

CORPORATE MATTERS: F.I.R.R.M.A. PROPOSED REGULATIONS EXPAND C.F.I.U.S. OVERSIGHT ON FOREIGN INVESTMENT

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F.I.R.R.M.A.

Foreign Investment

INTRODUCTION

On August 13, 2018, the Foreign Investment Risk Review Modernization Act of 2018 (“F.I.R.R.M.A.”) was signed into law after receiving broad bipartisan support in Congress. F.I.R.R.M.A. strengthens and modernizes the Committee on Foreign Investment in the United States (“C.F.I.U.S.”) review process and marks the most sweeping changes to C.F.I.U.S. in over a decade. C.F.I.U.S. operates pursuant to Section 721 of the Defense Production Act of 1950. It is an interagency committee authorized to review certain transactions involving foreign investment in the U.S. (“covered transactions”). Its mandate is to determine the effect of such transactions on the national security of the U.S. and, where appropriate, to deny approval to the transaction. F.I.R.R.M.A. addresses national security concerns arising from certain foreign non-controlling investments and real estate transactions that previously fell outside C.F.I.U.S.’s jurisdiction.

At the time of adoption of F.I.R.R.M.A., C.F.I.U.S. was directed to consider the following matters in making its determinations:

- Does a foreign person engaging in a covered transaction with a U.S. business have a history of complying with U.S. laws?
- How likely is it that a covered transaction will expose personally identifiable information, genetic information, or other sensitive data of U.S. citizens to a foreign government or foreign person that may exploit that information in a manner that threatens national security?
- How likely is it that a covered transaction will exacerbate or create new cybersecurity vulnerabilities in the U.S. or is likely to result in a foreign government gaining a significant new capability to engage in malicious cyber-enabled activities against the U.S., including such activities designed to affect the outcome of any election for Federal office?

Given the timing of the enactment of F.I.R.R.M.A., it is likely that ongoing concerns about Chinese investment in the U.S. and the activities of Russia around the election played a significant part in its drafting.

More than one year after its enactment, the Department of the Treasury has now issued proposed regulations that would comprehensively implement F.I.R.R.M.A. The public has been given until October 17, 2019, to provide the Treasury Department with comments on the proposed regulations. The comment period concludes on October 17, 2019.

The F.I.R.R.M.A. statutory provisions and the regulations issued by the Department of the Treasury are laid out below.

EXTENDED C.F.I.U.S. JURISDICTION

C.F.I.U.S.'s jurisdiction to approve or disapprove a transaction is no longer limited to transactions that could result in foreign control of certain U.S. businesses. Under F.I.R.R.M.A., its jurisdiction covers certain foreign investments where the investment fails to provide the investor with control. In addition, F.I.R.R.M.A. expands the term "covered transactions" to include the following categories:

- Real estate transactions
- Non-controlling "other investments" that change a foreign person's rights
- Evasion

Consequently, C.F.I.U.S. is now able to review certain non-controlling investments by a foreign person in an unaffiliated U.S. business depending on the circumstances.

Factors to be Considered

Factors to be considered with regard to a non-controlling other investment include any of the following:

- Does the U.S. business own, manufacture, supply, or service critical infrastructure?
- Does the U.S. business produce or develop critical technologies?
- Does the U.S. business maintain or collect personal data of U.S. citizens that may be exploited in a way that threatens U.S. national security?

Other Investments

Other investments include any direct or indirect investment that would not otherwise qualify as a covered transaction but allows the foreign person to have certain rights and powers outlined below:

- Access to any material nonpublic technical information in possession of the U.S. business
- Membership or observer rights on the board of directors or equivalent governing body or the right to nominate a person to the board
- Involvement, other than voting of shares, in any substantive decision-making rights regarding the use and safekeeping of sensitive personal data of U.S. citizens, use development or management of critical infrastructure, or critical technology

Non-controlling transactions become covered transactions only when they involve U.S. critical infrastructure, critical technology, or personal data and at least one of the listed factors is present.

CRITICAL INFRASTRUCTURE

Critical infrastructure refers to systems and assets, whether physical or virtual, so vital to the U.S. that its incapacity or destruction would have a debilitating impact on

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national security. The term “critical technologies” includes, *inter alia*, the following items:

- Defense articles or defense services that appear on the U.S. Munitions List of the International Traffic in Arms Regulations
- Items that appear on the Commerce Control List of the Export Administration Regulations that are controlled by multilateral regimes (for reasons such as national security, chemical or biological weapons proliferation, nuclear non-proliferation, or missile technology) or for reasons relating to regional stability or surreptitious listening
- Nuclear equipment, facilities, materials, software, and technology subject to export regulations by the Department of Energy or Nuclear Regulatory Commission.
- Select agents and toxins
- Emerging and foundational technologies

Carve-Out for Investment in Certain Funds

A carve-out from the expanded definition of covered transactions is provided for investment in funds when certain requirements are met regarding control issues. A fund that affords a foreign person membership as a limited partner or equivalent on an advisory board will not be considered an other investment that triggers expanded C.F.I.U.S. review jurisdiction when all the following requirements are met:

- The fund is managed exclusively by a general partner, managing member, or equivalent that is not a foreign person.
- Neither the advisory board nor the foreign person has the ability to control investment decisions or other decisions related to entities in which the fund is invested, including veto rights.
- The foreign person cannot unilaterally control the hiring, dismissal, or compensation of the general partner.
- The foreign person does not have access to material nonpublic technical information as a result of its participation in the advisory board.

Real Estate

Under F.I.R.R.M.A., certain real estate transactions require C.F.I.U.S. approval. The real estate transactions covered under F.I.R.R.M.A. include those in which a foreign person leases or purchases private or public real estate either at an air or maritime port or in close proximity to a U.S. military base or other sensitive U.S. government facility. An exception is provided for real estate transactions related to single-family housing units or real estate in urbanized areas.

Change in Rights

A covered transaction now includes a foreign person whose rights have changed with respect to a U.S. business, if the change results in foreign control of the U.S. business or it meets the criteria of an “other investment” as defined above.

Evasion

Any transaction or arrangement that is designed or intended to evade or circumvent the jurisdiction of C.F.I.U.S. is subject to C.F.I.U.S. scrutiny.

F.I.R.R.M.A. PILOT PROGRAM

In General

F.I.R.R.M.A. authorizes C.F.I.U.S. to conduct pilot programs to implement the F.I.R.R.M.A. provisions. In October 2018, interim regulations were issued to conduct a pilot program, which authorizes C.F.I.U.S. to review non-controlling foreign investments in U.S. businesses involved in critical technologies related to specific industries. The pilot program went into effect on November 10, 2018.

Investment Policy

In a set of Q&A's published in connection with the pilot program, the Treasury Department emphasized that the program does not single out any specific country. Rather, C.F.I.U.S.'s authorities may be applied to address the national security risks posed by foreign investment in the U.S. regardless of the place where an investment originates.

In addition, the Treasury Department reiterated that the U.S. welcomes foreign investment in the technology industry and maintains a strong commitment to the rule of law and the protection of intellectual property. Neither F.I.R.R.M.A. nor the pilot program changes this investment environment. C.F.I.U.S. will continue to assess, on a case-by-case basis through its current process and the pilot program, whether the facts and circumstances of a particular transaction (regardless of industry) pose a risk to U.S. national security.

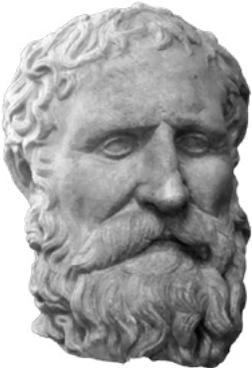
The pilot program was adopted to enable C.F.I.U.S. to understand and examine, in a comprehensive manner, the nature of foreign direct investment as it relates to critical technologies and the select pilot program industries. The pilot program addresses ongoing risks to U.S. national security arising from the rapid pace of technological change in certain U.S. industries and the nature of some foreign investments aimed at affecting certain decisions regarding, or to obtain certain information relating to, critical technologies.

The pilot program will end no later than the date on which the regulations fully implementing F.I.R.R.M.A. become effective and in no event later than March 5, 2020, the date that is 570 days after the enactment of F.I.R.R.M.A.

Mandatory Reporting

Foreign investors are now required to file mandatory declarations for transactions that fall within the scope of the pilot program. The mandatory declarations are abbreviated notices that generally do not exceed five pages in length. The pilot program covers 27 specific industries, identified by their respective North American Industry Classification System code.

Pursuant to the pilot program, parties must determine whether a proposed foreign investment in a U.S. business triggers the mandatory declaration and, if so, decide



whether the covered U.S. business is involved with critical technology related to the 27 industries covered under the pilot program. The 27 identified industries range from manufacturing operations for aircraft and space vehicles to high technology businesses focused on computer storage devices and semiconductor machinery. This includes the defense manufacturing industry with specific concern for military armored vehicles.

The pilot program was the first regulation implemented by the Treasury Department pursuant to F.I.R.R.M.A. The pilot program does not apply to non-controlling investments in critical infrastructure and sensitive personal data of U.S. persons, nor to real estate investments.

PROPOSED TREASURY REGULATIONS

The proposed regulations continue a largely voluntary reporting process, which involves filing a notice or submitting a short-form declaration notifying C.F.I.U.S. of a covered investment in order to receive a potential “safe harbor” letter. Once the letter is issued, C.F.I.U.S. generally does not initiate a review of a transaction except in certain limited circumstances.

Mandatory Filing

In certain circumstances, filing a declaration is mandatory. The regulations explain that a mandatory filing obligation exists for certain for specified covered transactions where a foreign government has a “substantial interest” in the investment.

Additionally, F.I.R.R.M.A. authorizes C.F.I.U.S. to mandate declarations for covered transactions involving certain U.S. businesses that produce, design, test, manufacture, fabricate, or develop one or more critical technologies.

The new provisions on covered investments only apply to investments in U.S. businesses involved in specified ways with critical technologies, critical infrastructure, or sensitive personal data – referred to as “T.I.D. U.S. businesses” for technology, infrastructure, and data.

Critical Technologies

The proposed regulations authorize C.F.I.U.S. to review transactions related to U.S. businesses that design, test, manufacture, fabricate, or develop one or more critical technologies.

The definition of critical technologies includes certain items subject to export controls and other existing regulatory schemes, as well as emerging and foundational technologies controlled pursuant to the Export Control Reform Act of 2018.

Critical Infrastructure

C.F.I.U.S. may review transactions related to U.S. businesses that perform specified functions, such as owning, operating, manufacturing, supplying, or servicing, with respect to critical infrastructure across subsectors including telecommunications, utilities, energy, and transportation. These functions are identified in [Appendix I](#) to this article.

“Investments from all foreign persons remain subject to C.F.I.U.S.’s jurisdiction over transactions that could result in foreign control of a U.S. business.”

Sensitive Personal Data

C.F.I.U.S. may review transactions related to U.S. businesses that maintain or collect sensitive personal data of U.S. citizens that may be exploited in a manner that threatens national security. Sensitive personal data is defined to include ten categories of data maintained or collected by U.S. businesses that meet any of the following criteria:

- The U.S. business targets or tailors products or services to sensitive populations, including U.S. military members and employees of Federal agencies involved in national security.
- It collects or maintains such data on at least one million individuals.
- It has a demonstrated business objective to maintain or collect such data on greater than one million individuals and such data is an integrated part of the U.S. business’s primary products or services.

The categories of data include types of financial, geolocation, and health data, among others. Genetic information is also included in the definition regardless of whether it meets the criteria listed above

Foreign Person and Excepted Investor

The proposed regulations create an exception from covered investments for certain foreign persons that are “excepted investors” based on their (i) ties to certain countries identified as “excepted foreign states” and (ii) compliance with certain laws, orders, and regulations.

Note that the proposed regulations do not except any person from control transactions previously subject to C.F.I.U.S. jurisdiction. Investments from all foreign persons remain subject to C.F.I.U.S.’s jurisdiction over transactions that could result in foreign control of a U.S. business.

Proposed Regulations Covering Real Estate Transactions

Types of Transactions Covered

The proposed regulations regarding real estate transactions cover the purchase or lease by, or a concession to, a foreign person of certain real estate in the U.S. that affords the foreign person three or more of the following property rights:

- The right to physically access the property
- The right to exclude physical access to another
- The right to improve or develop the property
- The right to affix structures or objects on the property

Voluntary Process

There is no mandatory filing requirement for real estate transactions. Parties may file a notice or submit a short-form declaration notifying C.F.I.U.S. of a covered real estate transaction in order to potentially qualify for a safe harbor letter that prevents

C.F.I.U.S. from initiating a review of the transaction except in certain limited circumstances.

Covered Sites

Coverage is focused on transactions in or around specific airports, maritime ports, and military installations. The relevant military installations are listed by name and location in [Appendix II](#) to this article. The relevant airports and maritime ports are on lists published by the Department of Transportation.

Locations Around Covered Sites

If real estate is located in or around a covered site, the following characteristics of the real property are relevant:

- Whether the real estate is, is within, or will function as part of an air or maritime port
- Whether the real estate is within close proximity (*i.e.*, one mile) of certain specified U.S. military installations
- Whether the real estate is within the extended range (between one and 100 miles) of certain military installations
- Whether the real estate is within certain geographic areas associated with missile fields and offshore ranges

Foreign Person and Excepted Real Estate Investor

The regulations create exceptions from coverage applicable for real estate transactions by certain foreign persons defined as “excepted real estate investors” based on their (i) ties to certain countries identified as “excepted real estate foreign states” and (ii) compliance with certain laws, orders, and regulations.

Urbanized Areas and Urban Clusters

The proposed regulations create exceptions from coverage for real estate transactions in an urbanized area or urban cluster, as defined by the Census Bureau. However, the exception does not apply to urbanized areas and clusters relating to relevant ports and those in close proximity to certain military installations.

Other Excepted Real Estate Transactions

The proposed regulations provide exceptions from coverage for certain real estate transactions:

- The purchase, lease, or concession of a single housing unit, as defined by the Census Bureau
- Transactions involving certain commercial office space in a multi-unit commercial office building

Interaction with Other C.F.I.U.S. Regulations

It should be noted that real estate transactions that are also subject to C.F.I.U.S.’s existing and proposed regulations regarding control transactions and non-controlling

investments involving U.S. businesses are to be analyzed under those other regulations.

CONCLUSION

As previously mentioned, the comment period concludes on October 17, 2019. It is anticipated that final regulations will be issued soon after the close of the comment period. The target date for final regulations is not later than March 5, 2020, the date that is 570 days after the enactment of F.I.R.R.M.A.