

# CFIUS and Its Proposed Regulations Expanding Jurisdiction - Foreign Investment in the United States will Face More National Security Reviews

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The U.S. Department of the Treasury's Office of Investment Security published proposed regulations on September 24 ("Proposed Regulations"). Under the Proposed Regulations, more foreign investment transactions will be subject to scrutiny by the Committee on Foreign Investment in the United States ("CFIUS"). The expanded scope of transactions that will become subject to CFIUS jurisdiction would include certain foreign non-controlling stakes in U.S. businesses whose operations involve critical infrastructure, export-controlled technologies, or sensitive personal data, as well as real estate transactions that involve properties in close proximity to certain military installations or that are part of certain airports or seaports. In addition, the Proposed Regulations impose mandatory reporting to CFIUS of certain transactions by foreign governments and their subsidiaries in U.S. businesses.

The scope of potentially affected transactions under the Proposed Regulations includes those in aerospace, architecture and construction, aviation, civil engineering, defense, electric power generation and transmission, electronics, energy, healthcare, insurance, public utilities, real estate, telecommunications, and many others. Accordingly, U.S. businesses and foreign investors considering new investment transactions in the United States should consider seriously the Proposed Regulations alongside the current CFIUS regulations in 31 CFR Part 800 and 31 CFR Part 801. Such parties should carefully weigh whether a declaration filing with CFIUS is mandated or would be prudent to shield the parties from later adverse action by CFIUS. The Proposed Regulations (in one form or another) will become effective in early 2020.

## Expanded CFIUS Jurisdiction for Non-Controlling Foreign Investment

The Proposed Regulations would expand CFIUS jurisdiction to cover certain investments in "*TID U.S. Businesses*." A "*TID U.S. Business*" means any U.S. business involved in critical technologies (the "*T*"), critical *infrastructure* (the "*I*"), or sensitive personal *data* (the "*D*") that satisfy the following criteria:

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- **Critical Technologies.** The term “*critical technologies*” in the Proposed Regulations means any goods, software, or technology controlled under U.S. export controls and subject to particular licensing requirements under the International Traffic in Arms Regulations (“ITAR”), the Export Administration Regulations (“EAR”), or any other U.S. export control regimes administered for non-proliferation reasons (e.g., nuclear or missile technologies, select agents and toxins, chemical weapons). CFIUS has already imposed a mandatory reporting requirement for non-controlling foreign investment in U.S. businesses with certain critical technologies through its Pilot Program that went into effect on November 10, 2018 (see our earlier update on the Pilot Program [here](#)). CFIUS continues to review the Pilot Program and may revise the mandatory reporting requirements imposed by the Pilot Program in conjunction with finalization of the Proposed Regulations. The list of “critical technologies” will expand with new regulations on “foundational and emerging technologies,” which are expected before the end of the year.
- **Critical Infrastructure.** The term “*critical infrastructure*” in the Proposed Regulations is defined broadly as certain activities in industries listed in an annex (“Annex”) to the Proposed Regulations, covering many energy, government contracts, telecommunications, transportation, and other products and services. The Annex identifies the type of critical infrastructure as well as the specified U.S. activities relating to that infrastructure. To be considered a U.S. business involved with critical infrastructure under the Proposed Regulations, the U.S. business must be *both* involved with the type of critical infrastructure *and* the type of activities for that infrastructure specified in the Annex.
- **Sensitive Personal Data.** Under the Proposed Regulations, the term “*sensitive personal data*” means data that can distinguish or trace an individual’s identity and is collected or maintained by a U.S. business about: (i) any number of sensitive U.S. persons (e.g., U.S. military personnel or federal employees), (ii) one million or more individuals, or (iii) less than one million individuals where the business intends to collect or maintain data on one million or more individuals in the future. This definition would include many U.S. companies that serve large numbers of individual customers or that otherwise maintain data relating to large numbers of individuals. Some key sectors where such databases of sensitive data may be necessary for an effective U.S. business would include financial services, retail (either online or offline), and healthcare.

The definitions of a “*TID U.S. Business*” would sweep in many more companies, industries, and sectors than were previously subject to CFIUS jurisdiction. In particular, in the past, many U.S. companies involved with the design, construction, or support of critical infrastructure (e.g., in highway or bridge construction) or in the handling of large amounts of sensitive personal data probably never considered themselves of interest to CFIUS, but the Proposed Regulations now make clear that CFIUS is interested in reviewing certain transactions involving foreign investment in such companies. Accordingly, the Proposed Regulations would expand the volume of foreign investment activity that would be subject to CFIUS scrutiny.

Not all foreign investments in TID U.S. Businesses would be considered “*covered investments*” under the Proposed Regulations. A “*covered investment*” is broadly defined in the Proposed Regulations as a non-controlling foreign investment that gives one of the following to the foreign investor related to a “*TID U.S. Business*”: (i) access to material nonpublic technical information about the U.S. business’s “*critical infrastructure*” or “*critical technology*”; (ii) a seat on the U.S. business’s board of directors or observer

rights, or the ability to nominate someone for such positions; or (iii) decision-making authority concerning any “*critical technology*,” “*critical infrastructure*,” or “*sensitive personal data*.”

If a foreign investor makes a “covered transaction” (meaning either a transaction that leads to a change in control, or a non-controlling “*covered investment*”) in a “*TID U.S. Business*,” the parties will need to consider whether to file a voluntary notice with CFIUS. If the parties decline to voluntarily notify CFIUS about such a transaction, they must accept the risk that CFIUS could, either before or after closing of the transaction, require that the parties take measures to mitigate any perceived national security impacts of the transaction, up to and including the required divestiture of any interest acquired by the foreign investor in the U.S. business. On the other hand, if the parties decide to submit a voluntary notice to CFIUS, the parties may submit an abbreviated declaration that would lead to a 30-day review period after which CFIUS could respond by telling the parties there is no national security issue in the proposed transaction or, alternatively, that there is such an issue and the parties must file a full-length notice to CFIUS. However, as an alternative to such a declaration, the Proposed Regulations allow the parties to immediately submit a voluntary notice to CFIUS and thus skip the declaration step completely. CFIUS review and investigation of a full notice could last 45 days to 105 days.

The Proposed Regulations additionally impose mandatory reporting requirements for investments in the United States made by foreign government investors or investors whose ultimate owners are a foreign government. In particular, mandatory reporting is triggered for a “*covered transaction*” in a “*TID U.S. Business*” that transfers 25% or more interests to foreign investors that are themselves 49% or more owned by a foreign government. Under the Proposed Regulations, a foreign government is deemed to have a 100% interest in any entity in which it acts as a parent by virtue of majority ownership of voting rights or in which the foreign government has rights to the majority of the profits of the entity. Accordingly, if a foreign government holds the majority of the ownership, either directly or indirectly, of a foreign investor, that investor would be considered to be acting on behalf of the foreign government under the Proposed Regulations.

The Proposed Regulations also include two potentially significant exceptions to what CFIUS would consider to be a “*covered investment*.” First, CFIUS may establish a mechanism by which it can designate a foreign country as “*excepted*,” meaning that such a listed country and its investors generally will not be considered to make non-controlling “*covered investments*.” The Proposed Regulations do not specify the criteria that CFIUS would use to designate such an excepted foreign country. However, even an excepted country’s foreign investment in a U.S. business would remain subject to CFIUS jurisdiction if such an investment results in foreign control of a U.S. business. Second, under the Proposed Regulations, a covered investment would not include those transactions made by certain investment funds in which a foreign person holds only a passive interest and such foreign person is not controlling the investment fund’s decisions.

## **Expanded CFIUS Jurisdiction for Real Estate Transactions**

In addition, FIRRMA required CFIUS to promulgate new regulations to deal with certain real estate transactions. The Proposed Regulations thus include a new 31 C.F.R. Part 802 to govern CFIUS reviews of real estate transactions that involve either: (i) real property relating to key U.S. airports and seaports, or (ii) real property that is in close proximity to a U.S. military installation or other U.S. Government site that is sensitive for national security reasons. The Proposed Regulations give detailed criteria that define the scope of such covered real estate transactions. CFIUS provides a finite list of U.S. airports, seaports, and military installations, including the relevant distance from those locations that are covered under the Proposed Regulations. For the most part, in urban areas, the new proposed rules generally cover only sites that are within a radius of one mile of listed U.S. military installations. Outside of urban areas, with respect to certain specified U.S. military installations that are viewed as particularly sensitive, this “proximity” concern extends to 100 miles on land (approximately 160 km), 12 nautical miles (approximately 22.22 km) offshore, and even entire counties.

The Proposed Regulations also create certain blanket exemptions for some forms of real estate. Under the Proposed Regulations, within urban areas, transactions that do not involve property located on a listed U.S. seaport or airport or that are not within one mile of a listed U.S. military installation are exempt. The Proposed Regulations also exempt single housing units, lease or concession of commercial retail space in an airport or seaport, commercial office space where foreign owners and tenants do not exceed 10% of the total office space in the building, and land that is either owned by a Native American village, group, or corporation, or held in trust by the U.S. Government for the benefit of a Native American tribe or other entity. The Proposed Regulations also would exempt certain transactions by securities underwriters and insurers. The Proposed Regulations further contemplate the future exemption of foreign real estate investors from certain countries if those investors have not committed any serious U.S. law violations, including any U.S. export control or economic sanctions violations.

Of great relevance for non-U.S. mortgage lenders and other creditors, the Proposed Regulations cover lending transactions that would grant any contingent property rights to the foreign creditor. The Proposed Regulations would treat a credit default or imminent credit default as a triggering event that can create CFIUS jurisdiction. The new rules also indicate that a property transfer in the context of bankruptcy proceedings could create a covered transaction. Thus, if a foreign creditor intends to rely substantially upon such contingent property rights as security for its credit, it would be well for such a foreign creditor to review its CFIUS exposure *before* extending the credit facility.

As with the Proposed Regulations summarized above, the new real estate transaction rules would allow parties in any covered real estate transaction to voluntarily submit either a declaration to CFIUS with a review period of 30 days or a standard voluntary notice to CFIUS with a review and possibly investigation of between 45 and 105 days.

## **Filing Fees**

FIRRMA also granted CFIUS authority to impose filing fees upon the filing of declarations or notices about proposed transactions that are subject to its regulations. However, to date, CFIUS has not proposed any such filing fees. That said, CFIUS expressly noted in its Frequently Asked Questions (“FAQs”) released at the same time as the Proposed Regulations that it would “publish separate proposed regulations regarding fees at a later date.”

Dorsey & Whitney attorneys have had decades of experience helping clients navigate CFIUS issues in the context of proposed investment, acquisition, or other transactions and in reporting and clearing such proposed transactions with CFIUS under Section 721.