

CFIUS Issues Proposed FIRRMA Regulations

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Introduction

On September 17, 2019, the Treasury Department issued highly anticipated proposed final regulations intended to implement fully the reforms in the foreign investment review process wrought by the [Foreign Investment Risk Review Modernization Act of 2018](#) (“FIRRMA”), passed in August 2018.¹ The proposed regulations are divided into two parts. First and most significantly, the [Provisions Pertaining to Certain Investments in the United States by Foreign Persons](#) would replace the existing regulations in 31 C.F.R. Part 800. This rule would, among other things: (i) permanently expand the jurisdiction of the Committee on Foreign Investment in the United States (“CFIUS”) to reach non-controlling investments in certain U.S. businesses; (ii) create exceptions to this expanded authority for certain types of investors; (iii) expand the scope of mandatory filing transactions beyond the current “Pilot Program,”² which CFIUS implemented in the fall of 2018;³ and (iv) establish a streamlined voluntary declaration process for covered transactions to supplement the voluntary notice option.

CFIUS also issued a separate proposed rule on transactions involving real estate, [Provisions Pertaining to Certain Transactions by Foreign Persons Involving Real Estate in the United States](#), which, for the first time in CFIUS’s history, asserts jurisdiction over real property even if that property is not part of a U.S. business.

The proposed regulations are not effective immediately. They are subject to public comments, which are due on October 17. Treasury is required to consider and respond to all comments submitted when it issues the final regulations. Given the expected volume of comments, Treasury may take several months before finalizing its rules. The final regulations will take effect the earlier of February 13, 2020, or 30 days after publication in the Federal Register of a determination by the CFIUS Chairperson that the regulations, organizational structure, personnel, and other resources

¹ Please see our prior memorandum discussing FIRRMA, [New CFIUS Legislation Enacted](#).

² See 31 C.F.R. part 801.

³ The Pilot Program, which covers transactions involving U.S. businesses that produce, design, test, manufacture, fabricate, or develop one or more critical technologies, will remain in place until the final regulations are issued. Those final regulations are expected to incorporate some version of the pilot program on a permanent basis. See our prior memorandum, [CFIUS Pilot Program Implements FIRRMA Reforms Targeting Certain “Critical Technologies” and Requiring Mandatory Declarations](#).

necessary to administer the new provisions are in place. As currently drafted, the proposed regulations would not apply to any transaction that was signed (including through a binding agreement establishing the material terms of the transaction) prior to their effective date.

Overview and High-Level Takeaways

- **Broader Reach:** As expected, the draft CFIUS regulations implement the dramatic expansion of the Committee’s jurisdiction authorized by FIRRMA last year.
- **Additional Complexity:** The proposed regulations offer welcome clarity on certain issues and definitions, but, in doing so, create an environment of assessment, review, execution and post-closing supervision that is far more complex than we have seen in CFIUS’s 30-year history. Complexity will lead to confusion and errors, despite good faith on the part of transaction parties and CFIUS. It may well take a year or more from the regulations’ effective date before a new equilibrium emerges.
- **Less Than Meets the Eye?** Most of the new jurisdiction, new vocabulary and new concepts introduced by the proposed regulations relate to non-controlling “covered investments,” defined to distinguish them from the traditional “covered transactions,” in which there is an acquisition of control.⁴ For control transactions, which generally need only involve an acquisition of over 10 percent of a target’s equity, rather little has changed. Investors in which a non-U.S. government holds a “substantial interest” will face a wider range of mandatory filings, even as compared to the current Pilot Program regime, but high-profile, high-value M&A transactions by foreign private investors will face largely the same opportunities, conflicts and considerations they have been balancing for the last several years.
- **But Context Matters:** Even for private, control acquisitions, the proposed regulations’ elaboration of factors affecting non-control investments will establish the environment in which decisions about national security threats and vulnerabilities are made. The elaboration of “covered investment critical infrastructure” in Appendix A to Part 800, for instance, sets some floors for what the broader, vaguer definition of “critical infrastructure” must cover, even though that definition has not changed since the 2008 regulations. CFIUS reviews will remain a dynamic process with practices and expectations constantly evolving.

⁴ As discussed below, traditional “covered transactions” are now referred to as “covered control transactions,” while “covered transactions” now encompass both control and non-control investments.

- **Increased Case Load Expected:** The CFIUS member agencies have substantially increased their staffing, but the proposed regulations estimate that case volume will rise appreciably, suggesting that processing times are unlikely to drop significantly, at least in the short term. The Committee’s forecast that short-form declarations will substantially outnumber traditional notifications will depend on whether parties find that such declarations result in faster clearances.
- **Early Onset:** As has been the case for the last year, dealmakers will have to evaluate CFIUS issues and make at least preliminary decisions earlier in the deal planning and negotiation processes than has historically been necessary, often before there has been an opportunity for due diligence.
- **Comments Matter:** CFIUS must respond to comments submitted on the proposed regulations. History demonstrates that the responses to interested party comments remain a vibrant part of the ongoing interpretive process for years after final regulations become effective.
- **Deals Will Be Cleared:** The regulations impose appreciable new burdens on foreign investors, but the U.S. government continues to welcome foreign direct investment and recognize the importance of foreign capital in the U.S. economy. Moreover, CFIUS has reaffirmed its commitment to focus solely on national security issues. We therefore remain confident that, despite additional hurdles, complexity and even some prohibitions, most investments submitted to CFIUS will be cleared. Below we discuss some of the key features of the proposed regulations.

Notable Changes Effectuated by the Proposed Regulations

Definition of “U.S. Business”

Under the existing CFIUS regime, the term “U.S. business” is defined as any entity “engaged in interstate commerce in the United States, but only to the extent of its activities in interstate commerce” (emphasis added). FIRRMA, and therefore the proposed regulations, intentionally omit the underlined phrase, which has historically limited CFIUS’s official jurisdiction to the U.S. portion of a global business targeted for foreign investment. Thus, in an acquisition of an entity headquartered in Morocco but with manufacturing facilities in France, China, and the United States, only the U.S. facilities would be within CFIUS’s jurisdiction and potentially subject to mitigation measures. By contrast, if read aggressively, the new definition could be used to assert jurisdiction over the entirety of a global transaction, even if the U.S. subsidiary posed no threat to national security. For example, if a Swiss company’s U.S. subsidiary makes chairs and its German subsidiary manufactures semiconductor chips, under the proposed regulations, the ex-U.S. semiconductor manufacturing could potentially be part of a “U.S. business” and, hence, subject to CFIUS review if a non-U.S. investor proposed to acquire or invest in the Swiss parent. That said, the first “example” CFIUS provides in the proposed regulations for the definition of “U.S. business” remains unchanged from the current regulations, and

provides that where a corporation organized under foreign law has a branch or subsidiary engaged in interstate commerce in the United States, the “branch or subsidiary is a U.S. business.” Arguably, had CFIUS intended to capture the entire organization, rather than just the branch or subsidiary in this example, it would have said so. Additional clarity from CFIUS on this point would be helpful; this definition is too fundamental to the CFIUS framework for ambiguity or unfettered discretion.

Covered Transactions

The proposed regulations broaden the definition of covered transactions to include:

- Any “covered control transaction” (i.e., “covered transactions” in the existing regulations);
- Any covered investment;
- A change in the rights that a foreign person has with respect to a U.S. business in which the foreign person has an investment, if that change could result in a covered control transaction or a covered investment; or
- Any other transaction, transfer, agreement, or arrangement, the structure of which is designed or intended to evade CFIUS’s jurisdiction.

Covered Investments: Non-Controlling Investments in “TID” Businesses

The proposed regulations implement CFIUS’s authority, as expanded by FIRRMA, to review certain **non-controlling** investments.⁵ Under the current regime, such investments are outside CFIUS’s jurisdiction, except for transactions covered by the Pilot Program. As discussed below, a subset of these investments will trigger a mandatory filing rule, but for most, filings will be voluntary.

“Covered investments” (as opposed to “covered control transactions”) are defined as non-controlling equity investments in “unaffiliated”⁶

Technology, Infrastructure and Data businesses (“TID U.S. Businesses”), defined as U.S. businesses involved in certain activities related to:

- critical **technologies**,
- critical **infrastructure**, or
- sensitive **personal data** of U.S. citizens

that afford a foreign person (other than an “excepted investor,” discussed below):

- **access** to certain information in the possession of,
- **certain rights** in, or
- **involvement** in certain decision-making of the TID U.S. Business.

The types of access, rights, or involvement that result in a covered investment are those that afford the foreign person:

⁵ CFIUS’s practice has evolved around the concept of “control” over a target entity, in contrast to a “passive” investor that holds 10 percent or less of a company’s equity (among other factors). Accordingly, “control” in the CFIUS context has been seen to start at the 10 percent equity ownership level (far below the traditional view of “control” arising at 50 percent equity ownership), with investments below 10 percent being considered “non-controlling” investments.

⁶ These exclude entities in which the foreign person already holds a majority of the voting interest or the right to appoint the majority of the entity’s board or equivalent governing body.

Critical technologies

- Defense articles or defense services included on the United States Munitions List set forth in the International Traffic in Arms Regulations;
- Items included on the Commerce Control List set forth in Supplement No. 1 to part 774 of the Export Administration Regulations, and controlled—
- Pursuant to multilateral regimes, including for reasons relating to national security, chemical and biological weapons proliferation, nuclear nonproliferation, or missile technology; or
- For reasons relating to regional stability or surreptitious listening;
- Specially designed and prepared nuclear equipment, parts and components, materials, software, and technology covered by 10 CFR part 810 (relating to assistance to foreign atomic energy activities);
- Nuclear facilities, equipment, and material covered by 10 CFR part 110 (relating to export and import of nuclear equipment and material);
- Select agents and toxins covered by 7 CFR part 331, 9 CFR part 121, or 42 CFR part 73; and
- Emerging and foundational technologies controlled pursuant to section 1758 of the Export Control Reform Act of 2018.

- access to material non-public technical information (defined as certain information relating to critical infrastructure or critical technologies, but not financial information) in the possession of the U.S. business,
- membership or observer rights on, or the right to nominate an individual to, the board of directors (or equivalent body) of the U.S. business, or
- any involvement in substantive decision-making⁷ of the U.S. business related to certain actions involving critical technologies, certain critical infrastructure, or sensitive personal data.

Critical Technologies

Consistent with the existing Pilot Program, the proposed regulations would formalize CFIUS's expanded jurisdiction over covered investments by a foreign person in an unaffiliated U.S. business that produces, designs, tests, manufactures, fabricates, or develops one or more critical technologies. The definition of critical technologies has been imported directly from the Pilot Program. (See sidebar.)

Because emerging and foundational technologies have not yet been defined pursuant to section 1758 of the Export Control Reform Act of 2018, the full breadth of the definition of critical technologies is not yet established.

Covered Investment Critical Infrastructure

Businesses that perform certain “functions” — namely, owning, operating, manufacturing, supplying, or servicing — “covered investment critical infrastructure” constitute a second category of TID U.S. Businesses. Covered investment critical infrastructure is a subset of “critical infrastructure.” This category of TID U.S. Businesses comprises those that perform the specific functions listed in Column 2 of Appendix A of the proposed regulations with respect to the categories of covered critical infrastructure set forth in Column 1 of Appendix A. Importantly, CFIUS will continue to construe the concept of critical infrastructure broadly for purposes of its national security analysis of covered transactions that are not covered investments, including control transactions.⁸

⁷ The Regulations define “substantive decision-making” as the process through which decisions regarding significant matters affecting an entity are undertaken, including, among others, pricing, sales and specific contracts; the transfer of sensitive personal data to third parties; supply arrangements; corporate strategy, research and development (including budget and location); manufacturing locations; access to critical technologies, certain critical infrastructure, material non-public technical information, or sensitive personal data; physical and cybersecurity protocols; procedures governing the collection, use or storage of sensitive personal data; and strategic partnerships.

⁸ The term “critical infrastructure” in this broader sense is separately defined in the proposed regulations as “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.”

Sensitive personal data

(a) the following identifiable data:

- data that could be used to analyze or determine financial distress or hardship;
- the set of data in a consumer report;
- the set of data in an application for insurance (health, long-term care, professional liability, mortgage, life);
- data relating to an individual's physical, mental, or psychological health condition;
- non-public electronic communications between or among users of a U.S. businesses' products or services if a primary purpose of the product or service is to facilitate third-party user communications;
- geolocation data;
- biometric enrollment data;
- data stored and processed for generating a government identification card;
- data concerning U.S. government personnel security clearance status; or
- the set of data in an application for a U.S. government personnel security clearance or an application for employment in a position of public trust;

if such data are maintained or collected by a U.S. business that:

- targets or tailors products or services to any U.S. executive branch agency or military department with intelligence, national security, or homeland security responsibilities, or to personnel and contractors thereof;
- has maintained or collected such data on more than one million individuals at any point over the preceding 12 months; or
- has a demonstrated business objective to maintain or collect such data on more than one million individuals and such data are an integrated part of the U.S. business's primary products or services; and

(b) genetic data;

except that data maintained or collected by a U.S. business concerning its own employees or data that is a matter of public record are not considered sensitive personal data. Excepted from that exception, however, is data of employees of U.S. government contractors who are cleared to handle classified information.

Sensitive Data

The third category of TID U.S. Businesses encompasses ventures that maintain or collect “sensitive personal data” of U.S. citizens that, as FIRRMA indicates, “may be exploited in a manner that threatens to harm national security.” The proposed regulations include a detailed definition of sensitive personal data that combines two major elements: the content of the information itself and the characteristics of the individuals, including the likelihood of their link to U.S. national security. (See sidebar.)

CFIUS’s approach to personal data protection seems designed to recognize the ubiquity of personal data in the U.S. economy and to concentrate on information or groups of people reflecting the greatest national security vulnerabilities. CFIUS’s proposal seems to recognize that many U.S. businesses collect data from U.S. citizens (beyond employees) and that too broad a definition could sweep most investments in U.S. companies into the TID category. One can easily imagine the treatment of personal data under CFIUS’s regulations to require frequent adjustment, given rapid technological changes that affect both threat and vulnerability.

Mandatory Filings for Certain Covered Transactions Involving Foreign Governments

The proposed regulations expand the category of mandatory filings to cover acquisitions of a “substantial interest” in a TID U.S. Business by a foreign person in which a foreign government has a substantial interest. Substantial interest has two different thresholds at different stages in this analysis. A foreign investor acquiring a 25 percent or greater stake in the TID U.S. Business is deemed to have acquired a substantial interest in the U.S. business, and a foreign government stake of 49 percent or more in the foreign investor is considered a substantial interest. This general rule is modified for investments by multi-investor funds or similar structures, as discussed below.⁹ For the limited partnerships typical of private equity investments, the proposed regulations provide that a foreign government is deemed to have a substantial interest in the partnership where it holds 49 percent of the voting interests in the general partner or where it holds 49 percent or more of the voting interests of the limited partners. Accordingly, an investor in which a foreign sovereign wealth fund holds 49 percent of the limited partner interests (assuming they qualify as “limited partner voting interests”) would be subject to a mandatory declaration if the fund were to acquire a 25 percent voting equity stake in a TID U.S. Business, even if the general partner were a U.S. person.

⁹ The proposed regulations also provide for a mandatory declaration for any transaction involving a TID business that meets the substantial government interest test, regardless of the rights obtained by the investor.

Carve-Outs from Covered Investment Rule

Notably, the proposed regulations expressly exclude certain types of non-controlling covered investments from CFIUS's jurisdiction. These carve-outs do not apply to foreign person acquisitions of control of a U.S. business.

Minimum Excepted Ownership Requirements

A specified percentage of the ownership of the entity (consisting of both voting interest and economic interest) must be held by persons who are (i) not foreign persons, (ii) foreign nationals who are nationals of one or more excepted foreign states and not nationals of a foreign state that is not an excepted foreign state, (iii) a foreign government of an excepted foreign state, or (iv) a foreign entity organized under the laws of an excepted foreign state with a principal place of business in an excepted foreign state or the United States.

The ownership percentage threshold that must be met to satisfy these requirements varies based on where the entity is located and/or where its shares are traded. For an entity whose equity securities are primarily traded on an exchange in an excepted foreign state or the United States, the minimum excepted ownership is anything over 50 percent. For an entity whose equity securities are not publicly traded or are not primarily traded on an exchange in an excepted foreign state or the United States, the minimum excepted ownership is 90 percent or more.

Excepted Investors: No "White List"

As FIRRMA was being debated, Congress considered whether the legislation should create a list of certain countries whose investors would not be subject to CFIUS's expanded jurisdiction over non-controlling investments. Rather than a categorical list of exempted countries, the proposed regulations establish complicated exceptions that condition jurisdictional relief on the strength of an "excepted investor's" links to an "excepted foreign state," as well as the investor's satisfaction of certain individual criteria.

To qualify as an excepted investor, a foreign person must be: (1) solely a foreign national of an excepted foreign state; (2) a foreign government of an excepted foreign state; or (3) a foreign entity that meets certain additional criteria, including, among others that: (i) the entity and its parents are organized under the laws of an excepted foreign state or the United States; (ii) the entity's principal place of business is in an excepted foreign state or the United States; (iii) each board member and observer is a national of the United States or one or more excepted foreign states and not also of any non-excepted foreign state; and (iv) five percent or greater shareholders must meet requirements related to nationality (for individuals) or place of incorporation and place of principal business (for entities).

To qualify as an "excepted investor," a foreign entity must also satisfy "minimum excepted ownership" requirements, meaning that a certain percentage of the equity must be held by persons meeting certain nationality requirements. (See side bar.)

An excepted foreign state must be so designated by the Secretary of the Treasury with the agreement of two-thirds of CFIUS member agencies.¹⁰ Starting two years from the effective date of the final regulations, in order to be designated (or remain) as an excepted foreign state, the CFIUS Chairperson (with the agreement of two-thirds of CFIUS member agencies) must determine that the foreign state has established and is effectively utilizing a robust process to assess foreign investments for national security risks and is coordinating with the United States on matters relating to investment security.

A foreign person will not qualify as an excepted investor if, in the five years prior to the completion date of the transaction under examination, it or any of its parents or subsidiaries committed any of the following "bad acts":

¹⁰ This is the first time that CFIUS has provided for decisions by less than a full consensus.

- received written notice from CFIUS that it has submitted a material misstatement or omission in a notice or declaration or made a false certification;
- received written notice from CFIUS that it has violated a material provision of a mitigation agreement entered into with, material condition imposed by, or an order issued by, CFIUS or a lead agency under Section 721(l) of the Defense Production Act of 1950 (the “DPA”);
- been subject to action by the President under Section 721 of the DPA;
- received a written Finding of Violation or Penalty Notice imposing a civil monetary penalty from the Department of the Treasury Office of Foreign Assets Control (“OFAC”) or entered into a settlement agreement with OFAC with respect to apparent violations of U.S. sanctions laws administered by OFAC;
- received a written notice of debarment from the Department of State Directorate of Defense Trade Controls;
- been a respondent or party in a final order, including a settlement order, issued by the Department of Commerce Bureau of Industry and Security (“BIS”) regarding violations of U.S. export control laws administered by BIS;
- received a final decision from the Department of Energy National Nuclear Security Administration imposing a civil penalty with respect to a violation of section 57 b. of the Atomic Energy Act of 1954; or
- been convicted of a crime under, or has entered into a deferred prosecution agreement or non-prosecution agreement with the Department of Justice with respect to a violation of, any felony crime in any jurisdiction within the United States.

In addition, a foreign person does not qualify as an excepted investor if the foreign person or any of its parents or subsidiaries is listed on either the BIS Unverified List or Entity List in 15 CFR part 744.

To focus on just one example, the OFAC criterion seems to be a draconian collateral consequence for entering into a settlement agreement with OFAC, especially as such agreements typically include language expressly disclaiming any finding of fault and penalty notices can be appealed.

Further, if at any time during the three-year period following the completion date of a transaction, the foreign person ceases to meet all the excepted investor criteria, the transaction is treated as having been by a “normal” investor from the completion date onward. This provision creates the possibility of retroactive jurisdiction over a transaction, meaning that a transaction can close while outside CFIUS’s jurisdiction, and fall back within CFIUS’s jurisdiction up to three years later, potentially warranting a filing at that time.

From CFIUS’s perspective, a retroactive revocation of an investor’s status may appear to trigger “only” an exposure to discretionary review with the

formerly excepted investor bearing the risk, but the mere possibility of a retroactive status change significantly undercuts the benefit of the excepted investor status as a whole. Private parties will try to assess this risk before entering into transactions, including evaluating excepted investors against U.S. investors, non-excepted investors and other excepted investors. An investor cannot fully control whether or when it might lose its excepted status — a subsidiary or affiliate could easily (and inadvertently) violate rapidly changing U.S. sanctions or export control laws — so few will be able responsibly to covenant that they will not lose their excepted status for at least three years from closing a covered investment. Excepted investor status is relevant only in non-control covered investments where, by definition, the target company and its predominantly U.S. shareholders remain involved and so will also suffer the consequences of the investor's change in status, which could, at least theoretically, include forced divestment with the attendant damage to enterprise value and share prices. Retroactive review based on changes in an excepted investor's status also seems unlikely to protect national security interests. Three years after an excepted investment, it seems likely that access to data, board participation, or the ability to affect decisions will already have affected the target U.S. business. A review dating back to the completion date appears unlikely to redress those harms.

Investment Funds

The proposed regulations implement FIRREA's provisions relating to "investment funds."¹¹ This exception to CFIUS jurisdiction closely mirrors the equivalent carve-out in the Pilot Program.

Specifically, an indirect investment by a foreign person in a TID U.S. Business through an investment fund that affords the foreign person (or a designee of the foreign person) membership as a limited partner or equivalent on an advisory board or a committee of the fund is not considered a covered investment if:

- the fund is managed exclusively by a general partner, a managing member, or an equivalent;
- the foreign person is not the general partner, managing member, or equivalent;¹²
- the advisory board or committee does not have the ability to approve, disapprove, or otherwise control: (i) investment decisions of the investment fund; or (ii) decisions made by the general

¹¹ "Investment fund" means any entity that is an "investment company," as defined in section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-1 *et seq.*), or would be an "investment company" but for one or more of the exemptions provided in section 3(b) or 3(c) thereunder.

¹² This is a change from the statute itself, and the Pilot Program, which provide that to qualify for this special treatment of funds, the general partner may not be a foreign person. Under the proposed regulations, the general partner or equivalent may not be the foreign investor, but another foreign person can serve in this capacity.

partner, managing member, or equivalent related to entities in which the investment fund is invested;

- the foreign person does not otherwise have the ability to control the investment fund;¹³
- the foreign person does not have access to material non-public technical information as a result of its participation on the advisory board or committee; and
- the investment does not afford the foreign person any of the access, rights, or involvement specified in the definition of covered investment.

Declarations

FIRRMA introduced an abbreviated filing process through the submission of a declaration, which allows parties to submit basic information regarding a transaction to CFIUS and theoretically receive an expedited review. Under the Proposed Regulations, a declaration may be submitted for any transaction. Moreover, where a mandatory filing rule applies, the parties may satisfy the requirement by submitting a declaration. The proposed regulations provide that mandatory declarations be submitted to CFIUS at least 30 days in advance of the transaction completion date¹⁴ and permit parties to file a notice instead of declaration to satisfy the mandatory declaration requirement.

The proposed regulations also implement FIRRMA's voluntary declaration provision permitting parties to file a declaration instead of a written notice.

Declarations differ from notices in the following three key ways:

- they are shorter in length, generally not exceeding five pages (not including exhibits);
- the timeline for CFIUS to take action on declarations is shorter — 30 days for a declaration versus 45 days for review and an additional 45 days for investigation (with a possibility of a 15-day extension) for a notice; and
- FIRRMA provides CFIUS with several potential responses to a declaration, and does not require CFIUS to make a final

¹³ The ability to “control the investment fund” includes the authority to (i) approve, disapprove, or otherwise control investment decisions of the investment fund, or decisions made by the general partner, managing member, or equivalent related to entities in which the investment fund is invested; or (ii) to unilaterally dismiss, prevent the dismissal of, select, or determine the compensation of the general partner, managing member, or equivalent.

¹⁴ “Completion date” means the earliest date upon which any ownership interest, including a contingent equity interest, is conveyed, assigned, delivered, or otherwise transferred to a person, or a change in rights that could result in a covered control transaction or covered investment occurs. Therefore, in the event that a covered transaction will be effectuated through multiple or staged closings, the completion date is the earliest date on which any transfer of interest or change in rights that constitutes a covered transaction occurs.

determination with respect to action under Section 721 of the DPA on the basis of a declaration.

As a practical matter, this third point may determine whether the declaration filing option proves to be a valuable tool for parties to a covered transaction or a rarely used choice that exists mostly in theory.¹⁵ Assuming that the declaration submitted is complete and accurate, after completing its review, CFIUS may: (i) request a formal written notice; (ii) essentially make no decision and inform the parties that they may file a notice; (iii) initiate a unilateral review; or (iv) provide a written clearance. In the case of the first two options, declarations may not save parties significant time, or may even cost more time, if the declaration delays a filing that could have been made earlier. The prospect of a clearance in 30 days, however, could be highly valuable to parties to transactions for which CFIUS is the gating item for closing. Voluntary declarations may become valuable for repeat filers and non-controversial transactions.

Procedure and Content of Declarations

Mandatory and voluntary declarations are subject to the same criteria and procedures. Parties must provide the information required by § 800.404 and may voluntarily stipulate that the transaction is a covered transaction and, if so, whether the transaction is a foreign government-controlled transaction. CFIUS must take action on a declaration within 30 days of acceptance by the CFIUS Staff Chairperson, and may invite the parties to attend a meeting to clarify issues pertaining to the transaction. CFIUS may reject a declaration if it is incomplete, there is a material change in the transaction, or the parties fail to provide information requested by CFIUS within two business days of such request. The parties may withdraw a declaration, but may not submit a new declaration for the same transaction without prior CFIUS approval.

Notices

While the proposed regulations do not significantly change the procedures and requirements for traditional notices, they do require parties to provide certain additional categories of information that were not previously required to be included in a notice, including statements as to whether the U.S. business:

- produces, designs, tests, manufactures, fabricates, or develops one or more critical technologies;
- performs any of the functions with respect to covered investment critical infrastructure as set forth in Column 2 of Appendix A; and
- maintains or collects sensitive personal data on U.S. citizens.

¹⁵ The preamble to the proposed regulation estimates 200 respondents per year for notices and 550 respondents per year for declarations — this would be a huge increase in filings overall, but a drop in full notices from peak years.

As with declarations, FIRRMA allows parties to stipulate in a notice that the transaction is a covered transaction and, if so, whether the transaction is a foreign-government controlled transaction. If the parties so stipulate, CFIUS must either provide comments or accept the notice within 10 business days of submission. Options for reducing the long, undefined “pre-filing” period are apt to be quite attractive to investors.

Incremental Acquisitions

Under the proposed regulations, if CFIUS clears a covered investment by a foreign person and that person is party to a later transaction involving the U.S. business, the later transaction may be a covered transaction. CFIUS’s clearance of the covered investment does not provide a safe harbor with respect to subsequent transactions. This contrasts with CFIUS’s traditional approach to incremental acquisitions after a covered control transaction has been cleared.

In addition, when deciding whether to file a declaration, parties should be aware that if CFIUS clears an investment based on a declaration, rather than a notice, subsequent additional investments in the U.S. business by the same foreign investor may be subject to CFIUS’s review.

Proposed Regulations on Real Estate Transactions

In one of the most significant changes to the traditional CFIUS regime, FIRRMA expanded CFIUS’s jurisdiction to certain investments in real property in the United States that do not involve any U.S. business. To implement this expanded authority, Treasury issued separate proposed regulations for certain real estate transactions.

Notably, the real estate proposed regulations replicate many of the provisions of the proposed regulations for covered transactions, and more than half of the defined terms were incorporated wholesale (with non-substantive conforming changes) from those proposed regulations. Accordingly, this section of the memorandum focuses primarily on those provisions in the real estate proposed regulations that are distinct to such regulations.

The real estate proposed regulations have no effect on the existing foreign investment review process for investments in U.S. businesses. “Covered transactions” under both the existing CFIUS regulations and the proposed regulations are outside the scope of the real estate proposed regulations, and in reviewing covered transactions, CFIUS will presumably continue the persistent co-location national security analysis that it has applied for years. The innovation of the real estate proposed regulations, rather, is to extend CFIUS’s jurisdiction to deals that historically would be wholly exempt from CFIUS scrutiny, including the purchase of a parcel of land (without the accompanying elements of a business) or the lease of office space. In addition, the substance of the real estate proposed regulations may be instructive for foreign person investments in U.S. businesses in that the conditions that trigger CFIUS jurisdiction under the real estate proposed regulations — namely, acquisition of real property rights in proximity to specific, sensitive U.S. government locations — provide useful insights into vulnerability assessments in covered transaction reviews.

Covered Real Estate Transaction

Under the real estate proposed regulations, all “covered real estate transactions” are subject to CFIUS’s jurisdiction.¹⁶ Covered real estate transactions include, unless excepted, any purchase or lease by, or concession to, a foreign person of “covered real estate” that affords the foreign person certain property rights. In general, this concept applies to two categories of transactions:

- specified types of investments in real property by a foreign person in covered real estate that affords the foreign person at least three of a defined list of “property rights;” and
- changes in the rights of a foreign person with respect to covered real estate in which that foreign person has an existing investment, if that change could result in the foreign person having at least three of the defined property rights.

In each case, certain “excepted real estate transactions” are carved out from the definition. Finally, in addition to the two primary categories of covered real estate transactions, the real estate proposed regulations apply to other transactions or arrangements designed or intended to evade or circumvent CFIUS’s jurisdiction.

Covered Real Estate

Under the real estate proposed regulations, covered real estate falls into two categories. The first category encompasses real estate that is located within or will function as part of an “airport or maritime port,” where “airport” includes major passenger and cargo airports in the United States as well as “joint use airports” shared by military and civilian aircraft. Maritime ports include strategic seaports within the National Port Readiness Network and “Top 25” tonnage, container, or dry bulk ports.

The second category covers real estate within a specified distance of certain military installations or other U.S. government facilities, and includes four subcategories:

- Real estate that is within “close proximity” of a facility or military installation listed in part 1 or part 2 of the Appendix to the Real Estate Proposed Regulations (the “R.E. Appendix”). Close proximity means the area that extends outward one mile from the boundary of the relevant installation, facility, or property;
- Real estate that is within the “extended range” of a military installation listed in part 2 of the R.E. Appendix. “Extended range” means the area that extends 99 miles outward from the outer boundary of close proximity to the installation. Where applicable,

¹⁶ “Real estate” means any land, including subsurface or submerged land, any structure attached to land, and any building or part thereof, that is located in the United States.

extended range does not cover an area more than 12 nautical miles seaward of the coastline of the United States;

- Real estate in any county or other geographic area listed in part 3 of the R.E. Appendix; and
- Real estate located within any part of a Navy offshore range complex or offshore operating area listed in part 4 of the R.E. Appendix that is within 12 nautical miles seaward of the U.S. coastline.

Transaction Types

The real estate proposed regulations apply only to purchases, leases, and concessions.

- A “purchase” is an arrangement conveying an ownership interest of real estate to a person in exchange for consideration.
- A “lease” is an arrangement conveying a possessory interest in real estate that is less than ownership, to another person for a specified time and in exchange for consideration (including subleases).
- A concession is an arrangement other than a purchase or a lease by which a “U.S. public entity” grants the right to use real estate for the purpose of developing or operating infrastructure for an airport or maritime port. This definition captures a subsequent assignment of a concession by a party who is not a U.S. public entity. A public entity includes essentially any government entity, whether federal, state, or local.

Property Rights

A covered real estate transaction occurs only where the transaction results in a foreign person acquiring three or more of the following property rights:

- to physically access the real estate;
- to exclude others from physical access to the real estate;
- to improve or develop the real estate; and
- to attach fixed or immovable structures or objects to the real estate.

Excepted Real Estate Transactions

The following categories of transactions that would otherwise meet the definition of covered real estate transaction have been expressly carved out from CFIUS’s jurisdiction:

- Covered real estate transactions by an “excepted real estate investor,” which essentially mirrors the definition of “excepted investor” in the covered transaction proposed regulations. The most notable difference in these definitions is that the standards for being an “excepted real estate foreign state” under Part 802 are easier to meet than the standards for being an excepted foreign state under Part 800. As a result, the set of “excepted real estate investors” may be broader than the set of excepted investors under Part 800;

- Transactions that are covered transactions under Part 800; i.e., a transaction cannot be both a covered transaction and a covered real estate transaction simultaneously;
- Certain transactions involving real estate within an “urbanized area” or “urban cluster”¹⁷ (both of which are defined by reference to the U.S. census), which should exclude most urban areas; and
- Real estate transactions involving commercial office space within a multi-unit commercial office building if: (i) the foreign person (together with its affiliates) does not acquire property rights for commercial office space constituting more than 10 percent of the total square footage of the total commercial office space for the building and (ii) the foreign person and its affiliates (counted separately) do not represent more than 10 percent of the total number of tenants in the building.

Real Estate Declarations

Unlike the covered transaction proposed regulations, the real estate proposed regulations do not mandate filings for any real estate covered transactions — all filings are voluntary. The procedural elements for *voluntary* declarations, however, are virtually identical for both sets of regulations.

Declarations filed under the real estate proposed regulations must include details regarding the covered real estate at issue, including the location (both address and geographic coordinates); the name of the relevant airport, military installation, or other facility that caused the property to be covered; the size, nature, current use, and expected use of the property, including structures that may be built on the property; and the rights of the foreign person with respect to the property.

Notices

The procedural elements for notices filed under the real estate proposed regulations largely mirror the requirements for notices under the other regulations but also require details regarding the nature of the property and how it is intended to be used by the new buyer.

¹⁷ The urban cluster and urbanized area exceptions do not apply where the covered real estate is in close proximity or is, is within, or will function as part of, an airport or maritime port. In addition, the urbanized area exclusion does not apply where the covered real estate is in close proximity to a specified military installation or another U.S. government sensitive facility or property.

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Conclusion

In order to balance between FIRRMA's sweeping mandate and the potential to drive away potential investors, CFIUS has written rules of some restraint, but also of significant complexity. As noted in the overview above, much of that new complexity relates to investments not conveying control of a U.S. business. More classic mergers and acquisitions constituting changes of control over U.S. businesses will see fewer definitional and procedural changes than might be expected from 300 or so pages of proposed regulations, although the environment has changed fundamentally even since FIRRMA was introduced in Congress in late 2017.

Over the past several years, CFIUS has become a far more significant consideration for a wider range of investors than in the past. Moreover, the advent of mandatory filings under the Pilot Program has pushed CFIUS considerations, especially their likely effect on the regulatory risk and execution risk of any given transaction, ever earlier into the deal-making process. The proposed regulations do nothing to abate that trend. Only time and practice will disclose the extent to which the new regulations, once final, affect capital inflows and net investment into the United States. We will also watch with great interest how other countries react with respect to the enactment or enhancement of their own reviews of direct foreign investment.

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