

## CFIUS Releases 2018 Annual Report to Congress

### Key Takeaways

- On May 19, 2020, the US Treasury Department, as chair of the Committee on Foreign Investment in the United States (“CFIUS” or the “Committee”), published its Annual Report to Congress on all notices filed with CFIUS in 2018, the most recent year for which data has been declassified, and all reviews or investigations completed during the year (“Annual Report”).
- The Annual Report is particularly important as it marks the first data set for reviews and investigations completed since the [Foreign Investment Risk Review Modernization Act of 2018](#) (“FIRRMA”) became law (though only certain changes to CFIUS regulations made by FIRRMA were effective in 2018).
- The report holds important insights for foreign acquirers contemplating acquisitions and other investments in the United States.

| 2018 At A Glance |                                                           |
|------------------|-----------------------------------------------------------|
| 229              | Notices were filed with CFIUS for review                  |
| 34               | Notices were withdrawn and refiled                        |
| 32               | Notices were withdrawn and not refiled                    |
| 158              | Investigations were initiated                             |
| 2                | Notices were rejected for failing to satisfy requirements |
| 1                | Transaction was referred to the President and blocked     |

Below, we highlight some of the key data in the Annual Report.

### Background

CFIUS, an interagency committee principally comprising nine members and chaired by the Secretary of the Treasury, has broad powers to review foreign investments in and acquisitions of U.S. businesses to determine the potential impact on U.S. national security. CFIUS has the authority to impose mitigation measures, suspend transactions, and, where appropriate recommend that the President block or unwind transactions.

On August 13, 2018, President Trump signed into law the [Foreign Investment Risk Review Modernization Act of 2018](#) (“FIRRMA”), which made several substantial changes to the CFIUS process, including by:

- Expanding the scope of CFIUS jurisdiction to permit review of a wider range of transactions;
- Authorizing CFIUS to mandate notifications regarding certain types of transactions involving critical technologies;
- Adopting a new, short-form declaration process to notify the Committee about potentially covered transactions;
- Authorizing collection of filing fees with respect to covered transactions for which a written notice is filed; and
- Strengthening the Committee’s authority to restrict transactions that threaten U.S national security.

FIRRMA’s implementation has since been rolled out in phases, starting with the implementation of the so-called “Pilot Program” in October 2018 and culminating with the release of final regulations in January 2020. Our coverage of final regulations for transactions involving critical technology, critical infrastructure, and sensitive personal data (“[TID Final Regulations](#)”) and the final regulations pertaining to provisions of FIRRMA that expand CFIUS jurisdiction over certain real estate transactions (“[Real Estate Final Regulations](#)”) is available [here](#) and [here](#).

Implementation of FIRRMA and fine tuning of the national security review process remains ongoing. For example, in March 2020, CFIUS released a proposed rule to establish filing fees for CFIUS reviews of notices of transactions (“[Proposed Filing Fee Rule](#)”) and subsequently published an interim rule to begin collecting filing fees for transaction notices filed after May 1, 2020 (“[Interim Filing Fee Rule](#)”). Our coverage of the filing fee Proposed Filing Fee Rule and Interim Filing Fee Rule is available [here](#) and [here](#). In addition, on May 21, 2020, CFIUS published a proposed rule that would modify the mandatory declaration provision for covered transactions involving critical technology and clarifies the “substantial interest” test used for determining mandatory declaration requirements for certain investments by non-U.S. governments (the “[Proposed Rule](#)”). Our coverage of those changes is available [here](#).

### Annual Report Highlights for Dealmakers

**1. Dealmakers should be conservative when estimating the length of the CFIUS review period.**

| Closing in Review (Pre-FIRRMA) |                       | Closing in Review (Post-FIRRMA) |                       | Closing in Investigation |                       |
|--------------------------------|-----------------------|---------------------------------|-----------------------|--------------------------|-----------------------|
| 30                             | Average Calendar Days | 44                              | Average Calendar Days | 74                       | Average Calendar Days |
| 30                             | Median Calendar Days  | 45                              | Median Calendar Days  | 75                       | Median Calendar Days  |

Pre-FIRRMA, the longest possible review timeline before CFIUS might refer a matter to the President for an ultimate decision was 75 days: CFIUS would conduct a 30-day review and could conduct an additional investigation of up to 45 days under certain circumstances. Under FIRRMA the longest possible review timeline is 105 days: the initial review period was extended to a 45-day review, after which CFIUS can conduct an additional 45-day investigation if determined necessary and, in extraordinary circumstances, can extend the investigation period by an additional 15 days.

The Annual Report illustrates that the Committee is utilizing the additional time afforded it under FIRRMA, which extended the average CFIUS review timeline by 15 days (two weeks) on average.

While as recently as 2016 less than half of all reviews proceeded to investigation, that number increased to 73% in 2017, and in 2018 69% of all reviews were investigated. More than ever before, practitioners need to anticipate the likelihood that a CFIUS review of a potential investment transaction now will constitute both a review and an investigation.

| % of Transactions that Required an Investigation |                                  |
|--------------------------------------------------|----------------------------------|
| 2016                                             | 45% of transactions under review |
| 2017                                             | 73% of transactions under review |
| 2018                                             | 69% of transactions under review |

**2. 2018 marked the 5th Presidential Order in CFIUS’ 40 year history.**

In March 2018, President Trump blocked microchip maker Broadcom Ltd. from acquiring Qualcomm Inc. and ordered the parties to immediately, and permanently, abandon the \$117 billion proposed transaction. The Presidential Order was only the fifth of its kind and the second issued by President Trump at the time

(President Trump blocked another deal in 2020). In addition, while there was only one transaction blocked by the President in 2018, the amount of abandoned transactions described below indicates that the number may have been higher had the abandoned covered transactions undergone a complete CFIUS review.

| CFIUS Presidential Orders |                                                                                                                                                                                                    |
|---------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1990                      | President Bush directed the China National Aero-Technology Import and Export Corporation, a Chinese state owned entity, to divest its acquisition of the airplane components manufacturer MAMCO.   |
| 2012                      | President Obama directed the Ralls Corporation, a privately-owned Chinese company, to divest itself of an Oregon wind farm project.                                                                |
| 2016                      | President Obama blocked the acquisition of Aixtron, a semiconductor company, for \$670 million by Fujian Grand Chip Investment Fund, a privately owned Chinese fund                                |
| 2017                      | President Trump blocked the acquisition of Lattice Semiconductor Corp. for \$1.3 billion by Canyon Bridge Capital Partners, a Chinese investment firm partially funded by the Chinese Government   |
| 2018                      | President Trump blocked the \$117 billion acquisition of semiconductor chip maker Qualcomm by Broadcom, a Singapore based company                                                                  |
| 2020                      | President Trump ordered Beijing Shiji Information Technology Co, a subsidiary of the public Chinese company Shiji Group, to divest its acquisition of the U.S. hotel software developer Stayntouch |

**3. A high number of abandoned transactions highlights the complexities of the post-FIRRMA CFIUS review process.**

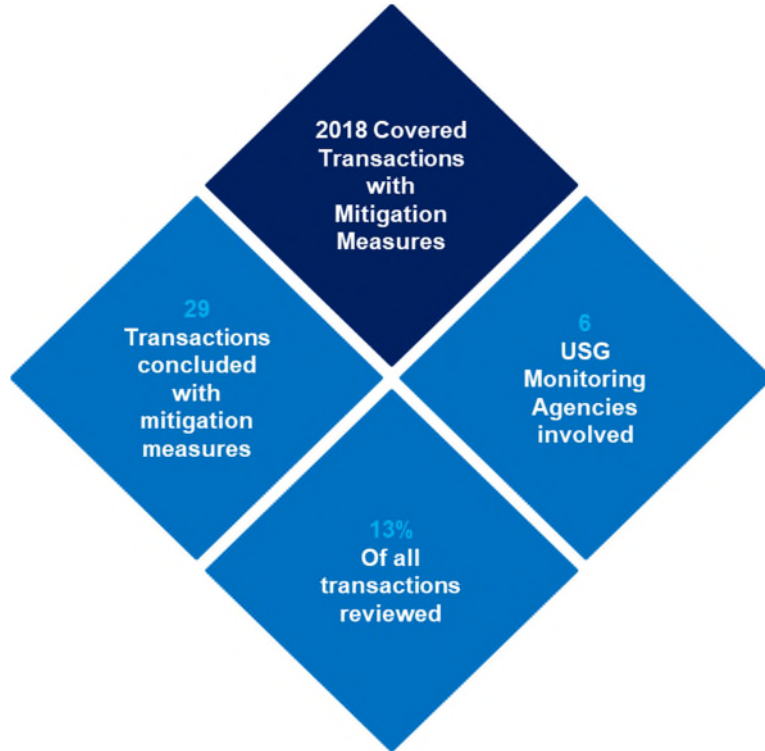
A closer look at the withdrawal data in the Annual Report highlights that FIRRMA’s implementation has added considerable complexity to the CFIUS review process.

There was a six-fold increase in the number of transactions abandoned due to the parties and CFIUS not agreeing on mitigation measures to allay the Committee’s national security concerns or the parties not accepting the proposed mitigation measures.

| A Closer Look: Withdrawn Notices |                                                                                                                                                                                                                                                    |
|----------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 32                               | Notices were withdrawn and not refiled                                                                                                                                                                                                             |
| 8                                | Were refiled in 2019                                                                                                                                                                                                                               |
| 18                               | Notices (and transactions) abandoned after CFIUS informed the parties that it was unable to identify mitigation measures that would resolve its national security concerns or it proposed mitigation measures that the parties chose not to accept |
| 1                                | Was withdrawn after failing to satisfy the CFIUS process requirements                                                                                                                                                                              |
| 3                                | Were withdrawn and the transactions abandoned for commercial reasons                                                                                                                                                                               |
| 2                                | Were withdrawn subject to certain conditions                                                                                                                                                                                                       |

**4. An increase in mitigation measures underscores the importance of considering potential mitigation early on in the transaction process.**

In 2018, the number of transactions involving mitigation measures nearly doubled as compared to 2017.



Should the data in the Annual Report represent the beginning of an upward trend in transactions requiring mitigation measures, it will be important for parties to consider the possibility of mitigation measures in their transaction agreements: what measures would the parties be willing to accept, and which would they not?

The Annual Report provides examples of mitigation measures negotiated and adopted in 2018 that required the parties involved to take specific and verifiable actions.

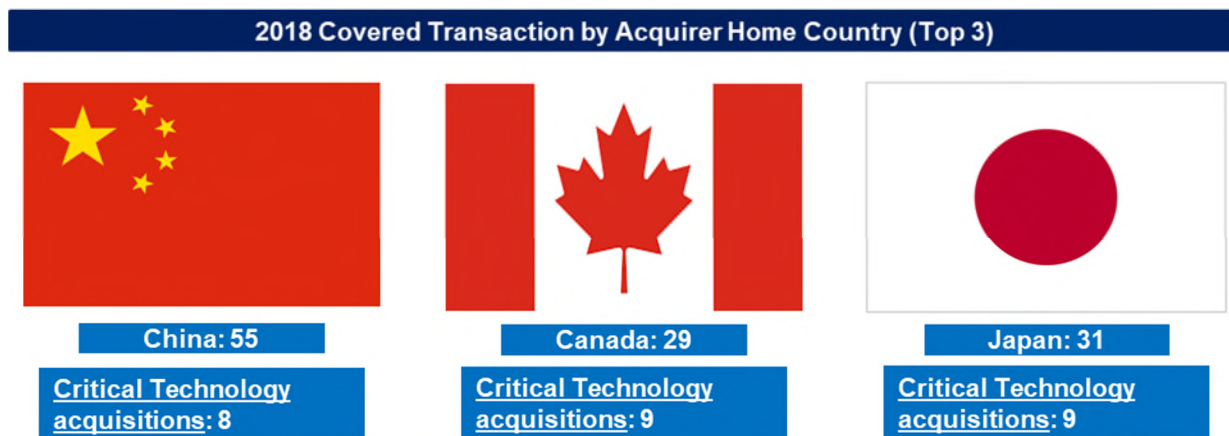
These actions included the following:

- Prohibiting or limiting the transfer or sharing of certain intellectual property, trade secrets, or know-how;
- Establishing guidelines and terms for handling existing or future USG contracts, USG customer information, and other sensitive information;
- Ensuring that only authorized persons have access to certain technology, that only authorized persons have access to USG, company or customer information; and that the foreign acquirer not have direct or remote access to systems that hold such information;
- Ensuring that only U.S. citizens handle certain products and services, and ensuring that certain activities and products are located only in the United States;
- Establishing a Corporate Security Committee and other mechanisms to ensure compliance with all required actions, including the appointment of a USG-approved security officer or member of the board of directors and requirements for security policies, annual reports, and independent audits;
- Exclusion of certain sensitive assets from the proposed transaction; and
- Divestiture of all or part of the U.S. business.

**5. China, Canada and Japan represent the top three countries for FDI in the United States.**

Foreign acquirers from China, Canada and Japan accounted for 50% of all notices filed with the Committee in 2018 (with Chinese acquirers responsible for the largest share) and 34% of all transactions involving critical technology.

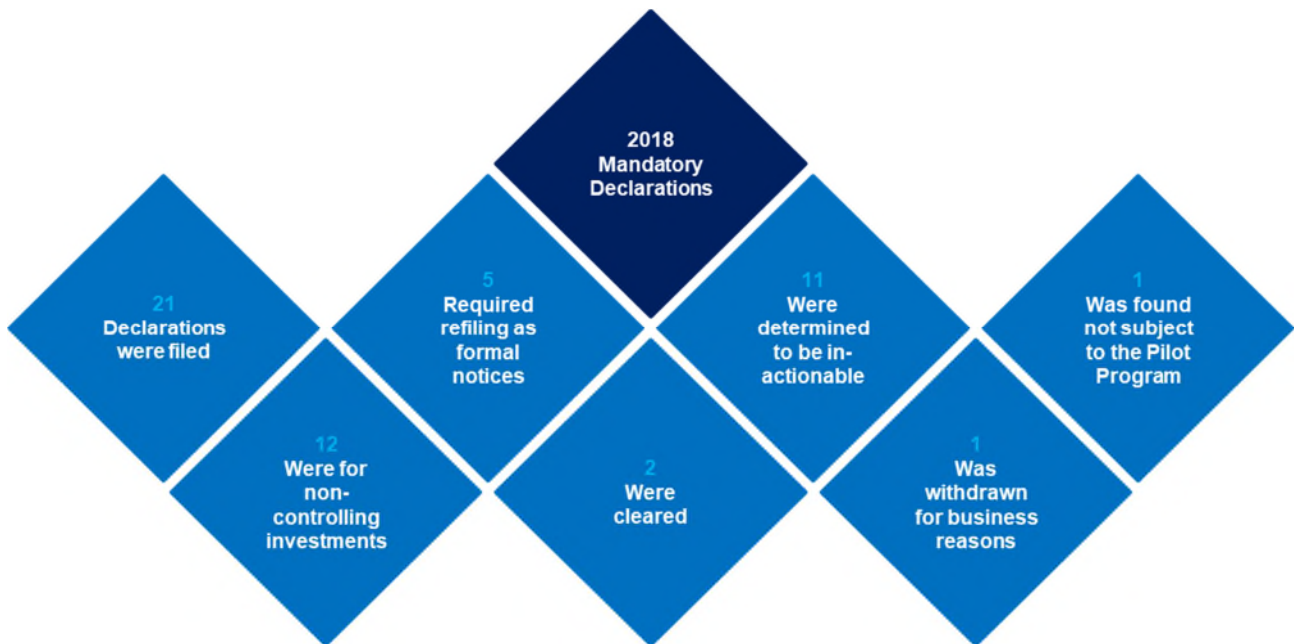
While much of the data in the Annual Report reveals the new complexities in the CFIUS review process, it is clear that parties are still able to navigate the CFIUS process and receive clearances even for transactions involving Chinese acquirers, which generally are perceived as being subject to heightened scrutiny by CFIUS.



**6. Only two mandatory declarations filed were cleared.**

One of the key changes under FIRRMA was the introduction of a mandatory filing requirement for certain covered transactions. In October 2018, CFIUS launched a Critical Technology Pilot Program (the “Pilot Program”) to protect the U.S. national security innovation base and to address what policymakers view as key shortfalls in regulators’ ability to secure the predominance of U.S. innovation and the industries and businesses that support it. The Pilot Program was intended to expire in March 2020, but has been formally adopted as part of the TID Regulations.

The mandatory declarations must be no longer than five pages, and must be filed at least 45 days prior to the expected completion date of the proposed transaction. CFIUS may respond to a declaration by informing parties that it: (1) has cleared the transaction, (2) is initiating a unilateral review, (3) is requesting that the parties submit a full formal notice, or (4) is unable to reach a decision regarding clearance on the basis of the declaration alone. The data from the Annual Report shows how these options played out in real time during the first year of implementation.



CFIUS did not take action in over 50% of the declarations filed and 24% of the proposed transactions required the submission of a formal filing. Parties should seriously consider whether it is preferable to submit a full formal notice from the outset so as to be guaranteed a final response from CFIUS that will provide investor certainty with (relatively) less delay.

### Conclusion

The Annual Report shows how FIRRMA's implementation has changed the CFIUS review landscape: longer timelines, more mitigation measures and more deals withdrawn in the face of CFIUS concerns. The key takeaway is that foreign acquirers should enter the CFIUS process prepared and consider CFIUS implications early on when developing plans to pursue investments in or acquisitions of U.S. businesses.

Dechert has represented many clients through CFIUS reviews, including major operators and investors in the high tech, telecommunications, energy, defense, and infrastructure industries. We regularly advise foreign and domestic entities ("buyers" and "sellers," as well as other interested third parties) through the CFIUS review process, helping them determine whether or not to bring a transaction before the committee (and whether or not CFIUS review is required), to assemble the required information and materials for a filing, and then (as necessary) to negotiate national security agreements with CFIUS in a manner that minimizes both delay and the imposition of conditions that might threaten the transaction. We also give counsel on strategies for identifying and addressing political and policy considerations that may arise.