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Reform Proposes Sweeping Changes to CFIUS Reviews

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Over the past year, a bipartisan group of legislators in Congress has been drafting and soliciting support for a new statute that, if passed, would dramatically reform national security reviews performed by the Committee on Foreign Investment in the United States (CFIUS). The Foreign Investment Risk Review Modernization Act of 2017 (FIRRMA) was introduced on November 8, 2017, with ultimate goals of maintaining American leadership in certain critical technology industries and protecting against evolving threats to American national security and critical infrastructure.

FIRRMA's lead sponsors, U.S. Sen. John Cornyn, R-Texas, and U.S. Rep. Robert Pittenger, R-N.C., promoted the bill throughout December 2017. On December 14, 2017, the House Financial Services Subcommittee on Monetary Policy and Trade held a hearing on FIRRMA, the first in a series of congressional hearings on CFIUS reform and oversight. The subcommittee held a second hearing on FIRRMA on January 9, 2018. In addition, a number of key policymakers and industry representatives signaled their support for the bill, including Treasury Secretary Steven Mnuchin, Defense Secretary James Mattis, Attorney General Jeff Sessions and Oracle Corporation. Senate Banking Committee Chairman Mike Crapo, R-Idaho, has pushed back against the bill, but overall these developments demonstrate the sponsors' commitment to moving the bill forward in 2018.

The legislation attempts to address growing concerns that foreign entities may be using acquisitions of and partnerships with U.S. businesses to chip away at American technological leadership. Many policymakers are concerned that certain companies may be circumventing the CFIUS process by using creative structuring in their transactions to avoid CFIUS jurisdiction. Such transactions could present a harm to U.S. national security.

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FIRRMA would address this concern through a wholesale revamp of the CFIUS process. Most notably, the legislation would bring additional types of transactions under the committee's purview and establish mandatory notification for certain transactions. The bill also would expand CFIUS

authority to allow the committee to require risk mitigation measures and, if necessary, monitor and enforce them. And the bill would establish a filing fee to address concerns about resource constraints.

Although Chinese investments and partnerships in the U.S. received particular scrutiny during the House hearing, both the bill's sponsors and the witnesses testifying before the House were committed to the belief that any changes to CFIUS operations should reject economic protectionism. Entities from "countries of special concern" may face additional hurdles in the CFIUS review process if the new legislation passes, but the proposed bill is not intended to serve as the pretext for the creation of a foreign investment blacklist, according to its sponsors.

Key provisions of FIRRMA (see our November 10, 2017, client alert "[Legislation Proposes Sweeping New Foreign Investment Review Authorities](#)") include:

Expanding the Set of Covered Transactions. CFIUS jurisdiction would be expanded to include, among others, joint ventures and strategic partnerships, certain licensing agreements, noncontrolling investments in U.S. critical technology and infrastructure companies, and purchases or leases of real estate near sensitive U.S. government properties.

Establishing Short-Form and Mandatory Notification Procedures. FIRRMA would expand the CFIUS notice options by adding a "short-form" declaration that could be filed to ascertain whether CFIUS has sufficient interest in a given transaction to request a full notice and review. In certain circumstances, the bill would make the filing of these short declarations mandatory. The bill also would empower the committee to impose civil penalties on parties that do not comply with the mandatory notification requirements.

Emphasizing Countries of Special Concern. An additional component of the committee's analysis under the new bill would be the transaction's nexus with "countries of special concern" — *i.e.*, those that "pose[] a significant threat to the national security interests of the United States." CFIUS would not be required to maintain a list of these countries but would have the flexibility to analyze a particular transaction through a country-specific lens in conjunction with other risk factors.

Mitigating Transaction Risks Through CFIUS Action. FIRRMA would maintain CFIUS' broad authority to mitigate the risk posed by covered transactions and provide the committee with the authority to suspend a transaction while it is under review. The bill also contemplates the use of independent, third-party entities to monitor compliance — an increasingly common component of mitigation agreements under the current statutory framework.

Mitigating Transaction Risks Through Presidential Authorities. In addition to measures taken to suspend or prohibit a transaction, or to require divestiture, the president also may "take any additional action the President considers appropriate to address the risk to [...] national security."

Enforcing Mitigation. In the event of noncompliance with a mitigation agreement, the legislation would authorize CFIUS to (1) negotiate with the transaction parties to remediate the

noncompliance, (2) require that the parties submit for review any covered transaction initiated after the date of noncompliance, or (3) seek injunctive relief.

Monitoring Non-Notified Transactions and Revisiting Previously Mitigated Transactions. The bill would require CFIUS to establish a monitoring mechanism to identify covered transactions that were not submitted for review and for which information is reasonably available. In addition, the bill would expand CFIUS' ability to revisit transactions in which the parties are in material breach and lower the bar for overcoming the "safe harbor" that restricts reviews of previously cleared transactions.

Establishing a Filing Fee and Extending CFIUS Review Timing. The bill would establish a fee for CFIUS submissions, set up to the lesser of 1 percent of the value of the transaction or \$300,000, adjusted annually for inflation. In addition, the bill would lengthen the initial review phase from 30 days to 45 days and under some circumstances permit the secondary investigation phase to be extended for one 30-day period. Thus, the combined review and investigation process could total 120 days from acceptance of the CFIUS notice.

Key Takeaways

The proposed legislation would have far-reaching consequences for transactions between U.S. and foreign parties. Should FIRRMA pass, careful structuring and advance consideration of potential national security issues will be paramount. As a result, transaction parties would be well-advised to address CFIUS issues proactively when considering cross-border investments and commercial opportunities. International business partners also may need to consider CFIUS issues in their commercial negotiations. All cross-border investors should be prepared for thorough and potentially lengthy CFIUS investigations.

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Changes to the review process also must be considered in light of the U.S. trade relationship with China, which is increasingly marked by accusations of unfair practices. The U.S. trade representative recently launched a Section 301 investigation into China's alleged theft of U.S. intellectual property, and U.S. companies complain that they face barriers and discriminatory treatment in seeking to invest in the Chinese market. In this context, the broadening of CFIUS jurisdiction and authority is a way to address ongoing trade disputes while protecting U.S. national security interests.

The expansion of CFIUS jurisdiction also could be viewed as an attempt to address limitations to the U.S. export control system. CFIUS already has the authority to mitigate national security risks that are not adequately addressed by export control regimes. However, by expanding the scope of CFIUS jurisdiction, FIRMMA would enable CFIUS to exert that authority over more transactions and effectively strengthen export control. Nevertheless, there is debate as to whether the CFIUS review

process should be reformed to address gaps in the export control system or whether that system in the U.S. should be reformed separately. While some overlap in jurisdiction currently occurs, some policymakers have expressed fears that CFIUS would be unable to fulfill its legislative mandate if its jurisdiction were expanded too broadly. Changes to the CFIUS review process would unfold over the months following the legislation's passage as the committee increases its staffing and writes new regulations, but the ultimate effect will be profound.

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