

COVID-19: Implications for CFIUS

April 1, 2020

CFIUS

Greetings from Washington, D.C. Our first thought in these uncertain times is for the health and safety of you — our clients and friends — as well as your families.

The scope and scale of recent events is almost inconceivable. All of us — including the Committee on Foreign Investment in the United States (“CFIUS”) — are sailing in uncharted waters. That said, while we may not have all of the answers, we are able to share some insights from the CFIUS front lines regarding how the challenges presented by the COVID-19 pandemic are impacting the process and substance of the Committee’s reviews. We present these thoughts in a question and answer format below. Transaction parties will want to keep these considerations in mind when planning for any matter that may implicate a CFIUS review in the coming weeks and months.

1. Is CFIUS closed?

No. Like other U.S. government agencies in the Washington, D.C. area, the CFIUS member agencies have substantially reduced their in-office operations. Nonetheless, CFIUS staff across the agencies — including the U.S. Intelligence Community elements supporting the threat assessment process — continue to carry out the Committee’s operations, both remotely and in the office, albeit less efficiently than under normal conditions. The staff are putting in long hours in very difficult circumstances.

2. How are reduced in-office operations affecting CFIUS’s review of current active cases?

Transactions that CFIUS already has formally accepted for review appear to be experiencing relatively minimal impact from the government’s reduced operations. In this regard, we are seeing the agencies make substantial efforts to continue the substantive review of active cases and to conclude those reviews within the statutory review periods. For cases involving full notices (as opposed to declarations) where the U.S. Intelligence Community’s threat assessment has been completed and there are no identified national security concerns, we expect the Committee to conclude all action on most of those cases in a timely manner, allowing for approval. For notices where the threat assessment is complete and there are mitigation discussions in progress, we expect that CFIUS member agencies will be able to continue those discussions while working remotely, to develop and finalize mitigation agreements, and to pave the way for approval of those matters within the statutory review period as well.

There is more uncertainty, however, with respect to transactions that still are in the early stages of the review period, when the required threat assessment is not yet complete.¹ Because it relies on classified information, the threat assessment — which also requires coordination within the U.S. Intelligence Community — can be processed solely on secure U.S. government networks that cannot be accessed via the public Internet (*i.e.*, by analysts who may need to work from home on unclassified systems). Moreover, because the assessment is classified, its contents can be discussed only in security-cleared government spaces or via government-secured telecommunications systems. Accordingly, remote U.S. government working arrangements could inhibit the production, dissemination, and digestion of the threat report. This almost certainly will, in turn, impact the timeliness of the Committee’s deliberations on transactions. This is particularly true for matters presenting potential national security concerns because the Committee’s risk assessment for each matter is based in significant part on the threat assessment; the risk assessment, in turn, is essential to the Committee’s consideration of the need for and potential scope of risk mitigation. It therefore is likely that at least some cases will require considerably more time than usual for CFIUS to conclude its review.

3. How will reduced in-office operations affect cases that have been filed in draft with CFIUS or have not yet been filed? Will there be differences in how CFIUS manages full notices and declarations?

Although CFIUS continues to review and provide comments on full notices filed in draft, CFIUS has slowed considerably its pace in accepting and commencing review of full formal joint voluntary notices. This is due in substantial part to the limitations on remote access to classified information and networks. As described above, reduced in-office operations create practical challenges for performing the critical threat assessment and the follow-on risk analysis of the Committee. If these constraints persist or worsen, CFIUS may be compelled to slow even further — or even cease altogether — the formal acceptance of new cases so that it can manage its docket and the inefficiencies imposed by having so many of its staff working remotely.

This may be true even in cases where parties stipulate to CFIUS jurisdiction in order to avail themselves of the 10-day formal acceptance timeline provided in the new regulations. Under FIRREA, the Committee can extend this timeline if necessary so long as it can provide Congress with “an explanation of the causes of such delays, including whether such delays are caused by resource shortages, unusual fluctuations in the volume of notices, transaction characteristics, or other factors.” The unprecedented impact of COVID-19 on U.S. government operations presumably would offer *prima facie* justification for delaying the acceptance of notices even when the requisite stipulations are made.

CFIUS also is required to continue processing declarations that are filed with it. That said, given the constraints under which the CFIUS agencies are operating, we believe it is inevitable that more declarations will conclude with only a “no action” response from CFIUS; we expect this to be true even for transactions that do not pose any particular national security concerns. “No action” responses indicate that the Committee is unable to complete action on the basis of the declaration, and that the parties may choose to file a written notice if they wish to obtain the

¹ The Foreign Investment Risk Review Modernization Act (“FIRREA”) requires that, by Day 30 of the initial 45-day review period for full notices, the Director of National Intelligence complete a full analysis of threats to U.S. national security posed by a transaction.

statutory safe harbor for their transaction or they may proceed to close the transaction without that safe harbor.

In normal circumstances, we and others have tended to regard such “no action” responses, in many cases, almost as a form of advisory opinion from the Committee; *i.e.*, a signal that the agencies were unable to conduct a full analysis of the matter within the declaration timeframe, but that the review undertaken did not yield material national security concerns. In the context of the current public health emergency, by contrast, we believe such “no action” responses likely are more indicative of the Committee’s operating challenges and, accordingly, generally will be less meaningful as a signal of whether CFIUS truly has concluded that it does not have an interest in the transaction. Because a “no action” response does not provide a safe harbor, transaction parties will need to consider carefully whether consummating the transaction based solely on the “no action” response may entail a risk of later CFIUS action. Alternatively, CFIUS may request that the parties file a full notice so that the Committee can undertake a more comprehensive review of the transaction. In these circumstances, and as described above, the timing of CFIUS’s acceptance and review of the full notice will be less certain and more encumbered by challenges, at least in the near term.

4. What are the potential planning considerations for transaction parties if they face timing or financial exigencies that require closing a transaction quickly?

If parties have timing exigencies for closing a transaction and CFIUS has not yet commenced its review — or its review becomes protracted — transaction parties will need to evaluate carefully any perceived national security risks presented by the transaction and their own risk tolerance for closing a transaction without having received formal CFIUS approval. The same considerations apply if transaction parties are facing financial stresses requiring immediate capital, including financial stress stemming from COVID-19.

If CFIUS is likely to perceive a transaction to present little or no national security risk, and if the CFIUS filing is permissive rather than mandatory, transaction parties may consider closing the transaction in certain situations in which, under normal circumstances, they would have waited for CFIUS approval before closing. However, if a transaction presents potential national security concerns, such a strategy raises significant risks that CFIUS could identify the transaction, develop national security concerns at a later time, and seek to review — and even decide to mitigate or unwind — the transaction. In such circumstances, despite the likely delays, transaction parties may conclude that the net benefit of CFIUS approval prior to closing outweighs the likely delays and possible added costs of waiting for CFIUS to be in a position to conduct a full review.

Parties facing timing or financial exigencies also will need to evaluate carefully whether their transaction is subject to a mandatory CFIUS filing requirement. Importantly, if a CFIUS filing is mandatory and if the parties do not file at least a declaration at least 30 days in advance of closing the transaction, CFIUS then has the authority to assess a civil monetary penalty up to the value of the transaction. Additionally, if CFIUS identifies national security risks after a transaction has closed, CFIUS often finds that its options for mitigating such risks are more limited than would have been the case prior to closing, as the risk may already have manifested; the possibility of a forced divestiture therefore increases.

If transaction parties in exigent circumstances determine that a mandatory filing is required, one tactical option to consider is to use the declaration process to satisfy the legal filing requirement and close the transaction 30 days or more after filing the declaration. This would avoid potential

monetary penalties, although — as described above — the present limitations on CFIUS's ability to review cases meaningfully may result in CFIUS issuing a “no action” letter that is less useful than in more routine situations; alternatively, CFIUS may issue a request for a full notice.

If transaction parties facing exigent circumstances are unable to wait to close even the 30 days after filing a declaration, parties may be able to mitigate CFIUS concerns at least somewhat by adopting affirmative, prophylactic measures. Such measures could include engaging with CFIUS in advance of closing; providing transparency about the transaction and the circumstances necessitating closing the transaction without a CFIUS approval; and affirmatively implementing measures to address potential CFIUS concerns, such as limiting access to or governance rights over critical technology, critical infrastructure, or sensitive personal data until CFIUS approval ultimately is received.

Finally, if transaction parties have filed a full notice that has been formally accepted for review, and the parties at that point wish to pivot to the declaration process, permission of the CFIUS Staff Chair is required to make such a change. On the other hand, if the parties have not yet filed, or have only filed in draft, they can elect to file a declaration without seeking permission.

5. Will CFIUS change its evaluation of national security risks presented by transactions involving distressed assets?

The COVID-19 situation already is causing severe economic stress in certain U.S. and global sectors, creating capital demands and opportunities for investment that may be met by foreign investors. During the previous 2008 financial crisis, there was a strong federal government policy supporting foreign investment in the United States, including foreign government-controlled investment. CFIUS approved many such investments as a reflection of that policy. Twelve years later, the nature of the U.S. government's and CFIUS's concerns regarding foreign investment — including investment in certain sectors and by investors from specific countries — has evolved significantly. There has been talk, both in some U.S. government circles and in certain foreign governments, of holding foreign investment during these troubled times to higher levels of scrutiny. While we expect CFIUS to maintain its current policy of open investment, it frankly still is too early to say whether CFIUS may modify certain elements of its approach in response to the unprecedented economic challenges posed by COVID-19.

* * *

CFIUS

If you have any questions concerning the material discussed in this client alert, please contact the following members of our CFIUS practice group:

<u>Mark Plotkin</u>	+1 202 662 5656	mplotkin@cov.com
<u>David Fagan</u>	+1 202 662 5291	dfagan@cov.com
<u>Stuart Eizenstat</u>	+1 202 662 5519	seizenstat@cov.com
<u>Alan Larson</u>	+1 202 662 5756	alarson@cov.com
<u>Peter Lichtenbaum</u>	+1 202 662 5557	plichtenbaum@cov.com
<u>John Veroneau</u>	+1 202 662 5034	jveroneau@cov.com
<u>David Marchick</u>	+1 202 662 5514	dmarchick@cov.com
<u>Heather Finstuen</u>	+1 202 662 5823	hfinstuen@cov.com
<u>Brian Williams</u>	+1 202 662 5270	bwilliams@cov.com
<u>Zachary Mears</u>	+1 202 662 5414	zmears@cov.com
<u>Jonathan Wakely</u>	+1 202 662 5387	jwakely@cov.com
<u>Charles Buker</u>	+1 202 662 5139	cbuker@cov.com
<u>B.J. Altvater</u>	+1 202 662 5160	baltvater@cov.com
<u>Samuel Karson</u>	+1 202 662 5341	skarson@cov.com
<u>Jenny Reich</u>	+1 202 662 5885	jreich@cov.com
<u>Claire Kim</u>	+1 202 662 5071	ckim@cov.com

This information is not intended as legal advice. Readers should seek specific legal advice before acting with regard to the subjects mentioned herein.

Covington & Burling LLP, an international law firm, provides corporate, litigation and regulatory expertise to enable clients to achieve their goals. This communication is intended to bring relevant developments to our clients and other interested colleagues. Please send an email to unsubscribe@cov.com if you do not wish to receive future emails or electronic alerts.