

# Navigating the New CFIUS Landscape for Foreign Investment in the U.S.

## I. Introduction

New rules that became final on February 13, 2020 dramatically expand the jurisdiction of the Committee on Foreign Investment in the United States (CFIUS). Where CFIUS was once concerned only with transactions that would result in foreign control of a U.S. business, the Committee's authority now extends to **non-controlling** investments in a broad range of U.S. businesses involved with critical technology, critical infrastructure, or sensitive personal data – collectively denominated “TID U.S. businesses” – as well as in certain real estate.<sup>1</sup>

The new rules significantly affect foreign investment in **hi-tech** (including social media), **biotech**, **health care**, **finance**, **insurance**, and **critical infrastructure**, among other sectors. And they make it essential for foreign investors (and U.S. targets) to **know the U.S. export classification** of the target's technology – even if the target does not engage in any export activity.

Further, because the rules apply to both direct and indirect foreign investment, CFIUS issues can arise in the context of investments from **funds with foreign limited partners**, or **U.S. companies controlled by foreign persons**, or foreign investments into a **foreign company that has a U.S. subsidiary**.

Parties who fail to seek CFIUS approval where applicable do so at their peril: the Committee can not only recommend **blocking of proposed transactions**, but also **unwinding of completed investments/acquisitions**. More commonly, the Committee will propose **mitigation conditions restricting foreign investor/acquiror rights**, such as rights to participate in substantive decision-making or to access the target's intellectual property.

While notification to CFIUS is at the parties' discretion in many cases (subject to the risk of unwinding/forced mitigation if notification is not made), **CFIUS notification is mandatory** when the investment will result in a significant **foreign government interest**, and when the target develops, produces, or tests certain **export-controlled and other sensitive technology** – a category that goes well beyond obviously sensitive military technology and captures a much wider range of commercial technologies than many investors realize. Where filing is mandatory, failure to comply can lead not only to unwinding or imposition of mitigation conditions, but also **penalties** of value of the transaction or \$250,000, whichever is greater.

## II. Triggers for CFIUS jurisdiction

At a high level, CFIUS jurisdiction turns on two pivots: (i) the rights the foreign investor will receive; and (ii) the kind of business or real estate into which the investment is being made. **Table 1** summarizes these triggers.

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<sup>1</sup> A portion of the rules involving non-controlling investments in certain U.S. businesses that deal in critical technologies was implemented as a pilot program beginning in October 2018. But the new rules go much further.

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Table 1

TYPE OF RIGHTS	TYPE OF BUSINESS/REAL ESTATE
<ul style="list-style-type: none"> <li>■ Control</li> </ul>	<ul style="list-style-type: none"> <li>■ Any business with respect to which CFIUS could perceive a threat to national security, broadly defined</li> </ul>
<ul style="list-style-type: none"> <li>■ Membership or observer rights on, or nomination rights regarding, the target's board; or</li> <li>■ Involvement, other than through voting of shares, in substantive decision-making; or</li> <li>■ Access to material nonpublic technical information in the possession of the target/target's U.S. office/subsidiary</li> </ul>	<ul style="list-style-type: none"> <li>■ Business that designs, develops, produces, fabricates, manufactures, or tests "critical technology"; or</li> <li>■ Business that owns, operates, or provides certain services to, "critical infrastructure"; or</li> <li>■ Business that (directly or indirectly) collects or maintains "sensitive personal data of U.S. citizens"</li> </ul>
<ul style="list-style-type: none"> <li>■ Any purchase, lease, or concession that affords one or more of the following property rights: right to physically access; right to exclude others from access; right to improve or develop; right to attach fixed or immovable objects or structures</li> </ul>	<ul style="list-style-type: none"> <li>■ Located within, or functioning as a part of, a "covered port," as defined in <b>31 CFR 802.210</b></li> <li>■ Located within one (1) mile of the boundary of a U.S. government facility identified in <b>31 CFR 802, App. A, Pt. 1 or 2</b></li> <li>■ Located within 100 miles of a U.S. government facility identified in <b>31 CFR 802, App. A, Pt.2</b></li> <li>■ Located within certain townships/ranges identified in <b>31 CFR 802, App. A, Pt.3</b></li> <li>■ Located within certain offshore areas identified in <b>31 CFR 802, App. A, Pt.4</b></li> </ul>

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### III. How hi-tech, biotech, health care, finance, and insurance investments are captured

Two terms are key to understanding why the new rules are so significant for the hi-tech, biotech, health care, finance, and insurance sectors: (1) "critical technologies" and (2) "sensitive personal data of U.S. citizens."

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## A. Critical Technologies

The term “[critical technologies](#)” means technologies that are subject to certain U.S. export controls, specifically: items on the [United States Munitions List](#) (USML); items on the [Commerce Control List](#) (CCL) pursuant to multilateral regimes (including reasons relating to national security, chemical and biological weapons, nuclear nonproliferation, or missile technology), or based on unilateral controls (regional stability, surreptitious listening, or emerging and foundational technology); nuclear-related items covered by 10 CFR 110 or 810; and select agents and toxins covered by 7 CFR 331, 9 CFR 121, or 42 CFR 73.

In practice, these controls apply to a wide range of technologies, well beyond what many investors may think of as sensitive tech: for example, “critical technologies” include software that uses encryption for data protection purposes, and lentiviral packaging plasmids commonly used in biomedical research that contain the G gene from the Vesicular Stomatitis Virus (VSV).

If a U.S. business designs, develops, produces, fabricates, manufactures, or tests critical technologies, CFIUS jurisdiction will exist for controlling investments and may very well also exist for non-controlling investments (depending on the rights the foreign investor will acquire). Therefore, it is essential for investors to know the export classification of a target’s technology. That in turn means extra steps in due diligence. Investors should be aware that accurate determination of export classification can be complex, and may result in substantial delay if a target has never engaged in export activities and therefore never identified the export classification of its technology. The technology of a target’s U.S. subsidiaries may also need to be evaluated.

## B. Sensitive Personal Data

The term “[sensitive personal data of U.S. citizens](#)” includes the following categories:

▪ Genetic test results	▪ Information on an individual’s mental or physical health
▪ Geolocation data	▪ Non-public electronic communications (texts, chats, email, etc.) between users of the target’s products if those products’ primary purpose is to facilitate third-party communications.
▪ Biometric data	
▪ Insurance application data	▪ Data concerning U.S. government security clearance status
▪ The set of data in a consumer report	▪ Data in an application for government security clearance or employment in a position of public trust
▪ Detailed financial data	▪ Data for generating a government identification card

While this list sounds, and is, sweeping, the definition is subject to some important limits, including the following:

- The data must be identifiable, and not a matter of public record.
- Data collected or maintained by a business concerning its employees does not count, except with respect to employees of U.S. government contractors with personnel security clearances.

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- Genetic test results derived from federal government databases and routinely made available to private parties for research are excluded.
- Except with respect to genetic test results, data that falls into the categories above does not count as sensitive unless the target either:
  - (i) targets or tailors goods or services to U.S. executive branch agencies, contractors, or employees with military, intelligence, national security, or homeland security responsibilities; or
  - (ii) has collected or maintained, or has a demonstrated business objective to collect or maintain, data on 1 million individuals (not necessarily all U.S. citizens).

Even with the limitations described above, this definition of sensitive personal data sweeps in all kinds of U.S. businesses that may never even have dreamt that a committee like CFIUS exists. It is also critical to note that CFIUS will have jurisdiction where the U.S. business collects or maintains the relevant kind of data directly or indirectly. As a result, as examples embedded in the rules make clear, if a business outsources collection or storage of sensitive personal data within the scope of the definition to a subsidiary or a third party provider, both the business and the subsidiary or provider will be considered TID U.S. businesses and will need to consider CFIUS issues with respect to direct or indirect foreign investment. See [31 CFR 800.248](#), Examples 11-12.

### IV. Mandatory filings, and exemptions

In most cases, notification to CFIUS is a voluntary process, subject to the risk of unwinding/forced mitigation if notification is not made but the Committee develops concerns about the transaction. However, the new rules make prior notification to CFIUS mandatory in two circumstances:

- (i) If the foreign investment will result in an interest of 25% or more by a foreign person in which a foreign government other than UK, Canada or Australia has a 49% or greater interest; and
- (ii) If the foreign investment target designs, develops, produces, fabricates, manufactures, or tests “critical technologies” that it either (i) specifically designed for, or (ii) uses in connection with its activities in, one of 27 industries specified in 31 CFR Appendix B.<sup>2</sup>

The rules provide several significant exemptions from the mandatory filing requirements, which we have summarized in **Table 2**.

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<sup>2</sup> According to official commentary accompanying the new rules, the Treasury Department intends to revise the rule for mandatory declarations in the context of critical technology by replacing the test based on industry codes with a test based on “export control licensing requirements.” 85 FR 3112, 3121 (January 17, 2020). However, no proposed rule articulating this change has yet been published.

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Table 2

## EXCEPTIONS TO THE MANDATORY FILING REQUIREMENTS.

The new rules provide several exceptions to the mandatory filing requirements, as follows:

REQUIRED FEATURES OF TRANSACTION	EXEMPTION
Investment by a fund that affords a foreign person (or designee) membership as a limited partner or equivalent on an advisory board or committee of the fund, provided that: <ul style="list-style-type: none"> <li>(i) the fund is managed exclusively by a general partner (or equivalent);</li> <li>(ii) the GP (or equivalent) is not a foreign person;</li> <li>(iii) the advisory board or committee on which the foreign person sits does not have the ability to approve, disapprove, or otherwise control: investment decisions of the fund, or GP decisions related to entities in which the fund is invested; and</li> <li>(iv) the foreign person cannot otherwise control the investment fund, including via the authority to approve/disapprove/otherwise control investment decisions or decisions of the GP related to entities in which the fund is invested, or to unilaterally dismiss, prevent the dismissal of, select, or determine the compensation of the GP.</li> </ul>	Exempt from mandatory filing for both critical technology transactions and transactions with a substantial foreign government interest. (For critical technology transactions, the exemption is slightly broader, applying even if the GP is a foreign person as long as the GP is “ultimately controlled exclusively by U.S. nationals.”)
<b>Control</b> transaction involving an air carrier that holds a certificate from the Secretary of Transportation under 49 USC 41102	Exempt from mandatory filing for both critical technology transactions and transactions with a substantial foreign government interest
Transaction by an <b>excepted investor</b>	Exempt from mandatory filing for non-controlling investments in critical technology businesses
Indirect foreign investment via a FOCI-mitigated entity operating under a valid security clearance	
An investment by a foreign person who satisfied the criteria for “excepted investor” status at the time of the transaction, but no longer meets all the criteria in 31 CFR 800.219(a)(1), (a)(2), (a)(3)(i), (a)(3)(ii), (a)(3)(iii), (c)(1)(i), (c)(1)(ii), and (c)(1)(iii).	
An investment that is subject to CFIUS jurisdiction <b>solely</b> because the target/target’s U.S. office/subsidiary produces, designs, tests, manufactures, fabricates, or develops one or more critical technologies that is eligible for export, reexport, or transfer (in country) pursuant to License Exception ENC of the Export Administration Regulations (15 CFR 740.17) – e.g., certain kinds of software with encryption capabilities.	

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The exemption for “excepted investors” ([31 CFR 800.219](#)) merits some additional examination. While it sounds promising, in practice it is rather limited, because:

- 1) It applies only to non-controlling investments in TID U.S. businesses; control transactions remain subject to CFIUS jurisdiction even if the foreign party qualifies as an “excepted investor.”
- 2) The category “excepted investor” is defined by reference to “excepted foreign states,” of which there are currently only three: the U.K., Australia, and Canada.

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- 3) The exemption requires satisfaction of a complex set of nationality-related conditions, as set out in **Table 3**. While these criteria may be workable for individual investors, it will likely be difficult to gather the necessary information with respect to corporate investors.

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Table 3

Table 3 - Criteria for Qualification as an “Excepted Investor”
(1) the government of Australia, Canada, or the U.K.; or
(2) a natural foreign person who: <ul style="list-style-type: none"> <li>a. is a national of Australia, Canada, and/or the UK, <u>and</u> is <u>not</u> also a national of any other foreign state (“excepted state-only national”), <u>and</u></li> <li>b. satisfies the conditions in (3)(f)-(h) below</li> </ul>
(3) a legal person that satisfies all the following criteria <u>with respect to itself and each of its parent entities</u> : <ul style="list-style-type: none"> <li>a. *is organized under the laws of the U.S., Australia, Canada, or the U.K.;</li> <li>b. *has its principal place of business in the U.S., Australia, Canada, or the U.K.;</li> <li>c. *at least 75% of the board members and observers (or equivalent) are excepted state-only nationals;</li> <li>d. each foreign person who (individually or with other foreign persons) holds an interest of 10% or more is: an excepted state-only national; an excepted state government entity; or an entity organized in and having its principal place of business in an excepted state;</li> <li>e. the “minimum excepted ownership” is held by persons who are not foreign persons, or who are excepted state-only nationals, excepted state government entities, or entities organized in and having their principal place of business in the U.S. or an excepted foreign state.               <ul style="list-style-type: none"> <li>i. For entities with securities primarily traded on an exchange in the U.S., Canada, Australia, or the U.K., “minimum excepted ownership” means a majority of voting interest, the right to a majority of profits, and the right in the event of dissolution to a majority of assets.</li> <li>ii. In other cases, it means 80 percent or more of voting interest, the right to 80 percent or more of profits, and the right in the event of dissolution to 80 percent or more of assets.</li> </ul> </li> <li>f. neither the foreign person nor any of its parents nor any entity of which it is a parent is listed on the BIS Entity List or Unverified List;</li> <li>g. in the five years prior to the completion date of the transaction, neither the foreign person nor any of its parents nor any entity of which it is a parent has:               <ul style="list-style-type: none"> <li>i. *received notice from CFIUS that it made a material misstatement, omission, or false certification in a filing or violated a mitigation agreement/material condition/order;</li> <li>ii. *been subject to action by the President under section 721(d) of the Defense Production Act of 1950 (suspending or prohibiting transactions); or</li> <li>iii. entered into a settlement agreement with or received a finding of violation or penalty notice from OFAC regarding violations of economic sanctions; received notice of debarment from DDTC regarding violations of the International Traffic in Arms Regulations; been party to a final order by BIS regarding violations of export control laws; received a civil penalty from the National Nuclear Security Administration; or been convicted of or entered into a DOJ DPA or non-pros for a felony in any U.S. jurisdiction;</li> </ul> </li> <li>h. the foreign person continues to satisfy the criteria marked with an asterisk above for three years following completion. If the investor ceases to satisfy the relevant conditions, its excepted investor status will be retroactively lost and the transaction deemed to have involved a foreign person who was not an excepted investor.</li> </ul>

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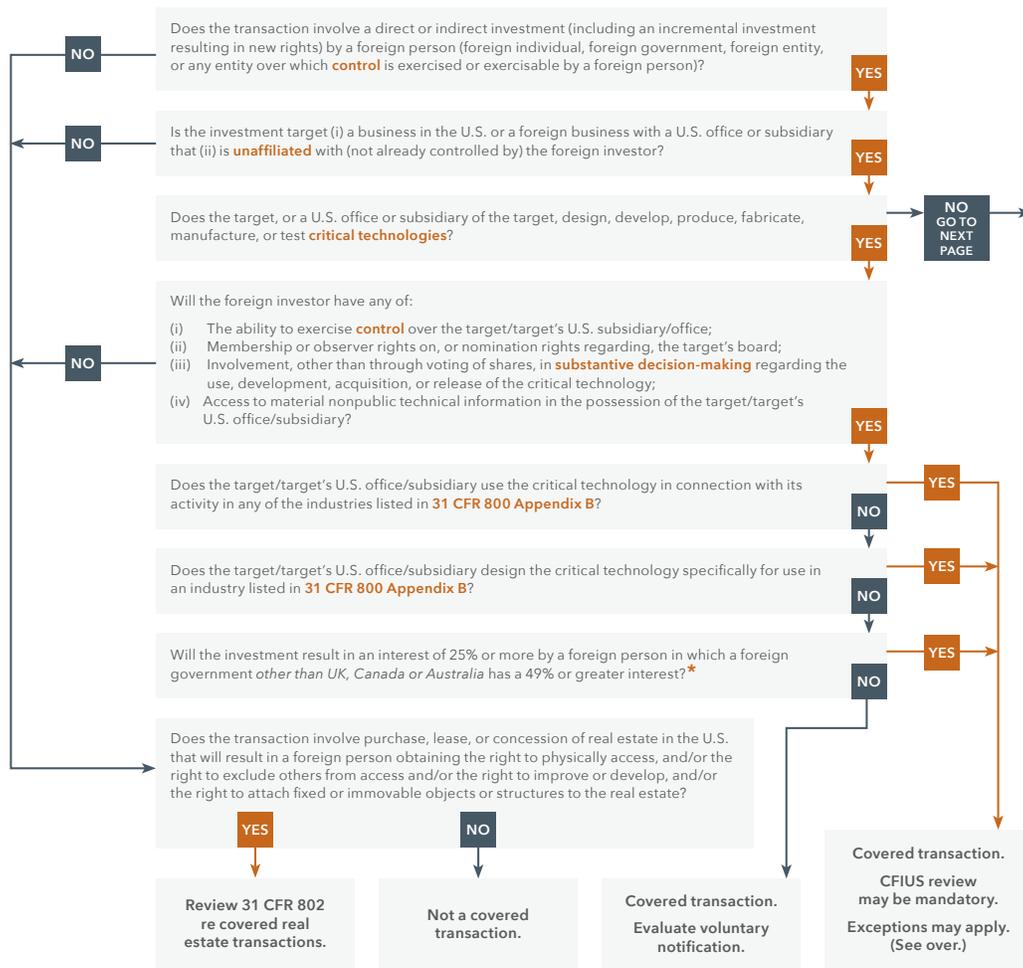
### **V. Navigating the jurisdictional maze**

The new rules are complex (occupying over 200 pages in the Federal Register) and impossible to summarize in just a couple of pages. The full text of the rules can be found [here](#) and (for real estate transactions) [here](#). But to assist in orienting investors and their counsel to the new landscape, we offer the following **flow chart**.

For more information on the new CFIUS rules and advice on whether and how to seek CFIUS approval for a covered transaction, please contact [Tahlia Townsend](#) or [David Hall](#) of Wiggin and Dana's International Trade Compliance practice.

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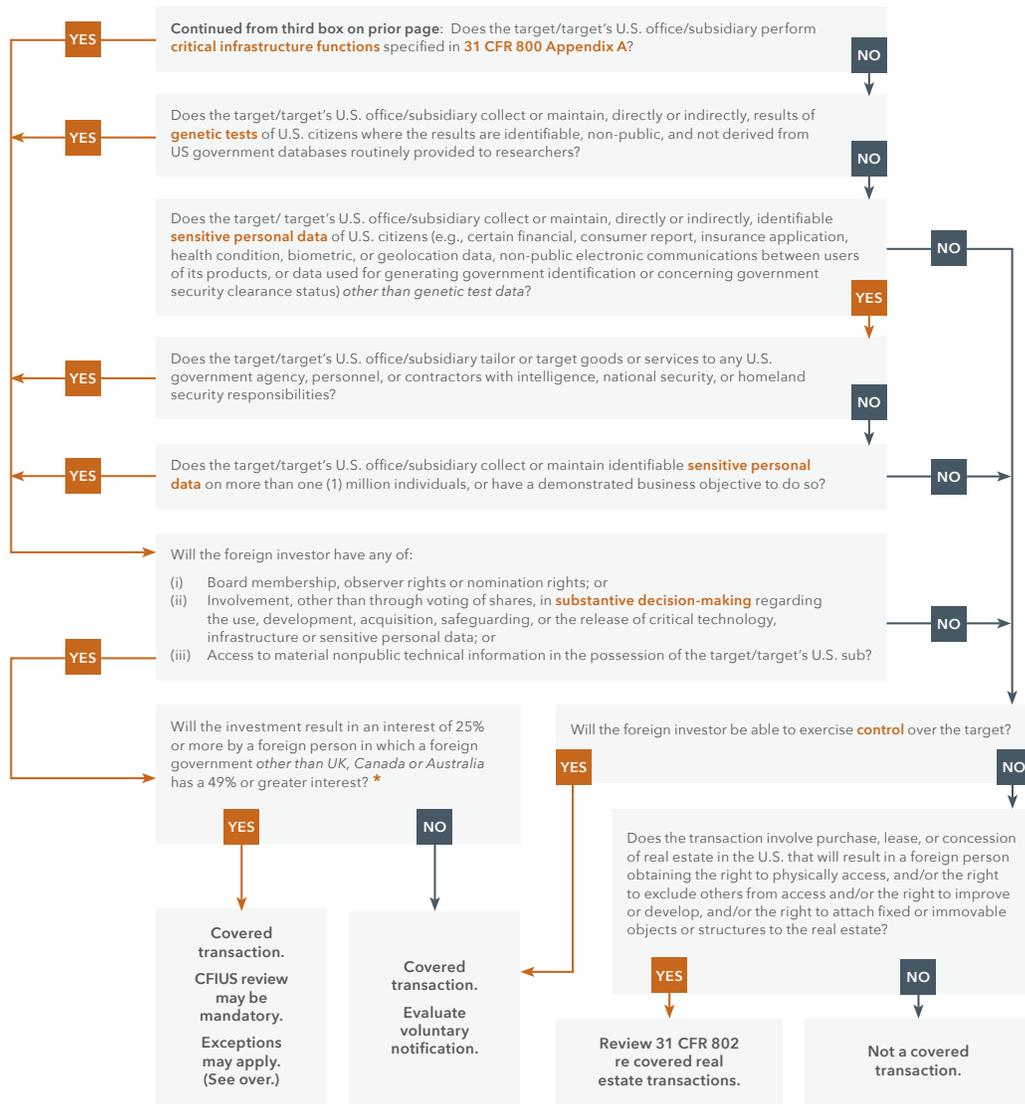
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\* The UK, Canada, and Australia have excepted foreign state status until February 13, 2022, at which point CFIUS must decide whether these countries' own foreign investment rules are sufficiently robust to justify continuation of the status. Other foreign states may also be added in future.

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## Glossary of additional terms

**Control:** The power, direct or indirect, whether or not exercised, through the ownership of a majority or a dominant minority of the total outstanding voting interest or otherwise (e.g., board representation, proxy voting, contractual arrangements) to determine, direct, or decide “important matters affecting an entity,” such as: disposition of assets; reorganization/merger/dissolution; closing/relocation/alteration of facilities; major expenditures/investments; issuance of debt/equity; approval of operating budget; selection of new ventures; entry into/termination of significant contracts; appointment or dismissal of officers, senior managers, or general partner; appointment or dismissal of employees with access to sensitive technology; policies/procedures from handling non-public technical, financial or other proprietary data; amendment of organizational documents with respect to the foregoing matters. Excludes standard minority shareholder protections, i.e., the right to purchase an additional interest in an entity to prevent dilution, and the power to prevent: the sale or pledge of all or substantially all of the assets of an entity or a voluntary filing for bankruptcy or liquidation; contracts with majority investors or their affiliates; guaranteeing of the obligations of majority investors or their affiliates; change of existing legal rights or preferences of a particular class of stock held by minority investors; or amendment of the Articles of Incorporation other organizational documents regarding such matters. See [31 CFR 800.208](#).

**Genetic tests:** “An analysis of human DNA, RNA, chromosomes, proteins, or metabolites, that detects genotypes, mutations, or chromosomal changes,” but “does not mean – (i) an analysis of proteins or metabolites that does not detect genotypes, mutations, or chromosomal changes; or (ii) an analysis of proteins or metabolites that is directly related to a manifested disease, disorder, or pathological condition that could reasonably be detected by a health care professional with appropriate training and expertise in the field of medicine involved.” [42 U.S.C. 300gg-91\(d\)\(17\)](#).

**Substantive decision-making:** Decision-making on significant matters such as: (1) Pricing, sales, and specific contracts, including the license, sale, or transfer of sensitive personal data to any third party, including pursuant to a customer, vendor, or joint venture agreement; (2) Supply arrangements; (3) Corporate strategy and business development; (4) Research and development, including location and budget allocation; (5) Manufacturing locations; (6) Access to critical technologies, covered investment critical infrastructure, material nonpublic technical information, or sensitive personal data, including pursuant to a customer, vendor, or joint venture agreement; (7) Physical and cyber security protocols, including the storage and protection of critical technologies, covered investment critical infrastructure, or sensitive personal data; (8) Practices, policies, and procedures governing the collection, use, or storage of sensitive personal data, including: (i) The establishment or maintenance of, or changes to, the architecture of information technology systems and networks used in collecting or maintaining sensitive personal data; or (ii) Privacy policies and agreements for individuals from whom sensitive personal data is collected setting forth parameters regarding whether and how sensitive personal data may be collected, maintained, accessed, or disseminated; or (9) Strategic partnerships.” Excludes “strictly administrative decisions.” See [31 CFR 800.245](#).