sector in the problematic position of being the only industry specifically mentioned as an example of critical infrastructure.[121] One practitioner familiar with the Sisyphean methods of CFIUS believes that this direct reference to energy assets is troublesome because "spotlighting energy assets has both compelled more

116. Weimar, *supra* note 104, at 673 (quoting Omnibus Trade and Competitiveness Act of 1988, 102 Stat. at 1107).

117. *Id.*

118. Peterson, *supra* note 73, at 1068 n.52.

119. Weimar, *supra* note 104, at 674 (emphasis added) (quoting Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246, 253–54 (codified at 50 U.S.C. app. § 2170 (2006 & Supp. 2011)).

120. *Id.* (quoting Foreign Investment and National Security Act of 2007 § 2(a)(6)) (internal quotation marks omitted). "Critical technologies" are, in contrast, defined as the "critical components, or critical technology items essential to national defense." *Id.* (quoting Foreign Investment and National Security Act of 2007 § 2(a)(7)) (internal quotation marks omitted).

121. *See* Zive, *supra* note 86, at 172.

parties involved in international energy transactions to file CFIUS notices in order to contain the risk of subsequent CFIUS review of those transactions and has resulted in those notices facing longer delays as a result of the FINSA provisions."[122]

C. Consultation, Pre-Notices, and the Timing of Review

The CFIUS review process begins with a "triggering event"—typically a voluntary filing by the interested parties before the proposed transaction is closed—but can be initiated even after the transaction's completion by any CFIUS member agency.[123] After the triggering event, an initial review period of thirty days to investigate the transaction follows, ending in a determination to either cease the investigation or continue the investigation into the transaction, up to a maximum of an additional forty-five days.[124] In the event of such a continued investigation, the President is required to announce a final decision within fifteen days of receiving CFIUS's final recommendation to either allow or deny the transaction.[125]

Before FINSA, parties contemplating a foreign transaction could file the voluntary notice of the transaction with CFIUS, and if the notice was completed according to the regulations, the thirty-day notice period would automatically begin upon CFIUS's receipt of the report.[126] After FINSA, CFIUS changed the regulations so that pre-filing "consultations" and "draft notices" took up a formal mantle.[127] Specifically, CFIUS has now stipulated that parties seeking CFIUS consideration are encouraged to both consult with CFIUS before filing their notice and to file draft notices at least five business days before filing their formal notice in appropriate cases.[128]

Both the consultation and the draft notices are ostensibly to assist CFIUS with its work, to streamline the process overall, and to prevent ugly surprises after the formal notice has been filed. Functionally, however, attorneys familiar with current CFIUS practice claim that the consultation process and pre-filing notices are now effectively mandatory and can delay the approval process.[129]

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122. *Id.* at 172–73.

123. *See* Weimar, *supra* note 104, at 672.

124. *See id.* An investigation not exceeding forty-five days must be conducted if "the transaction threatens to impair the national security of the United States and that threat has not been mitigated during or prior to the review of a covered transaction . . . ; the transaction is a foreign government-controlled transaction; . . . the transaction would result in control of any critical infrastructure," such as energy assets, that CFIUS determines could impair national security; or "the lead agency recommends, and [CFIUS] concurs, that an investigation [should] be undertaken." 50 U.S.C. app. § 2170(b)(2)(B) (2006 & Supp. 2011).

125. *See* Weimar, *supra* note 104, at 672.

126. *See* Mostaghel, *supra* note 74, at 594.

127. *See* Zive, *supra* note 86, at 173; *Committee on Foreign Investment in U.S.: Filing Instructions*, U.S. DEPARTMENT OF THE TREASURY, www.treasury.gov/resource-center/international/foreign-investment/Pages/cfius-filing-instructions.aspx (last visited Feb. 25, 2014).

128. *See* Zive, *supra* note 86, at 173 (citing 31 C.F.R. § 800.401(f) (2013)).

129. *See id.*

The draft notices must now essentially meet the criteria approved by CFIUS beforehand or CFIUS will reject the formal notice and the actual review process will not begin.[130]

All of these new requirements mean that significant time may be added to the approval process.[131] In addition to the forty-five day delay that may impact the review of transactions potentially affecting critical infrastructure, further delays caused by the continued back-and-forth between parties to a proposed transaction and CFIUS in the pre-filing consultation or draft notice stage are now common.[132] These delays are not definitively measureable, and their occurrence and length may be difficult to predict.[133] This fact, when combined with the price-sensitive nature of large transactions involving energy-related commodities and the properties associated therewith, could lead to attempts at re-trading the deal between the parties as delays continue, or even the cancellation of a transaction.[134] Furthermore, while parties to a proposed transaction—who are generally spread out over the globe—scramble to deliver requested information regarding energy assets—also often spread out—the thirty (or seventy-five) day time limit is not initiated, meaning CFIUS is not under any express time limit to decide the fate of the transaction.[135]

Concern has been raised that the additional forty-five day review period, which originally was triggered only when CFIUS found that national security risks made additional review necessary, has now become a fact of life for those seeking review of a transaction involving energy assets.[136] FINSA now requires the forty-five day additional investigation period "for any transaction that 'would result in control of any critical infrastructure of or within the United States' . . . if that transaction could 'impair national security.'"[137] Given the broad scope of critical infrastructure, virtually any transaction involving energy assets can be argued to impair national security.[138] This means that, as reported by those in practice, the "standard" length of CFIUS's analysis of an energy transaction has effectively been raised from thirty days to seventy-five days.[139]

D. Agencies Involved in FINSA Reviews

The compositions of the agencies that work with CFIUS greatly affect investigation timing and results. After the passage of FINSA and a subsequent

130. *See The Committee on Foreign Investment in the United States (CFIUS)*, U.S. DEPARTMENT OF THE TREASURY, http://www.treasury.gov/resource-center/international/Pages/Committee-on-Foreign-Investment-in-US.aspx (last visited Mar. 26, 2014).

131. *See* Zive, *supra* note 86, at 174.

132. *See id.*

133. *See id.* at 174–75.

134. *See id.* at 173.

135. *See id.* at 174–75.

136. *See id.* at 174 (quoting 50 U.S.C. app. § 2170(b)(2)(B) (2006 & Supp. 2011)).

137. *See id.*

138. *See id.* at 174–75.

139. *See id.* at 172.

Presidential Order by George W. Bush, CFIUS is currently comprised of the following members:

(1) the Secretary of the Treasury;
(2) the Department of Justice;
(3) the Department of Homeland Security;
(4) the Secretary of Commerce;
(5) the Secretary of Defense;
(6) the Secretary of State;
(7) the Department of Energy;
(8) the Office of the United States Trade Representative;
(9) the Office of Science & Technology Policy; and
(10) Any other office determined necessary by the President on a case-by-case basis.[140]

The Secretary of Labor and the Director of National Intelligence are non-voting, ex-officio members of CFIUS.[141] The Secretary of the Treasury acts as the chairman for CFIUS and has the authority to name one or more CFIUS members to be the "lead" agency or agencies acting on behalf of CFIUS for (i) each covered transaction and for negotiating any mitigation agreements, as described below, or other conditions necessary to protect national security; and (ii) for all issues regarding the future monitoring of entities involved in the completed transaction, to ensure compliance with the mitigation agreement.[142] If the Secretary of the Treasury requests, the Director of National Intelligence must conduct an independent review of all covered transactions to determine whether they pose a danger to national security.[143] FINSA also requires an annual report from CFIUS to Congress.[144] The main purpose of this report is to notify and direct Congress as to the existing standing of foreign ownership and control of critical domestic assets.[145] Because CFIUS was created by executive order, however, it is controlled by the President, rather than Congress.[146]

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140. Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246, 252 (codified at 50 U.S.C. app. § 2170(k)(2)); *Composition of CFIUS*, U.S. DEPARTMENT OF THE TREASURY, http://www.treasury.gov/resource-center/international/foreign-investment/Pages/cfius-members.aspx (last visited Mar. 26, 2014); *see* Exec. Order No. 13456, 73 Fed. Reg. 4,677 (Jan. 23, 2008).

141. *Composition of CFIUS*, *supra* note 140.

142. Foreign Investment and National Security Act of 2007 § 3.

143. *Id.* § 2.

144. *Id.* § 7. The report must include (a) a list of all notices and investigations, basic information about the business and its structure, as well as any decision or action by the President regarding the listed business; (b) trend information on the number of filings made with CFIUS and their country of origin; (c) information regarding whether companies withdrew notices to CFIUS that have been re-filed or abandoned at a later date; (d) the types of security conditions that CFIUS has used to mitigate national security concerns about a transaction, including a discussion of the methods that the Committee and any "lead" agency—as designated by CFIUS—are using to determine compliance with such arrangements or conditions; (e) and a detailed discussion of all perceived adverse effects to national security or critical infrastructure to the extent possible. *Id.*

145. *See id.*

146. *See* Exec. Order No. 13456, 73 Fed. Reg. 4,677 (Jan. 23, 2008).

FINSA gives CFIUS the power to mitigate agreements promulgated for transactions deemed to be a threat to national security.[147] The lead agency designated for the transaction by CFIUS is charged with formulating any threat-mitigation measures it believes reasonably necessary to address the risk.[148] Selected by the Secretary of the Treasury acting in his capacity as Chairman of CFIUS, the lead agency is one of the agencies that comprise CFIUS and that are charged with leading particular investigations.[149] Required mitigation measures might include, but are not limited to, approval or exclusion by CFIUS of certain officers involved in the "foreign government-controlled transaction,"[150] restrictions on access to certain facilities and data deemed particularly sensitive, annual reports and inspections by CFIUS, or any combination of these.[151] If denied, the affected parties' options are limited because FINSA provides that the presidential decision is not reviewable by courts; however, some believe affected parties could be due compensation through the Takings Clause of the Constitution if private property is taken and if they deserve just compensation for that taking.[152]

Potential foreign purchasers who file a voluntary notice to CFIUS are granted the protection of the "safe harbor" provision.[153] Under this provision, once the covered transaction is cleared by CFIUS, it will be allowed to stand unless CFIUS was provided false or misleading material statements or information.[154] While this safe harbor provides some measure of comfort, whether—and to what extent—"false or misleading" encompasses "incomplete in retrospect" has not yet been tested.[155] Should a transaction be allowed if it later comes under strict scrutiny for reasons of national security? It is unlikely that federal authorities would allow themselves to be entirely stymied by the safe harbor provision; retroactive threat mitigation strikes the author as a likely outcome in such a case.[156]

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147. Foreign Investment and National Security Act of 2007 § 5.

148. Ronald D. Lee & Nancy L. Perkins, *The National Security Guard Dog Gets a Few More Teeth: What the New Foreign Investment Security Act of 2007 Means for Foreign Acquisitions of U.S. Companies*, 11 M&A LAW., no. 9, 2007, at 4, *available at* http://www.arnoldporter.com/resources/documents/M&A lawyer_REPRINT_1007.pdf.

149. *Id.*

150. "[F]oreign government-controlled transaction" is defined in FINSA as "any covered transaction that could result in the control of any person engaged in interstate commerce in the United States by a foreign government or an entity controlled by or acting on behalf of a foreign government." Foreign Investment and National Security Act of 2007 § 2(a)(4). In turn, "covered transaction" is defined as "any merger, acquisition, or takeover . . . by or with any foreign person." *Id.* § 2(a)(3).

151. Lavey & Schlager, *supra* note 78, at 68.

152. Gregory S. Jacobs, *President Obama Follows CFIUS Recommendation, Orders Divestiture on Ralls Wind Farm Deal*, GLOBAL REG. ENFORCEMENT L. BLOG (Sept. 28, 2012), http://www.globalregulatoryenforcementlawblog.com/2012/09/articles/export-customs-trade/president-obama-follows-cfius-recommendation-orders-divestiture-on-ralls-wind-farm-deal/.

153. Foreign Investment and National Security Act of 2007 § 2(b)(1)–(2).

154. *Id.*

155. *Id.*

156. *See id.*

Each of the different agencies has a different skill set and a different focus on varying concerns.[157] One commentator has generally divided the agencies into two categories, one being more "security-focused," including the Departments of Defense, Homeland Security, and Justice, while the other category of agencies is focused more on trade and diplomacy, including the Departments of Commerce and State.[158] The two categories are alleged to have differed slightly in their responses to sales of energy assets to foreign entities, with the first more often seeking to stop or modify a proposed transaction and the second more often in favor of allowing a transaction to go through in the interest of international transactional freedom and an open investment policy.[159] Recently, the second consortium is alleged to have taken a more passive role, allowing the more "hawkish" agencies such as the Department of Defense to argue more effectively against foreign ownership as a way to combat foreign control of a critical computer network that could be used for a cyber-attack.[160]

CFIUS's prior actions show that it considers mineral right purchases to implicate interests that could be characterized as important for national defense and considers oil and gas interests to be strategic, as well as the companies that own them.[161] The only recent acquisitions of mineral rights by foreign entities that have given rise to CFIUS concerns have been proposed acquisitions of large corporations with extensive alien operations by foreign entities that are citizens of countries that represent a potential strategic challenge to the United States.[162] In addition, "passive" asset acquisitions do not generally require CFIUS review; therefore, the acquisition of a passive investment—for example, acquiring non-participating royalty interests (NPRIs), net profits interests, overriding royalty interests (ORRIs), or all three—probably does not require CFIUS review.[163]

1. Divestitures, Sellouts, and Mitigations

Because much of the review and investigatory skullduggery of CFIUS is confidential, intelligence regarding specific transactions remains sparse.[164] Much of the available information has bubbled up from company and third-party sources after approval has been denied, rather than from CFIUS, so it

157. Stephen Heifetz & Michael Gershberg, *Why Are Foreign Investments in Domestic Energy Projects Now Under CFIUS Scrutiny?*, 3 HARV. BUS. L. REV. ONLINE 201, 209 (2013), *available at* http://www.hblr.org/wp-content/uploads/2013/05/Heifetz-Gershberg_CFIUS-Scrutiny.pdf.

158. *Id.*

159. *Id.*

160. *Id.*

161. *Id.*

162. *See id.*

163. *See* JAMES K. JACKSON, CONG. RESEARCH SERV., RL33388, THE COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES (CFIUS) 13 (2014) [hereinafter JACKSON, CFIUS].

164. *See* JACKSON, EXON-FLORIO, *supra* note 111, at 20; *see also* Keith Goldberg, *No Letup in US Scrutiny of Foreign-Backed Energy Projects*, LAW360 (Oct. 11, 2013, 7:46 PM), http://www.morganlewis.com/pubs/Law360_ScrutinyOfForeignBackedEnergyProjects_11oct13.pdf.

remains unclear exactly which particular factors CFIUS considers detrimental to energy transactions.[165] Since the Exon-Florio Amendment was passed in 1988, the President has prohibited only two mergers or acquisitions on the basis of "national security."[166] Some of this mystery is due to utilization of the mitigation process as mitigation agreements often iron out wrinkles that otherwise might torpedo deals, such as restricting the parties to the proposed transaction to certain conditions, i.e., facility inspections.[167]

The United States remains a popular target for foreign investment. For the period from 1996 to 2011, 2007 had the highest number of acquisitions of a United States firm by foreign individuals or entities.[168] The subsequent drop can be partially attributed to the stricter FINSA requirements passed in 2007, but probably is mostly a result of the economic downturn in the United States.[169] China accounted for sixteen out of the 313 total mergers and acquisitions reviewed by CFIUS between 2008 and 2010, behind such countries as the United Kingdom, Israel, France, and Canada.[170]

TABLE 1.

Merger and Acquisition Activity in the United States: 1996–2011[171]				
Year	Avg. Total Number of Mergers & Acquisitions	U.S. Firms Acquiring U.S. Firms (Avg. by Year)	Non-U.S. Firms Acquiring U.S. Firms (Avg. by Year)	U.S. Firms Acquiring Non-U.S. Firms (Avg. by Year)
1996–1999	8,798	6,482	881	1,436
2000–2003	6,652	4,662	902	1,087
2004–2007	8,182	5,789	1,085	1,308
2008–2011	7,053	4,788	1,000	1,264

TABLE 2.

Country of Foreign Investors Reviewed by CFIUS: 2008–2010[172]		
Country	Total Number of Acquisitions Reviewed by CFIUS	Percentage of Total
United Kingdom	91	29.07%
France	25	7.99%

165. *See* JACKSON, CFIUS, *supra* note 163, at 17–19.
166. *See* JACKSON, EXON-FLORIO, *supra* note 111, at 20–21.
167. *See* JACKSON, CFIUS, *supra* note 163, at 19–21.
168. *Id.* at 22–24.
169. *Id.* at 21.
170. *Id.* at 24.
171. *See id.* at 22.
172. *See id.* at 24.

Israel	24	7.67%
Canada	24	7.67%
Japan	19	6.07%
China	16	5.11%
Others	38	12.14%
Total	**313**	**100%**

E. MAMCO Divestiture

In 1990, George H. W. Bush was the first president to prohibit a proposed transaction via FINSA.[173] The voided transaction was a proposed acquisition of MAMCO Manufacturing (MAMCO), a Seattle-based commercial airplane parts manufacturer, by China National Aero-Technology Import and Export Corporation (CATIC) for five million dollars.[174] Neither MAMCO nor CATIC requested a voluntary report of the transaction before completion.[175] After the deal was complete, CFIUS decided an investigation was appropriate to make sure the acquisition did not affect national security.[176] CATIC most likely triggered CFIUS's scrutiny because it was actually the purchasing agent of the Chinese government, charged by the communist regime with the task of acquiring the "material and technology for military aircraft and manufactur[ing] fighters, bombers and helicopters."[177] As a result of its investigation, CFIUS decided that CATIC might sell parts acquired through the contemplated transaction directly to China for use in its military.[178] CFIUS reported all of this to President Bush, along with a recommendation to dismantle the transaction, a recommendation President Bush later took on February 2, 1990.[179]

At this point, members of Congress took notice, particularly with the Tiananmen Square massacre by the Chinese communists the previous June still fresh in the public's mind.[180] Senator Exon, for whom the Exon-Florio amendment is partly named, opined that CATIC "certainly furthered China's military power, the same military power that was used to brutally crush the

173. Young, *supra* note 71, at 46.
174. Jim Mendenhall, *United States: Executive Authority to Divest Acquisitions Under the Exon-Florio Amendment—The MAMCO Divestiture*, 32 HARV. INT'L L.J. 286, 290–93 (1991); Young, *supra* note 71, at 46.
175. *See* Mendenhall, *supra* note 174, at 288–90.
176. Andrew Rosenthal, *Bush Urged to Void Sale of Airplane-Parts Maker to Chinese*, N.Y. TIMES (Feb. 2, 1990), http://www.nytimes.com/1990/02/02/world/bush-urged-to-void-sale-of-airplane-parts-maker-to-chinese.html.
177. *Id.*
178. *See* Mendenhall, *supra* note 174, at 290–92.
179. *Id.*; *see also* Harriet King, *China Ends Silence on Deal U.S. Rescinded*, N.Y. TIMES (Feb. 20, 1990), http://www.nytimes.com/1990/02/20/business/china-ends-silence-on-deal-us-rescinded.html.
180. *See id.*

Chinese democracy movement."[181] CATIC was implicated as being a purchasing agent for the Chinese military.[182] CATIC also developed a reputation for disregarding foreign export control laws in order to obtain sensitive Western technology.[183] Not surprisingly, governmental scrutiny of the proposed deal heightened because of these facts, even though MAMCO did not engineer or design the airplane parts or have any classified contracts with the federal government.[184]

Another complication arose regarding MAMCO's biggest customer, Boeing. The Exon-Florio amendments require that the President also consider the "character" of the purchaser when deciding whether to allow the transaction to take place.[185] MAMCO, whose largest customer was Boeing, insisted that its plant was capable of producing only small metallic brackets that, while not specifically designed for military use, could be used in *any* type of aircraft.[186] In the late 1980s, Boeing helped design such military aircraft as the B-2 Stealth Bomber; the thought of such important plans falling into the Chinese government's hands likely factored into President Bush's decision to void the proposed transaction between MAMCO and CATIC.[187]

After the President's decision, CATIC had to comply with this divesture order within three months, leading to the sale of MAMCO to DeCrane Aircraft Holdings Inc., an American company.[188] As it turned out, the Chinese military, interested in gathering secret information on the B-2 bomber, paid a design engineer working for Northrup named Noshir Gowadia at least $110,000 for information regarding the stealth technology employed by the bomber.[189]

While the Chinese were conducting this espionage, President Bush issued an emphatic message to Congress saying that his decision did "not change our open investment policy and was not a precedent for the future with regard to direct investment in the United States from the People's Republic of China or any other country."[190] Despite President Bush's disclaimer, the same country

181. Stuart Auerbach, *President Tells China to Sell Seattle Firm*, WASH. POST, Feb. 3, 1990, at A9 (quoting Senator James Exon).

182. *Id.*

183. *Id.*

184. Young, *supra* note 71, at 47.

185. *See* Press Release, Jim Exon News, President Invokes Exon Law to Force Chinese to Sell U.S. Co. (Feb. 2, 1990) (on file with author).

186. King, *supra* note 179.

187. *See* Rosenthal, *supra* note 176.

188. Mendenhall, *supra* note 174, at 292.

189. Press Release, U.S. Dep't of Justice, Hawaii Man Sentenced to 32 Years in Prison for Providing Defense Information and Services to People's Republic of China (Jan. 25, 2011), *available at* http://www.justice.gov/opa/pr/2011/January/11-nsd-104.html.

190. George Bush, *Message to the Congress on the China National Aero-Technology Import and Export Corporation Divestiture of MAMCO Manufacturing, Incorporated* (Feb. 1, 1990), http://www.presidency.ucsb.edu/ws/index.php?pid=18109&st=&st1=.

would take another turn in the limelight the next time national security was invoked to stymie foreign investment in the United States.[191]

F. Ralls Corporation Divestiture

The Ralls Corporation, a privately held Delaware corporation controlled by two Chinese senior executives, along with a Chinese heavy equipment manufacturer, the Sany Group Company, purchased and invested over $130 million in four wind farm projects along the Oregon coast, where they planned to install wind turbines acquired from Terna, a United States-based corporation.[192] Before Terna obtained the wind farms, the Federal Aviation Administration determined that the turbines would pose no aviation hazard, a necessary precondition for issuing permits.[193] This determination, which included a Department of Defense review, was required because of the very close (less than ten miles) proximity of the turbines to a naval bombing range and drone training area, which included restricted airspace.[194]

Multiple-area wind farms with multiple owners commonly used foreign-made turbines.[195] The wind farm was small, comprising 0.4% of the regional power grid's total generating capacity.[196] Ralls had a history of operating renewable energy projects and had previously operated a 10-megawatt wind farm project in Texas.[197]

Casting doubt on CFIUS's omnipotence—and perhaps the wisdom of voluntary reporting—CFIUS discovered the proposed sale from Terna to Ralls from an article in a magazine called *Wind Power Monthly*.[198] After mitigation efforts failed, CFIUS reported the transaction to President Obama.[199] President Obama's subsequent order "not only require[d] divestiture and removal of all

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191. Mendenhall, *supra* note 174, at 292; *see also* Frederick P. Waite & M. Roy Goldberg, *National Security Review of Foreign Investment in the United States: An Update on Exon-Florio and the Final Regulations Which Implement It*, 6 FLA. J. INT'L L. 191, 208–11 (1991) (discussing CFIUS investigations to determine the presence of national security threats).

192. Liu Jiayi, *Chinese Government Backs China Firm Suing Obama Over Wind Farm Veto*, ZDNET (Oct. 19, 2012, 10:42 AM), http://www.zdnet.com/chinese-government-backs-china-firm-suing-obama-over-wind-farm-veto-7000006052/.

193. Amended Complaint for Declaratory and Injunctive Relief at 2–16, Ralls Corp. v. Comm. on Foreign Inv. in the U.S., 926 F. Supp. 2d 71 (D.D.C. 2013) (No. 1:12-CV-015130-ABJ), 2012 WL 4931759.

194. *Id.*

195. *Id.* at 12 (including German, Indian, and Danish innovations).

196. Gregory S. Jacobs, *Presidential Dilemma on Ralls CFIUS Case*, GLOBAL REG. ENFORCEMENT L. BLOG (Sept. 27, 2012), http://www.globalregulatoryenforcementlawblog.com/2012/09/articles/export-customs-trade/presidential-dilemma-on-ralls-cfius-case/.

197. Jiayi, *supra* note 192.

198. Jacobs, *Presidential Dilemma on Ralls CFIUS Case*, *supra* note 196.

199. *Id.*

equipment, it also prohibit[ed] the Ralls owners and their representatives from physically entering the site."[200]

Due to the confidentiality of CFIUS reports, it is very difficult to obtain specifics about what factors trigger CFIUS scrutiny. Military considerations were likely the single biggest factor in the Ralls decision because the Ralls wind farms were located next to a United States naval base with restricted airspace.[201] It is unknown whether military factors other than the wind farms' proximity to the naval base played into President Obama's decision to block the transaction.

In the wake of the unraveling of its sale, Ralls was not able to ascertain exactly what credible evidence President Obama cited for his decision, but those affected believe it was simply a result of the Chinese connection to the deal.[202] President Obama, at an Iowa rally during his 2012 re-election campaign, said, "I don't want fuel-efficient cars and long-lasting batteries and wind turbines manufactured in China . . . . I want them made in the United States of America."[203] In the subsequent action brought by Ralls—litigation that was eventually dismissed in two rulings handed down on February 25, 2013, and October 9, 2013—the company argued that the President had generally exceeded his authority in stopping the deal, that it had no opportunity to test whether its acquisition would be blocked, and that it was denied due process.[204]

The Ralls decision strained relations between China and the United States. For example, China's Minster of Commerce has commented on the failed acquisition, saying, "As this involves an enterprise and a foreign government, the Chinese government is watching and investigating (the progress)."[205] Chinese government and business officials then suggested that European investment was now their main focus, rather than the United States.[206] This

200. Jacobs, *President Obama Follows CFIUS Recommendation, Orders Divestiture on Ralls Wind Farm Deal*, *supra* note 152; *see* Exec. Order Regarding the Acquisition of Four U.S. Wind Farm Project Companies by Ralls Corporation, 77 Fed. Reg. 60,281 (Sept. 28, 2012).

201. John Villasenor, *If You Want to Buy an American Company, Ask Permission, Not Forgiveness*, FORBES (Nov. 14, 2012, 1:19 PM), http://www.forbes.com/sites/johnvillasenor/2012/11/14/if-you-want-to-buy-an-american-company-ask-permission-not-forgiveness/.

202. Jiayi, *supra* note 192. One Sany executive claimed the transaction was targeted because of its Chinese connection saying, "This is discrimination . . . . There are 27 Danish wind power generators near our farms, and also other operational wind farms in this area. The orders are specifically against Chinese companies and discriminatory." *Id.* (quoting Ralls Corporation chief executive Wu Jialiang) (internal quotation marks omitted).

203. President Barack Obama, Remarks by the President at a Campaign Event in Davenport, Iowa (Oct. 24, 2012), *transcript available at* www.whitehouse.gov/the-press-office/2012/10/24/remarks-president-campaign-event-davenport-iowa.

204. Ralls Corp. v. Comm. on Foreign Inv. in the U.S., 926 F. Supp. 2d 71, 76 (D.D.C. 2013); *see* Goldberg, *supra* note 164.

205. *China Monitors Sany's Lawsuit Against Obama*, SHANGHAI DAILY (Mar. 6, 2013), *available at* http://www.china.org.cn/business/2013-03/06/content_28144019.htm (quoting China's Minister of Commerce, Chen Deming) (internal quotation marks omitted).

206. Anthony Lin, *Can China Change CFIUS?*, ASIAN LAW. (May 13, 2013), http://www.law.com/jsp/article.jsp?id=1202599753882&Can_China_Change_CFIUS&slreturn=20130419 184029.

threat became possibly less idle in April 2013, when an executive vice president of a Chinese technology firm said that the firm would no longer be investing in the United States.[207] One commentator notes that Chinese companies and individuals who have faced the CFIUS process believe that China is being singled out.[208] He further noted there is no way that Chinese corporations will receive the same treatment as Western corporations because "[t]he reality is that countries have different bilateral relationships, and that results in different levels of scrutiny in areas like this . . . . It's an uncomfortable reality, but it is the reality."[209]

G. The Dubai Ports World Sale

Just because a company clears the FINSA hurdle does not mean that it is out of the proverbial woods. Companies pondering energy purchases should take heed of the cautionary tale provided by Dubai Ports World, a company owned by the government of the United Arab Emirates, and its acquisition of the port management business of Peninsular and Oriental Steam Navigation Company (POSNC).[210] Dubai Ports World's purchase of POSNC provided for acquisition of leases for management of six large United States seaports.[211] After proper notification by Dubai Ports World and an investigation by CFIUS, CFIUS cleared the acquisition.[212] The approval by CFIUS was followed by an eruption of bad press, claims of foreign threats and subversion, and complaints about a process that would allow controls of ports to fall into foreign hands.[213] After taking a pummeling in the media and in Congressional hearings, Dubai Ports World eventually sold all of the United States assets of POSNC—including the leases—to a subsidiary of American International Group.[214]

H. Present Trends and Strategy for Purchasers and Sellers

Concerns about geographical proximity of an acquisition to sensitive areas—the deathblow to the acquisition sought by Ralls—and of cyber-attacks and data theft have been the two most important recent vectors of FINSA

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207. *Id.*

208. *Id.* Mark Plotkin is a patent attorney who helped Cnooc Ltd., a Chinese corporation, obtain CFIUS approval for a $15.1 billion acquisition of Nexen, a Canadian entity that had major operations in the United States, only after either Nexen removed from the transaction some of its Gulf of Mexico assets or prevented Chinese nationals from accessing its offshore rigs thereon. *Id.*

209. *Id.* (quoting Mark Plotkin) (internal quotation marks omitted).

210. *See* Mostaghel, *supra* note 74, at 606.

211. *Id.*

212. *Id.*

213. *See* Julio J. Rotemberg, *The Dubai Ports World Debacle and Its Aftermath*, HARV. BUS. SCH. (2006).

214. Neil King Jr. & Greg Hitt, *Dubai Ports World Sells U.S. Assets: AIG Unit Buys Operations that Ignited Controversy as Democrats Plan Changes*, WALL ST. J., Dec. 11, 2006, at A1, *available at* http://online.wsj.com/news/articles/SB116584567567746444.

concern.[215] The properties of concern in the Nexen acquisition were within fifty miles of a United States naval installation and subsea telecommunication cables.[216] Cyber-attacks on oil and gas companies have become almost commonplace.[217]

CFIUS currently reviews more than one hundred cases per year and finds security concerns in approximately ten to twenty of those.[218] These proposed transactions are typically targeted for mitigation procedures when, as we have seen, CFIUS demands changes to the deal structure and the proposing parties modify the deal structure in order to assuage the concerns of CFIUS.[219] If the concerns of CFIUS cannot be allayed with a risk mitigation agreement and the parties proposing the transaction refuse to pull their application, CFIUS will present the transaction to the President with the recommendation that the transaction be halted or put in stasis. Although it may be comforting that this has happened only twice, being on the wrong end of a Presidential cancellation of a transaction can be devastating.

Given the attention paid by the media to Presidential decisions to accept or deny proposed transactions, no President wants to be seen as "soft" when foreigners are seeking control of domestic critical infrastructure, assets, or both, and a government committee has advised the President to stop the deal.[220] Therefore, any checklist of things to do or avoid regarding the purchase of American energy assets must start with "avoid Presidential review at all costs."[221] If CFIUS asks for a mitigation agreement, then the parties to the proposed transaction need to give way as much as possible.

A corollary of this rule is that Presidential denials, given their unreviewability and seeming finality, probably indicate that all similar transactions will be denied in the future. Therefore, if CFIUS asks for mitigation, and the parties to the proposed transaction cannot justify going forward, it is better to halt the transaction than risk not only failure in the present case, but also risk having a Presidential denial create a presumption that future similar transactions should be denied.

A second current trend is obvious: involving China in a CFIUS-reviewable purchase of American assets is seemingly more likely to incur increased scrutiny, transactional modifications, delay, and maybe even deal cancellation.

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215. *See* Goldberg, *supra* note 164.

216. *Id.*

217. *See, e.g.*, Elizabeth MacDonald, *U.S. Oil and Gas at Greater Risk for Cyber Attacks*, FOX BUSINESS (June 26, 2012), http://www.foxbusiness.com/technology/2013/06/26/us-oil-and-gas-at-greater-risk-for-cyber-attacks/; Nicole Perlroth, *In Cyberattack on Saudi Firm, U.S. Sees Iran Firing Back*, N.Y. TIMES (Oct. 23, 2012), http://www.nytimes.com/2012/10/24/business/global/cyberattack-on-saudi-oil-firm-disquiets-us.html?pagewanted=all&__r=1&.

218. *See* COMM. ON FOREIGN INV. IN THE U.S., ANNUAL REPORT TO CONGRESS CY 2011 (Dec. 2012), *available at* http://www.treasury.gov/resource-center/international/foreign-investment/Documents/2012%20CFIUS%20Annual%20Report%20PUBLIC.pdf.

219. 50 U.S.C. app. § 2170(l)(1) (2006 & Supp. 2011).

220. *See supra* text accompanying notes 1–4.

221. *See* discussion *supra* Part II.A.1.

It is believed that this is largely because of worry about Chinese spying.[222] Chinese espionage directed at the United States is rampant.[223] During this aggression, China's investment in the United States is also growing, with one estimate describing a trajectory of $129 million in 2006, to $1.9 billion in 2009, to $6.5 billion in 2012.[224] This rising tide necessarily includes increasing Chinese investment in United States energy assets, and with China taking the stage as one of the world's leading energy consumers, it will continue.

Because international transactional practitioners often do not have control over the nationalities of prospective clients, the fact that a purchasing party is of Chinese origin may be immutable. However, care can be taken to make a transaction involving United States energy assets more accurately reflect the nature of its foreign origins. For example, if several principals get together from around the world—including some from China—to form a special-purpose entity to invest in United States energy assets, CFIUS scrutiny may be lightened if that entity was formed in a country other than China. Yes, further scrutiny may focus attention on the individual Chinese principals to the investing entity, but perhaps not always.

Third, parties contemplating a transaction should closely examine, and possibly parse out, various components of the deal. If the target company owns technology, computer, or other intellectual property that experience has shown is considered critical by FINSA, or if energy real property that will be transferred is located near United States military assets, shipyards, or other government installations, closer scrutiny by CFIUS should be expected.

If one part of the deal could trigger federal concern, either not going forward with that part or handling that part as a separate transaction may save time and prevent a problem that delays or even scuttles a larger transaction. If, for example, the deal involves the purchase of five parcels of minerals in contemplation of later development, five tank farms, or five lifting terminals, identifying and not attempting to purchase the one next to a military installation could be the wisest course.

If doubt exists about whether or not to make a voluntary filing, it certainly behooves the parties contemplating the transaction to ask an attorney experienced in CFIUS investigations and the recent history of FINSA filings whether the contemplated transaction is of a similar nature to other types of transactions for which voluntary filings are, or are not, typically made. Being out of step attracts scrutiny, and if the contemplated transaction is of a kind that typically results in a voluntary filing, not filing may raise doubts and trigger an "invitation" to file by CFIUS itself.[225] As one commentator noted, such invitations issued after CFIUS later discovers a transaction for which no

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222. *See* Heifetz and Gershberg, *supra* note 157, at 206–07.

223. *Id.*

224. *See Chinese Investment Monitor: Tracking Chinese Direct Investment in the U.S.*, RHODIUM GROUP, http://rhg.com/interactive/china-investment-monitor (last visited Mar. 26, 2014).

225. Zive, *supra* note 86.

voluntary filing was originally made means the process may begin in a cloud of suspicion.[226]

Fourth, the deal structure and associated corporate arrangement require contemplation. Transactions should be restructured if they would result in foreign governments or entities under their direct control owning or operating—or just *effectively* owning and operating in the judgment of CFIUS—a company with assets considered critical by CFIUS. If a third-party "blocker" company (described below) is created to be the interface between the foreign owners and the United States company, it is then important to consider the level of control a foreign power or government will have over that company or even the foreign owners themselves.

1. The Survey Act

Ownership or effective control of 10% or more of a corporation's voting securities activates the International Investment Survey Act of 1976 (the Survey Act).[227] The Bureau of Economic Analysis (the BEA) collects this information.[228]

Under the Survey Act, ownership or effective control of 10% or more of a corporation's voting securities sufficiently indicates a "lasting interest in" or a "degree of influence over" management of a corporation to constitute alien direct investment.[229] Therefore, alien direct investment in the United States is defined as the ownership or control, directly or indirectly, by one alien individual or alien entity of 10% or more of the voting securities of an incorporated United States business enterprise or the equivalent amount in an unincorporated United States business entity.[230]

While the Survey Act does not impose restrictions on domestic investment by alien entities, it does generally require that any alien investor (a) with more than five million dollars invested in domestic assets through direct investment, (b) that has more than five million dollars net income, or (c) that owns more than 200 acres of land (including minerals), submit initial and subsequent periodic reports, as well as reports of certain business activities as they occur.[231]

More specifically, these reports require information on the balance of payments and the direct investment position data, financial and operating data

226. *Id.*

227. *See* 22 U.S.C. §§ 3101–08 (2012).

228. Foreign Direct Investment and Financial Data Improvements Act of 1990, Pub. L. No. 101-533, § 6(A), 104 Stat. 2344, 2350–51 (providing an overview of the Surface Act).

229. Alicia M. Quijano, *A Guide to BEA Statistics on Foreign Direct Investment in the United States*, BUREAU OF ECON. ANALYSIS: SURV. OF CURRENT BUS. 29 (Feb. 1990), *available at* http://www.bea.gov/scb/pdf/internat/fd/invest/1990/0290iid.pdf.

230. *Id.*

231. *Id.* at 34 (noting that there are several exemptions mentioned in the statute that may except certain foreign entities from being required to file the reports).

of United States affiliates, and entity establishment and acquisition data.[232] The reports also must contain disclosures including abbreviated income statements and balance sheets; employment and employee compensation; a separation of sales data into components, including bills of sale, sales of services, and sales to United States citizens or to foreign persons; structure and sources of external financing; capital expenditures; changes in property, plant, and equipment; research and development expenditures; taxes paid; trade in goods; and numerous other data.[233]

In addition, every five years, the United States Department of Commerce issues a mandatory survey requesting information on the amount and type of foreign direct investment in United States business enterprises.[234] This survey is known as the Form BE-12 Benchmark Survey. All alien corporations, organizations, associations, branches, or ventures investing in United States real property must complete the report.[235] The data obtained remains confidential and is used by the BEA for evaluating the effect of foreign investment on the United States economy. Failure to report may subject the foreign entity to a civil penalty of $2,500 to $25,000.[236] A willful refusal to file may result in a criminal penalty of up to $10,000, up to one year in prison, or both.[237]

2. Restrictions on Foreign Ownership of Domestic Mineral Property & Export Bans of Crude Oil

Under the laws and regulations of the United States, various restrictions or controls exist on foreigners and foreign companies for holding a mineral right or for being a shareholder of a holder of a mineral right.[238] Various federal laws touch upon foreign ownership of mineral rights. Generally, if the alien corporation is based in a country hostile to the United States, ownership of mineral rights is disallowed or seriously curtailed.[239] Similarly, if ownership is sought by an alien corporation from a country that does not, in turn, allow entities from the United States to own mineral rights in the foreign country, then the potential for the alien corporation's ownership of American mineral rights is likewise curtailed.[240] "If any appreciable percentage of stock of a corporation is held by aliens who are citizens of a country denying similar or like privileges to United States citizens, that corporation's application or bid for

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232. *Id.* at 29.

233. *Id.* at 34; *see* Ralph H. Kozlow, Foreign Direct Investment in the United States - Bureau of Economic Analysis, Directorate for Economic Co-operation and Development (OECD) Workshop on International Investment Statistics (Mar. 22–24, 2004).

234. Quijano, *supra* note 229, at 34, 36.

235. *Id.* at 31, 34.

236. Kozlow, *supra* note 233.

237. *Id.*

238. *See* 43 C.F.R. § 3472.1-2(d) (2012).

239. *Id.*

240. *Id.*

[an oil and gas mineral right will] be rejected, and that corporation's [mineral right is] subject to cancellation."[241]

Some states have restrictions and reporting requirements, but no state has a complete prohibition on alien ownership. Differences between the states abound. Some states (for example, Texas and New Mexico) have passed laws that expressly give all aliens the right to buy and own real property.[242] Other states (for example, Oklahoma) permit aliens to own non-agricultural land, but limit ownership of agricultural land and ownership of other rural lands in excess of what is "necessary" for the purpose of the business.[243] A smaller group of states (for example, Mississippi) distinguishes between non-resident and resident aliens, and these states permit ownership only by aliens "residing" in that state.[244]

a. Federal

Mineral rights in oil and gas under public domain lands and lands returned to the public domain are subject to lease under the General Leasing Act of 1920 and its amendments. Aliens may acquire and hold mineral rights only through stock ownership, holding or control of a corporation, and only if the laws, customs, or regulations of their country do not deny similar privileges to citizens or corporations of the United States.[245] Alien corporations "may not acquire or hold any direct or indirect interest in [mineral prospecting permits or mineral rights], except that they may own or control stock in corporations" organized under the laws of the United States or of any state or territory holding such permit or mineral rights "if the laws of their country do not deny similar or like privileges to citizens [or corporations] of the United States."[246] The law is clear that ownership must be through a corporation and not through another form.[247]

No joint venture is expressly required in the case in which an alien or alien company is a shareholder or owner of domestic mineral rights.[248] However, because alien companies cannot directly own federally issued oil and gas leases or other mineral rights issued by the federal government, an American subsidiary corporation is typically formed to own or control stock in

241. *Id.*
242. N.M. STAT. ANN. § 45-2-111 (West 2013); TEX. PROP. CODE ANN. § 5.005 (West 2004).
243. *See* OKLA. STAT. ANN. tit. 60, §§ 121–22 (West 2010).
244. *See* MISS. CODE ANN. § 89-1-23 (2011).
245. Act of Feb. 25, 1920, ch. 1, 41 Stat. 437 (codified as amended at 30 U.S.C. § 181 et seq. (2012)).
246. 43 C.F.R. §§ 3102.1 (2012), 3102.10 (2012), 3472.1-2(d) (2012), 3502.13 (2012); *see* 30 U.S.C. § 181. Qualification Stipulations for alien ownership of mineral rights are described in 43 C.F.R. § 3502.10 (2012).
247. 43 C.F.R. § 3502.10. While there might be several tiers of various entity forms, there must always be a federal, state, or territorial corporation between the alien individual or entity and the lease for public lands somewhere in the structure. *Id.*
248. *See id.*

corporations that hold such permits, leases, or mineral rights.[249] Alien companies can own other non-federal minerals and leases in the United States—those bought or issued from private owners or even states.[250] If the minerals or leases entail a "strategic interest" of the United States, however, it will trigger the FINSA and CFIUS regulations.[251] If the minerals and leases entail uranium or another mineral or chemical that, if exported, could result in a serious security threat to the United States, not only will FINSA/CFIUS scrutiny be intense, but presumably, scrutiny from other federal intelligence agencies will be entailed as well.[252]

i. Territorial Land Act of 1887

Congress enacted the Territorial Land Act of 1887 (the Territorial Act) to prohibit non-resident aliens who had not declared their intent to become United States citizens from purchasing land in United States Territories.[253] The Territorial Act was intended to prevent aliens from acquiring large tracts of land in the Western territories.[254] The law remains effective, long after the Western territories were settled and became states.[255] While the law does not generally apply to individual states, the regulations recite that "[a]liens may not acquire or hold any direct or indirect interest in [oil and gas leases with federal lessors (that is, leases from a federal agency)], except that [aliens] may own or control stock in corporations holding leases if the laws of their country [of citizenship] do not deny similar or like privileges to citizens of the United States."[256] "If any appreciable percentage of [the] stock of a corporation is held by aliens who are citizens of a country denying similar or like privileges to United States citizens," the application of that corporation to lease or to accept an assignment of a lease will be denied.[257] Research into the reciprocal laws of a foreign power regarding foreign investment must occur before a party or entity from that power acquires assets that are subject to the Territorial Act.[258]

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249. *See supra* Part II.B. Other business and tax reasons exist for the use of such a "blocker" corporation. Such discussion is beyond the scope of this Article.

250. *See* JOHN S. LOWE ET AL., CASES AND MATERIALS ON OIL AND GAS LAW 116 (6th ed. 2013).

251. *See* Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246.

252. *Id.*

253. 48 U.S.C. § 1501 (2006).

254. Larkin v. Wash. Loan & Trust Co., 31 F.2d 635, 637 (D.C. Cir. 1929).

255. *See* 48 U.S.C. § 1501.

256. 43 C.F.R. § 3472.1-2(d) (2012).

257. 43 C.F.R. §§ 3102.1 (2012), 3472.1-2(d). Leases or interests therein may be acquired and held only by citizens of the United States; associations (including partnerships and trusts) of such citizens; "corporations organized under the laws of the United States or of any state [or territory] thereof"; and municipalities. 43 C.F.R. § 3102.1.

258. *See* 43 C.F.R. § 3472.1-2(d).

ii. Trading with the Enemy Act

The Trading with the Enemy Act of 1917, which contains the Foreign Assets Control Regulations and the Alien Property Custodian Regulations, represents federal attempts to curtail investment by and in countries deemed to be hostile to the United States (for example, Cuba).[259] Investment in mineral real property by foreign entities from these restricted countries is prohibited.[260] The Office of Foreign Assets Control, an agency within the Department of the Treasury, administrates and enforces the regulations promulgated under the Trading with the Enemy Act and similar acts.[261]

b. States

Alien corporations are typically considered the same as foreign corporations by state laws in most (and perhaps all) of the traditional oil and gas-producing states.[262] Foreign and alien mineral right operators must register to do business in the state where the oil and gas mineral interest is owned.[263] This process is typically called "domestication" or "qualification" to transact business in the state.[264] Foreign and alien non-operating owners typically do not have to register to do business in the state where the oil and gas interest is located.[265] Several parties may own oil and gas real property at once, in various percentages, with the parties splitting the costs and profits according to the appropriate percentage or through the terms of other agreements between them.[266] In the case of such split ownership of mineral rights, one party is typically designated the "operator," and the other parties are thereby "non-operators."[267] Operators actively develop the oil and gas rights and hire contractors to provide necessary assistance.[268] The non-operators pay the operator their share of the development costs but typically take no active part in the development themselves.[269]

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259. *See* 12 U.S.C. § 95a (2012); 50 U.S.C. app. § 5 (2006).
260. *See* 12 U.S.C. § 95a; 50 U.S.C. app. § 5.
261. *See* 12 U.S.C. § 95a; 50 U.S.C. app. § 5.
262. *See* LA. REV. STAT. ANN. § 12:1(k) (2010); N.M. STAT. ANN. § 53-11-2(B) (West 2013); OKLA. STAT. ANN. tit. 18, § 2001(6), (8) (West 2012); TEX. BUS. ORGS. CODE. ANN. § 1.002(28) (West 2012 & Supp. 2013).
263. LA. REV. STAT. ANN. § 12:301 (2010); N.M. STAT. ANN. § 53-19-48 (West 2013); OKLA. STAT. ANN. tit. 18, § 1130(B) (West 2012); TEX. BUS. ORGS. CODE. ANN. § 9.001 (West 2012).
264. William H. Clark, Jr. & George W. Coleman, Ad Hoc Comm. on Entity Rationalization, *Proposed Model Inter-Entity Transactions Act*, 57 BUS. LAW 1569, 1570 (2002); Joyce Yeager, *Borders and Barriers, Definitions of Authority to Do Business as a Foreign Corporation*, 102 COM. L.J. 398, 400 (1997).
265. *See* LA. REV. STAT. ANN. § 12:302(J) (2010); N.M. STAT. ANN. § 54-1A-1104 (a)(9) (West 2013); OKLA. STAT. ANN. tit. 18, § 2049 (A)(12) (West 2012); TEX. BUS. ORGS. CODE ANN. § 9.251(13) (West 2012).
266. *See* LOWE ET AL., *supra* note 250, at 998–99.
267. *See id.*
268. *Id.*
269. *Id.*

Foreign companies may own both operating and non-operating working interests in Texas, New Mexico, Oklahoma, and Louisiana, as well as (probably) all other states.[270] In Texas and New Mexico, for example, a non-operating foreign company may acquire the interests without first registering to do business as a foreign limited partnership, corporation, or limited liability company in the state.[271] However, to own non-operating working interests in Oklahoma and Louisiana, for example, a foreign or alien corporation must first register to do business in the state.[272] Below are examples of the laws of five states, all with significant hydrocarbon reserves and development activity, that describe the requirements of alien and foreign corporations to achieve legal ownership of mineral real property.

Ownership of non-participating interests, such as royalty, NPRI, and ORRI, does not require domestication in most oil-producing states.[273] However, this may not always be the case. The Louisiana statute does not expressly exclude owning royalty, NPRI, and ORRI from activities considered "transacting business" in the state, and thus, domestication may be required in Louisiana.[274]

Domestication requires a processing fee, which varies in amount depending on the state, and a renewal every year.[275] All such domestication costs seen by the author have been nominal. Costs and losses associated with not filing for and maintaining domestication, however, can result in losing the right to file suit in state courts until domestication is approved.[276] Losing a cause of action to the statute of limitations can be ghastly. The alien entity should qualify or domesticate in each state in which it owns a working interest because, when the time for sale of that interest comes, the purchaser typically requires a representation that the (alien) seller is qualified to transact business in all jurisdictions in which the seller owns the properties being sold.[277]

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270. The author knows of no instances in which foreign operators are not required to register or domesticate in the state where the oil and gas right is located, thus subjecting it to the jurisdiction of the laws, taxation, and courts of that state.

271. *See* N.M. STAT. ANN. § 54-1A-1104(a)(9) (West 2013); TEX. BUS. ORGS. CODE. ANN. § 9.251(13) (West 2012).

272. *See* LA. REV. STAT. ANN. § 12:302 (2012) (failing to expressly include owning non-operating working interests from activities not constituting business transactions); OKLA. STAT. ANN. tit. 18, § 2049(A) (West 2012).

273. *See* N.M. STAT. ANN. §§ 53-17-1 (K) (West 2013), 54-1A-1104; OKLA. STAT. tit. 18, § 2049(A)(12).

274. *See* LA. REV. STAT. ANN. § 12:302.

275. LA. REV. STAT. ANN. § 12:305(A) (2010); N.M. STAT. ANN. § 53-19-49 (West 2013); OKLA. STAT. ANN. tit. 18, § 1130(c) (West 2012).

276. *See* LA. REV. STAT. ANN. § 12:314 (2010); N.M. STAT. ANN. § 53-19-53(B) (West 2013); OKLA. STAT. ANN. tit. 18, § 1137(A) (West 2012); TEX. BUS. ORGS. CODE ANN. § 9.051(b) (West 2012).

277. The author thanks Michael Cooper, a seasoned Texas oil and gas attorney, for providing this practice point.

i. Louisiana

Under the Louisiana Constitution, every person has the right to buy, own, and sell real property.[278] The Louisiana Corporations Code regards alien corporations as "foreign corporations" and requires that they domesticate by acquiring a "certificate of authority" from the Louisiana Secretary of State before conducting any business in the state.[279] Alien corporations also need this certificate of authority to benefit from the rights and privileges that Louisiana-formed corporations enjoy, including powers to buy and sell real property.[280] In Louisiana, a foreign corporation cannot be denied a certificate of authority because the laws of the state or country under which the corporation is organized differ from the laws of Louisiana.[281] Although not expressly defined, Louisiana appears to view an alien limited liability company (LLC) as a foreign LLC until a certificate of authority is awarded.[282] Many of the rules that apply to foreign LLCs and partnerships in Louisiana are similar to the rules that apply to foreign corporations.

ii. Mississippi

The Mississippi Constitution permits the legislature of the state to enact laws prohibiting the ownership of domestic real property by non-resident aliens.[283] Mississippi is one of a small number of states that differentiate between resident and non-resident aliens. It permits ownership of real property only by those categorized as resident aliens.[284] Non-resident aliens are statutorily prohibited from acquiring or holding land—except upon foreclosure of a loan—and are subject to the penalty of escheat.[285]

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278. LA. CONST. OF 1974, art. 1, § 4 ("Every person has the right to acquire, own, control, use, enjoy, protect, and dispose of private property. This right is subject to reasonable statutory restrictions and the reasonable exercise of the police power.").

279. LA. REV. STAT. ANN. §§ 12:1(k) (2010) (defining "foreign corporation"), 12:301 (2010) (referencing "foreign corporation").

280. LA. REV. STAT. ANN. §§ 12:306(2) (2010) (discussing powers of foreign corporations), 12:41(b)(4) (2012) (discussing powers of domestic corporations).

281. LA. REV. STAT. ANN. § 12:301.

282. *See* LA. REV. STAT. ANN. § 12:1342 (2010) ("A foreign limited liability company shall not be denied a certificate of authority because the laws of the state *or other jurisdiction* under which such limited liability company is organized differ from the laws of this state." (emphasis added)).

283. MISS. CONST. art. 4, § 84 (2005) ("The Legislature shall enact laws to limit, restrict, or prevent the acquiring and holding of land in this State by nonresident aliens, and may limit or restrict the acquiring or holding of lands by corporations.").

284. MISS. CODE ANN. § 89-1-23 (2011). Escheat involves a reversion of the property to the State due to the inability of the alien to own the property. *Id.*

285. *Id.* Exceptions are provided, inter alia, for non-resident aliens who "(i) hold or acquire land through enforcement of a lien, provided it is divested to a citizen or the alien becomes a United States citizen within twenty years; (ii) declare an intention to become a citizen; or (iii) are citizens of Syria or Lebanon inheriting from citizens or residents of Mississippi." *Id.*

Alien corporations are treated as foreign corporations.[286] By qualifying to do business in the state, however, foreign corporations enjoy the same rights and privileges as domestic corporations, including the power to buy and sell real property.[287] Alien limited partnerships are regarded as foreign limited partnerships, and foreign LLCs are categorized as unincorporated associations organized under laws outside Mississippi.[288] Both types of entities can do business in Mississippi if they become domesticated by qualifying to do business in the state.[289] Non-resident aliens, corporations (except certain banks), and associations of persons composed in whole or in part of non-resident aliens cannot, directly or indirectly, purchase or own public lands.[290]

Although the Mississippi Code does not expressly address whether ownership of royalty or NPRI connected to oil and gas real property constitutes transacting business in the State of Mississippi, the list of activities that are excluded from the definition of transacting business includes "[c]reating or acquiring indebtedness, mortgages and security interests in real or personal property."[291] This language strongly suggests that ownership of these interests does not constitute transacting business in the state.

iii. New Mexico

After the Territory of New Mexico was admitted into the United States, the original 1910 New Mexico Constitution guaranteed that there would be no distinction between resident aliens and citizens regarding the ownership of property.[292] This section was amended in 1921, fueled by concerns among the native population regarding an influx of Asian immigrants. Until quite recently, the Constitution of New Mexico stated that:

> Until otherwise provided by law no alien, ineligible to citizenship under the laws of the United States, or corporation, copartnership or association, a majority of the stock or interest in which is owned or held by such aliens, shall acquire title, leasehold or other interest in or to real estate in New Mexico.[293]

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286. MISS. CODE ANN. §§ 79-4-1.40(20) (2013) (defining "foreign corporation"), 79-4-15.01 (2013) (referencing "foreign corporation"), 79-4-15.20 (2013) (referencing "foreign corporation").

287. *Compare* MISS. CODE ANN. § 79-11-365 (2013) (discussing the effect of a certificate of authority on the powers of foreign corporation), *with* MISS. CODE ANN. § 79-4-3.02 (2013) (discussing general corporate powers).

288. MISS. CODE ANN. §§ 79-14-101(7) (2013) (defining "foreign limited partnership"); 79-29-103(h) (2013) (defining "foreign limited liability companies"), *amended by* 2014 Miss. Laws SB2322.

289. MISS. CODE ANN. §§ 79-14-902 (2013), 79-29-1003 (2013).

290. MISS. CODE ANN. § 29-1-75 (2010).

291. MISS. CODE ANN. § 79-4-15.01(b)(7) (2013). In addition, the code states that "[t]he list of activities in subsection (b) is not exhaustive." *Id.* § 79-4-15.01(c).

292. N.M. CONST. art. II, § 22 (amendment of 1921).

293. *Id.*

Legislation in 1975 rendered this section ineffective by permitting aliens to take title to property, but the section is indicative of the sort of targeted laws one finds in various state constitutions.[294] On November 9, 2006, New Mexicans voted to repeal the provision and allow ownership of land by persons not eligible for citizenship.[295] No state barrier currently remains to alien ownership of real property in New Mexico.

Alien corporations are statutorily treated as foreign corporations.[296] In order to enjoy the same rights and privileges as domestic corporations, including powers to buy and sell real property, a foreign corporation must become qualified to do business in the state by acquiring a "certificate of authority."[297] Foreign corporations are not "transacting business" in New Mexico—and thus do not need to acquire a certificate of authority—by merely investing in or acquiring royalties and other non-operating mineral interests or participating in the execution of division orders, contracts of sale, and other instruments incidental to the ownership of the non-operating mineral interests.[298]

Alien LLPs appear to be statutorily treated the same way as foreign LLPs.[299] Alien LLCs are expressly considered foreign LLCs.[300] Before transacting business in New Mexico, a foreign LLP must file a "statement of foreign qualification."[301] New Mexico law provides that foreign LLPs are governed by the laws of the jurisdiction in which they are formed and cannot be denied a statement of foreign qualification because of differences between the laws of New Mexico and the laws of the state or country of origin of the partnership.[302] As with foreign corporations, both foreign LLPs and LLCs are not considered to be transacting business in New Mexico by purchasing or owning securities such as royalties and other non-operating mineral interests or conducting such activities related to owning them, such as executing division orders or entering contracts of sale and other instruments.[303]

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294. N.M. STAT. ANN. § 45-2-111 (West 2013).

295. S.J. Res. 10, 109th Cong. (2005).

296. N.M. STAT. ANN. §§ 53-11-2(B) (West 2013) (defining "foreign corporation"), 53-17-1 (West 2013) (referencing "foreign country"), 53-17-5 (West 2013) (referencing "foreign country").

297. N.M. STAT. ANN. §§ 53-17-2 (West 2013), 53-11-4(D)–(E) (West 2013) (outlining powers of foreign and domestic corporations).

298. N.M. STAT. ANN. § 53-17-1(K).

299. N.M. STAT. ANN. § 54-1A-101(4) (West 2013) ("'[F]oreign limited liability partnership' means a partnership that is formed under laws other than the laws of this state and has the status of a limited liability partnership under those laws.").

300. N.M. STAT. ANN. § 53-19-2 (West 2013)

301. N.M. STAT. ANN. § 54-1A-1102 (West 2013).

302. N.M. STAT. ANN. § 54-1A-1101 (West 2013).

303. N.M. STAT. ANN. §§ 53-19-54(A)(9) (West 2013) (defining characteristics of LLCs), 54-1A-1104 (West 2013) (defining characteristics of LLPs).

iv. Oklahoma

Oklahoma appears to be very restrictive regarding alien ownership of real property, although from a practical standpoint, the restrictions may be avoided with proper planning. The Oklahoma Constitution prohibits ownership of land in Oklahoma by non-resident aliens.[304] In general, aliens may not acquire or own real property in Oklahoma.[305] The Oklahoma statutes, however, provide two exceptions under conditions set out in § 121 and the sections following.[306] First, aliens in possession of real property at the time the state adopted the restrictions are exempted from them (that is, they are "grandfathered").[307] Second, and more relevant for aliens considering the purchase of oil and gas real property in Oklahoma, the law allows resident aliens to purchase real property.[308] If the alien ceases to be domiciled in Oklahoma while owning real property, the alien must sell the property within five years of leaving the state or the property escheats to the State.[309] The Oklahoma Property Code takes a dim view of attempts to circumvent this prohibition on alien ownership:

> Provided, however, that if any such conveyance shall be made by such alien either to an alien or a citizen of the United States in trust, and for the purpose and with the intention of evading the provisions of this article, or the provisions of the Constitution of this state, such conveyance shall be null and void, and any such lands so conveyed shall be forfeited and escheated to the state absolutely.[310]

Oklahoma statutes provide more limitations on the ownership of real property by corporations in general. First, both the state constitution and the statutes of Oklahoma prohibit all corporations from owning or holding real property other than that located in an incorporated town, village, or city.[311] No corporation of any sort, whether defined as such by the Oklahoma General Corporation Act or not, can purchase and own real property in Oklahoma, except "[s]uch real estate as is necessary and proper for carrying on the business for which any corporation has been lawfully formed or domesticated in [Oklahoma]."[312] The apparent reason for including this section is not to prevent private corporations from owning real property, but to prevent land companies from buying agricultural land and to prevent private corporations from buying more rural land than necessary for their operations. The restriction

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304. OKLA. CONST. art. 22, § 1 (2001).
305. OKLA. STAT. ANN. tit. 60, § 121 (West 2010).
306. 76 Okla. Att'y Gen. Op. 253 (1976)
307. OKLA. STAT. ANN. tit. 60, § 122 (West 2010).
308. *Id.*
309. *Id.* The statute defines the requirement as being a "bona fide inhabitant of this state." *Id.*
310. OKLA. STAT. ANN. tit. 60, § 124 (West 2010).
311. OKLA. STAT. ANN. tit. 18, § 1020(A) (West 2012).
312. *Id.* § 1020(B)(1).

is intended to encourage the ownership of private rural homes.[313] A foreign corporation, if domesticated by qualifying to do business in the state, is considered a "bona fide resident[]" of the state within the meaning of the statutes that restrict ownership of land by aliens, and thus, is no longer subject to such restrictions.[314] This section of the Oklahoma Constitution does not prevent a corporation from taking a lease to prospect land for oil and gas, nor does it prohibit a domesticated foreign corporation authorized by its Oklahoma charter from engaging in production, storage, manufacture, and sale of oil and gas or to acquire real and personal property for those uses.[315] Foreign corporations can own oil and gas and mineral leases and mineral rights and interests and can hold fee simple title in lands where they are specifically useful and proper in the general operation of the corporation's business.[316]

With respect to property acquired for speculative purposes (that is, for resale to another party), the Oklahoma Statutes allow acquisitions that are intended for lease or sale to another entity if the latter entity could have legally acquired the same real property by itself originally.[317] Substantial penalties are assessed based on a percentage of the allocated value of the real property for entities that violate this statutory restriction.[318]

In addition, like most states, Oklahoma defines corporations organized outside the United States as "foreign corporations," which enjoy the same rights as corporations domestic to Oklahoma after qualifying to do business in the state.[319] A 1979 Oklahoma Attorney General opinion expressed the position that corporations organized outside the United States face the same incapacity on real property ownership as individual foreigners.[320] Oklahoma case law has established that foreign corporations, while considered alien individuals for purposes of restrictions upon ownership of real property prior to the time they become qualified to do business in the state, do not face such incapacity after they become qualified to do business in Oklahoma.[321] Alien LLCs and limited partnerships are considered the same as foreign LLCs and limited partnerships, respectively.[322] Upon qualifying to do business in Oklahoma, both alien and

313. LeForce v. Bullard, 454 P.2d 297, 299 (Okla. 1969).

314. State *ex rel*. Cartwright v. Hillcrest Invs., Ltd., 630 P.2d 1253, 1258 (Okla. 1981). For an in-depth description, see *Recent Developments*–Corporations*: Alien Corporations that Domesticate in Oklahoma May Hold Land*, 34 OKLA. L. REV. 194 (1981).

315. McCray v. Miller, 184 P. 781, 781 (Okla. 1919).

316. Tex. Co. v. State *ex rel.* Coryell, 180 P.2d 631, 641 (Okla. 1947).

317. OKLA. STAT. ANN. tit. 18, § 1020(B)(5).

318. *Id.* § 1020(G)(1).

319. OKLA. STAT. ANN. tit. 18, §§ 1130(D) (West 2012), 2001(8) (West 2012).

320. 79 Okla. Att'y Gen. Op. 286 (1979) (withdrawing 74 Okla. Att'y Gen. Op. 214 (1974)).

321. State *ex rel.* Cartwright v. Hillcrest Invs., Ltd., 630 P.2d 1253, 1259 (Okla. 1981).

322. OKLA. STAT. ANN. tit. 18, § 2001(9) (defining "foreign limited liability company"); OKLA. STAT. ANN. tit. 54, § 302(4) (defining "limited partnership"), *repealed by* 2010 Okla. Sess. Laws Ch. 384, § 108.

foreign LLCs and limited partnerships are authorized to do business in Oklahoma.[323]

Like other states, Oklahoma recognizes that owning passive, nonworking interests in oil and gas real property does not require being qualified to transact business in the state.[324] Foreign corporations that passively own title to mineral interests and mineral leases in Oklahoma are not "engaging in or transacting business" in the state and do not need to acquire a certificate of domestication.[325] The Oklahoma Corporation Code effectively provides that LLCs "[i]nvesting in or acquiring royalties or other non-operating mineral or leasehold interests and the execution of division orders, contracts for sale, leases and other instruments incidental to the ownership of the nonoperating interests" are not transacting business in Oklahoma.[326]

v. Texas

The Texas Business Organizations Code contains a provision that expressly confers upon aliens the same rights to own real property in Texas as United States citizens.[327] The statute treats foreign corporations in the same manner as corporations organized under the laws of another state.[328] Upon registration with the Texas Secretary of State, such foreign corporations benefit from the same privileges and rights as domesticated corporations—including the power to buy and sell real property.[329] Other than the requirement to become qualified to do business in Texas, if the foreign corporation will actively manage assets in the state, then no other express restrictions on alien or alien-controlled corporations exist in Texas. Although the law is not expressly clear, the statutory language appears to view alien LLCs the same way as LLCs from other American states.[330] Foreign LLCs are permitted to conduct business in Texas when they have been qualified in the state.[331] Curiously, the statutory

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323. OKLA. STAT. ANN. tit. 18, § 2043 (West 2012) (referencing "limited liability company"); OKLA. STAT. ANN. tit. 54, § 350(A) (referencing "limited partnership"), *repealed by* 2010 Okla. Sess. Laws Ch. 384, § 108.

324. *See* Wilson v. Williams, 222 F.2d 692, 697 (10th Cir. 1955).

325. *Id.*

326. OKLA. STAT. ANN. tit. 18, § 2049(A)(12) (West 2012).

327. TEX. PROP. CODE ANN. § 5.005 (West 2007).

328. TEX. BUS. ORGS. CODE ANN. §§ 1.002(28) (West 2012 & Supp. 2013) (defining "foreign corporation"), 9.001 (West 2012) (referencing "foreign country").

329. TEX. BUS. ORGS. CODE ANN. §§ 1.105 (West 2012) (defining powers of foreign corporations), 2.101 (West 2012) (defining powers of domestic corporations).

330. TEX. BUS. ORGS. CODE ANN. §§ 9.003 (West 2012) (a foreign LLC is an entity formed under the laws of a jurisdiction other than the State of Texas), 9.004 (West 2012) (referencing a country in which a foreign LLC is formed).

331. TEX. BUS. ORGS. CODE ANN. § 9.008 (West 2012) (stating a certificate of authority is required to do business).

definition of a foreign limited partnership does not include an alien limited partnership.[332]

Some investment activities do not constitute doing business in Texas and do not require registration with the State. Activities such as investing in royalties (NPRI and ORRI in Texas), non-operating mineral interests, executing division orders, and conducting ancillary activities related to owning these interests (such as executing contracts of sale and division orders) are not considered to be transacting business in Texas and do not require domestication.[333]

c. Ban on Crude Exports

During the late 1970s, the federal government largely banned exportation of crude oil without a license in an effort to conserve oil reserves and hold the line against crude oil imports.[334] Neither goal was achieved, but the laws that gave rise to the ban—the Energy Policy and Conservation Act of 1975, supplemented by the Export Administration Act of 1979—remain.[335] Several categories of crude are exempted from the need to get an export license—such as United States crude exported to Canada—but most United States crude cannot be exported without a license from the Bureau of Industry and Security after a finding that crude oil exports sought are "consistent with the national interest and the purposes of the Energy Policy and Conservation Act."[336] Foreign investors considering purchasing property in the hope of exporting crude oil from the United States must be mindful of this restriction, particularly if they intend to purchase leases or mineral interests and then take production themselves in kind.[337]

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332. TEX. BUS. ORGS. CODE ANN. § 151.001 (clarifying that a "foreign limited partnership" means a limited partnership formed under the laws of another state and defining "state" as any state of jurisdiction of the United States). No basis exists for a distinction between foreign LLCs and foreign LLPs. *See id.* The only explanation for the distinction is that it is an oversight and will have no practical effect on the ability of an alien LLP to conduct business in the state. *See id.*

333. TEX. BUS. ORGS. CODE ANN. § 9.251(13)–(14) (West 2012) (covering foreign limited partnerships, foreign business trusts, foreign real estate investment trusts, foreign cooperatives, foreign public or private limited companies, or other foreign entities).

334. Blake Clayton, *The Case for Allowing U.S. Crude Oil Exports*, POL'Y INNOVATION MEMORANDUM, no. 34, July 2013, at 1, 1, *available at* http://www.cfr.org/oil/case-allowing-us-crude-oil-exports/p31005#cid=soc-email-at-policy_innovation_memorandum-the_case_for_allowing_us_crude-07 0113.

335. *Id.* (discussing the Energy Policy and Conservation Act, Pub. L. No. 94-163, 89 Stat. 871 (1975), and the Export Administration Act of 1979, Pub. L. No. 96-72, 93 Stat. 503).

336. *Id.*; *see* Energy Policy and Conservation Act § 103(b)(2).

337. *See generally* Bob Tippee, *U.S. Should Repeal Its Antique Ban on the Export of Crude*, OIL & GAS J. (May 17, 2013), http://www.ogj.com/articles/2013/05/us-should-repeal-its-antique-ban-on-the-export-of-crude.html (explaining the limitations placed on the export of crude oil and the need for reform).

3. Necessary Technical Levels, Financial Conditions and Compositions of Shareholders, and Technology Transfers

For operators, all federal and state jurisdictions require some kind of drilling permit and bonding to ensure that wells can be plugged and abandoned as specified by law.[338] Depending on how the oil and gas rights are owned and the jurisdiction where the development is to take place, a developmental plan may need to be filed with the appropriate authorities to demonstrate that the proposed exploration and primary and secondary development can be conducted in a way that follows the safety and environmental guidelines of the federal or state government.

Mineral rights issued by federal and state agencies generally do not have restrictions that require the prospective lessee to have a specific technical level or ability to *develop* the minerals.[339] The high cost to acquire mineral rights, particularly offshore, is usually an effective practical barrier to unsophisticated parties acquiring and developing a federal or state mineral lease.[340] Many professional brokers exist, however, who acquire leases without any intention of developing the minerals themselves. The lease brokers then assign these leases to other parties in return for money or a cut of the minerals as they are developed. No state or federal law known to the author curtails the ability of the holder of a federal or State-issued mineral right to assign that mineral right to another party, unless the assignee is not qualified because of alien status. Privately owned mineral interests may contain contractual clauses that disallow assignment of the mineral interest without the approval of the issuer of the mineral right.

Once offshore oil and gas development is undertaken, however, some technical and financial wherewithal must be demonstrated. With respect to both spills and discharges and substantial threats of the discharge of oil, the Oil Spill Financial Responsibility for Offshore Facilities (OSFR) provides the demonstrated capability and means by which a responsible party for a Covered Offshore Facility (COF) will need to meet removal costs and damages for which it is liable under Title I of the Oil Pollution Act of 1990, as amended.[341] It is not a specific insurance requirement, bond, letter of credit, or other deposit that must be paid up-front, but rather, a general tabulation of the financial ability of a company to clean up spills and dismantle COFs. The OSFR amount

338. *See* Clayton, *supra* note 334, at 1–2.

339. *See id.* No state requires any specific level of technical sophistication for registering to do business (i.e., to acquire "domestication" status) within that state. *See id.*

340. *See id.*

341. 76 Fed. Reg. 64,461-01 (Oct. 18, 2011) (to be codified at 30 C.F.R pt. 553 (2013)). COFs are defined in this section of the code. *See* 33 U.S.C. § 2701 (2012); 76 Fed. Reg. 64,461-01; *Oil Spill Financial Responsibility (OSFR) for Offshore Facilities*, BUREAU OF OCEAN ENERGY MGMT., http://www.gomr.boemre.gov/homepg/lsesale/osfr.html (last visited Mar. 26, 2014). A clearinghouse of information related to the OSFR for Offshore Facilities Act can be found on BOEM's website. *Oil Spill Financial Responsibility (OSFR) for Offshore Facilities*, *supra*.

for each applicant is determined by the barrels of oil equivalent (BOE) through an application and investigative process.[342] Generally, the lessor or operator must show it has a certain specified level of acceptable assets on hand with which it could presumably clean a spill or discharge or dismantle a COF.[343]

Each COF must have a single designated applicant.[344] The applicant is either the actual lessee or the designated operator. That party must show that it has the financial ability to pay for cleanup in the event of a spill or discharge of oil or other covered pollutant.[345] The amount it must show is dependent on the potential spill size of the largest COF in its portfolio of covered assets.[346] This amount is calculated using a chart located in the Code of Federal Regulations.[347]

Geological and geophysical (G&G) exploration and investigation of the outer continental shelf are regulated under 30 C.F.R. § 251 and § 280, including requirements of a permit or notice prior to exploration, periodic reporting, and certain data submission.[348] G&G work may be conducted under these regulations without obtaining any mining rights, as described in 30 C.F.R. § 251.2.[349] An alien company or person must first establish itself as a domestic entity to conduct such operations.[350] The holder of a geology and geophysics permit must be a "person" as defined in 30 C.F.R. § 251.1.[351]

A prime motivator of foreign investors is often not only to gain access to ideas and know-how for use outside the United States, but also to acquire and export actual technology and technical information. Foreign investors must remember that the intellectual property of the service providers they employ will not be acquired merely by hiring the contractor.[352] In addition, export restrictions may apply to technology exported from the United States via the Export Administration Act.[353]

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342. *See* Carol S. Williams, Bureau of Ocean Energy Mgmt., General Bond Requirements, Supplemental Bond Requirements and Oil Spill Financial Responsibility, Presented at the Rocky Mountain Mineral Law Foundation Bonding and Oil Spill Financial Responsibility (Jan. 23–25, 2013) (notes available at http://www.boem.gov/uploadeddFiles/BOEM/BOEM/newsroom/Speeches/2013/RMMLF-Presentation-Williams-20130123.pdf).

343. *See id.*

344. *See id.*

345. *See id.*

346. *Id.*

347. *See* 30 C.F.R. § 553.13(3) (2013).

348. 30 C.F.R. §§ 251.1–.15 (2012), 280.20–.24 (2013).

349. 30 C.F.R. § 551.2 (2013).

350. 30 C.F.R. § 185 (2013).

351. *See* 30 C.F.R. §§ 251.1, 551.4–.5 (2013). Although the word "person" does not appear in portions of the regulations, the word "you"—as stated in the definitions—refers to a "person." *Id.* Therefore, the "you" as used in 30 C.F.R. §§ 551.4–.5 must be a "person." *See* 30 C.F.R. §§ 551.4–.5. This analysis was confirmed by George Dellagiarino, an officer with the BOEM in Washington D.C. Ships with foreign registries that seek to conduct scientific surveys on the OCS for which the data collected shall be made publicly available must register with the Foreign Vessel Clearance Office. *See* 19 U.S.C. § 1434 (2012).

352. Michael P. Darden, Challenges in Doing U.S. Oil and Gas Deals with Foreign Entities, Presented at the 31st Annual Oil, Gas, and Energy Resources Law Course of the State Bar of Texas (Oct. 4, 2013).

353. Export Administration Act of 1979, Pub. L. No. 96-72, 93 Stat. 503.

4. *Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) & Other Tax Considerations*

a. *Foreign Investment in Real Property Tax Act of 1980*

Foreign owners of real property in the United States face a last hurdle when they divest their assets. In 1980, the United States Congress passed FIRPTA to make equal the tax treatment of domestic and foreign investors in United States real property, including mineral rights.[354] Before the passage of FIRPTA, profits from the sale of real property were taxed only if "effectively connected" to a trade or business of the United States.[355] In contrast, FIRPTA subjects all income from sales of United States real property to federal taxation because FIRPTA treats all dispositions of domestic real property interests by alien entities as "effectively connected" to a trade or business of the United States.[356]

Through FIRPTA, prospective buyers of oil and gas real property owned by foreigners are required to withhold 10% of the final sales price.[357] Before the closing date of the sale, the seller of the oil and gas real property may petition the Internal Revenue Service (IRS) to have this withheld 10% reduced to the amount of estimated tax required.[358] While foreigners are generally not taxed on capital gains, FIRPTA requires foreigners to be taxed on capital gains from the sale of real property, including as-yet unproduced oil and gas.[359]

FIRPTA utilizes broader tax valuation parameters to calculate the amount owed. Specifically, the taxable gain is equal to the difference between the amount of proceeds from the sale and the amount of the adjusted basis of the property exchanged.[360] If the amount of the proceeds received is subject to one or more contingencies, the proceeds received are not final until the contingency is settled.[361] The tax is typically paid the year of the sale or proportionately over the span of years that the foreign seller receives sales proceeds. Significant penalties accrue to those who do not pay the tax within twenty days

354. Foreign Investment in Real Property Tax Act of 1980, Pub. L. No. 96-499, 94 Stat. 2682.

355. *See id.*

356. *See* 26 U.S.C. § 861 (2012).

357. 26 U.S.C. § 1445 (2012). Several exceptions exist absolving the purchaser from the requirement to withhold the 10% of the purchase price, such as in the instance in which the purchaser is buying property for use as a residence for a price of $300,000 or less, but none are significantly applicable to oil and gas real property. *Id.*

358. *Id.* The IRS maintains the necessary petition form (Form 8288-B) and instructions for completing it. *Form 8288-B: Application for Withholding Certificate for Dispositions by Foreign Persons of U.S. Real Property Interests*, DEPARTMENT OF THE TREASURY, INTERNAL REVENUE SERVICE, http://www.irs.gov/pub/irs-pdf/f88288b.pdf (last revised Aug. 2013); *Instructions for Form 8288*, DEPARTMENT OF THE TREASURY, INTERNAL REVENUE SERVICE, http://www.irs.gov/pub/irs-pdf/i8288.pdf (last revised Aug. 2013).

359. Foreign Investment in Real Property Tax Act of 1980.

360. 26 U.S.C. § 1001 (2012).

361. See 26 U.S.C. § 871 (2012).

of the sale or either (i) withhold the 10%, or (ii) withhold the amount approved by the IRS in the seller's petition.[362]

b. Tax Partnerships, Revenue Ruling 77-176, and Blocker Companies

i. Tax Partnerships & Revenue Ruling 77-176

In addition to FIRPTA, some types of mineral acquisitions may make establishing a tax partnership desirable. In the oil and gas industry, even the simplest and most informal agreement may have significant tax implications. For example, farmout agreements are very common in the foreign investor context. "A farmout is basically an agreement under which one who owns an oil and gas lease"—called the "farmor"—"assigns an interest in it" (or even the entire lease) to another party—called the "farmee"—if the second party, often a foreign investor seeking to break into a productive field that has already been leased, conducts exploration and drilling activities.[363] Farmout agreements often cover a large tract of land, with the farmee obligated to drill on one or more portions of the tract.[364] Subsequently, the farmout often provides that the farmee is then assigned all of the leasehold and operating working interest in the tract comprising the completed well and an undivided portion of the leasehold working interest in the original tract, exclusive of the spacing unit around the well.[365] Before 1977, the oil industry as a whole typically treated such a common farmout as not giving rise to any taxable income under the "pool of capital" concept.[366] Under this paradigm, the farmee was not thought to have received compensation for services performed—drilling the well—but instead as having contributed to the pool of capital needed for development of the prospect.[367]

In 1977, the IRS released Revenue Ruling 77-176, which split apart the two types of transferred tracts described above.[368] The tract comprising the drill site spacing unit still did not give rise to any taxable income, but the assignment of the rest of the leasehold, which Revenue Ruling 77-176 treated as separate property, now gives rise to a taxable income event that potentially results in adverse tax consequences to both parties.[369] Tax partnerships are seen as a way to get around this tax liability because typically no gain or loss is realized by the partnership or its partners from real property contributions to the partnership

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362. 26 U.S.C. § 1445(e)(4) (2012); *Form 8288-B: Application for Withholding Certificate for Dispositions by Foreign Persons of U.S. Real Property Interests*, *supra* note 358.
363. LOWE ET AL., *supra* note 250, at 961.
364. *Id.* at 961–62.
365. *Id.* at 962, 967.
366. *Id.* at 967.
367. *Id.*
368. Rev. Rul. 77-174, 1977-1 C.B. 77.
369. *Id.*

upon formation.[370] The partnership agreement determines each partner's share of each item of income and expense or, if the agreement is silent as to a particular item, each partner's distributive shares are determined by the partner's respective shares of the taxable income or loss.[371] The partnership agreement can provide for a special allocation that is disproportionate to the partner's individual capital contributions, but not if it is deemed to purposefully avoid taxation.[372] If a tax partnership is properly set up to cover the farmout scenario described above, the parties can probably obtain the same income tax consequences for their arrangement as existed prior to Revenue Ruling 77-176.

ii. Blocker Corporations

Generally, foreign investors who otherwise may not be subject to United States income tax may have to pay taxes when conducting business in the United States; in such case they are required to pay on the same terms as an American corporation or individual.[373] In the case of a partnership—for example, one formed to explore and develop minerals via a farmout agreement—each individual partner's income from the partnership could be considered to be derived from taxable United States business.[374] To prevent this, an entity known as a "blocker corporation" may be established.[375] Now the foreign investor can invest through the blocker corporation and thus can avoid being personally categorized as a partner and facing personal tax consequences.[376] Of course, the blocker corporation will have to pay taxes on its share of the partnership's income.[377]

III. CONCLUSION

Each of the areas of law and acts described above is very broad, complex, and far-reaching; attorneys and scholars have spent their entire careers practicing in and writing about them. This Article does not seek to examine any one of them completely, but rather to blaze a descriptive trail through the salient areas and acts of law encountered by foreign investors in United States oil and gas real property assets.

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370. Arnold C. Wegher, *Taxation of Earned Interests—The Impact of Revenue Ruling 77-176*, 24 ROCKY MTN. MIN. L. INST. 521, 540 (1978).

371. *Id.* at 542.

372. *Id.*

373. 26 U.S.C. § 1361(c)(2)(A) (2012).

374. 26 U.S.C. § 702(a)(8) (2012).

375. Samuel D. Brunson, *Repatriating Tax-Exempt Investments: Tax Havens, Blocker Corporations, and Unrelated Debt-Financed Income*, 106 NW. U. L. REV. 225, 235, 241 (2012).

376. *Id*. at 243.

377. *Id*. at 244–45.

At the national level, FINSA has developed into the largest threat for foreign energy investors.[378] With the potential ability to unravel entire transactions—even those completed before CFIUS takes notice—along with the negative press that can accompany such a fiasco, foreign investors must take great care to structure possibly troublesome deals to withstand both scrutiny and delay. Fortunately, past hardships have provided a relatively good record of possible obstacles such that astute practitioners with flexible corporate clients should be able to avoid the worst-case scenarios, depending on the deal terms.[379]

Further, the Survey Act and the general federal use and ownership limitations are relatively predictable in their scope and broad application.[380] While these laws can add costs when specialists are hired to help navigate compliance demands, frustration at the work involved (the Survey Act), and the stark limitations (federal use and ownership limitations), the danger of large transactions being retroactively unraveled, as with FINSA, is small.

With regards to state laws affecting real property, the safest route for any potential foreign investor is to hire local counsel from the state wherein the property is located. Whereas a large firm with a national reach, perhaps based in New York or Washington D.C., can certainly help with federal laws and the laws of local states and will have personnel in other offices with experience in distant large states, the advent of unconventional plays in over twenty states means that oil and gas assets are often found in remote states with low populations, such as Wyoming, West Virginia, or North Dakota. As the examination of just five states shows, great variance can be encountered from state to state in the way real property can be held by foreigners.[381]

Ultimately, potential foreign purchasers of American energy assets face not a 100-yard dash, but rather, a longer race with hurdles. In order to prevent self-inflicted strife, such purchasers must plan ahead to jump each hurdle and be flexible enough to respond to deal structure changes and delays. If you want to buy American oil and gas assets, seek permission, not forgiveness.

378. *See supra* Part II.B.
379. *See supra* Part II.E–G.
380. *See supra* Part II.H.1.
381. *See supra* Part II.H.2.b.