

On September 17, 2019, the US Department of the Treasury issued proposed regulations to implement the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA), the statute expanding the authorities of the Committee on Foreign Investment in the United States (CFIUS). These regulations define the paradigm shift that we have anticipated since late last year (see, generally, [our article](#) summarizing FIRRMA). Since the passage of the Exon-Florio Amendment in 1988, CFIUS has extended its authority over acquisitions of control through an ever-expanding understanding of national security interests. FIRRMA shifts from that “control-based” test to now include sensitive business-based tests. While CFIUS continues to have the authority to review any transaction resulting in foreign person control of a US business, CFIUS will have the authority to review any non-controlling investment by a foreign person in certain sensitive US businesses, and in two cases, CFIUS review is or will be mandatory. FIRRMA also extends CFIUS’s authority to real estate interests (even if not a US business) in proximity to national security interests.

The following is a guide to CFIUS’ authority, and voluntary versus mandatory filing.

	CFIUS Review Authority	Implementation	Filing
<b>Control-based Test</b>	Transaction resulting in foreign person control (or a change in foreign person control) of a US business	Historic CFIUS authority Continues under FIRRMA	Voluntary
<b>Sensitive Industry-based Test</b>	Transaction at any level or form of equity interest, including a non-controlling interest, that affords a foreign person access, rights or involvement in US businesses involved in: <ul style="list-style-type: none"> <li>• Critical technologies</li> <li>• Critical infrastructure</li> <li>• Sensitive personal data</li> </ul>	Effective November 10, 2018: Critical technology and Pilot Program industry	Mandatory
		Proposed rule: Sensitive industry and substantial foreign government interest	Mandatory
		Proposed rule: All other non-controlling foreign interest in a sensitive industry	Voluntary
<b>Real Estate Proximity Test</b>	Transaction granting property interest to a foreign person within a specified distance to a sensitive national security installation	Proposed rule	Voluntary



## Sensitive Industry-based Test: CFIUS Review of Non-controlling Investments

FIRRMA expands CFIUS's authority beyond acquisitions of control to include authority over non-controlling investments ("covered investments") that afford a foreign person certain access, rights or involvement in US businesses involved in certain critical technologies, critical infrastructure or sensitive personal data (referred to as "TID US businesses," an abbreviation for **t**echnology, **i**nfrastructure and **d**ata). How these concepts are defined for the purpose of covered investments determines the scope of CFIUS's authority over these non-controlling investments. Critical technology retains the same definition it has in the Pilot Program, but new concepts were created in relation to critical infrastructure and sensitive personal data.

- **Critical technology** – Under the proposed rule, covered investments include investments in a US business that "produces, designs, tests, manufactures, fabricates, or develops" any critical technology. The regulations use FIRRMA's definition of critical technologies, which include defense articles or defense services under the International Traffic in Arms Regulations (ITAR), certain nuclear-related products regulated by the Nuclear Regulatory Commission Controls, and certain technologies on the Commerce Control List (CCL) under the Export Administration Regulations (EAR). The EAR-covered technologies include export control classification numbers (ECCNs) on the CCL that are controlled for any of the following reasons: national security, chemical and biological weapons proliferation, nuclear nonproliferation, missile technology, regional stability and surreptitious listening, as well as certain agents and toxins, and if controlled pursuant to multilateral regimes. Critical technologies will also include all emerging and foundational technologies, which are currently being defined pending rule-making authorized by the Export Control Reform Act of 2018.
- **Covered investment critical infrastructure** – Under the proposed rule, covered investments include investments in US businesses that engage in certain "functions" (i.e., owns, operates, manufactures, supplies or services) related to a covered investment critical infrastructure. The covered investment critical infrastructure list includes traditional infrastructure items (e.g., communications networks, utilities, oil and gas, power plants), but also materials (e.g., samarium-cobalt magnets; neodymium-iron-boron magnets; tungsten metal powder or heavy alloy), specialty metals (e.g., certain alloys of steel; nickel, iron-nickel and cobalt; titanium; zirconium) and certain items in the defense supply chain, or made with defense funding. The full list is located in the regulations, but for convenience, we will produce an annotated form. [Subscribe](#) to our *Trade Practitioner* blog to be notified when the annotated version is available. Companies with operations that would implicate these industries should assess whether any non-US ownership changes or future investment could trigger CFIUS review.
- **Sensitive personal data** – Under the proposed rule, covered investments include any US business that "maintains or collects sensitive personal data of US citizens that may be exploited in a manner that threatens national security." The proposed rule defines two types of US businesses with sensitive personal data: (1) any US business that has "genetic information" (e.g., results of genetic tests, knowledge of the manifestation of a disease or disorder in family members of such individual, or involvement with genetic services); or (2) any US business that has 10 enumerated categories of personal data (e.g., financial information, healthcare information, confidential communications and geolocation data) and the US business either (a) targets or tailors business to US government personnel; or (b) maintains or collects, or has the objective to maintain or collect, such data on more than 1 million individuals as part of the business' primary products or services.

The proposed rule requires a mandatory declaration filing for acquisitions by foreign person investors of a "substantial interest" in a TID US business where a foreign government holds, directly or indirectly, a substantial interest in the foreign person investor. (Note: FIRRMA also authorized CFIUS to create mandatory declaration filing requirements for covered transactions involving US businesses involved in critical technologies, which CFIUS put into effect via a Pilot Program in November 2018 – see [our previous publication](#) on the Pilot Program.) Whether a company's investments will trigger a mandatory CFIUS declaration filing depends on the definition of a substantial interest. The proposed rule defines what qualifies as a substantial interest in a TID US business, and another definition for what qualifies as a substantial interest held, directly or indirectly, in the foreign person investor.

- **Substantial interest investment in a TID US business** – For the purposes of determining whether an investment qualifies as an acquisition of a substantial interest in a TID US business, the proposed rule defines substantial interest as a voting interest, direct or indirect, of 25% or more.
- **Substantial interest held by a foreign government in a foreign person investor** – For the purposes of determining whether a foreign person qualifies as having a substantial interest held, directly or indirectly, by a foreign government, the proposed rule defines substantial interest as a voting interest, direct or indirect, of 49% or more. In the case of limited partnerships, a foreign government will be considered to have a substantial interest if it holds 49% or more of the voting interest in the general partner, or 49% or more of the voting interest of the limited partners.

## Real Estate Proximity Test: CFIUS Review of Real Estate Transactions

The proposed rule implements the new CFIUS authority over certain real estate transactions (“covered real estate transactions”), which involve the purchase or lease by, or concession to, a foreign person of certain real estate in “close proximity” to sensitive US locations, in or within an air or maritime port, or as regulated by CFIUS. The proposed rule contains the following concepts that will impact which investments will now fall under this CFIUS authority over real estate.

**Property rights** – To be a covered real estate transaction, the foreign person must acquire, through the purchase, lease or concession of covered real estate, at least three of the following property rights:

- To physically access the real estate
- To exclude others from physical access to the real estate
- To improve or develop the real estate
- To affix structures or objects to the real estate

### Covered real estate:

- **Airports** – A subset of airports in the US that includes the major passenger and cargo airports, and joint-use airports (military/civilian aircraft usage).
- **Maritime ports** – The top 25 tonnage, container and dry bulk ports, as well as strategic seaports.
- **Proximity to military facilities** – The proposed rule provides a list of US military installations grouped into four categories. Depending on which category has a US military installation in proximity to the proposed real estate investment, the covered real estate investment will be judged according to the following proximities:
  - Close proximity, defined as within one mile
  - Extended range, defined as between one mile and 100 miles
  - Within the county or other geographic areas (e.g., missile fields)
  - Within 12 nautical miles seaward off the US coastline

This rule puts the diligence burden on the investor to check the location of the proposed investment in proximity to the military facilities listed by CFIUS, which will be constantly updated according to the introduction to the proposed rule.

## CFIUS Review Exception for Covered Investments and Real Estate Transactions

FIRRMA authorizes CFIUS to draft regulations that define which foreign investors are subject to the new covered transaction authorities (covered investments and covered real estate transactions). Under the proposed rule, certain “excepted investors” (or “excepted real estate investors”) who are from certain “excepted foreign states” (or “excepted real estate foreign states”) will not be subject to CFIUS’s authority over covered investments or covered real estate transactions (such investors will still be subject to CFIUS’s authority over covered transactions involving the acquisition of control). These concepts operate together to remove CFIUS’s jurisdiction over covered investments or covered real estate transactions. Non-US companies or US companies with non-US ownership may conduct business transactions outside the scope of CFIUS’s authority, depending on how the final rules are developed.

- **Excepted investors/excepted real estate investors** – An excepted investor (or excepted real estate investor), and any of its parent entities, must have a substantial connection (e.g., through the nationality of the ultimate beneficial owners and the place of incorporation) in an excepted foreign state. Under the proposed rule, to be an excepted investor (or excepted real estate investor), an investor must meet each of the following conditions with respect to itself and each of its parents, if any:
  - It is organized under the laws of an excepted foreign state (or excepted real estate foreign state) or in the US
  - Its principal place of business is in an excepted foreign state (or excepted real estate foreign state) or in the US
  - Each member or observer of the board of directors, or a similar body of such entity, is a US national only or a national of one or more excepted foreign states (or excepted real estate foreign states)
  - Any holders of 5% or more of the outstanding voting interest, holders of the right to 5% or more of the profits, holders of 5% or more of the assets upon dissolution, or any persons that can exercise control are also excepted investors (or excepted real estate investors), or US nationals
  - The investor has a minimum excepted ownership held by excepted investors (or excepted real estate investors) or US nationals
- **Disqualification for conduct of investor and corporate family** – Even if a foreign investor meets the criteria stated herein, the proposed rule denies excepted investor status (or excepted real estate investor status) to any foreign person if it, or any of its parents or subsidiaries, in the prior five years, has violated certain US laws, has had certain regulatory actions taken against it (including by CFIUS), or is subject to export restrictions because of inclusion on a restricted party list or unverified list.

- **Post-closing disqualification if criteria is not met** – Under the proposed rule, even if a foreign investor meets the criteria of an excepted investor (or excepted real estate investor) and closes the transaction, the foreign investor can lose excepted investor status (or excepted real estate investor status) if, at any time during the three-year period following closing, the foreign investor no longer meets all the criteria (unless the only change is that CFIUS removed the status of a country as an excepted foreign state). If this happens, CFIUS will have authority over the investment that was, at the time of closing, an excepted transaction outside of CFIUS’s jurisdiction.
- **Excepted foreign state/excepted real estate foreign states** – The proposed regulation defines an excepted foreign state (or excepted real estate foreign state) as any foreign state determined by CFIUS, based on a super-majority vote of CFIUS member agencies, (1) to have a robust process to assess foreign investments for national security risks; and (2) to coordinate with the US on matters relating to investment security. The announcement by CFIUS of the proposed rule also stated that CFIUS is preparing additional factors that it will consider in assessing whether a foreign state has established a robust process to assess foreign investments for national security risks and is coordinating with the US on matters relating to investment security. It also noted that CFIUS is considering delaying this requirement to provide countries time to enhance foreign investment review processes and bilateral cooperation. CFIUS initially intends to designate a limited number of eligible foreign states at first, then potentially expand the number of eligible foreign states.
- **Minimum excepted ownership** – Under the proposed rule, a minimum excepted ownership must be held by excepted investors (or excepted real estate investors). This term is defined differently depending on whether an entity is publicly traded or is private. For publicly traded entities, minimum excepted ownership means “a majority of its voting interest, the right to a majority of its profits, and the right in the event of dissolution to a majority of its assets.” For private entities, the term means “90 percent or more of its voting interest, the right to 90 percent or more of its profits, and the right in the event of dissolution to 90 percent or more of its assets.”

## Contacts

### George Grammas

Partner and Co-Chair, International Trade Practice – Trade Compliance and National Security, Washington DC/London  
 T +1 202 626 6234 (Washington DC)  
 T +44 20 7655 1301 (London)  
 E [george.grammas@squirepb.com](mailto:george.grammas@squirepb.com)

### Peter Alfano

Senior Associate, Washington DC  
 T +1 202 626 6263  
 E [peter.alfano@squirepb.com](mailto:peter.alfano@squirepb.com)

### Jeff Turner

Partner, Washington DC  
 T +1 202 457 6434  
 E [jeff.turner@squirepb.com](mailto:jeff.turner@squirepb.com)

### Karen Harbaugh

Partner, Washington DC  
 T +1 202 457 6485  
 E [karen.harbaugh@squirepb.com](mailto:karen.harbaugh@squirepb.com)

### Pablo Carrillo

Of Counsel, Washington DC  
 T +1 202 457 6415  
 E [pablo.carrillo@squirepb.com](mailto:pablo.carrillo@squirepb.com)

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