



## **Ep. 9: CFIUS and FIRRMA: What You Need to Know**

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**Jose Garriga:**

Hello, and welcome to *OnAir with Akin Gump*. I'm your host, Jose Garriga.

The Committee on Foreign Investment in the United States, or CFIUS, is an interagency committee authorized to review certain transactions involving foreign investment in the United States in order to determine the effect of such transactions on the national security of the United States.

Created during the Ford administration, CFIUS reviews proposed investments in U.S. companies by a wide variety of countries, from Japan to Israel, the U.K. to South Korea. However, most recently, CFIUS's role in monitoring the national security implications of investment from China has been spotlighted by the Trump administration against the backdrop of the larger trade war between the U.S. and the PRC, even as efforts to reform CFIUS and make it more stringent are well under way.

We have with us today Akin Gump international trade partners Tatman Savio, who works in the firm's Hong Kong office, and Christian Davis in Washington, D.C. They'll discuss the ongoing efforts to reform CFIUS, the projected impact on business in Asia and elsewhere, and what businesspeople should know about these changes.

Welcome to the podcast.

Tatman, Christian, thank you for appearing on the show today. This is a major change in U.S. trade policy and regulation, so, maybe we can start with a bit of background. Tatman, could you tell us please, what prompted the need to reform CFIUS?

**Tatman Savio:**

Thanks, Jose, and thanks for having me. I'm happy to dive into this, and I think that you introduced it quite well. As you said, the CFIUS regime was recently amended by the Foreign Investment Risk Review Modernization Act, otherwise known as FIRRMA, which was the law that was enacted in August of this year. In order to understand how FIRRMA changed and will continue to change the CFIUS regime moving forward, I do think it's important to understand some fundamentals about CFIUS at the outset. As you described at eye-level, CFIUS is a U.S. government interagency committee, chaired by the U.S. Department of the Treasury, that conducts national security reviews of what are known as "covered transactions."

Now, pre-FIRRMA, “covered transaction” was a defined term limited to any investment that could result in a non-U.S. person gaining the ability to control a U.S. business. And control has really been a central concept and part of that definition and CFIUS's jurisdiction. CFIUS has a great deal of discretion in evaluating covered transactions, and it also has a significant amount of authority in terms of the scope and result of its review. So, let's just review quickly what it can do. It can initiate reviews of covered transactions and pose litigation measures to address national security concerns that it may have and recommend that the President watch pending transactions, or even order divestitures of completed transactions to the extent that they have not gone through a review process and gotten clearance from CFIUS.

Historically, pre-FIRRMA, the CFIUS process was voluntary, but many companies decided to subject their transaction to review to avoid problems down the line in the event that CFIUS had national security concerns related to them at a later point. So, with this baseline understanding of CFIUS as it has existed for the past many years, I think we can get into FIRRMA and, specifically, why it was passed. And the reason for the reform is quite simply China and China's efforts and success in gaining access to U.S. critical technologies and sensitive information in the United States through investments and acquisitions.

CFIUS has made clear that its rules apply equally to all countries on which investment may originate. With that being said, for many months, going back to 2017, the discussion about CFIUS reform has really centered around China and China's industrial policy known as Made in China 2025. It's focused on expanding its high-tech sectors and developing its advanced manufacturing base. And various stakeholders in the U.S. government, including the U.S. Congress, have been concerned about trends in Chinese investment and the way in which China has been able to use passive or minority investment, or joint venture arrangement and other mechanisms to make successful investments in the U.S. economy and obtain critical technology or access to critical infrastructure or other sensitive information.

So, the concern is that China's development and dominance in this high-technology area in a program subsidized by the state could affect U.S. leadership in areas related to national security, and that's where FIRRMA comes in to address this perceived national security threat by filling in the so-called gaps, where China's acquisition of technology has been occurring.

**Jose Garriga:** Well, Christian actually—thank you, Tatman—from the Washington perspective, could you explain how exactly does FIRRMA reform the CFIUS process?

**Christian Davis:** Sure, happy to discuss that. I mean, really, FIRRMA does a variety of different things, and it's quite an extensive bill and law that's now in effect. It changes CFIUS in ways that are entirely new, that just did not exist previously, but also it puts into law some of the practices that CFIUS had developed over the years. The first thing to mention, and, I think, one of the two key changes, is that it expands the jurisdiction of CFIUS. And as Tatman mentioned previously, CFIUS only applied to covered transactions that resulted in a foreign person getting the ability to control a U.S. business. Now, that expands to four new categories.

The first one being the purchase, lease, concession, by or to, a foreign person of U.S. real estate that is in a sensitive location near a U.S. government facility or is in or part of

a U.S. port, including both maritime and airports. That is one change. So, previously, you had to have a U.S. business that a foreign person was going to gain control of; now, it applies to real estate transactions, regardless of business.

Second, any change in rights of a foreign investor in an acquisition that they have made—this is after the actual acquisition is made—any change in rights that could lead to control or a change in rights that could provide a covered noncontrolling investment, which we'll discuss in a moment. So, really, this changes the idea of CFIUS being something that just happens at the time of a transaction and really creates the potential CFIUS risk as an ongoing concern, particularly in the context of a joint venture.

Third, is any investment that is designed to evade CFIUS jurisdiction, which is somewhat of an interesting point. The question, what is evading CFIUS jurisdiction as opposed to what is avoiding it? And that's something I think that we'll see over time, in terms of how CFIUS looks at that. But, really thinking about whether or not your transaction could be brought into CFIUS review, even though it doesn't meet the criteria, because there's an evasion that has occurred.

Lastly, in terms of expanded jurisdiction is this concept of other investments that are noncontrolling investments in U.S. businesses that are involved in critical infrastructure, critical technology and sensitive personal data. Previously, it was only a control test, and it applied to all businesses. Now, these noncontrolling investments that are in these certain sectors—critical infrastructure, critical technology or have sensitive personal data—could be brought into CFIUS jurisdiction.

The second major thing I think to discuss is mandatory reporting. Previously, as Tatman mentioned, we were only in a system where there was voluntary filings unless CFIUS actually directed you to file on a specific transaction. Under FIRRMA, there are mandatory filing requirements for foreign government-backed investments, where a foreign government acquires a substantial interest in a U.S. business and also in investments in certain critical technology companies. The statutes gave CFIUS discretion in terms of defining what critical technology companies would be included in the mandatory reporting requirement, which became part of this pilot program, which we'll discuss in a moment.

So, number one, expanded jurisdiction, number two, mandatory reporting—I think those are probably the most important factors and changes that occurred as part of FIRRMA. The other one I would mention though is that the timeline of CFIUS reviews has changed. It's generally been extended, and it's changed in a variety of different ways, but generally been extended. I think this really helps companies, though, in the long run because it gives CFIUS more time to review cases in a single filing period, as opposed to forcing parties to withdraw and refile their application, which can lead to longer and longer reviews. So, that is one change that we've seen so far, or that is part of the bill, is extended timelines.

And another one are, instead of just one means of filing with CFIUS, where you do a full review and a pretty extensive filing, there is now a short-form process to get an expedited review with a short filing. Hopefully, in less complex cases, that will be used and effective in terms of getting clearance on an expedited basis. FIRRMA also introduces filing fees, which can be up to \$300,000 per filing for a full written notice. FIRRMA also adds additional resources to CFIUS staff and really beefs up the staffing of

CFIUS. And lastly, it creates a more robust process for identifying non-notified transactions—in other words, transactions that haven't been submitted to CFIUS—and monitors those and decides whether or not they present national security risks and gives CFIUS the authority to bring those in and direct filings.

CFIUS had this authority already, but, in practice, it used this authority, but this change creates statutory direction to monitor non-notified transactions.

**Jose Garriga:**

Thank you, Christian. You've mentioned something that I'd like to go into a bit: pilot program. FIRRMA is going to go through a phased implementation, and, so, the pilot implementation program, the first bit of it, started last week. So, which changes are immediately affected?

**Christian Davis:**

Sure, so, as you mentioned Jose, it's really a phased implementation, and there's really three phases. There are those changes that went into effect in August, when the bill was passed, and then there are changes that went into effect this past weekend through a pilot program, and then the third phase and final phase will be the changes that are actually included in the final rules that are developed to fully implement FIRRMA, which will go through a notice-and-comment period. And we expect that to happen probably by the end of next summer or thereabout.

So, in terms of the actual pilot program, what does this do? Really, it does two things. One is that it expands CFIUS jurisdiction to capture certain non-controlling investments, and that went into effect on November 10th. And secondly, it creates mandatory reporting requirements that are also now in effect. And, really, the key aspect of this is, this only applies on a limited scope, and it applies to U.S. businesses that are, quote-unquote, "pilot program U.S. businesses." And the definition of a pilot program U.S. business is a U.S. business that produces, designs, tests, manufactures, fabricates or develops a critical technology. And a critical technology is really a technology that's subject to export controls. and it's controlled for export on a variety of U.S. government lists.

So, if a U.S. business has one of these technologies and uses it in one of those ways, that's the first prong of the test. The second aspect of this is that that business uses that technology in a targeted industry, or it designs that technology for a targeted industry. And a targeted industry is one of 27 different industry sectors that CFIUS has identified as part of this pilot program.

It really covers a really broad swath of the economy. These sectors are linked up to the Made in 2025 plan that China has put forward, and Tatman mentioned earlier. But it covers things such as aircraft manufacturing, petrochemical manufacturing, the defense industry in a variety of ways, batteries, biotechnology, nanotechnology, semiconductors, a lot of computer devices, chemical manufacturing.

So, it really covers a lot of the economy and a lot of sectors. If you go through and identify: Is your company qualified as a U.S. pilot program U.S. business because it has this technology that it uses in a certain way, and it also uses that technology in one of these targeted industries, then your business is a pilot program U.S. business. And if a foreign person makes a controlling investment in that business, that would trigger mandatory reporting underneath the pilot program.

Also, if there's a noncontrolling investment—and this is the expanded jurisdiction in a pilot program U.S. business—and that noncontrolling investment results in access to material nonpublic technical information; any board rights with respect to the U.S. business, including observer rights; or any ability to direct how that company uses critical technology, then that would be now subject to CFIUS jurisdiction, even though it's not a controlling investment, and would be subject to mandatory reporting. So, really, now, any controlling or noncontrolling covered transaction in a pilot program business is subject to mandatory reporting.

Really, what that means is that 45 days in advance of closing that transaction you must file with CFIUS to, at the very least, notify them of the transaction. You also have the option of doing a full CFIUS notice at that point. You can either do a declaration, which is a short-form filing, or as I mentioned the full written notice.

So you have that decision at that point. If you do not take that path, there are penalties that could apply, which go up to the value of the transaction. There are significant penalties that could apply if not complying with the buyout program, and, as I mentioned, that went into effect this past weekend, November 10th.

**Jose Garriga:**

Thank you, Christian. A reminder, listeners, that we're here today with Akin Gump international trade partners Tatman Savio and Christian Davis discussing CFIUS, FIRRMA and national security aspects of overseas investment in the United States.

Now, Tatman, you're in Hong Kong. You're working with clients who might be looking at investment in the United States. What does FIRRMA, then, mean, in practical terms, for these clients or businesses looking at statebound investment?

**Tatman Savio:**

Sure. As Christian described, there are a lot of changes resulting from the new law and the pilot programs, and we don't have final implementing regulations yet; there will be more changes to come. It's important to note that the changes apply as a general matter at this point, not with respect to the particular nationality of the investor, and the changes will have both a practical and legal effect on companies that are seeking to pursue investment, and not only U.S. companies but, more broadly, even non-U.S. companies that have operations in the United States.

One example of the practical changes that companies will face is the potential longer lead times. Pre-FIRRMA, the sequential review plus investigation process could take up to [75] days. Now, post-FIRRMA, the review timeline may take up to 105 days.

This is important because, in corporate transactions, timing can be everything, and it will be necessary for companies to build in these longer lead times for CFIUS approval. Now, it's worth noting, as Christian touched on, that even though the review timeline was shorter pre-FIRRMA, the committee was often unable to complete its reviews on a timely basis within those parameters, which meant that companies were often forced to withdraw their CFIUS notices and then refile them and start the review timeline all over again.

So, for that reason, it could be the case that, even though the review period is theoretically longer, CFIUS may be able to conclude its reviews on a more timely and streamlined basis, especially given that it will now have additional resources resulting from many filing fees and corresponding staffing increases.

From a legal perspective, more transactions are now covered transactions, and it's now mandatory to submit a CFIUS notice, with corresponding penalties if it's not. And I think this is really significant because, pre-FIRRMA, many companies would analyze their transactions and make determinations not to file CFIUS notices, either because 1) they could make a determination on their own that a particular transaction didn't meet the definition of a covered transaction, often on the basis that the foreign investor didn't have control rights, or 2) companies would make a risk-based determination not to file a notice. And, with FIRRMA, these two fundamentals of the approach to CFIUS review and analysis have changed. And, so, it's now the case that more transactions will be covered transactions, and that parties may not have discretion as to whether or not they submit a filing.

So that brings us specifically to China, and how that will impact Chinese investors.

As to the particular impact on China-based investors, this will, of course, have an impact, focused on the Made in China 2025 sectors, especially in connection with other measures that the U.S. government is pursuing against China, including a new export control reform law and other recent enforcement actions that are focused on tightening up U.S. technology controls.

So, in effect, China's effort to acquire U.S. technology by acquisition or other investment may become more challenging, but I wouldn't say that Chinese investments into the U.S. will be impossible. In this regard, it's important to note that it has already become increasingly difficult for Chinese companies to invest in the United States, with several high-profile investments falling or falling apart during CFIUS review, but with some others getting through.

And at least now with FIRRMA, some of the rules and requirements are clearer and more transparent, which will allow companies to be smarter and more realistic about their transaction planning. And in addition to that, CFIUS review has been and remains case by case. In each transaction, CFIUS is looking at the potential threat posed by a particular investor, the vulnerability of the investment target and the consequence of the transaction, and FIRRMA doesn't change that calculus.

So, there may be cases where CFIUS does not identify national security issues associated with a particular China-based transaction, or it sees one that can be mitigated somehow.

Another point that I want to raise in this regard to which I alluded a bit earlier is the new export control restriction. Concurrent with FIRRMA, Congress also passed a new export control law known as the Export Control Reform Act, and this law speaks to address concerns about foreign countries attaining access to sensitive U.S. technology that currently isn't controlled, specifically what are called "emerging and foundational technologies."

At one point, there was discussion about the new export control requirement becoming a part of the CFIUS process and a part of FIRRMA. Many people fought back against this concept because they wanted to keep the CFIUS regime separate from the export control regime, and with the parallel passage of FIRRMA and the new Export Control Reform Act, that separation does remain, but the emerging and foundational

technologies identified under the export control regime will be considered as critical technologies in the CFIUS regime.

So, that interplay is still there, and I think that interplay will continue to reinforce some of the concerns and export restrictions that are focused on China.

**Jose Garriga:** Thank you, Tatman. Let's pull back a bit and, beyond China, what other overseas investment might immediately, or perhaps in the longer term, feel the impact of the FIRRMA reform?

**Christian Davis:** Happy to answer that, Jose. I think, just thinking about this generally, and I think that the pilot program is a good example of this, the way that it was implemented it did not apply specifically to China. It applied to all countries. Even though that was the intended goal of FIRRMA, to address the risk associated with China, the way the law actually goes into effect is that it applies to all countries.

With respect how that really impacts overseas investment, all investment will have to go through this expanded jurisdiction and mandatory reporting requirements, at least underneath the pilot program. We'll see how it shakes out underneath the final rules.

As a result of that, it really results in increased diligence requirements for any inbound investment into the U.S., because, again, you have civil penalties that could apply to your investment if you do not make a filing in advance, and it fits within the pilot program. At the very least, you have to do that diligence to determine whether or not your transaction is caught underneath the pilot program and, potentially, under the full FIRRMA requirements if they go into effect at a later date.

Secondly, if you are caught under the expanded jurisdiction and mandatory reporting, then you'll have another regulatory hurdle that you must go through as a part of your deal process, which can impact the timing of your transaction and needs to be factored into the deal.

Third, and I think this mainly applies in the China context but can also apply outside of that, there's going to be a small set of transactions that will go through the process, and CFIUS will actually have objections to. There likely will be more deals that are actually blocked by CFIUS as a result of this because that wider net has been cast by CFIUS to force more deals through. So, we'll likely see additional transactions that are caught up, even though, as Tatman mentioned, really, the overall analysis and criteria identifying national security risk has not changed as a result of FIRRMA.

**Jose Garriga:** I think you all have done a great job of sketching out what it is that CFIUS and FIRRMA now are intended to do. I guess my question at this point is, will the CFIUS process, once fully reformed, once FIRRMA is fully implemented, will it achieve the stated goals, and if not, why not?

**Christian Davis:** In answering that question, I think you hit the nail on the head a bit there, Jose. It's a bit too early to tell exactly how this is shaking out so far. We don't know exactly how, for instance, CFIUS will respond to the increased filings that will come as a result of mandatory reporting requirements, for instance, underneath the pilot program. We also don't know yet the full scope of how CFIUS will draft the regulations, which will have a

big impact on how broad the expanded jurisdiction actually applies to transactions and how broad the mandatory reporting requirements are.

So, that being said, that's still out there, but I think, at the end of the day, the real question will be ... I think it's likely that the national security issues will be addressed through this, or many of them will be addressed, in that CFIUS will be able to get insight into more transactions as a result of FIRRMA, but I think the real question is whether, at the end of the day, FIRRMA results in less foreign direct investment in the U.S. that is actually beneficial to the U.S., whether it really discourages folks, foreign investors, from investing in the U.S., which is not the intended goal of FIRRMA.

**Jose Garriga:** That's a good point. Well, to close then, both of you have covered a lot of great material here, so, let's see if we can crystallize this a bit. What are a few takeaways that you can offer listeners who might be looking to invest in the United States or to seek investment from overseas, and I'll add a little maybe a nudge towards one possible answer in that respect is: Which questions regarding the scope and specific of this process remain unanswered? What lacunae are out there that people just don't even know can apply to this ongoing process of reform?

**Tatman Savio:** Well, I think that Christian touched on some of the unknowns still. We're still many months away from the deadline by which CFIUS must publish its final implementing regulations, and we expect that CFIUS will take the experience of the pilot program, evaluate it and maybe incorporating, as well as adding to, the current interim regulations based on the reviews that it has done up until that point. So, more remains to be developed in that regard.

There are certain things that are clearer at this juncture, which is that there will be mandatory filing requirements and expanded definitions for what is a covered transaction.

It will be really important for companies to do good, solid, comprehensive due diligence on their investment deals, both with respect to the investor really going up the chain of beneficial ownership and identifying whether there's a foreign government-controlled entity at the helm, because there may be mandatory requirements depending upon the interest of a foreign government-controlled entity in a transaction, as well as with respect to the investment target and looking at that target and doing diligence to determine whether it is dealing in critical technology, because that can also subject the transaction to mandatory requirements. So, it will be really important to do good, solid, well-rounded due diligence on all aspects of the transaction.

I think that the other thing to look to in terms of future trajectory as we await the implementing regulations is what also is going on from a geopolitical economic standpoint, vis-à-vis China. It would be a mistake to view FIRRMA in isolation on its own. It's really necessary to view it in relation to the export control reform law that I mentioned earlier, as well as the broader US/China trade war, which has at its root as well concerns about IP theft and Made In China 2025 industrial policy.

CFIUS is a legal regime. It is a regulatory process, but as we've seen in prior transactions, and we don't expect it to change, it can become very politicized, and for this reason, it's important to have clear transaction planning and strategy, which can include not only a legal strategy, but also a public policy one and a public relations one.



That's something that we've seen historically, and we don't see that changing in the future, and perhaps it will become even more important.

The last thing that I would note with respect to some takeaways to offer listeners, and Jose, this also goes back to your point as to what should people be looking for, the U.S. government will have what's called a notice-and-comment period with respect to the regulations that it's developing. So, it will conduct and solicit feedback from industry in formulating regulations, both with respect to FIRRMA and the new export control law. So, with respect to that upcoming process, we're encouraging and will continue to encourage companies to participate in the process to ensure that CFIUS has the benefit of their input.

**Jose Garriga:** Thank you, Tatman. Christian, what do you have for listeners that might be a couple points that they'd want to take away and think about regarding CFIUS and FIRRMA process?

**Christian Davis:** I would generally just reiterate the points that Tatman mentioned, with a specific focus on a couple things. One is under the pilot program, I think it's become increasingly important to identify whether or not you have export control technology that could qualify as critical technology. Many companies, particularly earlier-stage companies, have not done that analysis, and that can be an issue that will pop up in the deal process, and companies will not be prepared for that, and we've seen that happen in multiple examples already underneath the pilot program.

In terms of focusing on the full implementation, I think, specifically, the points that I think are most interesting to see how they play out: One is understanding the full and true scope of the real estate provision and how that will be crystallized in the final regulations, because it could capture a broad swath of real estate, or it could be very focused, and I think that remains to be seen in terms of how broad that will be. Secondly, noncontrolling investment in companies involved in critical infrastructure. The statute dictates that "critical infrastructure" be defined somewhat narrowly for purposes of this test, but I think others think that CFIUS will try to expand it broadly, and seeing where that balance is and what critical infrastructure is captured in the noncontrolling investment version will be something that will be important to watch.

Lastly, the mandatory reporting requirement for foreign government investors. The term "substantial interest" is largely undefined at this point, and understanding what really constitutes a substantial interest by a foreign government in a U.S. business that triggers mandatory reporting will have a big impact on the number of cases and transactions that are forced into the mandatory reporting process. Those are the three things that I'd be really watching with respect to the notice-and-comment period, and as I mentioned before, I think we're expecting to see a final rule by the end of next summer, most likely, and a proposed rule before then.

**Jose Garriga:** Thank you. Thank you, Christian. Listeners, you've been listening today to the Akin Gump international trade partners, Tatman Savio in Hong Kong and Christian Davis here in Washington DC. Thanks to you both. That was a great overview and analysis of a really significant change in the investment environment, the international trade policy from the United States.

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