

CFIUS Releases 2019 Annual Report to Congress

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On July 30, 2020, the Committee on Foreign Investment in the United States (CFIUS or the Committee) released its annual report to Congress for calendar year 2019. CFIUS, an interagency committee led by the U.S. Department of the Treasury, reviews certain foreign investment transactions for national security risks. The 2019 annual report, which was issued only two months after CFIUS issued its 2018 annual report, provides the first full year of data since Congress passed the Foreign Investment Risk Review Modernization Act (FIRRMA) in August 2018. Because the 2019 annual report covers the calendar year before the final regulations implementing FIRRMA went into effect, the report reflects the impact of: (1) FIRRMA provisions that did not require implementing regulations, such as the longer timeline for the review phase of a CFIUS proceeding; and (2) the CFIUS Pilot Program for critical technology transactions, which the Committee launched in November 2018 through temporary regulations.

Below, we summarize three key takeaways from the report.

Short-Form Declarations Drive Apparent Increase in Overall Caseload, but Notices Hold Steady

The report confirms that the total number of voluntary notices filed with CFIUS remained relatively constant in 2019. Notices inched upward, from 229 in 2018 to 231 in 2019, yet fell below the Committee's all-time high of 237 notices filed in 2017.

The Committee also received 94 short-form declarations in 2019 through the CFIUS Pilot Program. Among its many innovations, FIRRMA enabled parties to submit short-form declarations instead of full notices, and it provided for such short-form declarations to be reviewed on an expedited basis (30 days). FIRRMA authorized, but did not require, CFIUS to make it mandatory for parties to file such declarations (or, at the parties' option, full notices) in certain transactions that involved critical technology.¹

Through temporary regulations, CFIUS established the Pilot Program to implement this authority and required parties to file short-form declarations if the U.S. business produced, designed, tested, manufactured, fabricated or developed a critical technology that met certain criteria. In such cases, a filing would be mandatory if the transaction gave the foreign investor control over the U.S. business or, alternatively, if it gave the foreign investor certain rights that fell short of control (*i.e.*, access to nonpublic technical information, membership or observer rights on the board of directors, or involvement in substantive decision-making regarding the critical technology). By requiring such filings, CFIUS sought greater visibility into a broader range of transactions — particularly noncontrolling investments. CFIUS replaced the Pilot Program with final regulations in February 2020.

As a result of the new critical technology declaration process, the total number of cases before CFIUS — taking into account both the number of full notices (231) and short-form declarations (94) — likely rose in 2019.² Out of the 94 declarations filed, CFIUS asked parties to file a full notice in 26 cases, notified parties that it was “unable to complete action” in 32 cases and cleared the transaction in 35 cases.³ In many of these cases, parties that had initially filed a declaration went on to file a full notice (reflected

¹ See our October 11, 2018, client alert titled “CFIUS Pilot Program Expands Jurisdiction to Certain Noncontrolling Investments, Requires Mandatory Declarations for Some Critical Technology Investments.”

² By comparison, 229 notices and 20 declarations were filed in 2018, reflecting the fact that the Pilot Program did not go into effect until November 2018.

³ Parties withdrew one declaration in 2019 for business reasons.

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in the annual total of 231). Even if one considers only the 35 declarations that were cleared in review, the total number of cases filed with CFIUS — reflected in notices (231) and declarations that did not lead to notices (at least 35) — likely rose in 2019, albeit less than many had predicted.

As parties (and the Committee) become more comfortable with the declaration process — an option now available in all transactions — we expect that the proportion of declarations to full notices filed with the Committee will rise.

Longer Review Period and More CFIUS Resources Lead to Fewer Investigations

The 2019 annual report also confirms the impact of another change generated by FIRRMA — *i.e.*, the extension of the first-stage review period from 30 days to 45 days. The data shows, not surprisingly, that this longer time period has allowed CFIUS to dispose of more cases in review, without the need for a second-stage national security investigation. While the number of transactions before CFIUS appears to have risen in 2019, the number of cases going to investigation fell from 158 in 2018 to 111 in 2019 — a 30% drop.

We also suspect that this decline is attributable, in part, to the substantial hiring and staffing efforts of CFIUS agencies since the passage of FIRRMA. Anticipating a higher caseload, CFIUS agencies have increased funding for their participation in CFIUS and have actively recruited and expanded their staff. With these greater resources, CFIUS appears to be running with greater efficiency, and it is able to respond to and dispose of cases more quickly. In some cases, this may obviate the need for a second-stage investigation.

These developments bode well for CFIUS going forward. The Committee seems well-positioned to handle the influx of cases that are anticipated now that it has issued final regulations implementing FIRRMA. Even the relatively timely release of the 2019 Annual Report reflects CFIUS' ability to better keep up with its workload; in the past, the Committee has often been up to two years behind on its annual reporting responsibilities.

Further Decline in Filings Involving Chinese Investors

For the first time in three years, China no longer accounts for the largest number of notices filed with CFIUS. The number of notices filed in cases with Chinese investors fell by more than half over the past three years (*i.e.*, 60 in 2017, 55 in 2018, 25 in 2019). Moreover, Chinese investors accounted for only three out of the 94 short-form declarations filed in 2019 (*i.e.*, roughly 3%). By contrast, over the past three years, the number of notices filed by Japanese investors more than doubled (20 in 2017, 31 in 2018, 46 in 2019). Japanese investment now accounts for more CFIUS filings than any other country.

The decline in filings by Chinese investors since 2017 mirrors the overall decline in Chinese investment in the United States. During this period, the Chinese government discouraged Chinese companies from making certain types of investment — for instance, in areas such as real estate. The passage of FIRRMA also appears to have had a chilling effect on Chinese investment, as the legislation was prompted in part by concerns about China. After FIRRMA, Chinese investors concluded that the “CFIUS risk” of investing in the United States would be higher going forward and in some cases looked for alternative investment opportunities in other jurisdictions. Trade tensions with China also may have contributed to this decline. It bears watching whether this trend continues.