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The Trump Administration Expands the Scope of Investments Covered By National Security Reviews, Imposes New Mandatory Filing Requirements

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On October 11, 2018, the U.S. Treasury Department issued new interim regulations that significantly expand the scope of national security reviews of in-bound foreign investments in U.S. companies and make filings with the Committee on Foreign Investment in the United States (CFIUS) mandatory under certain circumstances. These new regulations implement portions of the Foreign Investment Risk Review Modernization Act (FIRRMA) that was signed into law on August 13, 2018, as part of the John S. McCain National Defense Authorization Act for Fiscal Year 2019. As discussed previously, FIRRMA is a response to growing concerns over the trade and industrial policies of certain foreign countries (especially China) and is aimed at increasing CFIUS' authority to review and regulate investments in U.S. businesses and critical U.S. technology and infrastructure that may implicate U.S. national security concerns.

The new regulations issued by CFIUS do two things. First, they implement largely technical changes to the existing CFIUS review process. This process allows foreign investors in U.S. businesses to obtain "safe harbor" protection for their investments by filing detailed voluntary disclosures with CFIUS. Absent such safe harbor reviews, CFIUS can order the blocking or unwinding of transactions that CFIUS determines afford the foreign investor "control" via a merger, acquisition, or takeover of a U.S. business that implicates U.S. national security concerns.[1] FIRRMA made a number of technical changes to this existing review process, including further defining the scope of covered transactions and including a new category of export-controlled "emerging and foundational technologies" under the list of industries and technologies presumed to raise national security concerns. The latest interim regulations implement many of these changes and apply to all covered transactions subject to CFIUS reviews on or after October 11, 2018.

Second, the new regulations dramatically expand the scope of CFIUS jurisdiction to cover controlling and certain non-controlling investments in any U.S. business that produces, designs, tests, manufactures, fabricates or develops a critical technology utilized in connection with (or otherwise designed by the U.S. business for use in) one or more covered industries, as defined by 27 categories under the North American Industry Classification System (NAICS):

Aircraft Manufacturing NAICS Code: 336411 Powder Metallurgy Part Manufacturing NAICS Code: 332117 Aircraft Engine and Engine Parts Manufacturing NAICS Code: 336412 Power, Distribution, and Specialty Transformer Manufacturing NAICS Code: 335311 Alumina Refining and Primary Aluminum Production NAICS Code: 331313 Primary Battery Manufacturing NAICS Code: 335912 Ball and Roller Bearing Manufacturing NAICS Code: 332991 Radio and Television Broadcasting and Wireless Communications Equipment Manufacturing NAICS Code: 334220 Computer Storage Device Manufacturing NAICS Code: 334112 Research and Development in Nanotechnoloy NAICS Code: 541713 Electronic Computer Manufacturing NAICS Code: 334111 Research and Development in Biotechnology (except Nanobiotechnology) NAICS Code: 541714 Guided Missile and Space Vehicle Manufacturing NAICS Code: 336414 Secondary Smelting and Alloying of Aluminum NAICS Code: 331314 Guided Missile and Space Vehicle Propulsion Unit and Propulsion Unit Parts Manufacturing NAICS Code: 336415 Search, Detection, Navigation, Guidance, Aeronautical, and Nautical System and Instrument Manufacturing NAICS Code: 334511 Military Armored Vehicle, Tank, and Tank Component Manufacturing NAICS Code: 336992 Semiconductor and Related Device Manufacturing NAICS Code: 334413 Nuclear Electric Power Generation NAICS Code: 221113 Semiconductor Machinery Manufacturing NAICS Code: 333242 Optical Instrument and Lens Manufacturing NAICS Code: 333314 Storage Battery Manufacturing NAICS Code: 335911 Other Basic Inorganic Chemical Manufacturing NAICS Code: 325180 Telephone Apparatus Manufacturing NAICS Code: 334210 Other Guided Missile and Space Vehicle Parts and Auxiliary Equipment Manufacturing NAICS Code: 336419 Turbine and Turbine Generator Set Units Manufacturing NAICS Code: 333611 Petrochemical Manufacturing NAICS Code: 325110

Non-controlling investments in the above categories are subject to mandatory CFIUS reporting if they permit the foreign investor: (i) access to “any material nonpublic technical information” in possession of the U.S. business; (ii) membership or observer rights on the board of directors or equivalent governing body of the U.S. business, (iii) the right to nominate an individual to a position on the board of directors or equivalent governing body of the U.S. business; or (iv) any involvement, other than through voting of shares, in the substantive decision-making of the U.S. business regarding the use, development, acquisition or release of critical technology.

Mandatory reports can be made via a standard CFIUS notice filing or through a new short-form “declaration.” The declaration is an abbreviated notice that generally should not exceed five pages in length. Upon filing of a declaration, CFIUS has 30 days to respond. Within those 30 days, CFIUS can notify the parties that it has completed its review without action (effectively clearing the transaction), request the filing of a full notice, unilaterally initiate a full review, or inform the parties that the declaration was not sufficient to allow CFIUS to complete its review and that they may submit a full notice. If the declaration or full written notice is not submitted by the relevant deadline (i.e., on or “promptly after” November 10, 2018, for transactions expected to close between November 10 and December 25, 2018, or, for all other transactions, at least 45 days prior to the transaction’s expected closing), Treasury may assess civil penalties up to the value of the transaction.

Importantly, the new mandatory reporting requirements are not limited to investments by foreign persons from any specific countries. Accordingly, any investment by a foreign person in a U.S. business that develops or produces technology for or is involved in one of the 27 industries listed above should be carefully vetted from an export control and jurisdictional standpoint early on in the transaction.

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[1] The definition of “control” can vary with the facts and circumstances of each case but is typically presumed to exist in the case of transactions that result in the acquisition of voting shares in excess of 10 percent of total voting shares.

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