

FOREIGN DIRECT INVESTMENT IN THE UNITED STATES

**FIRRMMA'S EXPANSION OF CFIUS REVIEW OF FOREIGN
INVESTMENTS AND NEW MANDATORY FILING REQUIREMENTS**

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CFIUS BACKGROUND

WHAT IS CFIUS?

- The Committee on Foreign Investment in the United States (“CFIUS” or “the Committee”) is an inter-agency panel authorized to conduct national security reviews of transactions that could result in foreign control of a U.S. business and, in some cases, non-controlling investments (“covered transactions”)
- CFIUS evaluates whether such covered transactions will threaten the **national security** of the United States

CFIUS COMPOSITION

- The Committee consists of:
 - 9 Executive Branch departments/offices
 - 5 observing members
 - Others can be added for specific reviews (e.g., the U.S. Department of Agriculture (“USDA”), the U.S. Department of Health and Human Services (“HHS”))

Permanent Members			Observers/Ad hoc	
Dep’t of Treasury (chair)	Dep’t of Defense	Dep’t of Homeland Security	Office of Management & Budget	National Economic Council
Dep’t of Justice	Dep’t of State	Dep’t of Energy	Council of Economic Advisors	Homeland Security Council
Dep’t of Commerce	Office of the U.S. Trade Representative	Office of Science and Technology Policy	National Security Council	

CFIUS' JURISDICTIONAL ASSESSMENT

- CFIUS is empowered to review “covered transactions.”
- Covered Transaction = “any transaction ... by or with any **foreign person**, which could result in **control** of a **U.S. business** by a foreign person”*
- **“Foreign Person” –**
 - Includes any entity controlled by a foreign national
- **“Control” –**
 - “the power, direct or indirect, whether or not exercised ... to determine, direct, or decide important matters affecting an entity”
 - No bright-line test
 - Technically excludes strictly passive investments with 10% or less voting interest
- **“U.S. Business” –**
 - “any entity, regardless of the nationality of the persons that control it, engaged in interstate commerce in the United States”
 - Includes non-U.S. companies with U.S. operations
 - Excludes “greenfield investments”

*FIRRMA provides that CFIUS can now review certain non-controlling investments

CFIUS' NATIONAL SECURITY ASSESSMENT

The foreign person presents a **threat**.

- The buyer is from a country of concern
- The buyer has close commercial ties to a country of concern
- The buyer is controlled by or has connections to a foreign government
- The buyer has a history of noncompliance with U.S. laws and regulations.

The U.S. business exposes a **vulnerability**.

- The U.S. business serves government customers, directly or indirectly
- The U.S. business deals in export-controlled goods or technologies
- The U.S. business may constitute “critical infrastructure” or serve “critical infrastructure” customers
- The U.S. business collects personal information of U.S. citizens

CFIUS assesses the potential national security consequences of the interaction of the identified threat and vulnerability.

OUTCOMES OF CFIUS REVIEWS

Determine that a transaction is not within CFIUS' jurisdiction

“Clear” or approve a transaction

Condition approval of a transaction on the parties' acceptance of “mitigation measures”

Impose interim restrictions on transaction parties during a review

Refer the matter to the President, who may choose to (a) prohibit a pending deal, or (2) order divestiture in a completed transaction

RECENT CFIUS TRENDS

Steadily increasing workload

- 2018: 230+ reviews
- 2017: 238 reviews
- 2016: 172 reviews

Longer review periods

- CFIUS is taking longer to start its statutorily dictated review timeline following submission of draft pre-file notices
- CFIUS is asking more and different questions at all stages of reviews

More investigations of covered transactions

- Number of transactions subjected to the additional 45-day investigation period has increased, perhaps due to CFIUS' inability to complete its review in 30 days
- Includes 70% of reviews in 2017

Increase in “withdrawals and re-filings”

- This restarts the statutory clock, providing CFIUS with additional time to review the transaction
- CFIUS may choose to start the new filing period in the “investigation” phase

More Mitigation

- As many as 20% of transactions

RECENT FORCED DIVESTITURES

- **iCarbonX/PatientsLikeMe (2019).** In 2017, PatientsLikeMe, a U.S. company operating a healthcare patient network and real-time research platform, reportedly sold a majority stake to iCarbonX, a Chinese digital healthcare company. According to public reports, CFIUS notified CarbonX that it would be required to divest its majority stake forcing PatientsLikeMe to seek a new buyer for iCarbonX's stake in the company.
- **Beijing Wanwei Kunlun Technology Co. Ltd./Grindr (2019).** In 2018, Grindr, a U.S. company operating a homosexual dating application, was acquired by Beijing Wanwei Kunlun Technology Co. Ltd. ("Kunlun"), a Chinese gaming company that publishes games, provides online financial services. In March 2019, CFIUS ordered Kunlun to sell Grindr based on concerns that Kunlun could use personal information to blackmail or influence American government officials or others with security clearances.

RECENTLY ABANDONED TRANSACTIONS

- **HNA Group/Skybridge Capital (2018).** In April 2018, Chinese conglomerate HNA Group Co. dropped its pursuit of SkyBridge Capital, the investment firm founded by former White House communications chief Anthony Scaramucci, after resistance from a U.S. national security panel. According to public reports, CFIUS told both firms that it would only approve the deal subject to concessions that would have essentially left the two companies operating entirely separately.
- **Unic Capital Management/Xcerra Corporation (2018).** On February 22, 2018, Unic Capital Management, a subsidiary of Sino IC Capital, which is a China-based semiconductor investment fund, abandoned its proposed acquisition of U.S. semiconductor testing company Xcerra Corporation (“Xcerra”) for \$580 million. Xcerra designs and manufactures equipment to test semiconductors and circuit boards, but does not make semiconductors. We understand that: (i) Xcerra’s technology is indigenous to the United States and not yet available or used in China; and (ii) one of the government’s primary concerns was that Xcerra potentially has access to technology associated with cutting edge developments in the semiconductor industry.
- **Ant Financial/MoneyGram International, Inc. (2018).** Ant Financial recently abandoned its proposed acquisition of MoneyGram International, Inc. due to CFIUS concerns over money laundering and potential threats to the U.S. financial system associated with the deal. Two U.S. senators wrote a letter to the Secretary of Treasury in opposition of the transaction. Based on public reports, the parties withdrew and refiled the CFIUS notice in September 2017 for a third time to allow more time for CFIUS to review the transaction.
- **Biotest – Creat Group Corp. (2018).** Biotest was required to divest its U.S. operations as a condition of receiving CFIUS approval in connection with Creat’s acquisition of the German blood plasma products maker. Reportedly Biotest put the U.S. operations in a trust until a suitable buyer was identified. Approximately 20 percent of Biotest’s revenue was derived from the U.S.

Broadcom/Qualcomm

- On March 12, 2018, President Trump issued an executive order prohibiting Singapore-headquartered **Broadcom Limited** (“Broadcom”) from completing its hostile takeover of **Qualcomm Inc.** (“Qualcomm”), based on a recommendation from CFIUS.
 - This is only the fifth time a President has taken such action and the first time a President has exercised this authority over a non-Chinese entity.
- The announcement came just months after Broadcom’s CEO made a public statement from the Oval Office indicating that Broadcom would redomicile in the United States.
- **Takeaway:** CFIUS is willing to undertake measures perceived as extreme to accomplish its national security mission.
 - Normally, companies voluntarily file with CFIUS, but, in this instance, the U.S. Department of the Treasury reportedly filed a notice on behalf of Qualcomm and Broadcom following Qualcomm’s submission of a draft notice.
 - The Presidential order was atypical in that it was issued before CFIUS completed its statutorily dictated review timeline.

OVERVIEW OF FIRRMA

KEY POLICY DRIVERS OF CFIUS REFORM

Changes in Chinese investment strategy and targets (e.g., Made in China 2025)

Increase in digitalization of the U.S. economy

“Third Party Concerns”

Increase in transactions designed to avoid CFIUS jurisdiction

Increasingly complex transaction structures

Evolving relationship between the commercial and military space

Perceived gaps in export controls

OVERVIEW

- On August 13, 2018, President Trump signed into law the Foreign Investment Risk Review Modernization Act (“FIRRMA”) to strengthen and modernize CFIUS.
- Initially introduced in November 2017, FIRRMA enjoyed broad bipartisan support in Congress as well as support from the White House and national security policy community.
- FIRRMA reflects the most significant changes to CFIUS in its history.

“CFIUS plays a **critical role** in protecting the national security of the United States. FIRRMA greatly **strengthens that protection** and provides much needed CFIUS modernization.” – Secretary Mattis (Defense)

“The context for this legislation is **important and relatively straightforward**, and it’s **China**.” – Senator Cornyn (R-TX)

“This bill focuses on providing CFIUS with **updated tools** to address present and future security needs... we hope to build on the progress we’ve already made to update CFIUS and **address national security threats**.” – Senator Feinstein (D-CA)

HOW FIRREA CHANGES CFIUS*

Expands the scope of CFIUS jurisdiction

Delineates potential exemptions from CFIUS jurisdiction for investments made through funds

Allows short-form “declarations” to be submitted in lieu of a formal filing

Makes certain investments subject to mandatory notifications

Extends the timeline for CFIUS reviews

**This list is not exclusive.*

NEW TYPES OF “COVERED TRANSACTIONS”

CFIUS will have jurisdiction over **four new types of “covered transactions”**

1. Purchase, lease, or concession by or to a foreign person of **U.S. real estate** near sensitive U.S. government locations and ports,
 - Exceptions: single-housing units and real estate in urbanized areas.
2. Any **change in a foreign investor’s rights** that result in foreign control of a U.S. business or an “other investment,”
3. Any investment or transaction designed to **evade CFIUS review**, and
4. **“Other investments,”** which are **non-controlling investments** in an “unaffiliated” U.S. business involving critical infrastructure, critical technology, or sensitive personal data of U.S. citizens *under certain circumstances*.

“OTHER INVESTMENTS”

Two-step test to determine what is an “other investment”:

- **Step 1:** Is there an investment by a **foreign person** in an unaffiliated U.S. business that:
 - a) owns, operates, manufactures, supplies, or services “**critical infrastructure**”; *or*
 - b) produces, designs, tests, manufactures, fabricates, or develops one or more “**critical technologies**”; *or*
 - c) maintains or collects “**sensitive personal data**” of U.S. citizens that could be exploited in a manner that threatens U.S. national security.

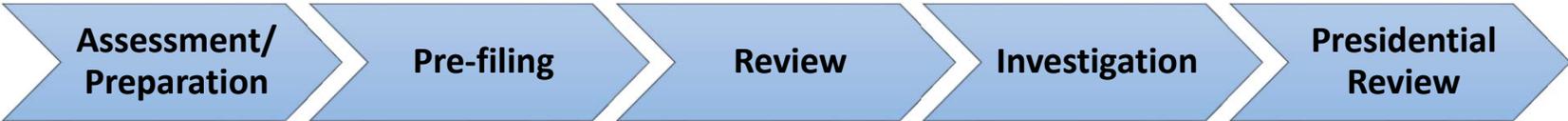
- **Step 2:** Does the **investment afford** the foreign person:
 - a) access to “**material nonpublic technical information**” possessed by the U.S. business; *or*
 - b) membership, observer or nomination **rights for the board** (or equivalent body) of the U.S. business; *or*
 - c) any involvement, other than through voting of shares, in **substantive decision making** related to sensitive personal data, critical technologies or critical infrastructure.

- This list should not be interpreted as exclusive. CFIUS may still find indicia of control based on other factors.

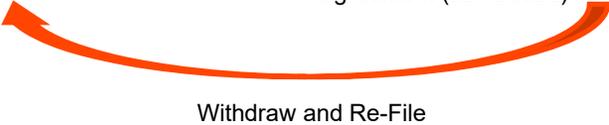
MANDATORY DECLARATIONS

- Declarations will be mandatory for “other investments” if:
 - The transaction involves an investment that results in the acquisition of a **substantial interest** in a U.S. business by a foreign person in which a **foreign government** has a substantial interest.
- Declarations may be mandatory for *any* investment in “critical technology” companies.
 - The scope of this provision forms the basis for the Mandatory Pilot Program effective November 10.

EXTENDED TIMELINE FOR REVIEWS



Current:	At least 3-4 weeks	2-3 weeks	30 days	45 days (as req'd)	15 days
FIRREA:	<u>No change.</u>	<u>Treasury staff will give comments on drafts/formal filings or accept filings for review within 10 business days if parties stipulate to "covered transaction"</u>	<u>Extended to 45 days</u>	<u>May be extended to 60 days under extraordinary circumstances</u>	N/A
Activities:	Assessment of CFIUS risk Preparation of CFIUS notice	Consult with CFIUS staff Submit draft notice for comments	Respond to information requests	Respond to information requests Negotiate mitigation agreement (as needed)	Most companies withdraw if CFIUS recommends blocking



OTHER KEY CHANGES

Expansion of Resources Available to CFIUS

- These resources will be used to ensure appropriate staffing for an anticipated larger caseload and review more non-notified transactions.

Enhanced Monitoring of Non-Notified Transactions

- FIRRMA requires CFIUS to establish a formal mechanism to identify any covered transaction or declaration has not been filed.

Filing Fees

- FIRRMA authorizes CFIUS to impose a filing fee for joint voluntary notices (i.e., not for short-form declarations) of 1 percent of the transaction value or USD \$300,000, whichever is less.

Emerging and Foundational Technology Process

- The Export Control Reform Act of 2018, a companion piece of legislation, creates an interagency process to identify “emerging” and “foundational” technology that warrants control.

CFIUS PILOT PROGRAM

CFIUS PILOT PROGRAM

- On October 10, the Department of the Treasury introduced a Pilot Program that mandates the filing of “Declarations” in connection with certain foreign investments in certain U.S. companies that deal with critical technology.
- The Pilot Program began November 10.
- The rule applies to controlling investments as well as certain non-controlling investments.

WHY SHOULD I CARE ABOUT THE PILOT PROGRAM?

- For the first time, the CFIUS process is Mandatory for certain investments
- CFIUS is authorized to penalize both parties up to the value of the transaction if companies fail to notify CFIUS when mandatory

OVERVIEW: WHEN IS A MANDATORY NOTICE REQUIRED?

Step 1: Is the U.S. business a “pilot program U.S. business”?

- Does the U.S. business produce, design, test, manufacture, fabricate, or develop a “critical technology”?
- If so, is it “[u]tilized in connection with the U.S. business’s activity in” or “designed . . . specifically for use in” a “pilot program industry”?

Step 2: Is the proposed transaction a “pilot program covered transaction”?

- Is it a “transaction by or with any foreign person that could result in foreign control of any pilot program U.S. business”?
- Does it afford the foreign person access to any material nonpublic technical information; membership, observer, or nomination rights on the board of directors or equivalent; or any involvement in substantive decision making regarding critical technology?

STEP ONE: WHAT IS “CRITICAL TECHNOLOGY”? THE FAMILIAR ONES

ITAR	Defense articles or defense services included on the United States Munitions List
EAR	Dual-use items listed on the Commerce Control List and controlled for reasons relating to national security, chemical and biological weapons proliferation, nuclear nonproliferation, missile technology, regional stability, or surreptitious listening
Foreign Atomic Energy Assistance	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 Exports/Imports	Nuclear facilities, equipment, and material covered by 10 CFR part 110 (relating to export and import of nuclear equipment and material)
Select Agents/Toxins	Select agents and toxins covered by 7 CFR part 331, 9 CFR part 121, or 42 CFR part 73

STEP ONE: WHAT IS “CRITICAL TECHNOLOGY”? THE NEW ADDITION

- Emerging and foundational technologies controlled pursuant to section 1758 of the Export Control Reform Act of 2018:
 - ❖ Not yet defined, but Commerce requested comments on the specific technologies that should and should not be export controlled
 - ❖ Covers technologies not are not controlled under existing regimes

EMERGING TECHNOLOGY CATEGORIES

- Biotechnology – such as: (i) Nanobiology; (ii) Synthetic biology; (iii) Genomic and genetic engineering; or (iv) Neurotech
- Artificial intelligence (AI) and machine learning technology
- Position, Navigation, and Timing (PNT) technology
- Microprocessor technology
- Advanced computing technology
- Data analytics technology
- Quantum information and sensing technology
- Logistics technology
- Additive manufacturing (e.g., 3D printing)
- Robotics
- Brain-computer interfaces
- Hypersonics
- Advanced Materials
- Advanced surveillance technologies

STEP ONE: IS THE CRITICAL TECHNOLOGY DESIGNED FOR OR UTILIZED IN A “PILOT PROGRAM INDUSTRY?”

To be a “pilot program U.S. business,” the U.S. business’s critical technology must be “[u]tilized in connection with the U.S. business’s activity in” or “designed . . . specifically for use in” one of the 27 “pilot program industries”

PILOT PROGRAM INDUSTRIES

- Aircraft Manufacturing NAICS Code: 336411
- Aircraft Engine and Engine Parts Manufacturing NAICS Code: 336412
- Alumina Refining and Primary Aluminum Production NAICS Code: 331313
- Ball and Roller Bearing Manufacturing NAICS Code: 332991
- Computer Storage Device Manufacturing NAICS Code: 334112
- Electronic Computer Manufacturing NAICS Code: 334111
- Guided Missile and Space Vehicle Manufacturing NAICS Code: 336414
- Guided Missile and Space Vehicle Propulsion Unit and Propulsion Unit Parts Manufacturing NAICS Code: 336415
- Military Armored Vehicle, Tank, and Tank Component Manufacturing NAICS Code: 336992
- Nuclear Electric Power Generation NAICS Code: 221113
- Optical Instrument and Lens Manufacturing NAICS Code: 333314
- Other Basic Inorganic Chemical Manufacturing NAICS Code: 325180
- Other Guided Missile and Space Vehicle Parts and Auxiliary Equipment Manufacturing NAICS Code: 336419

PILOT PROGRAM INDUSTRIES

- Petrochemical Manufacturing NAICS Code: 325110
- Powder Metallurgy Part Manufacturing NAICS Code: 332117
- Power, Distribution, and Specialty Transformer Manufacturing NAICS Code: 335311
- Primary Battery Manufacturing NAICS Code: 335912
- Radio and Television Broadcasting and Wireless Communications Equipment Manufacturing NAICS Code: 334220
- Research and Development in Nanotechnology NAICS Code: 541713
- Research and Development in Biotechnology (except Nanobiotechnology) NAICS Code: 541714
- Secondary Smelting and Alloying of Aluminum NAICS Code: 331314
- Search, Detection, Navigation, Guidance, Aeronautical, and Nautical System and Instrument Manufacturing NAICS Code: 334511
- Semiconductor and Related Device Manufacturing NAICS Code: 334413
- Semiconductor Machinery Manufacturing NAICS Code: 333242
- Storage Battery Manufacturing NAICS Code: 335911
- Telephone Apparatus Manufacturing NAICS Code: 334210
- Turbine and Turbine Generator Set Units Manufacturing NAICS Code: 333611

STEP TWO: IS THE TRANSACTION A “PILOT PROGRAM COVERED TRANSACTION”?

There are two types of “pilot program covered transactions”:

Pilot Program Covered
Transaction

Pilot Program Covered
Investment

STEP TWO: IS THE TRANSACTION A “PILOT PROGRAM COVERED TRANSACTION”?

- Covers traditional “controlling foreign investments”
- Defined as “[a]ny transaction by or with any foreign person that could result in foreign control of any pilot program U.S. business, including such a transaction carried out through a joint venture”

STEP TWO: IS THE TRANSACTION A “PILOT PROGRAM COVERED INVESTMENT”?

- Covers passive investments
- Defined as an investment, direct or indirect, by a foreign person in an unaffiliated pilot program U.S. business that could not result in control by a foreign person of a pilot program U.S. business and that affords the foreign person:
 - ❖ Access to any material nonpublic technical information in the possession of the pilot program U.S. business;
 - ❖ Membership or observer rights on the board of directors or equivalent governing body of the pilot program U.S. business or the right to nominate an individual to a position on the board of directors or equivalent governing body of the pilot program U.S. business; or
 - ❖ Any involvement, other than through voting of shares, in substantive decision-making of the pilot program U.S. business regarding the use, development, acquisition, or release of critical technology.

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