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CFIUS Proposes New Rules Scrutinizing Foreign Investment

Focus on US Technology, Infrastructure, and Data

On September 17, 2019, the Committee on Foreign Investment in the United States (“CFIUS”) published two Proposed Rules to implement most of the Foreign Investment Risk Review Modernization Act of 2018 (“FIRRMA”). CFIUS is an interagency committee that reviews foreign investments and makes recommendations regarding whether such transactions should be unwound, blocked, or subject to mitigation due to national security concerns. FIRRMA is the first major expansion to CFIUS’ jurisdiction and powers in a decade.

One Proposed Rule will expand CFIUS’ jurisdiction to certain *non-controlling* foreign investments in US businesses involving critical technology, critical infrastructure, and sensitive personal data (“TID businesses”) (“TID Proposed Rule”). The other Proposed Rule will expand CFIUS’ jurisdiction to certain foreign investments in US real estate when the transaction does not result in foreign control over a US business (“Real Estate Proposed Rule”).

Treasury Secretary Steven Mnuchin stated, “Today’s proposed regulations will provide clarity and certainty to investors regarding CFIUS’ enhanced authorities to address national security risks that arise from certain foreign investments, and continue modernizing the CFIUS process.”

CFIUS is soliciting comments until October 17, 2019, and it must publish the final regulations by February 13, 2020. Although the Proposed Rules are not effective yet, parties should keep them in mind when identifying deal partners, structuring transactions, and determining whether to make CFIUS filings because the Proposed Rules telegraph the types of transactions that CFIUS will consider sensitive from a national security perspective.



CRITICAL TECHNOLOGY, CRITICAL INFRASTRUCTURE, SENSITIVE PERSONAL DATA

CFIUS Voluntary Filing Jurisdiction

The TID Proposed Rule will expand the definition of “covered transactions” to include non-controlling investments in US critical technology, US critical infrastructure, and sensitive personal data (“SPD”) if the transaction affords the foreign investor: access to certain material non-public technical information; membership, observer, or nomination rights on the TID business’ board or similar governing body; or involvement in substantive decision-making beyond voting shares.

Critical Technology

The TID Proposed Rule will update the CFIUS regulations’ definition of “critical technologies” to conform to FIRRMA and the critical technology pilot program. In particular, the definition will be expanded to include “emerging and foundational technologies” controlled pursuant to the Export Control Reform Act of 2018. The Commerce Department is responsible for defining emerging and foundational technologies. To date, it has published an Advanced Notice of Proposed Rulemaking identifying broad proposed categories of emerging technologies (e.g., biotechnology, data analytics, artificial intelligence, additive manufacturing, microprocessors, semiconductors), but the full list of technology to be controlled for export and foreign investment purposes remains forthcoming.

The TID Proposed Rule will authorize CFIUS to review certain non-controlling foreign investment in US critical technology businesses. There are two main differences between the TID Proposed Rule and the critical technology pilot program. First, the TID Proposed Rule only focuses on whether a US business produces, designs, tests, manufactures, fabricates, or develops critical technology; there is no requirement that such activity occur in or primarily for use in one of 27 key US industries previously identified in the critical technology pilot program Interim Rule.¹ Second, the TID Proposed Rule will not require mandatory filings for *non-controlling private* foreign investment in US critical technology outside of the 27 key US industries. (See below for more detail on the new foreign government-related mandatory filing requirement.)

Finally, due to the TID Proposed Rule, CFIUS is considering whether to eliminate the mandatory declaration requirement under the critical technology pilot program Interim Rule. If CFIUS takes this step, foreign government-related investors still could trigger a mandatory filing requirement (see below for more detail), and such a requirement would not be linked to the 27 key US industries.

Critical Infrastructure

The TID Proposed Rule will authorize CFIUS to review certain non-controlling foreign investments in US businesses involved in a sensitive subset of critical infrastructure, defined as “covered investment critical infrastructure.” In particular, CFIUS will assert jurisdiction over such investments in US businesses that own, operate, manufacture, supply, or service (each a critical infrastructure “function”) specific types of critical infrastructure within the following categories, which are listed in greater detail at [TID Proposed Rule Appendix A](#):

- Telecom and information services, fiber optic cable that directly serves a military installation, IP networks with access to other IP networks via settlement-free peering, or internet exchange points supporting public peering;
- Certain submarine cables and co-located data centers or facilities;
- Satellites or satellite systems providing services directly to DOD or a component thereof;
- Certain defense industrial base industrial resources that are not commercial-off-the-shelf;
- US facilities manufacturing certain “specialty metal,” “covered material,” or carbon, alloy, and armor steel plate;



- Certain electric energy systems, or facilities providing electric power to or located near military installations;
- Petroleum and crude facilities above certain barrel-per-day (“bpd”) capacities, certain LNG terminals or storage facilities, or interstate petroleum and LNG pipelines above certain bpd capacities; and
- Systemically-important financial market utilities, securities exchanges, or certain technology service providers;
- DOD Strategic Rail Corridor Network rail lines; certain air and maritime ports and related marine terminals; and
- Public water systems serving a certain population size or military installation.

Importantly, TID Proposed Rule Appendix A Column 1 lists the type of critical infrastructure, and Column 2 lists the relevant function that will trigger CFIUS jurisdiction. In other words, only a non-controlling foreign investment in a US business that performs one of the functions in Column 2 with respect to the corresponding type of critical infrastructure listed in Column 1 will trigger the expanded CFIUS jurisdiction. For example, foreign investment in a US business that *owns or operates* a satellite directly serving DOD will be subject to CFIUS jurisdiction, but foreign investment in a US business that *manufactures, supplies, or services* such a satellite will not be subject to CFIUS jurisdiction.

Sensitive Personal Data

The TID Proposed Rule will authorize CFIUS to review certain non-controlling foreign investments in US businesses that maintain or collect SPD of US citizens that may be exploited in a manner that threatens national security. To determine whether a US business maintains or collects SPD, CFIUS will consider whether the US business: (1) “targets or tailors” products or services to sensitive populations (e.g., military or US government national security personnel); (2) collects or maintains SPD on at least 1 million individuals; or (3) has a demonstrated business objective to maintain or collect SPD on greater than 1 million individuals and the SPD is an integrated part of the US business’ primary products or services.

CFIUS is interested in many types of SPD (e.g., financial, geolocation, communication, health data, genetic information), and the scope is broader than personal identifier information (“PII”). For example, CFIUS will assert jurisdiction over a non-controlling foreign investment in a financial planning app that collects personal financial data and has is tailored to US military or foreign service personnel.

CFIUS Mandatory Filing Jurisdiction

The TID Proposed Rule expands the mandatory filing requirement for certain investments in TID businesses by foreign governments. A mandatory declaration will be required when a foreign person obtains a “substantial interest” in a US business where a foreign government in turn holds a “substantial interest” in the foreign person. Put more simply, if a foreign person’s investment in a TID business gives that foreign person a 25% or greater direct or indirect voting interest in the TID business, *and* a foreign government, in turn, holds a 49% direct or indirect interest in the foreign person making the investment, a mandatory declaration is required. The TID Proposed Rule sets out a formula for calculating such interests in the case of strategic versus limited partner investments.

As transaction structures continue to evolve in complexity, it will be important to determine whether a foreign investment in a TID business triggers this mandatory filing requirement, even if the direct acquisition entity does not appear to have state-owned enterprise, sovereign wealth fund, or other foreign government ownership.

REAL ESTATE TRANSACTIONS

If a foreign investment in US real estate results in foreign control over a US business, such investments remain subject to the traditional CFIUS voluntary filing jurisdiction. FIRRMA also authorized CFIUS to expand its jurisdiction to cover certain purchases or leases by, or concessions to, a foreign person of certain private and public US real estate when the transaction does *not* result in foreign control over a US business. Pursuant to the Real Estate Proposed Rule, CFIUS will



assert jurisdiction over transactions (including investments, acquisitions, bankruptcy, and debt defaults) that confer specific rights² to foreign persons and involve:

- Real estate within, or that will function within or as part of, airports and maritime ports, (i.e., major US passenger and cargo airports by volume, civil-military “joint use airports” designated by the Federal Aviation Administration; or
- Real estate within certain distances of US military installations and other US government property that is sensitive for national security reasons. CFIUS’ jurisdiction to review foreign investments potentially involving such sites will depend on the type of site and the proximity of the real estate involved in the transaction to the site.

CFIUS’ jurisdiction under the Real Estate Proposed Rule is broad and could extend to real estate located up to 99 miles away from military installations listed in Real Estate Proposed Rule Appendix A Part 2, unless a carve-out applies. For example, CFIUS will not exercise jurisdiction over real estate investments in single housing units or certain office space in a multi-unit commercial office building. In addition, CFIUS will not exercise jurisdiction over real estate investments in US Census-designated “urbanized areas” or “urban clusters,” unless the real estate is located within an air or maritime port or within one mile of any military installation identified in Real Estate Proposed Rule Appendix A Part 2.

Unlike the TID Proposed Rule, no foreign investments covered by the Real Estate Proposed Rule are subject to mandatory filing requirements.

CREATION OF “WHITE LIST” FOR CERTAIN COUNTRIES AND INVESTORS

FIRRMMA authorized CFIUS to implement a “country specification” that excepts certain countries, and individual and entity investors from those countries, from CFIUS review when making non-controlling investments in TID businesses and investments in real estate. CFIUS will apply a two-factor conjunctive test to identify excepted states:

- First, CFIUS plans to designate a limited group of eligible states and publish that list on the Treasury website. The Proposed Rules do not indicate the criteria CFIUS plans to use, but the national security factors CFIUS considers when reviewing a transaction may offer some clues: adherence of a country to nonproliferation controls regimes, treaties, and multilateral supply guidelines; a country’s relationship with the United States, specifically counterterrorism cooperation; and the potential for transshipment or diversion of dual-use technology in a country.
- Second, the Treasury Secretary will determine whether an eligible state has “established and is effectively utilizing a robust process to assess foreign investments for national security risk and to facilitate coordination with the United States on matters relating to investment security”. Determinations by the Secretary must be approved by two-thirds of CFIUS member agencies. CFIUS may delay this requirement to give eligible states time to enhance their investment review processes and bilateral cooperation.

Once CFIUS implements the country specification provision and publishes a list of excepted countries, certain nationals of excepted countries and certain entities that are formed and headquartered in excepted countries may be eligible to be “excepted investors.” If such investors meet a set of criteria and comply with certain laws, orders, and regulations, their non-controlling investments in TID businesses or investments in real estate that do not confer foreign control over a US business will not trigger CFIUS jurisdiction.

KEY PROCEDURAL DEVELOPMENTS AND WHAT’S NEXT

The Proposed Rules include a number of procedural and administrative updates, as well as identify future decisions that CFIUS has yet to implement. Several key developments and future decisions include:

- *Voluntary Declarations*: Both Proposed Rules will authorize parties whose transactions are subject to CFIUS jurisdiction but not a mandatory filing requirement to file short-form voluntary declarations instead of requiring full



notices (which parties still may choose to file). CFIUS plans to base such voluntary declarations on the critical technology pilot program mandatory declaration templates, with adjustments for different types of industries.

- **Filing Fees:** FIRRMA authorizes CFIUS to assess filing fees not in excess of the lesser of 1% of the value of the transaction or \$300,000 (inflation-adjusted), with any such fee schedule taking into account the value of the transaction, the effect of the fee on small business concerns, CFIUS costs, and the effect of the fee on foreign investment. CFIUS stated in the TID Proposed Rule that it will publish a filing fee proposed rule at a later date.
- **Comments:** Until October 17, 2019, CFIUS will accept comments from industry and the public on the Proposed Rules as well as the pilot program Interim Rule. Accordingly, interested entities and industry associations should determine whether it would be beneficial to file comments. After the comment period ends, CFIUS will review the comments and begin preparing the final regulations, which must be implemented by February 13, 2020.

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¹ US Dep't of the Treas., Determination and Temporary Provisions Pertaining to a Pilot Program to Review Certain Transactions Involving Foreign Persons and Critical Technologies, 83 Fed. Reg. 51322 (Oct. 11, 2018).

² CFIUS only has jurisdiction over transactions that afford the foreign person at least three of the following property rights: the right to physically access the real estate; the right to exclude others from physical access to the real estate; the right to improve or develop the real estate; and the right to attach fixed or immovable structures or objects to the real estate.