COVINGTON

CFIUS Reform Legislation Introduced in Congress

November 8, 2017

CFIUS

Earlier today, Senator John Cornyn (R-TX), the second-highest-ranking Republican in the Senate, introduced a bill to reform the authority and operation of the Committee on Foreign Investment in the United States ("CFIUS"). The bill is co-sponsored by Senator Dianne Feinstein (D-CA) and Senator Richard Burr (R-NC), the Chairman of the Senate Select Committee on Intelligence, among other senators. Representative Robert Pittenger (R-NC) introduced a substantially identical companion bill in the U.S. House of Representatives. The proposed legislation, which is formally titled the Foreign Investment Risk Review Modernization Act ("FIRRMA"), represents the most significant effort to reform the CFIUS process since the passage of the Foreign Investment and National Security Act of 2007 ("FINSA"), which has governed CFIUS for a decade.

As we reported earlier this year, the effort to reform CFIUS is motivated by a view among some legislators, including Senator Cornyn, that the Committee needs additional authorities to address an evolving threat environment to U.S. national security, especially from China. Consistent with that view, the bill expresses the sense of Congress that "the national security landscape has shifted in recent years, and so have the nature of the investments that pose the greatest potential risk to national security, which warrants a modernization of the processes and authorities" of CFIUS.

The potential impact on CFIUS of this reform effort, as represented by FIRRMA, would be wide-ranging. In some respects, it would codify existing practices of CFIUS that have evolved recently, including in response to the changing landscape of foreign investment in the United States generally. In other respects, however, the bill represents a significant departure from the manner in which CFIUS has operated. Key aspects of the bill include the following:

- **Expansion of CFIUS jurisdiction (with possible exemption for investors from certain countries):** The bill would expand CFIUS's jurisdiction to review transactions that, among other things, comprise any non-passive investment in a critical technology company, contributions—"other than through an ordinary customer relationship"—of intellectual property and associated support to a foreign person through any type of arrangement (including joint ventures) regardless of whether the transaction results in any control over the U.S. business, and any real estate transaction that is in proximity to sensitive military and national security facilities. However, the bill would also authorize CFIUS to develop exemptions to these expansions for investors from countries that meet certain criteria, such as having a treaty alliance with the United States, a mutual investment security arrangement with the United States, and a process akin to CFIUS. There also are new definitions of "investment" and "United States Business" that,

depending on how they are construed, could signal further expansions of CFIUS jurisdiction.

- **Clarification on "passive" investments:** Under existing law, acquisitions of minority equity interests of a U.S. business are not subject to CFIUS jurisdiction provided that they are solely "for purposes of passive investment." In practice, CFIUS has construed this requirement strictly in certain circumstances, narrowing it so that even very low minority ownership interests could constitute a covered transaction if coupled with other interests, such as board observer rights, other strategic partnerships (such as joint ventures abroad), or extensions of credit. The bill now would codify this strict standard, thereby providing CFIUS with greater explicit authority to review minority investments.
- **Establishment of new "light filing":** The bill would create a new type of filing, known as a "declaration." The declaration, which would be no more than five pages, would be available to all parties, and would be intended to enable CFIUS to ascertain whether to seek a full formal filing or determine that no further action is necessary, thereby providing the parties with a legal safe harbor. CFIUS would "endeavor" to respond to declarations within 30 days.
- **Mandatory "light filings," or "declarations" for certain transactions:** Filing with CFIUS would remain voluntary for most transactions. However, submitting a light filing or "declaration" would be mandatory for certain types of transactions, including any acquisition of "a voting interest of at least 25 percent in a United States business by a foreign person in which a foreign government owns, directly or indirectly, at least a 25 percent voting interest."
- **Erosion of safe-harbor:** Filing with CFIUS provides transaction parties with a "safe harbor"—once CFIUS has approved a transaction, neither the President nor CFIUS may later take action with respect to the transaction unless there has been a material breach of a mitigation agreement or material misrepresentation or omission to CFIUS. FIRRMA notably would lower the threshold for when CFIUS could unilaterally initiate a subsequent review of a previously cleared transaction, including for breaches of mitigation agreements that are not intentional.
- **Longer timeframe for CFIUS reviews:** CFIUS currently undertakes an initial 30-day review, with the option to undertake an additional 45-day investigation. FIRRMA would (i) extend the review period to 45 days, (ii) retain the optional second-stage 45-day investigation; and (iii) authorize CFIUS to extend an investigation for one 30-day period. As a result, a single complete CFIUS review process potentially could take as long as 120 days, as opposed to 75 days under current law. That said, the 30-day extension also could shorten somewhat the overall timeframe for those transactions that currently must be withdrawn and refiled if CFIUS has not completed its review within the initial 75 days. Those transactions today generally are subject to a second full 75-day process, for a total of 150 days, whereas the 30-day extension, theoretically, could permit at least some such transactions to be completed without the need for a refiling.
- **Potential reduced use of mitigation; requirement for higher standard for mitigating national security risks:** FIRRMA would impose heightened standards for CFIUS before the Committee can conclude that any risks presented by a transaction may be addressed through mitigation. This requirement reflects an inherent skepticism among certain Committee members with respect to the use of mitigation as a tool to address national security concerns, and is consistent with the practice that has emerged within

CFIUS in recent months to utilize mitigation only rarely and predominantly in non-Chinese transactions.

- **Enhance CFIUS authorities to suspend transactions and refer transactions to the President:** Under the current law, CFIUS has the authority to review and investigate any pending transaction, and to impose interim mitigation measures to address national security concerns in the event a transaction has closed without filing with CFIUS. The bill would confirm these authorities, but also add the ability for CFIUS affirmatively to suspend a transaction during its review and investigation, as well as to cut short its investigation and refer the matter directly to the President for action (i.e., a formal prohibition or divestiture order). CFIUS also would have expanded authority to impose interim mitigation measures in the period of time that a transaction is before the Committee.
- **Further limits on judicial review:** Decisions by the President to suspend or prohibit a transaction already are not subject to judicial review. FIRRMA would extend such immunity to decisions of CFIUS itself, except that parties who voluntarily file could seek to vindicate certain constitutional rights only in the U.S. Court of Appeals for the District of Columbia Circuit.
- **Filing fee:** There currently is no fee to file with CFIUS. FIRRMA would permit CFIUS to charge a fee of no more than one percent of the value of the transaction or $300,000, whichever is less.

As expected, the bill does not include a "net benefit" or "reciprocity" test; Senator Cornyn has previously rejected proposals by some other Senators to expand CFIUS to address economic considerations. In addition, FIRRMA would not add new members to CFIUS, expand CFIUS generally to cover greenfield investment, prohibit investments in any particular sector, or apply different standards of review to investors from different countries.

While it is an extremely challenging environment to pass any legislation at the moment, we believe the bill has a greater potential to become law than any other effort to reform CFIUS in the past decade. There undoubtedly will be important concerns among the investment community and transaction parties with the unprecedented expansions of CFIUS authority set forth in the bill. That said, FIRRMA's prospects for enactment are strengthened by the fact that it is being presented as a bi-partisan and bi-cameral effort, driven by views among several key members in Congress and senior officials in the U.S. defense and intelligence agencies that CFIUS must be strengthened to address a changed risk environment for foreign investment. The bill notably also appears to have been extensively coordinated with key departments and agencies of the Trump Administration; we consequently expect that it ultimately will receive the formal support of the Executive Branch. In these circumstances, unlike certain other periodic legislative efforts to effect reform that have rapidly faded from view, we believe that FIRRMA merits very close attention from the business community.

Background

The proposed legislation comes at a time of dramatic change in the composition of foreign investment in the United States. There now is a much greater proportion of direct investment from developing markets, especially China. In the three-year period from 2013 to 2015, CFIUS reviewed a total of 74 transactions involving Chinese acquirers. By contrast, we believe that CFIUS reviewed at least that many Chinese transactions in 2016 alone, out of a total of

approximately 180 transactions, its highest-ever volume in a single year. Reflecting this changed composition of investment, CFIUS's caseload is on track this year once again to set an all-time record.

These changes have drawn greater interest from the Congress in CFIUS. Last year, Members of the House of Representatives asked the Government Accountability Office to investigate whether CFIUS has adequate authority to address the risks arising from the evolving investment landscape, with a particular focus on investment from China and Russia. Over the past several months, multiple senior members of the U.S. national security establishment have publicly echoed comments made by Sen. Cornyn in a speech at the Council on Foreign Relations this summer—namely, that China has sought to "weaponize" investment as part of a strategy to leapfrog the United States' advantages in technology. Other Cabinet members of CFIUS notably have called recently for CFIUS to receive enhanced authorities to review joint ventures abroad. Then, in September, the Senate Committee on Banking, Housing, and Urban Affairs ("Senate Banking Committee")—the Senate committee of jurisdiction with respect to CFIUS—held an open hearing entitled "Examining the Committee on Foreign Investment in the United States." This was the first hearing in a decade by the Senate Banking Committee to address CFIUS meaningfully and reflected a bipartisan recognition among most members of the Committee that any adjustments to CFIUS should be only one part of a broader, multifaceted solution to enhance U.S. national security and promote foreign investment.

Reflecting this environment, FIRRMA begins with a "Sense of Congress" section that, among other things, recognizes the "substantial economic benefits to the United States" of foreign direct investment and takes the position that the United States should continue to "enthusiastically welcome and support foreign investment," but then notes that "the national security landscape has shifted in recent years, and so have the nature of the investments that pose the greatest potential risk to national security, which warrants a modernization of the processes and authorities" of CFIUS. Reflecting a view that investment-related national security threats increasingly are multinational in nature, FIRRMA also calls on the President to "conduct a more robust international outreach effort to urge and help allies and partners of the United States to establish processes that parallel" CFIUS, as well as working with allies to "develop a new, stronger multilateral export control regime."

An In-Depth Look at FIRRMA

The following is a more detailed summary of key aspects of FIRRMA and how they would affect the CFIUS process:

Expansion of CFIUS Jurisdiction

CFIUS currently has jurisdiction to review transactions that result in control by a foreign person of a U.S. business. While the scope of that jurisdiction is extremely broad—extending to minority investments comprising as little as ten (10)-percent equity interest (or potentially even less, if certain other rights are present)—FIRRMA would expand it in several respects, including as follows:

- Real estate acquisitions in close proximity to military and sensitive sites: The bill would expand CFIUS's authority to review real estate transactions, by purchase or lease by a foreign person, "of private or public real estate that is located . . . in close proximity to a United States military installation or to another facility or property of the United States

Government that is sensitive for reasons relating to national security" and meets other criteria that CFIUS may prescribe by regulation. Section 3(a)(5)(B)(ii). Although proximity already is considered by CFIUS in covered transactions, this provision expressly expands the definition of "covered transaction" to include acquisitions of certain real estate outside the context of an acquisition of control of existing businesses. The meaning of "close proximity" is left to CFIUS to define by regulation, but this is a potentially broad expansion of CFIUS jurisdiction that could cover, in theory, a purchase of undeveloped land near a military base—or even non-military facilities deemed "sensitive."

- Transfer of critical technology or investment in critical infrastructure: CFIUS would have jurisdiction to review any non-passive *investment* by a foreign person in "any United States critical technology company or United States critical infrastructure company." Section 3(a)(5)(B)(iii). Notably, the legislation also introduces a definition for "investment" to include "the acquisition of equity interest, including contingent equity interest, as further defined in regulations prescribed by the Committee." Section 3(a)(12). Thus, any investment, including potentially a convertible interest, into a critical technology or critical infrastructure company would be subject to review, even if it falls short of CFIUS's definition of "control."
  - The definition of "critical technology," which would be subject to further explication in regulation, means "technology, components, or technology items that are essential or could be essential to national security." Section 3(a)(8)(A). The definition also includes defense articles or defense services on the U.S. Munitions List, certain items included on the Commerce Control List, and certain nuclear related items. Section 3(a)(8)(B).
  - Notably, the definition includes "[o]ther emerging technologies that could be essential for maintaining or increasing the technological advantage of the United States over countries of special concern with respect to national, defense, intelligence, or other areas of national security, or gaining such an advantage over such countries in areas where such an advantage may not currently exist." Section 3(a)(8)(B)(vi).
- Contribution of critical technology: While CFIUS already has jurisdiction to review joint ventures that result in foreign control of U.S. businesses, FIRRMA would expand the Committee's jurisdiction to review contributions—"other than through an ordinary customer relationship"—by a critical technology company of both intellectual property and "associated support" through any type of arrangement, including joint ventures, but excluding "ordinary customer relationships." However, with respect to the scope of the provision, the bill notably does not appear to require that the technology be located in the United States; it accordingly appears possible that this provision could be interpreted to permit CFIUS to review the transfer by a U.S. critical technology company of technology that already resides exclusively outside the United States.
- Changes in the rights of foreign persons: FIRRMA would expand CFIUS's authority to review changes to a foreign person's rights with respect to a U.S. business where those changes could confer control or involve an investment in a critical technology or critical infrastructure company, even if such change is outside the context of a transaction. Section 3(a)(5)(B)(iv).

While the foregoing would represent a significant expansion of CFIUS's jurisdiction, the bill would permit CFIUS to create exemptions from the provisions related to critical technologies and real estate for foreign investors from certain countries, such as those that have a formal

treaty alliance with the United States, a mutual investment security arrangement, or a national security-based foreign investment review process.

Finally, there is another potential definitional expansion embedded in the legislation. Specifically, under its existing regulations, CFIUS defines the scope of a "U.S. business" for its jurisdictional purposes to encompass "any entity . . . engaged in interstate commerce in the United States, *but only to the extent of its activities in interstate commerce*." 31 C.F.R. § 800.226 (emphasis added). FIRRMA, however, in defining "United States Business" omits the last phrase, so that the statutory definition is simply "a person engaged in interstate commerce in the United States." The bill therefore could be interpreted to capture any entity anywhere in the world so long as it conducts business in the United States. It is unclear whether the foregoing omission was intentional.

Focus on Countries of Special Concern

The legislation introduces the concept of "countries of special concern" by adding an explicit new country-specific framework that would require the Committee to apply heightened scrutiny to transactions involving certain countries—which would include "a country that poses a significant threat to the national security interests of the United States." Section 3(a)(4). The bill would not require CFIUS to maintain a list of such countries, but it is widely believed and understood that the designation would capture countries such as China and Russia that elsewhere have been identified by the U.S. government as presenting threats to U.S. national security.

New Dual-Filing System, Including "Declarations"

Filing with CFIUS currently is voluntary, although CFIUS agencies have the authority to initiate their own filings and the potential consequences of not filing a transaction that later is determined to have an impact on U.S. national security can be severe. As such, the process is designed to incentivize parties to notify CFIUS of transactions that potentially could implicate national security interests.

FIRRMA does not alter this fundamental framework for notices, but it does afford the parties the opportunity—albeit mandatory in some instances—to submit a newly defined "declaration" "not later than 45 days before the completion of the transaction." Section 5. These "declarations" are essentially "light filings" for covered transactions that could be filed with CFIUS in lieu of the more expansive traditional notice and would not necessarily trigger a 30-day review period—let alone a 45-day investigation. Such declarations are subject to further regulation, but "the Committee shall ensure that such declarations are submitted as abbreviated notifications that would not generally exceed 5 pages in length." Section 5. The timeframe for CFIUS action would be 30 days. Depending upon the identity of the foreign investor and the nature of the investment, filing a "declaration" instead of a notice may offer timing and cost advantages in certain cases. However, if CFIUS were to elect to require a filing, the initial declaratory filing, with its 30-day review period, could extend the timing for other transactions.

- Voluntary declarations: FIRRMA would allow most parties to a covered transaction to file a "declaration with the basic information regarding the transaction instead of a written notice." Section 5. CFIUS could, however, following the filing of declaration "request that the parties to the transaction file a written notice." Section 5. Such voluntary declarations, therefore, primarily would benefit sophisticated investors who previously have filed with CFIUS and are pursuing a transaction with no anticipated national

security implications. Other investors, especially those undertaking more complex transactions, may not benefit as much from such a filing because their time and resources may be more efficiently utilized by filing a formal notice and moving directly into the initial 45-day review period.

- Mandatory declarations: FIRRMA would mandate declarations if a covered transaction "involves the acquisition of a voting interest of at least 25 percent . . . by a foreign person in which a foreign government owns, directly or indirectly, at least a 25 percent voting interest." Section 5. Subject to further regulation, mandatory declarations also would be required "at the discretion" of CFIUS and based on a number of factors, including "the technology, industry, economic sector, or economic subsector" in which the U.S. business is a part of, the "difficulty of remedying the harm to national security" that could result, and "the difficulty of obtaining information on the type of covered transaction through other means." Section 5.

Modifications to Existing CFIUS Processes

In addition to the new concept of "declarations," the bill would modify CFIUS's processes in a number of other important respects:

- Timing for "review" period: CFIUS currently has 30 days to conduct an initial "review" of the transaction, FIRRMA would extend this time period to 45 days. Section 8. Notably, this extends the CFIUS review period beyond the 30-day waiting period required for certain transactions under the Hart–Scott–Rodino Antitrust Improvements Act of 1976 (HSR).
- Timing for investigations": Under current law, following the initial 30-day review period, CFIUS may conduct a 45-day "investigation" if the Committee has not resolved all national security concerns in the initial 30-day review period. FIRRMA would allow CFIUS, in "extraordinary circumstances" as subject to regulation, to extend an investigation for one 30-day period. Section 8. Together with the extension of the "review" period noted above, this means that CFIUS would have the ability to extend its total review period to as long as 120 days, by comparison to 75 days under current law.
- Timing for intelligence community threat assessment: Under current law, the Director of National Intelligence (DNI) is required to provide CFIUS with its National Security Threat Assessment in the first 20 days of CFIUS's review. FIRRMA would extend this to 30 days. Further, the assessment must include "a thorough analysis of any threat to the national security of the United States posed" by the transaction. Section 11. FIRRMA does, however, afford the DNI the option to submit to CFIUS a pared-down assessment when (1) the DNI previously submitted a threat assessment to CFIUS "involving each foreign person that is a party to the transaction" in the prior 12 months; (2) a transaction involves the purchase or lease by a foreign person of real estate in close proximity to a military or other sensitive national security facility; or (3) the transaction "otherwise meets criteria agreed upon" by CFIUS and the DNI. Section 11.
- Information sharing: FIRRMA would clarify that existing confidentiality rules do not prevent CFIUS or other entities, at the direction of the CFIUS Staff Chairperson, from sharing information gained during the CFIUS process with foreign governments "to the extent necessary for national security purposes." Section 12. This section reflects a growing view in the security establishment that protection of U.S. national security requires the U.S. government to cooperate with allied countries, especially in Europe, to take measures to protect against transactions that present national security concerns.

- Introduction of filing fee: FIRRMA would, for the first time, permit CFIUS to establish a filing fee for covered transactions that are filed with the Committee. Section 19. The provision limits any such fee to the lesser of one percent of the "value of the transaction"—which term is not defined—or $300,000. Filing fee proceeds would be deposited into a new fund to be established to support CFIUS operations, and would be in addition to any funds appropriated by Congress for the Committee's use. The statutory limits for the fee are notably higher than the current regulatory fee structure for HSR filings.
- Executive Branch certifications: The CFIUS chairperson and the head of the lead agency have statutory obligations to certify to Congress that "there are no unresolved national security concerns with the transaction." For transactions that underwent an investigation, current law allows this obligation to be delegated to "the Deputy position or the equivalent thereof at the lead agency." FIRRMA, however, would afford the chairperson with broad authority to determine the appropriate level of delegation authority—including delegation, in some instances, to the level of a Deputy Assistant Secretary. Section 10. This change could substantially limit the parties' ability to effectively engage more senior decision makers and collaborate on methods to mitigate national security concerns.
- Enhanced reporting to Congress: Currently, CFIUS provides a certification to a select group of Members within Congress when it approves a transaction: the Chairmen and Ranking Members of the two committees of jurisdiction (the Senate Banking Committee and House Financial Services committee), and the leadership in the Senate and House. FIRRMA would expand this list to include the Chairmen and Ranking Members of the two intelligence committees in Congress. It also requires the Committee to include the threat analysis conducted by the Director of National Intelligence in its reporting to Congress upon concluding a review.

Enhancements to CFIUS's Authority

In addition to expanding CFIUS's jurisdiction and modifying the Committee's processes, FIRRMA also would enhance the Committee's authority in certain respects and insulate the Committee further from judicial review.

- Erosion of the statutory "safe harbor": Filing with CFIUS provides transaction parties with a "safe harbor"; once CFIUS has approved a transaction, the President or CFIUS cannot later take adverse action with respect to a transaction unless there has been a material and intentional breach of a mitigation agreement or material misrepresentation to CFIUS. One significant impact of FIRRMA would be the degradation of this safe harbor—the provision that transaction parties fundamentally rely on when considering whether to file with CFIUS. Thus, FIRRMA lowers the threshold for when CFIUS may initiate unilaterally a subsequent review of a previously cleared transaction. Section 7. Specifically, whereas FINSA allowed the reopening of review only if a party *intentionally* and materially breached a condition of a mitigation agreement or condition of approval, FIRRMA strikes the intentionality requirement. Accordingly, if *any* material breach occurs, CFIUS would have the authority to reopen a previous case and initiate a subsequent review. CFIUS also would maintain its authority to initiate a new review unilaterally if the parties submit false or misleading material to CFIUS, or omit material information.
- Higher standard for mitigation: In addition to lowering the threshold for when CFIUS can reopen a case should there be a breach of the mitigation agreement, FIRRMA would

prohibit CFIUS from entering in to such an agreement "*unless* the Committee determines that the agreement or condition resolves the national security concerns posed by the transaction, taking into consideration whether the agreement or condition is reasonably calculated to (i) be effective, (ii) allow for compliance with the terms of the agreement or condition in an appropriately verifiable way;" and (3) would enable effective monitoring of compliance in order to enforce the agreement. Section 16 (emphasis added). This heightened standard, which effectively reverses the current policy presumptions in the statute, likely will result in fewer mitigation agreements, while simultaneously increasing the number of transactions in which CFIUS determines to recommend Presidential action because the Committee, on its own, cannot mitigate the national security risks presented by the transaction.

- Enhanced and clarifying requirements on mitigation: FIRRMA would clarify and enhance certain authorities of CFIUS in relation to mitigation agreements that the Committee enters into with transaction parties. For example, the bill would repeal existing language that requires the Committee to avoid placing unnecessary burdens on the parties. It also would authorize CFIUS to use certain additional mechanisms to address noncompliance with mitigation agreements, including, among other things, requiring the parties to submit for CFIUS review any new covered transaction for a period of five years. At the same time, the bill also would impose certain obligations on the CFIUS agencies responsible for monitoring compliance with mitigation agreements for how they will monitor compliance, and notes that if CFIUS utilizes a third-party monitor to assist with compliance, such a monitor shall have no fiduciary responsibility to the parties.
- Suspension of transactions: FIRRMA would give CFIUS the authority, through the Staff Chairperson, to "suspend a proposed or pending covered transaction that may pose a risk to the national security of the United States" during the pendency of review or investigation. Section 16. This addition would resolve an ambiguity in the law concerning whether there are limits on the scope of CFIUS's authority to impose interim mitigation measures by its own authority and without securing a presidential order during the pendency of a review.
- Actions by the President: FIRRMA would grant the President authority, in addition to suspending or prohibiting a transaction, to "take any additional action . . . to address the risk to the national security of the United States"—ensuring the President has the authority to mitigate any national security risks should the parties attempt to evade a presidential suspension or prohibition order. Section 13.
- Judicial review: FIRRMA would further constrain transaction parties' ability to seek judicial review of actions by CFIUS or the President. The President's actions under FINSA are already exempt from judicial review, but FIRRMA would extend the exemption of judicial review, except on narrow constitutional grounds, to designees of the President and CFIUS itself. Section 14. The right to file a petition is further limited to parties who initiated a written notice or declaration, thereby precluding compelled filings or unilateral action by CFIUS from judicial review. FIRRMA would also require that parties seeking judicial review file a petition in the United States Court of Appeals for the District of Columbia Circuit (the "D.C. Circuit") within "60 days after the date on which the President or the Committee takes an action" regarding the transaction. The D.C. Circuit would have exclusive jurisdiction to challenges of CFIUS's or the President's actions and could only consider the record before CFIUS in deciding such matters.

Codification of Other Aspects of CFIUS's Current Operation

As noted, the CFIUS statute was most recently amended in 2007 through FINSA. In many respects that law did not break new ground, but rather codified in legislation the way that CFIUS had already come to operate. Likewise, some aspects of FIRRMA codify practices that CFIUS has adopted. Notably however, it appears to codify how CFIUS operates *today*, which is different to how the Committee operated even a year ago, and reflects a less flexible approach. Specifically:

- Passive investments: As noted, CFIUS under its current regulations does not review acquisitions that are "for purposes of passive investment." CFIUS recently has strictly construed the meaning of "passive investment" so as to review even acquisitions of small minority investments where there are other control rights or relationships between the parties. FIRRMA appears to codify this practice by strictly defining a passive investment as one that does not result in control by a foreign person and does not afford the foreign person (i) access to any nonpublic technical information in the possession of the U.S. business, (ii) access to any nontechnical information in the possession of the United States business that is not available to all investors, (iii) membership or observer rights on the board of directors or equivalent governing body of the United States business or the right to nominate an individual to such a position, or (iv) any involvement, other than through voting of shares, in substantive decision-making pertaining to any matter involving the United States business. Section 3(a)(5)(D). Further, any "parallel strategic partnership or other material financial relationship" between the foreign person and the U.S. business would be sufficient to bring an otherwise passive investment within the scope of CFIUS's jurisdiction. Section 3(a)(5)(D).
- Monitoring of non-notified transactions: CFIUS already actively monitors a range of sources, including U.S. and foreign press, to identify non-notified transactions that the Committee may want to review. FIRRMA would codify this practice by requiring CFIUS to "establish a mechanism to identify covered transactions" that were not previously notified to CFIUS. Section 9.
- Notice contents: FIRRMA would require that any notice submitted to CFIUS include "a copy of any partnership agreements, integration agreements, or other side agreements relating to the transaction, including any such agreements relating to the transfer of intellectual property" as specified by regulation. Section 4. Although CFIUS currently can request such information (and often does), this section would create an affirmative obligation on the parties to include copies of such documents with the notice.
- Risk-based assessments: FIRRMA would codify CFIUS's existing internal practice of requiring a formal risk-based assessment addressing the threat posed by the foreign acquirer, vulnerabilities relating to the U.S. business, and the transaction's consequences to U.S. national security before entering into mitigation. The bill would also provide that any CFIUS member agency that dissents from the consensus of the Committee must produce its own analysis and justification for an alternative recommendation.
- Factors to be considered: Current law sets forth a non-exhaustive list of factors that CFIUS may consider as part of its national security analysis. FIRRMA would modify four of these factors and add nine new factors. In most respects, these additions and modifications reflect how CFIUS already conducts its analysis. For example, CFIUS in

recent years has been acutely focused on the protection of personal information of Americans, even though that factor appears nowhere in existing law. However, the codification of these factors should provide some further clarity on the types of issues that CFIUS scrutinizes. New factors include whether the transaction would:

- Create new U.S. cybersecurity vulnerabilities or exacerbate existing ones.
- Expose personally identifiable, genetic, or other sensitive data of U.S. persons.
- Increase the cost to the U.S. government of acquiring or maintaining systems necessary for defense, intelligence, or other national security reason.
- Involves a "country of special concern" and the acquisition of critical technology that the country of special concern has a demonstrated or declared interest in acquiring.
- Present national security-related risks caused by a shift in the cumulative market share of any "one type of infrastructure, energy asset, critical material, or critical technology" by a foreign person.
- Involve parties with a history of complying with U.S. laws and regulations, including relating to the protection of intellectual property and immigration.
- Allow a foreign government to gain a "significant new capability to engage in malicious cyber-enabled activities against the United States," including those that would "affect the outcome of any election for Federal office."
- Facilitate criminal or fraudulent activity affecting U.S. national security.
- Expose any sensitive law enforcement information.

FIRRMA would also modify the factors set forth in FINSA to include: (1) whether the transaction would reduce U.S. technological and industrial advantage, relative to any country of concern; (2) whether the transaction would contribute to the loss or other adverse effects on technologies that are the foundation of the United States' strategic advantage; (3) whether the transaction would result in an increased reliance on foreign suppliers to meet U.S. national defense needs; and (4) the national security impacts on transportation assets.

What FIRRMA Would Not Do

While the foregoing would be substantial changes to CFIUS that would materially impact the Committee's authority and operation, FIRRMA rejects other recently discussed potential reforms:

- Continued focus on national security; no "net benefit" or "reciprocity" test: There have been a number of proposals over the years to expand CFIUS's remit to address economic issues, such as requiring that transactions present a "net benefit" to the United States, or requiring CFIUS to consider whether a foreign investor's home country would permit a reciprocal investment by a U.S. company in the same industry.
- No expansion to cover greenfield investment: With the exception of the expansion of CFIUS authority to review real estate transactions and certain acquisitions of technology, FIRRMA would maintain CFIUS's focus on transactions involving existing U.S. businesses. It generally would not expand the Committee's jurisdiction to cover startup—or "greenfield"—investments.
- No new CFIUS members: There have been several proposals over the years to add new members to CFIUS. FIRRMA would not add any new members to CFIUS.

- No "calling out" specific countries: Although Senator Cornyn previously made clear that concerns about China are the principal drivers of the legislation, FIRRMA does not identify any country by name.
- No ban on investment: The bill does not call for a "ban" on any particular investment or from particular countries.

What We Expect Moving Forward

We expect that the introduction of this bill will generate significant interest in Congress and in the broader investment community and CFIUS regulatory environment. We also anticipate that the Senate Banking Committee and the House Committee on Financial Services, the two Congressional committees with jurisdiction over CFIUS, may hold further hearings on CFIUS reform later this year. As FIRRMA moves through the legislative process, we expect numerous amendments to be filed, including potential amendments that would draw CFIUS away from its narrow focus on national security.

To be sure, there are strong potential challenges to passing any significant legislation. In the most bi-partisan of times, it is not easy to move legislation; the current environment in Washington is, to say the least, something less than bi-partisan. Plus, other issues wholly unrelated to investment or CFIUS are occupying, and will continue to occupy, congressional attention for the rest of this year. But there are also reasons to believe that the bill (or a version of it) may ultimately become law. Senator Cornyn is among the most influential members of the Senate, and there appears to be an emerging bi-partisan consensus that CFIUS should be strengthened, principally to address growing concerns about Chinese investment. Senator Cornyn also has been discussing the bill with key members of the Trump Administration, including Treasury Secretary Steven Mnuchin. Within the last several months, all the leaders of the U.S. intelligence community, as well as Secretary of Defense Mattis, Secretary of Commerce Ross, and Secretary of the Treasury Mnuchin, have expressed support for CFIUS reform. These comments from Administration officials indicate potential momentum behind Senator Cornyn's efforts to reform CFIUS. For these reasons, we believe FIRRMA merits close attention, and we will continue to keep our clients apprised of developments in this area.

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We hope that you find this analysis useful. Please do not hesitate to contact the following members of our CFIUS practice if you would like to discuss any aspect of the foregoing in further detail:

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