

Treasury Proposes Revisions to CFIUS Rules for Mandatory Filings

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On May 21, 2020, the U.S. Department of the Treasury (Treasury) published a proposed rule that would make two significant changes to the Committee on Foreign Investment in the United States (CFIUS) regulations at 31 C.F.R. Part 800. First, the proposed rule would modify the mandatory filing provision for critical technology transactions by using export control requirements as the trigger for a mandatory notification. Second, the proposed rule would change the language of 31 C.F.R. § 800.244 to clarify the definition of “Substantial Interest.” Written comments on the proposed rule are due June 22, 2020.

Treasury issued this proposed rule pursuant to its authority under the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA). Under FIRRMA and the Defense Production Act of 1950, CFIUS has jurisdiction to review any transaction which could result in foreign control of any U.S. business and certain non-controlling investments and real estate transactions that give rise to national security concerns, including certain foreign investments in certain U.S. critical technology businesses.

Nixing the NAICS Nexus

The CFIUS regulations that established mandatory filing requirements took effect in November 2018. Since then, covered transactions involving U.S. businesses that produce, design, test, manufacture, fabricate, or develop a critical technology trigger a mandatory notification where the technology is designed for use in one or more critical technology industries. The specific industries are currently identified by reference to the North American Industry Classification System (NAICS).

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Practice Areas

Committee on Foreign Investment in the
United States (CFIUS)
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Treasury's proposed rule would remove the requirement that the critical technologies have a nexus to a specific NAICS code and replace it with a requirement that the critical technologies have a nexus to one of the four main U.S. export control regimes—those administered by the Departments of Commerce, Energy, State, and the Nuclear Regulatory Commission. Under the proposed regulations, a transaction would trigger a mandatory declaration if the U.S. business would be required to obtain U.S. government authorization or license to export, re-export, transfer (in country), or retransfer the critical technology to the foreign investor.

In other words, if the U.S. business would need government authorization to export the critical technology to the controlling foreign person(s) involved in the transaction—or certain controlling foreign persons in the ownership chain—then a declaration with CFIUS is mandatory for the foreign person in order to invest in the U.S. business. Treasury explains that this change “leverages the national security foundations of the export control regimes, which require licensing or authorization in certain cases based on an analysis of the particular item and end user, and the particular foreign country.”

The proposed rule also includes language that explains how to analyze filing requirements in the context of the export control regimes. For example, notification to CFIUS would be mandatory even if a license exemption may be available under the State Department's International Traffic in Arms Regulations.

Defining “Substantial Interest”

FIRRMA also requires notifications for certain covered transactions in which a foreign government has a “substantial interest” in a foreign person that will acquire a substantial interest in certain types of U.S. businesses. The proposed rule clarifies the definition of “Substantial Interest” at 31 C.F.R. 800.244(b) and (c). This provision explains how to determine the percentage of interest an entity indirectly holds in another entity. The proposed rule clarifies that paragraph 800.244(b) “applies only where a general partner, managing member, or equivalent primarily directs, controls, or coordinates the activities of the entity.”

Wiley has an unparalleled ability to assist clients on investments that raise national security concerns. Our team has direct experience within government managing the CFIUS process and here at Wiley assisting clients on CFIUS reviews. We have more than two decades of experience handling matters involving national security, including CFIUS, export controls, Team Telecom, and the Defense Counterintelligence and Security Agency (DCSA), and have counseled clients in transactions that involve nearly every industry sector subject to CFIUS review. Please reach out to any of the attorneys listed on this alert should you have any questions about the new regulations implementing FIRRMA.