

## MEMORANDUM

April 09, 2019

RE: Impact of the Foreign Investment Risk Review Modernization Act (“FIRRMA”) and CFIUS Pilot Program

### *Summary*

On August 13, 2018, President Trump signed into law the Foreign Investment Risk Review Modernization Act of 2018 (“FIRRMA”) to better protect U.S. national security interests in a changed risk landscape—specifically, foreign transactions involving U.S. businesses engaged or with access to “critical technologies” and “critical infrastructure.” FIRRMA serves to amend and broaden provisions already in effect under the Committee on Foreign Investment in the United States (“CFIUS”), which was established in 1988.

To determine whether a U.S. business has CFIUS written notice or mandatory declaration requirements pursuant to changes under FIRRMA, an analysis must now include activities beyond traditional acquisition of a controlling interest of a U.S. business by a non-U.S. investor. These include activities where the U.S. business has a nexus to critical technologies or critical infrastructure and where the potential exists for transfer of such technology, information, or data as a result of the activity proposed between the U.S. and non-U.S. businesses (regardless of controlling ownership). For example, joint ventures, alliance, collaborations, changes in structures or organization, or other activities that may provide access to a non-U.S. investor a U.S. business’ sensitive information, data, or technology the U.S. business possesses; or enable the non-U.S. investor to purchase, lease, or by concession, be in “close proximity” of real estate sensitive to U.S. government security interests; or within or function as a part of an air or maritime port, are now covered. It is also important to note that under FIRRMA, approval of outbound transfers (i.e., exports) remain under the jurisdiction of the Department of Commerce, including deemed export transfers, which involve the transfer of controlled technology subject to U.S. export licensing requirements to a non-U.S. person in the U.S.

During the updated review process, CFIUS may take into consideration such factors as the non-U.S. investor’s compliance history and the aggregate impact of the investments made by such investor, as well as a host of additional factors that may impact national security. CFIUS requested conditions and mitigation – including compliance processes – may also be more rigorously applied and monitored under the new regulations, which allow for greater penalties.

In addition, FIRRMA provided CFIUS with the authority to launch pilot programs that implement it’s expanded authority. On November 10, 2018, a Critical Technology Pilot Program (“FIRRMA Pilot Program”) went into effect, to end on or before March 5, 2020. The U.S. concern that certain industries and technologies need to be prioritized for security reasons prompted the

FIRRMA Pilot Program launch, and provides an opportunity for CFIUS to observe whether the streamlined review process operates as intended.

Corporate policies and procedures should be analyzed, and as appropriate, revised to ensure operational compliance with the expanded notice and declaration requirements and new timelines. FIRRMA developments should continue to be monitored as CFIUS moves to implement more of the FIRRMA provisions, and greater penalties may be applied by CFIUS under FIRRMA.

## **FIRRMA**

In addition to the existing CFIUS requirements that remain in effect, FIRRMA updates the process and expands the scope of CFIUS review where a non-U.S. investor (“Foreign Investor”) will make a non-controlling investment in certain U.S. businesses (previously a controlling interest generally triggered review).

U.S. businesses impacted specifically under FIRRMA are those that: (a) own, operate, manufacture, supply, or service “critical infrastructure”; or (b) produce, design, test, manufacture, fabricate, or develop one or more “critical technologies”; or (c) maintain or collect sensitive personal data of U.S. citizens that may be exploited in a manner that threatens national security.

The focal issues are whether the Foreign Investor may:

1. Access material, non-public technical or sensitive information in the U.S. business’ possession; obtain membership on the board of directions; or other decision-making rights other than through the voting of shares;
2. Purchase or lease real estate (including concessions), regardless of whether it is developed or undeveloped, in “close proximity” to a sensitive government property, including military installations, or is within or will function as a part of a U.S. air or maritime port;
  - ◆ “close proximity” is to be defined by CFIUS regulations (versus relying on CFIUS past practice or analysis method)
3. Change their rights resulting in non-U.S. control of the U.S. business or “other investment” in the U.S. business; or
4. Engage in any transaction or other type of transfer, agreement or arrangement designed to circumvent CFIUS jurisdiction.

In addition, FIRRMA expands and clarifies CFIUS to:

1. Change the review period to 45 days (previously 30), with the possibility of a 15-day, one-time extension in “extraordinary circumstances”;

2. Provide for a civil penalty of up to the value of the transaction for failing to submit a mandatory declaration or a material misstatement or omission, or a violation of a CFIUS imposed condition;
3. Impose a CFIUS review fee capped at the *lesser* of \$300,000 or 1% of the value of the transaction (previously, no fee);
4. Cover U.S. inbound technology transfers (outbound U.S. technology transfers are covered under the U.S. export control rules);
5. Conduct one or more pilot programs to implement FIRRMA provisions, which can include mandatory filing requirements (previously, largely voluntary);
6. Establish an abbreviated filing process through “declarations” that may result in shorter review timelines; and
7. Use mitigation agreements more, including compliance plans.

### ***FIRRMA Critical Technology Pilot Program***

U.S. businesses impacted by FIRRMA Pilot Program requirements are those that produce, design, test, manufacture, fabricate, or develop a “critical technology”: (a) used in connection with the U.S. business’ activity in one or more industries covered by the FIRRMA Pilot Program; or (b) designed by the U.S. business specifically for use in one or more of the specified industries covered by the FIRRMA Pilot Program.

Mandatory declarations are required under the FIRRMA Pilot Program where a Foreign Investor may gain:

1. access to any material non-public technical information that involves the sensitive personal data of U.S. citizens, “critical technologies”, or “critical infrastructure” in the possession of a “pilot program U.S. business”;
2. 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 such a position of a “pilot program U.S. business”;
3. any involvement in “substantive decision-making”<sup>1</sup> of a “pilot program U.S. business” regarding the use, development, acquisition, or release of “critical technology” (e.g.: licensing; pricing, sales, and specific contracts; supply arrangements; corporate strategy and business development; research and product development, including budget allocation; manufacturing locations; access to “critical technology”; storage or protection of “critical technology”; appointment or removal of personnel or management with operational oversight; or strategic partnerships) .

Under the FIRRMA Pilot Program, a “pilot program U.S. business” is a U.S. business that produces, designs, tests, manufactures, fabricates or develops a “critical technology” used in

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<sup>1</sup> Does not include strictly administrative decisions (see 31 CFR 801.209(c)); however, final decision-making authority is not a necessary precondition to be included.

connection with one or more of the 27 industries specifically identified by NAICS code in the FIRMMA Pilot Program regulations.<sup>2</sup>

There is no *de minimis* level of investment and no voting interest is required to trigger the mandatory declaration requirement.<sup>3</sup> Investment fund investments, where the non-U.S. person merely purchases shares in a U.S. investment fund and takes no active involvement in the fund management or decision-making, and otherwise has no control over the fund or access to non-public or sensitive technical information or data, are not covered.<sup>4</sup>

### ***What rises to the level of CFIUS review and FIRRMA Pilot Program submission requirements***

To recap, in addition to existing CFIUS notice requirements, FIRRMA now includes Foreign Investor activities with U.S. businesses that have a nexus to “critical technologies” and “critical infrastructure” that may, directly or indirectly, provide the Foreign Investor with the following:

1. Access to material, non-public technical or sensitive information in the U.S. business’ possession, membership on the board of directions; or other decision-making rights other than through the voting of shares;
2. Developed or undeveloped real estate (whether through purchase, lease or concession) in “close proximity” (not yet defined by regulation) to a sensitive government property, including a military installation, or is within or will function as a part of a U.S. air or maritime port;
3. Change their rights resulting in non-U.S. control of the U.S. business or “other investment” in the U.S. business; or
4. Engage in any transaction or other type of transfer, agreement or arrangement designed to circumvent CFIUS jurisdiction is also covered.

U.S. businesses must first have a clear understanding of whether they may possess or have access to “critical technologies” or “critical infrastructure”; or have real estate, leases, or concessions that may enable access to areas “closely proximate” to sensitive U.S. government locations; or access to sensitive personal information or data, regardless as to the mode of the activity—whether a merger, acquisition, joint venture, strategic alliance, or other form of collaboration or transfer. The U.S. business must then determine whether the proposed activity is a covered activity under FIRRMA or the FIRRMA Pilot Program, as some exceptions do exist. Lastly, the U.S. business should determine whether the proposed activity with the Foreign Investor will directly or indirectly provide access or some form of control, whether through possession, decision-making influence or otherwise, by the Foreign Investor.

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<sup>2</sup> See 31 CFR Annex A to, reproduced on Attachment A

<sup>3</sup> The mandatory short-form declaration is five (5) pages long. A template is available at: [https://home.treasury.gov/system/files/206/Declaration-Submission-Form-for-Critical-Technology-Pilot-Program\\_0.pdf](https://home.treasury.gov/system/files/206/Declaration-Submission-Form-for-Critical-Technology-Pilot-Program_0.pdf)

<sup>4</sup> See 31 CFR 801.304.

Under the FIRRMA Pilot Program, the first step is to determine whether a nexus exists with any of the specified industries and if the activities involved may implicate any of activities of concern specified, namely, (i) access to material non-public technical information in the possession of the “pilot program U.S. business”; (ii) membership or observer rights on the board of directors or equivalent governing body of the “pilot program U.S. business” or the right to nominate an individual to a position on the board of directors or equivalent governing body of the “pilot program U.S. business”; or (iii) any involvement, other than through voting of shares, in “substantive decision-making” in the “pilot program U.S. business” regarding the use, development, acquisition, or release of “critical technology”.

A complication in conducting the analysis is that not all of the definitions of terms provided for in FIRRMA or the FIRRMA Pilot Program regulations have been promulgated. For example, “Critical technologies” are not fully defined in the regulations. The stated definition includes U.S. Munitions List (“USML”) articles or services, Commerce Control List (“CCL”) items beyond items controlled for Anti-terrorism (“AT”) reasons, nuclear facilities, equipment, and material under 10 CFR 110; select agents and toxins; “emerging technologies” and “foundational technologies” under the Export Control regulations. However, the latter two terms, “emerging technologies” and “foundational technologies” are under or will be under review using the federal rulemaking process by the Department of Commerce and therefore subject to expansion.<sup>5</sup>

“Critical infrastructure” is defined as systems and assets, whether physical or otherwise, are deemed vital to U.S. interests. Again, this definition may be subject to additional clarification in future.

Currently, the FIRRMA Pilot Program’s new, short form declaration process is open only for transactions that fall within the scope of mandatory declaration requirements. Nonetheless, parties have the option of filing a full CFIUS written notice instead of a declaration if they deem the activity warrants greater detail be submitted for consideration. CFIUS also retains the right to respond to a declaration submission by requesting the parties submit a full CFIUS written notice. Mandatory declaration requirements cover:

## Conclusion

Parties to a proposed activity involving any kind of investment by a non-U.S. business, broadly defined now with FIRRMA, should consider whether a CFIUS written notice is warranted, as well as whether the proposed activity may be subject to FIRRMA Pilot Program mandatory

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<sup>5</sup> A Federal Register advance notice of proposed rulemaking seeking comments on an “emerging technologies” definition was published on November 19, 2018 and closed on January 10, 2019 (*see*: 83 Fed. Reg. 58201 (Nov. 19, 2018) and 83 Fed. Reg. 64299 (Dec. 14, 2018)). Examples of “emerging technology”, which are only illustrative and not determinative of whether such technology is covered include robotics, data analytics, technology, additive manufacturing (e.g., 3D printing), biotechnology, etc. It is anticipated that a Federal Register notice seeking comments on how to define “foundational technologies” will be issued by the Department of Commerce Bureau of Industry and Security (“BIS”) sometime later this year.

declaration requirements, and if the latter, whether to file a mandatory declaration or written notice.

Timing considerations should also be taken into account. If there is a possibility that a full CFIUS written notice is required, either under FIRRMA, the FIRRMA Pilot Project mandatory declaration requirements, or as a result of a CFIUS request in response to a mandatory declaration, the timeline should be in line with a full CFIUS written notice plus the minimum 45 days. In addition, if mitigation or other conditions are called for as a result of the CFIUS process, delays to the proposed activity may ensue to meet those requirements and additional time should be factored into the timeline.

## ATTACHMENT A: Annex A to 31 CFR 801

Aircraft Manufacturing <i>NAICS Code: 336411</i>	<i>NAICS Code: 334413</i>
Aircraft Engine and Engine Parts Manufacturing <i>NAICS Code: 336412</i>	Semiconductor Machinery Manufacturing <i>NAICS Code: 333242</i>
Alumina Refining and Primary Aluminum Production <i>NAICS Code: 331313</i>	Storage Battery Manufacturing <i>NAICS Code: 335911</i>
Ball and Roller Bearing Manufacturing <i>NAICS Code: 332991</i>	Telephone Apparatus Manufacturing <i>NAICS Code: 334210</i>
Computer Storage Device Manufacturing <i>NAICS Code: 334112</i>	Turbine and Turbine Generator Set Units Manufacturing <i>NAICS Code: 333611</i>
Electronic Computer Manufacturing <i>NAICS Code: 334111</i>	
Guided Missile and Space Vehicle Manufacturing <i>NAICS Code: 336414</i>	
Guided Missile and Space Vehicle Propulsion Unit and Propulsion Unit Parts Manufacturing <i>NAICS Code: 336415</i>	
Military Armored Vehicle, Tank, and Tank Component Manufacturing <i>NAICS Code: 336992</i>	
Nuclear Electric Power Generation <i>NAICS Code: 221113</i>	
Optical Instrument and Lens Manufacturing <i>NAICS Code: 333314</i>	
Other Basic Inorganic Chemical Manufacturing <i>NAICS Code: 325180</i>	
Other Guided Missile and Space Vehicle Parts and Auxiliary Equipment Manufacturing <i>NAICS Code: 336419</i>	
Petrochemical Manufacturing <i>NAICS Code: 325110</i>	
Powder Metallurgy Part Manufacturing <i>NAICS Code: 332117</i>	
Power, Distribution, and Specialty Transformer Manufacturing <i>NAICS Code: 335311</i>	
Primary Battery Manufacturing <i>NAICS Code: 335912</i>	
Radio and Television Broadcasting and Wireless Communications Equipment Manufacturing <i>NAICS Code: 334220</i>	
Research and Development in Nanotechnology <i>NAICS Code: 541713</i>	
Research and Development in Biotechnology (except Nanobiotechnology) <i>NAICS Code: 541714</i>	
Secondary Smelting and Alloying of Aluminum <i>NAICS Code: 331314</i>	
Search, Detection, Navigation, Guidance, Aeronautical, and Nautical System and Instrument Manufacturing <i>NAICS Code: 334511</i>	
Semiconductor and Related Device Manufacturing	