

Treasury Department Issues Interim Rules Creating Pilot Program For Expanded CFIUS Review And Mandatory Filings Effective November 10, 2018

As chair of the Committee on Foreign Investment in the United States (CFIUS), the U.S. Department of the Treasury issued interim regulations that include a “Pilot Program” designed to address national security concerns in accordance with recent legislation.¹ While notifications to CFIUS, the U.S. multi-agency committee that evaluates the implications of foreign investment on national security, used to be voluntary, for some transactions notification to CFIUS will be mandatory starting November 10, 2018, when the Pilot Program becomes effective. The Pilot Program will inform the regulations that CFIUS will eventually promulgate to fully implement FIRRMA.² The Pilot Program will:

1. require “declarations” (shortened filings) or full CFIUS notices for certain “critical technology” transactions; and
2. expand the scope of transactions subject to the jurisdiction of CFIUS to include minority foreign investments in some U.S. businesses that involve “critical technology”.

Companies that do not comply with the Pilot Program may be subject to civil fines up to the value of the transaction.³ Apart from the Pilot Program, transactions that have been subject to CFIUS review remain subject to its jurisdiction, and ordinary course voluntary CFIUS filings may still be advisable.

I. Key Aspects of the Pilot Program

The Pilot Program applies to (A) “covered investments”, (B) made by “foreign persons”, (C) in “U.S. businesses”, (D) engaged in “covered industries”, and (E) which involve “critical technologies.” Proposed transactions that meet all of these criteria are covered under the Pilot Program and require submission of mandatory declarations. The criteria are further defined below.

- A. Covered Investments:** The Pilot Program expands the scope of CFIUS’s jurisdiction to permit the review of investments by foreign persons that do not constitute an acquisition of control of a U.S. business but meet additional criteria.⁴ Thus, in addition to acquisitions of control, mandatory filing requirements may be triggered when a foreign person obtains a non-controlling interest in a covered U.S. business that is accompanied by any of the following rights:

¹ 31 C.F.R. § 801 (2018). Congress recently passed legislation expanding the jurisdiction and powers of CFIUS. The new law, the Foreign Investment Risk Review Modernization Act or FIRRMA, described in greater detail in our [August 15, 2018 Memorandum](#), significantly reforms the CFIUS review process. John S. McCain National Defense Authorization Act of 2019, H.R. 5515, 115th Cong. (2018) (adopted as H.R. Rep. No. 115-847 at 540-608 (2018)) (NDAA). The law authorized CFIUS to implement provisions that did not become effective immediately upon enactment through the use of a pilot program. U.S. Department of Treasury, Fact Sheet: Interim Regulations for FIRRMA Pilot Program (Oct. 10, 2018) <https://home.treasury.gov/system/files/206/Fact-Sheet-FIRRMA-Pilot-Program.pdf> (last visited Nov 5, 2018) (“Fact Sheet”).

² Fact Sheet. CFIUS may implement additional pilot programs until FIRRMA becomes fully implemented. The implementing regulations also make some changes to current CFIUS regulations to conform to FIRRMA. 31 C.F.R. § 800 (2018). The Pilot Program will end no later than March 5, 2020. 31 C.F.R. § 801.401(2018).

³ 31 C.F.R. § 801.409 (2018).

⁴ See 31 C.F.R. § 801.206 (2018).

- “Access to any material nonpublic technical information in the possession of the . . . U.S. business;
- Membership or observer rights on the board of directors or equivalent governing body of the U.S. business, or the right to nominate an individual to a position on the board of directors or equivalent governing body of the U.S. business; or
- Any involvement, other than through voting of shares, in substantive decision making of the U.S. business regarding the use, development, acquisition or release of critical technology.”⁵

Importantly, the Pilot Program does not cover indirect, passive investments in an investment fund by a foreign person – such as a limited partner – as long as the foreign person is not the general partner (or an equivalent), the general partner exclusively manages the fund, and the foreign limited partner has no ability to control the investment fund or general partner.⁶

B. Foreign Persons: The Pilot Program covers all foreign nationals, entities or governments, including countries that are allies of the U.S.⁷

C. U.S. Businesses: The Pilot Program covers any U.S. business that produces, designs, tests, manufactures, fabricates, or develops a “critical technology” that is: (1) utilized in connection with the U.S. business’s activity in one or more Pilot Program Industries; or (2) designed by the U.S. business specifically for use in one or more Pilot Program Industries.⁸

D. Covered Industries: The Pilot Program identifies 27 industries (“Pilot Program Industries”).⁹ The list was developed to include industries for which certain strategically motivated foreign investments could pose a threat to U.S. technological superiority and national security.

⁵ *Id.*

⁶ Control in this context includes the ability to (i) approve, disapprove, or otherwise control investment decisions of the investment fund, (ii) approve, disapprove, or otherwise control decisions made by the general partner related to the investment fund and the entities in which it is invested, or (iii) unilaterally dismiss, prevent the dismissal of, select, or determine the compensation of the general partner. 31 C.F.R. § 801.304 (2018).

⁷ Fact Sheet. A foreign person is any “foreign national, foreign government, or foreign entity” and “any entity over which control is exercised or exercisable by a foreign national, foreign government, or foreign entity.” 31 C.F.R. § 800.216 (2018).

⁸ 31 C.F.R. § 801.213 (2018).

⁹ Aircraft Manufacturing; Aircraft Engine and Engine Parts Manufacturing; Alumina Refining and Primary Aluminum Production; Ball and Roller Bearing; Computer Storage Device Manufacturing; Electronic Computer Manufacturing; Guided Missile and Space Vehicle Manufacturing; Guided Missile and Space Vehicle Propulsion Unit and Propulsion Unit Parts Manufacturing; Military Armored Vehicle, Tank, and Tank Component Manufacturing; Nuclear Electric Power Generation; Optical Instrument and Lens Manufacturing; Other Basic Inorganic Chemical Manufacturing; Other Guided Missile and Space Vehicle Parts and Auxiliary Equipment Manufacturing; Petrochemical Manufacturing Powder Metallurgy Part Manufacturing; Power, Distribution, and Specialty Transformer Manufacturing; Primary Battery Manufacturing; Radio and Television Broadcasting and Wireless Communications Equipment Manufacturing; Research and Development in Nanotechnology; Research and Development in Biotechnology (except Nano biotechnology); Secondary Smelting and Alloying of Aluminum; Search, Detection, Navigation, Guidance, Aeronautical, and Nautical System and Instrument Manufacturing; Semiconductor and Related Device Manufacturing; Semiconductor Machinery Manufacturing; Storage Battery Manufacturing; Telephone Apparatus Manufacturing; Turbine and Turbine Generator Set

E. Critical Technologies: U.S. Businesses covered by the Pilot Program must be involved (as defined above) in critical technologies, as defined by FIRRMA,¹⁰ which include the following:

- Defense articles or defense services included on the United States Munitions List set forth in the International Traffic in Arms Regulations (ITAR);
- Items included on the Commerce Control List set forth in [Supplement No. 1 to part 774](#) of the Export Administration Regulations (EAR) (15 CFR parts 730-774) and controlled:
 - Pursuant to multilateral regimes, including for reasons relating to national security, chemical and biological weapons proliferation, nuclear nonproliferation, or missile technology; or
 - For reasons relating to regional stability or surreptitious listening;
- Specially designed and prepared nuclear equipment, parts and components, materials, software, and technology covered by [10 CFR part 810](#) (relating to assistance to foreign atomic energy activities);
- Nuclear facilities, equipment, and material covered by [10 CFR part 110](#) (relating to export and import of nuclear equipment and material);
- Select agents and toxins covered by [7 CFR part 331](#), [9 CFR part 121](#), or [42 CFR part 73](#) or;
- Emerging and foundational technologies controlled pursuant to section 1758 of the Export Control Reform Act of 2018.¹¹

II. The Pilot Program's Mandatory Declarations Process

All transactions subject to the Pilot Program must submit an abbreviated declaration, including basic information about the parties and the transactions, at least 45 days before the transaction closes.¹²

A. The Declaration's Content: The abbreviated declaration¹³ must include information regarding the investor and its owners, the Pilot Program U.S. business, and the transaction itself, similar to what would be required in a full CFIUS notice. A substantial amount of information required in a full notice is not required in a declaration, such as personal identifier information for officers and directors of the investor and its owners. Other information requirements, however, are specific to a declaration.¹⁴

Units Manufacturing. 31 C.F.R. § 801 Annex A to Part 801—Industries (2018).

¹⁰ 31 C.F.R. § 801.204 (2018).

¹¹ NDAA § 1758 (This last category—emerging and foundational technologies—has yet to be defined and is subject to forthcoming guidance from the Commerce Department, which is expected soon.).

¹² NDAA § 1706.

¹³ Fact Sheet.

¹⁴ The required information also includes: All sources of financing for the transaction; Whether the Pilot Program U.S. business has multiple classes of ownership; A statement and explanation about the rights that the foreign person will acquire with respect to the Pilot Program US business; Whether the Pilot Program US business has had any U.S. Government contracts (including subcontracts) within the past three years, or within the past ten years if the contract included access to personally identifiable information of U.S. Government personnel; Whether the Pilot Program U.S. business has received any grants or funding from the Department of Defense or Energy, or has collaborated on any defense or energy program or product involving any critical technologies or Pilot Program industries within the past five

- B. *Timing:*** Parties subject to mandatory declaration requirement must file their declarations at least 45 days prior to a transaction’s expected completion date. For Pilot Program covered transactions that will close between November 10, 2018, and December 25, 2018, a mandatory declaration must be submitted by November 10, 2018, “or promptly thereafter.”¹⁵ The Committee will have 30 days to take action.¹⁶ Alternatively, parties may choose to file a full notice under CFIUS’s standard procedures rather than a declaration.
- C. *Penalties:*** The interim rule provides that any person who fails to comply with the mandatory declarations requirements under the Pilot Program may be liable for a civil penalty up to the value of the transaction.¹⁷
- D. *Effectiveness:*** The Pilot Program takes effect on November 10, 2018. It does not apply (a) to transactions that have closed prior to November 10, 2018, or (b) where prior to October 11, 2018, (i) the parties executed a binding written agreement or other document establishing the terms of the transaction, (ii) a party made a public offer to shareholders to buy shares of a Pilot Program U.S. business, or (iii) a shareholder solicited proxies in connection with the election of the board of directors of a Pilot Program U.S. business or has requested the conversion of convertible voting securities. The Pilot Program will end no later than March 5, 2020,¹⁸ when it is possible that some of the program’s requirements will become permanent under new regulations.
- E. *Committee Response to Declaration:*** The Committee may take one of four actions with respect to a declaration: (1) request that the parties file a full notice; (2) inform the parties that CFIUS cannot reach a decision on the basis of the declaration, and that they may file a full notice to seek written notification from the Committee that the Committee has completed all action with respect to the transaction; (3) initiate a unilateral review of the transaction through an agency notice; or (4) notify the parties that CFIUS has completed all action.¹⁹

years; Whether the Pilot Program U.S. business has participated in a Defense Production Act Title III Program within the past seven years; and Whether the Pilot Program U.S. business, the foreign investor, or any parent or subsidiary of the foreign investor has been convicted in the last ten years of a crime in any jurisdiction. 31 C.F.R. § 801.403 (2018).

¹⁵ 31 C.F.R. § 801.401(c)(1) (2018).

¹⁶ 31 C.F.R. § 801.404 (2018) However, the interim rule states that the 30-day period starts after the CFIUS Staff Chairperson has transmitted the declaration to the Committee—a process that happens after the Staff Chairperson has inspected the declaration for completeness and accepted it. The interim rule states that the Staff Chairperson shall “promptly” inspect the declaration and notify the parties of acceptance or return the declaration with specific guidance on what is necessary to complete it. Given that it typically takes at least a week and often longer for CFIUS to accept a formally filed joint voluntary notice, and that CFIUS remains understaffed—especially in relation to the likely increase in submissions due to implementation of the Pilot Program—the declaration process may take substantially longer than 30 days.

¹⁷ 31 C.F.R. § 801.409 (2018).

¹⁸ 31 C.F.R. § 801.401(2018).

¹⁹ 31 C.F.R. § 801.407 (2018).

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F. Full Notice: Parties have the option to submit a full notice in lieu of a declaration. The declaration process is only available for Pilot Program covered transactions; declarations may not be submitted for transactions that are not subject to the Pilot Program.²⁰

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Helene R. Banks at 212.701.3439 or hbanks@cahill.com; Bradley J. Bondi at 202.862.8910 or bbondi@cahill.com; Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Geoffrey E. Liebmann at 212.701.3313 or gliebmann@cahill.com; Elai Katz at 212.701.3039 or ekatz@cahill.com; Kimberly Petillo-Décossard at 212.701.3265 or kpetillo-decossard@cahill.com; Lauren Rackow at 212.701.3725 or lrackow@cahill.com; or Ethan Kaminsky at 212.701.3594 or ekaminsky@cahill.com.

²⁰ 31 C.F.R. § 801.401(b) (2018).