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## Foreign Investment

### Proposed Bill Seeks to Expand Scope of U.S. Foreign Investment Reviews

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On Nov. 8, 2017, Senators John Cornyn (R-Texas), Diane Feinstein (D-Calif.) and Richard Burr (R-N.C.) introduced legislation, titled the “Foreign Investment Risk Review Modernization Act,” (FIRRMA) (S. 2098), in the U.S. Senate that would dramatically expand the jurisdiction of the Committee on Foreign Investment in the United States (CFIUS or the “Committee”). Rep. Robert Pittenger (R-N.C.) introduced a companion bill by the same name (H.R. 4311) in the U.S. House of Representatives that also has bipartisan sponsorship. In addition to expanding CFIUS jurisdiction, the proposed bills would impose mandatory reporting requirements for certain types of transactions and introduce filing fees to the notification process. While the legislation has received bipartisan sponsorship, it remains to be seen whether the supporters of FIRRMA can garner the necessary votes for it to become law.

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**Background: The Current CFIUS Regime.** CFIUS is an interagency panel, chaired by the U.S. Department of the Treasury, with authority to review certain investments that could result in foreign control of U.S. businesses—referred to as “covered transactions”—for potential national security concerns. Under the current CFIUS regime, parties to a proposed transaction do not have an affirmative obligation to file a notice with CFIUS. However, the Committee has the authority to initiate a review and direct the submission of a notice if it becomes aware of a covered transaction that it believes implicates U.S. national security concerns. Parties often seek CFIUS approval in cases that present such potential issues to avoid the otherwise unextinguished liability that could arise following completion of a transaction.

The CFIUS review process involves a 30-day review, followed by a 45-day investigation if the Committee has unresolved national security concerns associated with the transaction. The potential outcomes of this process include CFIUS clearing the transaction, requiring a mitigation agreement before clearance or recommending that the President block the transaction.

The Committee has received increased attention in 2017, due to a recent surge of Chinese investment into the U.S. President Donald Trump’s decision to block the acquisition of Oregon-based Lattice Semiconductors by Canyon Bridge, a Chinese-backed private equity fund, drew headlines as only the fourth such presidential blocking action in CFIUS history. The past year has also seen a rising number of transactions with Chinese buyers stalled or abandoned as a result of CFIUS scrutiny. On top of this, the Committee is reportedly on pace to review a record number of deals this year despite being understaffed. These factors have resulted in a back-

log of pending cases and an increase in parties' having to withdraw their notices and refile them with CFIUS to restart the review clock.

Amidst growing concern for the national security implications of increased Chinese investment, legislators and Trump administration officials have voiced interest in expanding CFIUS's authority to scrutinize such deals. While discussing CFIUS reform in June, Sen. Cornyn referenced a February 2017 report from the Defense Innovation Unit Experimental (DIUx), a part of the Department of Defense, which expressed concern regarding Chinese investment in advanced technologies. Later, in mid-September, the Senate Committee on Banking, Housing and Urban Affairs, which oversees CFIUS, held a hearing on potential CFIUS reform. Within the Trump administration, Treasury Secretary Steven Mnuchin, Defense Secretary James Mattis, Commerce Secretary Wilbur Ross and Attorney General Jeff Sessions have all expressed support for strengthening the Committee's review process, which has been criticized by lawmakers from both parties.

**Key Provisions of the Reform Bill.** Sen. Cornyn and Rep. Pittenger introduced their proposed legislation following many months of consideration of how best to strengthen the CFIUS process without discouraging foreign direct investment in the U.S. In its current form, FIRRMA would bring a variety of adjustments to the CFIUS review process. Notably, its proposed amendments to the CFIUS regime remain focused on national security issues and do not encompass "economic security" or other seemingly protectionist issues that have also been the subject of debate among lawmakers. Some of FIRRMA's key modifications to the CFIUS process are described below.

**1. Expanded Definition of "Covered Transaction."** The proposed bill would substantially expand the definition of a "covered transaction." Currently, CFIUS has jurisdiction to review only transactions in which a non-U.S. person could gain the ability to control a U.S. business. FIRRMA would expand the scope of CFIUS review to cover the following transactions, which are not currently within the specific definitional scope of CFIUS jurisdiction:

- the purchase or lease by a non-U.S. person of private or public real estate that is located in close proximity to a U.S. military installation, other U.S. government facility or property that is sensitive for national security reasons;

- investments (other than "passive investment") by a non-U.S. person in any U.S. critical technology company, which means a U.S. business that produces, trades in, designs, tests, manufactures, services, or develops one or more critical technologies

- ▶ Notably, FIRRMA expands the current definition of "critical technologies" beyond export-controlled items to include "[o]ther emerging technologies that could be essential for maintaining or increasing the technological advantage of the United States over countries of special concern with respect to national defense, intelligence, or other areas of national security, or gaining such an advantage over such countries in areas where such an advantage may not currently exist." While it may be further clarified through regulations, this expanded category could create a shadow export control regime through the

CFIUS process and may also be difficult for companies to interpret.

- investments (other than "passive investment") by a non-U.S. person in any U.S. critical infrastructure company, which means a U.S. business that is, owns, operates or primarily provides services to an entity that operates within a critical infrastructure sector or sub-sector;

- any change in a non-U.S. person's rights with respect to a U.S. business in which the non-U.S. person has an investment, if that change could result in (i) foreign control of the U.S. business or (ii) an investment in a U.S. critical technology or critical infrastructure company;

- joint ventures or any other types of arrangements (other than an ordinary customer relationship) in which a U.S. critical technology company contributes both intellectual property and associated support to a non-U.S. person, which could potentially cover joint ventures established outside of the U.S.; and

- any other transaction, transfer, agreement, or arrangement designed or intended to evade or circumvent the CFIUS review process.

As noted above, FIRRMA builds in an exclusion for "passive investments" from CFIUS's jurisdiction in relation to certain investments and adds a more detailed definition of this concept. This new definition is narrow, capturing investments that do not provide (i) control; (ii) access to certain non-public information about the U.S. business; (iii) membership, observer, or nomination rights on the board of directors or equivalent body; (iv) involvement in any decision-making (beyond rights through voting shares); and (v) a parallel strategic partnership or other material financial relationship to the non-U.S. person and U.S. business. Moreover, as with other defined terms, CFIUS will have the discretion to develop other criteria for "passive investments" by regulation.

**2. Exemptions for Particular Countries.** To avoid capturing benign investments, the proposed legislation would allow the Committee to create a list of exempt countries (a so-called "white list") from which inbound investment would not be captured in the expanded definition of "covered transaction." Importantly, the aforementioned transactions would not be exempt from the existing scope of CFIUS jurisdiction. In identifying the white-listed countries, the bill directs the Committee to consider the following factors: (i) whether the U.S. has a mutual defense treaty in effect with the country; (ii) whether the U.S. has a mutual arrangement with the country to safeguard national security as it pertains to foreign investment; (iii) the national security review process for foreign investment of that country; and (iv) any other criteria the Committee deems appropriate.

**3. Voluntary and Mandatory Declarations.** FIRRMA also creates a new process for submitting short-form notices, called "declarations," that would apparently contain high-level information regarding the transaction. Under FIRRMA, these declarations can be submitted on a voluntary basis, in lieu of a full written notice, but they would also be mandatory in certain circumstances. Specifically, the mandatory declaration will apply to covered transactions involving the acquisition of a 25 percent or greater voting interest by a non-U.S. person in which a foreign government owns at least a 25 percent voting interest. CFIUS may also require the sub-

mission of a declaration for covered transactions based on the following factors or circumstances: (i) the technology, industry or economic sector in which the U.S. business trades; (ii) the difficulty of remedying the national security harm that may result if the transaction is completed; and (iii) the difficulty of obtaining information on the type of covered transaction through other means.

Parties must submit mandatory declarations no later than 45 days before the completion of the transaction. If the parties elect to submit a full notice in lieu of a mandatory declaration, the notice must be filed 90 days in advance of closing. The proposed legislation provides CFIUS with the authority to issue penalties if the parties fail to file a mandatory declaration or notice.

In response to a declaration, CFIUS will take one of the following steps: (i) clear the transaction; (ii) request that the parties file a full notice; or (iii) initiate a unilateral review of the transaction to further review the national security implications of the transaction. FIRRMA provides that CFIUS shall “endeavor” to take such action within 30 days of receiving the declaration.

**4. Extended Timeline.** As stated above, the timeline for the CFIUS review process is generally triggered upon the parties’ submission of a voluntary notification to CFIUS. FIRRMA proposes extending the initial 30-day review period to a 45-day review period. Moreover, in extraordinary circumstances, the proposed bill authorizes the Treasury Secretary to extend the subsequent 45-day investigation by 30 days. Given the record backlog of CFIUS cases currently pending, these extended review and investigation periods could reduce the need for parties to withdraw and refile notices with CFIUS by allowing more time for review and negotiation of mitigation terms. The bill also provides for tolling of the review period during a government shutdown, which is in response to delays that occurred in the last government shutdown of September-October 2013.

**5. Monitoring of Non-Notified Transactions.** The proposed bill establishes a requirement for CFIUS to monitor transactions for which no declaration or notice is submitted. As a practical matter, CFIUS staff and its member agencies already perform this function, but this change makes such monitoring an affirmative legal requirement. Specifically, FIRRMA requires CFIUS to establish a mechanism to identify non-notified and non-declared covered transactions for which “information is reasonably available.” The proposed legislation would also allow the CFIUS chairperson, in consultation with the Committee, to centralize this process and other appropriate functions within the Department of the Treasury.

**6. Expanded Authority for CFIUS and the President to Address National Security Concerns.** Under the proposed bill, the Committee may also “suspend a proposed or pending covered transaction that may pose a risk to the national security of the United States” while it is under review or investigation. It also provides the Committee with the authority to refer the transaction to the Presi-

dent at any time during the review or investigation. These authorities are not explicit under the current law.

In addition, the proposed bill states that CFIUS may negotiate, impose, and enforce any agreement or condition with any party to a completed transaction to mitigate any interim risks to U.S. national security that may arise as a result of the transaction until the Committee has completed its review or the President has taken appropriate action. The bill also expands the President’s authority so that he may “take any additional authority [he] considers appropriate to address the risk to the national security of the United States identified during the review and investigation of the transaction.”

**7. Filing Fees and Funding.** With respect to a covered transaction for which a written notice is submitted to the Committee, the proposed bill introduces a filing fee that may not exceed an amount equal to the lesser of 1 percent of the value of the transaction, or \$300,000, adjusted annually for inflation. This new fee will generate revenue for CFIUS for the first time, but it could discourage the voluntary submission of notices.

In addition, FIRRMA establishes a dedicated CFIUS fund to hold the filing fees and appropriations from Congress, which will fund the operation of the Committee. The proposed bill allows the CFIUS chairperson to transfer amounts from the new fund to other departments or agencies represented on the Committee for CFIUS-related activities. This dedicated funding will be critical for CFIUS to execute the new mandates of FIRRMA, particularly in light of the current backlog of cases at the Committee.

**Outlook and Potential Impact of FIRRMA.** The proposed legislation faces an uncertain fate. At this juncture, it is unclear whether it will be able to gain enough momentum to pass in both the House and the Senate. While the legislation has bipartisan sponsorship, the breadth and focus of this support have not yet crystallized. The level of commitment to CFIUS reform will be a critical factor in the passage of any legislation, given Congress’s packed legislative agenda and other priorities.

If the bill does become law, it would heighten scrutiny of deals involving non-U.S. buyers, especially those from China. Regardless of the size of their investment, non-U.S. investors dealing in sensitive industries and those from countries of interest would need to consider the CFIUS implications of transactions. The proposed bill could also substantially extend the time that parties to a transaction must build in for CFIUS review.

While formally heightening scrutiny on non-U.S. investors, the proposed legislation could also help clarify the scope and parameters of CFIUS review, aiding potential investors in structuring deals to minimize national security concerns. Given the current backlog and reports of stalled deals from China, the legislation may be seen as formalization of certain aspects of a CFIUS review process that has increased its level of scrutiny on inbound investments. Still, the proposed bill grants broad discretion to CFIUS, and therefore, it may raise as many questions as it answers.