

New CFIUS Report Offers First Full Picture of Data Collected Post-FIRRMA; Chinese Filings Drop Sharply

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Introduction

The Committee on Foreign Investment in the United States (“CFIUS” or the “Committee”) released its Annual Report to Congress regarding its review of certain transactions involving foreign investment during 2019. The current Annual Report was released just two and a half months after the previous Annual Report, covering 2018, demonstrating the Committee has continued its active effort to meet its Congressional reporting obligations. You can find our alert on the previous annual report [here](#).

This 2019 report reflects the first full year’s worth of data collected by the Committee following the enactment of the latest CFIUS reform legislation, the Foreign Investment Risk Review Modernization Act (“FIRRMA”), on August 13, 2018. While FIRRMA was only fully implemented through regulations that took effect on February 13, 2020, the U.S. Department of the Treasury, as chair of CFIUS, issued interim rules on October 10, 2018, which became effective a month later, implementing CFIUS’s expanded jurisdiction under FIRRMA over certain non-passive but non-controlling investments in U.S. businesses involved with “critical technologies.” Our analysis of these rules, known as the “Pilot Program,” can be found [here](#).

With the first full year of data on the Pilot Program, the 2019 report reflects the Committee’s and transaction parties’ continuing adjustment with respect to the procedural changes under the declaration process, the substantive expansion of the Committee’s jurisdiction, and the significant conceptual shift related to mandatory filings. While the data on declarations for 2019 shows that the Committee, as well as transaction parties and counsel, have become more accurate in identifying transactions suitable for the declaration process, with a nearly four-fold increase in declarations cleared compared to the initial implementation period in 2018, CFIUS still requested that nearly 30 percent of declarations be refiled as full notices. Ultimately, the relative proportions of declarations that were (a) cleared, (b) requested to be refiled as notices, or (c) received a determination that the Committee could not conclude action (but where CFIUS did not feel compelled to request a filing) were roughly equal. Optimal calibration of the declaration process would likely have a higher proportion of cleared transactions and a lower proportion of requested filings, which would reflect transaction parties are improving their ability to understand CFIUS’s expectations and discern which deals are best suited to the declaration process.

Beyond the Pilot Program, the report shows that CFIUS has improved the effectiveness of its case management post-FIRRMA, with significantly fewer notices proceeding to investigation and even fewer notices having to be withdrawn. Moreover, the report's statistics regarding notices filed by country continue to show a continuing decrease in Chinese transactions and a correlative increase in investment from allied countries, likely reflecting the broader geopolitical dynamic under the Trump administration. For the first time since 2011, filings by Chinese parties did not account for the greatest number of filings by country.

Discussion – Key Issues

We discuss first data on the Pilot Program before turning to the data on filings in general.

1. Encouraging Signs from the First Full Year of Data on Declarations Submitted Under the Pilot Program

The Pilot Program required parties to file a declaration or a notice with CFIUS before completing transactions that would result in a foreign person acquiring certain rights in a U.S. business that “produced, designed, tested, manufactured, fabricated, or developed” any “critical technologies” in connection with the designated Pilot Program industries. As noted above, the Pilot Program—the substantive provisions of which were made permanent by the final regulations implementing FIRRMA that went into effect on February 13, 2020—initially became effective on November 10, 2018. While the Annual Report for 2018 only reflected data on the first two months or so of the Pilot Program's existence, the Annual Report for 2019 reflected the first full year of data on declarations submitted under the Pilot Program. Over the course of 2019, parties filed 94 declarations that CFIUS determined to be subject to its jurisdiction. The report also provided for the first time a breakdown of declarations filed by country.

Of these 94 declarations, CFIUS cleared 35 transactions (approximately 37 percent) at the declaration stage and determined that it could not conclude action (but would not request a filing) as to another 32 declarations (approximately 34 percent, or approximately 71% altogether). This suggests that parties correctly assessed CFIUS's need for a full notice approximately 70 percent of the time. CFIUS also requested that 26 of the 94 declarations (approximately 28 percent) be filed as full notices, however, with one declaration being withdrawn for business reasons. The report did not specify the proportion of declarations determined to be non-controlling but non-passive investments, as opposed to control transactions, as it had in 2018.

On a country-by-country basis, Japan filed the greatest number of declarations (14), followed by Canada (12), the United Kingdom (11), South Korea (9), and Germany (7). Interestingly, investors from China filed three declarations, despite the ongoing tensions between the United States and China. Unfortunately, CFIUS did not provide data on the outcome of declarations by country, so we cannot directly assess the relative success rate from each country.

This first year of data reflects, to a degree, both encouraging signs and some ongoing challenges that parties and the Committee have encountered with the short-form declaration process, as previewed by the limited data from 2018. The rate of “approval” for declarations increased more than threefold from approximately 10 percent in 2018 to approximately 37 percent in 2019, while the proportion of cases on which the Committee determined it could not conclude action decreased from approximately 52 percent in 2018 to approximately 34 percent

in 2019. While parties who receive a “no action” determination do not receive the safe harbor that would accompany CFIUS clearance, we have generally regarded such non-determinations to be a form of advisory opinion, signaling that the Committee’s more limited review did not find sufficient areas of concern to demand a full review. In most cases, this still conveys valuable information to the parties that they can use to assess the merits of moving forward with the transaction more rapidly, without formal CFIUS clearance. Thus, the no-action determination can therefore still be a potentially important and useful procedural outcome for parties.

We do note, however, that while the proportion of declarations where CFIUS requested the parties to file a formal notice increased only modestly, from approximately 24 percent in 2018 to approximately 28 percent in 2019, that still means filing parties faced a nearly one-in-three chance that the CFIUS review process would last longer than it would have had the parties filed a formal notice at the outset. Therefore, there is likely still some room for improvement regarding calibration of the Committee’s and parties’ understanding and expectations around the declaration process, even if there are too many potential factors at play to ever get the calibration perfectly right.

2. While FIRRMA Offered Notable and Effective Measures to Help CFIUS Manage Its Caseload, Approximately Half of Notices Still Proceeded to Investigation

In our alerts on the combined 2016-2017 Annual Report and the 2018 Annual Report, we suggested that FIRRMA could contribute to the Committee’s increased effectiveness in case management, by providing a longer time period for review and increased resources for the Committee’s member agencies. These measures appear to have been effective, as borne out by the statistics discussed below.

As previewed in our alert for the 2018 Annual Report, the number of notices filed held remarkably steady, going from 229 in 2018 to 231 in 2019. The percentage of notices that proceeded to investigation dropped considerably, however, from approximately 69 percent in 2018 to approximately 49 percent in 2019. This is roughly in line with the percentage of cases proceeding to investigation in 2015 and 2016 (i.e., approximately 46 percent) demonstrating the relative success of the Committee’s ongoing effort to manage its increased caseload. Based on this data, transaction parties still had a roughly 50-50 chance of the Committee proceeding to investigation, though the true likelihood was almost certainly quite dependent on the facts of the specific transaction, including the country of origin of the acquirer and the nature of the target U.S. business.

The percentage of notices withdrawn also dropped precipitously, from approximately 29 percent in 2018 to approximately 13 percent in 2019. Likewise, the number of cases withdrawn and refiled dropped from approximately 18 percent in 2018 to approximately 8 percent in 2019. The number of withdrawn cases that were abandoned because of CFIUS-related national security concerns decreased in absolute terms from 18 in 2018 to 8 in 2019, likely as a result of the significant drop in Chinese transactions (as discussed more below). We note, though, that these remained consistent in terms of the percentage of total cases withdrawn, both representing approximately 27 percent of such cases. Overall, this again likely also reflects the Committee’s improved management of its caseload and success in concluding action within the statutory timeframe for most cases.

3. CFIUS Filings Reflected Decreased Investment by China and Increased Investment by Allies

Investments by country seemed to reflect that investors from allied countries sought to take advantage of decreased investment by Chinese investors, even as the total number of transactions reviewed by CFIUS (in terms of both declarations and notices) increased. As anticipated in our alert on the 2018 Annual Report, filings by Chinese parties have dropped by more than 50 percent, from 55 in 2018 to 25 in 2019, representing the first time since 2011 that filings by Chinese parties have not been the highest on a country-by-country basis.

Investors from Japan and Canada were the first and third most frequent filers respectively, with Japan increasing significantly from 31 filings in 2018 to 46 filings in 2019, and Canada decreasing modestly from 29 filings in 2018 to 23 filings in 2019. As noted, other allies mostly increased their filings, likely filling the gap left by the decrease in Chinese investment: Australia increased from 4 filings in 2018 to 11 filings in 2019; Germany increased from 12 filings in 2018 to 13 filings in 2019; Singapore increased from 5 filings in 2018 to 10 filings in 2019; South Korea increased from 4 filings in 2018 to 10 filings in 2019; and the United Kingdom increased from 5 filings in 2018 to 13 filings in 2019. While French investors filed at a rate on par with other allied countries, with 13 filings in 2019, that reflected a decrease from 21 filings in 2018.

Data on filings by sector reflected certain changes from 2018 to 2019. Whereas the Finance, Information, and Services sector had represented the greatest number of filings in 2018, as well as in 2017, the Manufacturing sector jumped from third to first place for 2019, representing 44 percent of transactions, whereas it had only represented 35 percent in 2018. The Finance, Information, and Services sector came second for 2019 at 39 percent of the filings, holding relatively constant since 2018, in which it represented 38 percent of filings. The portion of notices in the Mining, Utilities, and Construction sector decreased sharply from 21 percent in 2018 to only 9 percent of transactions filed in 2019. The Wholesale Trade, Retail Trade, and Transportation sector—representing the smallest portion of transactions filed by sector—increased slightly from 7 percent in 2018 to 8 percent in 2019.

Finally, as noted in our alert for the 2018 Annual Report, the percentage of filings cleared with mitigation measures has remained remarkably constant since 2017, with 29 filings cleared with mitigation in 2017 and 2018, and 28 filings cleared with mitigation in 2019. Such clearances accounted for approximately 12 percent of all notices filed in 2017, approximately 13 percent of all notices filed in 2018, and approximately 12 percent of all notices filed in 2019.

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