

Fried Frank International Trade and Investment *Alert*TM

CFIUS Announces Pilot Program Requiring Mandatory Filings for Investments in U.S. Critical Technology Companies

On October 11, 2018, the Committee on Foreign Investment in the United States (CFIUS) published an [interim rule](#) beginning a pilot program to implement parts of the wide-ranging [Foreign Investment Risk Review Modernization Act of 2018 \(FIRRMA\)](#). FIRRMA authorized CFIUS to conduct pilot programs to implement any provisions of the legislation that were not immediately effective upon enactment. This pilot program expands CFIUS jurisdiction over certain non-control foreign investment in U.S. critical technology companies in specified sensitive sectors. It also imposes mandatory CFIUS filings for all qualifying investments in such companies – both these new non-control investments as well as control transactions that had previously been under CFIUS jurisdiction. This pilot program will be in effect until March 2020 or until CFIUS issues final regulations implementing these parts of FIRRMA. CFIUS also published an [interim rule](#) to update its existing regulations for FIRRMA requirements that became effective when FIRRMA was signed into law.

Expanded CFIUS Jurisdiction

The pilot program implements FIRRMA's expansion of CFIUS jurisdiction to include non-controlling foreign investments in a U.S. business that designs, fabricates, develops, tests, produces or manufactures "critical technologies" in one of 27 sensitive industries, if the foreign investor has:

- (a) access to material non-public technical information,
- (b) membership or observer rights on the board of directors or equivalent governing body, or the right to nominate an individual to such a body, or
- (c) any involvement, other than through voting of shares, in substantive decision-making of the U.S. business regarding the critical technology.

"Critical technologies" continues to include most items controlled under the ITAR, EAR, and nuclear export controls, as well as "emerging and foundational technologies" that are to be controlled under forthcoming Commerce Department rules. The list of pilot program industries is included in Annex A to the regulations, and includes several defense areas, semiconductors, biotechnology, computers and storage, several areas of critical manufacturing, and certain telecommunications equipment manufacturing. If the U.S. business does not have critical technologies related to one of these 27 sectors, then a foreign investment may not fall under CFIUS jurisdiction under this pilot program.

Note that the pilot program covers all foreign persons. It is neither limited to certain countries of concern, nor does it include a “whitelist” of friendly or allied countries.

As required by FIRRMA, indirect investments by foreign limited partners through a U.S. investment fund are exempt (even if the foreign LP has membership on an advisory committee) if certain criteria are met:

- the fund is exclusively managed by a general partner or managing member (or equivalent) that is not the foreign LP,
- neither the foreign LP Nor the advisory committee has the ability to approve or control investment decisions or decisions by the GP/managing members regarding portfolio companies,
- the foreign LP does not have unilateral ability to select, dismiss, or determine the compensation of the GP/managing member, and
- the foreign LP does not have access to material non-public technical information.

Mandatory Declarations

This pilot program implements the first mandatory CFIUS filings, which applies to both non-control investments described above and control transactions in such U.S. businesses (the latter of which was already under CFIUS jurisdiction). Mandatory filers will not be required to submit the complete joint voluntary notice; instead, filers will be required to submit a short-form declaration (generally a maximum of five pages, with content listed in the notice) for all qualifying transactions at least 45 days before closing.

Required information in the declaration includes:

- (1) Basic information about the transaction: names of entities involved, description of the nature of the transaction and its structure, percentages of voting interest and economic interest acquired, total transaction value in USD, expected closing date, and all sources of financing for the transaction;
- (2) A statement regarding potential foreign government control of the U.S. business;
- (3) A statement as to whether the foreign person is acquiring material nonpublic technical information or certain indicia of control over the U.S. business;
- (4) Information regarding the U.S. business similar to that in a complete CFIUS filing, including basic information and information about export controlled items, and government contracts;
- (5) A description of critical technology in which the U.S. business deals;
- (6) Detailed information about the foreign acquirer similar to that in a complete CFIUS filing; and
- (7) CFIUS history, if any, relating to the parties to the transaction.

In addition to those requirements, parties may stipulate that the transaction is a covered transaction and, if relevant, a foreign government-controlled transaction. If the party does so, it acknowledges that the Committee and the President are entitled to rely on that stipulation and it waives the right to challenge such a determination. Making such stipulation may facilitate CFIUS’s review of the declaration.

The Committee review of a declaration will last 30 days after it is accepted as complete. After reviewing the short-form declaration, CFIUS can either:

- (1) approve the transition,

- (2) request the parties to file a joint voluntary notice,
- (3) unilaterally initiate the regular review period, or
- (4) notify parties that CFIUS cannot complete action and inviting the parties to file a complete joint voluntary notice to get formal resolution.

Additionally, parties have the option of filing the full CFIUS notice instead of the declaration. While the full CFIUS process is significantly longer than 30 days, this may be a useful option if the parties expect the transaction to be closely scrutinized and possibly the subject of a request for a full joint voluntary notice. Whether, and in which circumstances, the declaration process is actually faster than the current CFIUS process will depend on CFIUS practice as it begins to review and resolve declarations.

The regulations specify that if a transaction subject to the mandatory declaration requirement in the pilot program has a closing date between November 10, 2018 and December 25, 2018, parties must submit the declaration on, or promptly after, November 10, 2018.

The penalty for not filing a mandatory declaration is a potential civil penalty of up to the value of the covered transaction.

Extension of Review and Investigation Periods

Apart from the pilot program, CFIUS is amending its regulations to reflect the new time periods set forth in FIRRMA for regular CFIUS procedures. The review period has been extended from 30 to 45 days. The new regulations also grant CFIUS the ability to extend an investigation from 45 days to 60 days in “extraordinary circumstances. The regulations define “extraordinary circumstances” as those in which extension is necessary due to a force majeure event or to protect the national security of the United States. This broad definition allows CFIUS virtually unlimited authority to extend an investigation for any filing in which there are unresolved national security concerns. Again, it remains to be seen how often, and in which circumstances, CFIUS finds extraordinary circumstances. This change brings the potential timeline for a CFIUS notice (without withdrawing and refiling) to a potential 105 days.

Timing

The pilot program takes effect November 10, 2018, but excludes transactions that closed prior to November 11, 2018 or those for which a binding written agreement or other document establishing the material terms was executed prior to October 11, 2018. The program will last until March 5, 2020 or until CFIUS issues final regulations. CFIUS may also issue regulations or pilot programs in the coming months to implement other parts of FIRRMA, including expanded jurisdiction over non-control investments in critical infrastructure companies or those with access to personal data, new real estate transactions, and other mandatory declaration requirements.

Conclusion

CFIUS has begun the process of implementing FIRRMA and availing itself of the expanded authority that FIRRMA granted it. This pilot program includes both an expansion of CFIUS jurisdiction to certain non-controlling foreign investments and the first mandatory CFIUS filings. Any company involved in international mergers and acquisitions, private equity transactions, or private fund formation should become familiar with the new CFIUS pilot program.

If you have any questions regarding FIRRMA or this new pilot program, or how it may affect your business, please reach out to the contacts listed below.

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