

CFIUS: Insights and Overview

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AGENDA

CFIUS's **legal and regulatory** environment

CFIUS's **issues**

Risks and **risk mitigation**

What to look for during **due diligence**

Questions

LEGAL AND REGULATORY ENVIRONMENT

Identifies CFIUS as an executive branch authority and focuses on defense, military, and national security issues.

Originated in **1975** under President Gerald R. Ford

Managed solely by the **executive** branch without congressional input until **1988**

In 1988, Congress passed the **Exon-Florio** Amendment to the Defense Production Act

In 1993, Congress passed the **Byrd Amendment**

Mandated investigations of all transactions involving foreign governments or foreign government representatives.

LEGAL AND REGULATORY ENVIRONMENT

Expanded the definition of covered transactions by including covered control transactions and certain real estate transactions.

In 2007, Congress passed the Foreign Investment and National Security Act of 2007 (**FINSA**)

In 2018, Congress passed the Foreign Investment Risk Review Modernization Act of 2018 (**FIRRMA**)

In October 2018, the Department of the Treasury implemented a **pilot program** under FIRRMA

In September 2019, **proposed regulations** under FIRRMA issued

On February 13, 2020, **FIRRMA regulations finalized** and transactions subject to final rules

Based on the Dubai Ports acquisition. Expanded CFIUS's jurisdiction to cover critical infrastructure, including telecommunications, finance, banking, law enforcement and safety, public welfare, and research & development.

LEGAL AND REGULATORY ENVIRONMENT

CFIUS Composition, Mandate, and Process

FINSA means that CFIUS now provides for formal congressional oversight of CFIUS

- Including transaction reporting in classified and unclassified form

Composed of the major cabinet agencies

- Treasury, State, Defense, Homeland Security, Energy, Commerce, Justice, and the intelligence agencies

Additional participants on an as-needed basis

- The CIA, NSA, Agriculture, Transportation, FDA, USTR, Office of Science and Technology, OMB, various assistants to the President for National Security Affairs, Homeland Security, Economic Security and Counterterrorism, etc.

Chaired by Treasury with individual co-lead agencies for each transaction

Director of National Intelligence and Labor are ex officio members

- Provide input on the foreign parties involved in the transaction and industrial base labor issues

LEGAL AND REGULATORY ENVIRONMENT

CFIUS Composition, Mandate, and Process

Exon-Florio, FINSA, and now FIRREA mandate that CFIUS examine the national security implications of cross-border activities

- Mergers, acquisitions, investments, or other forms of ownership or control in US businesses
- Includes minority investments that allow access to "material non-public information" or certain governance rights even if there is no control

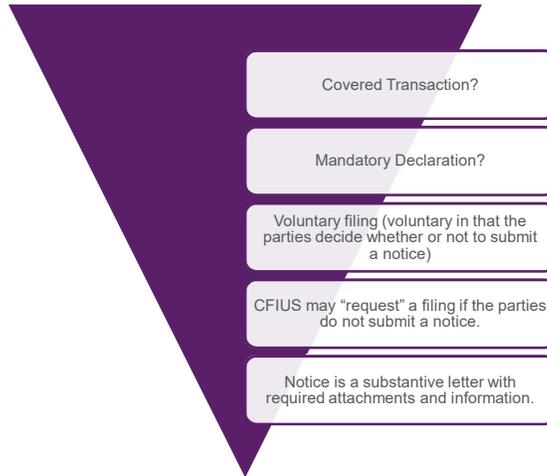
National security focus with an economic overlay

- All cross-border activities are examined in light of the United States' stated policy of encouraging foreign investment in the United States
- FIRREA contains exclusions for limited number of foreign countries to make investments without review

The constituent members of CFIUS bring their legal, policy, and regulatory predispositions to each transaction reviewed.

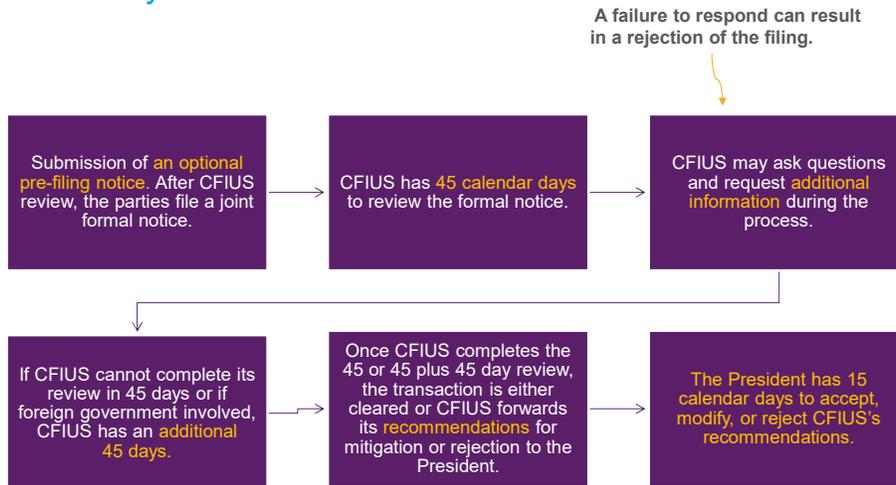
LEGAL AND REGULATORY ENVIRONMENT

Process



CFIUS Filing Process

Voluntary Notices



CFIUS Filing Process

Declarations (Mandatory or Voluntary)

An abbreviated form:

- 5-7 pages in length

Shorter timeline:

- Where required, must be filed 45 days prior to the transaction's expected completion date
- CFIUS has 30 days to review

Potential outcomes:

- Cleared; "request" a notice; inform parties they "may" file notice; undertake unilateral review

Mandatory for certain transactions:

- U.S. businesses involved in "critical technologies," "critical infrastructure," or "sensitive personal data" -- also known as TID U.S. businesses (see next slide).
- Specified covered transactions where a foreign government has a "substantial interest"

Failing to file when required can result in civil monetary penalty:

- Up to the value of the transaction

Proposed Rule

Mandatory Declaration Requirement for Critical Technologies

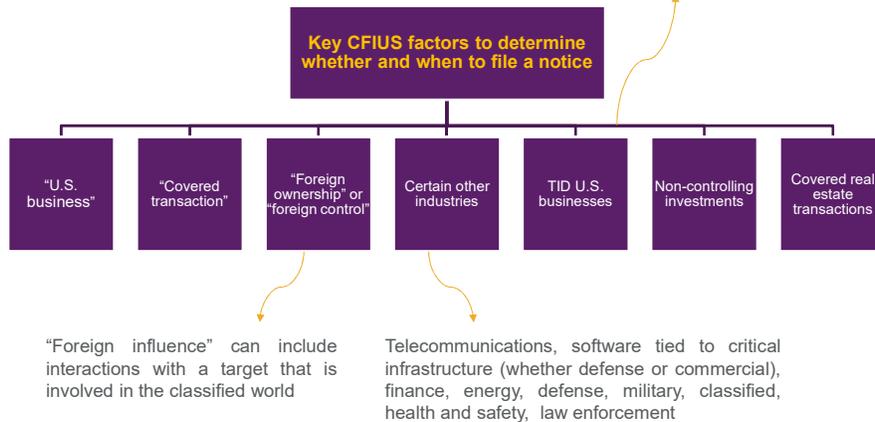
Current rule: Mandatory declaration required if, among other things, the U.S. business produces, designs, tests, manufactures, fabricates, or develops a critical technology utilized in connection with the U.S. business's activity in, or designed by the U.S. business for use in, one of 27 industries identified by NAICS codes.

Proposed Rule: Mandatory declarations required if the critical technologies that the U.S. business produces, designs, tests, manufactures, fabricates, or develops require a U.S. regulatory authorization to export, re-export, transfer, or retransfer to the foreign persons involved in the transaction or certain foreign persons in the ownership chain as specified in § 800.401(c)(1)(i)-(v).

- "U.S. regulatory authorization": license or authorization from the Department of State under the ITAR, the Department of Commerce under the EAR, the Department of Energy (10 CFR part 810), or the Nuclear Regulatory Commission (10 CFR part 110).

CFIUS Review Jurisdiction: “Covered Transactions”

U.S. businesses that produce, design, test, manufacture, fabricate, or develop a “critical technology,” involve “critical infrastructure” or hold or deal in “sensitive personal data” of U.S. citizens (TID U.S. Businesses)



CFIUS Review Jurisdiction: “Covered Transactions” “U.S. business” - Broadly Defined

Includes but not limited to:

- Existing U.S. manufacturing concerns
- Any entity in the U.S. that provides a service, product or technology in any form
- “Any person engaged in interstate commerce in the United States”
- Any “working” assets (combination of employees, IP, technology and/or customers in the U.S.)
- Whatever CFIUS “deems” a “U.S. business”

Could affect non-U.S. transactions that include U.S. assets

CFIUS Review Jurisdiction: “Covered Transactions”

Control

- Mergers
- Acquisitions - 100% or any percentage between 10% and 100% or if CFIUS considers it “covered” as a result of actual or potential control
- Credit Agreements
- Leases
- Joint Ventures
- Asset Purchases

Non-controlling investments

- Applies to TID U.S. Businesses
- Includes non-controlling investments at any level, provided specific coverage triggers are met:
 - (1) Access to material non-public information; and
 - (2) Specified governance / board membership rights

Certain real estate transactions

- Property or greenfield locations that are proximate to sensitive government installations
- Identified by geolocation and regulation annex

CFIUS Review Jurisdiction: “Covered Transactions”

Things that are *not* covered transactions

CFIUS regulations identify certain transactions or investments that are “presumptively” not covered:

10% or less foreign investment or interest **AND** only if for investment purposes

- No longer true for certain (“TID”) businesses under FIRRMA Rules

Stock splits

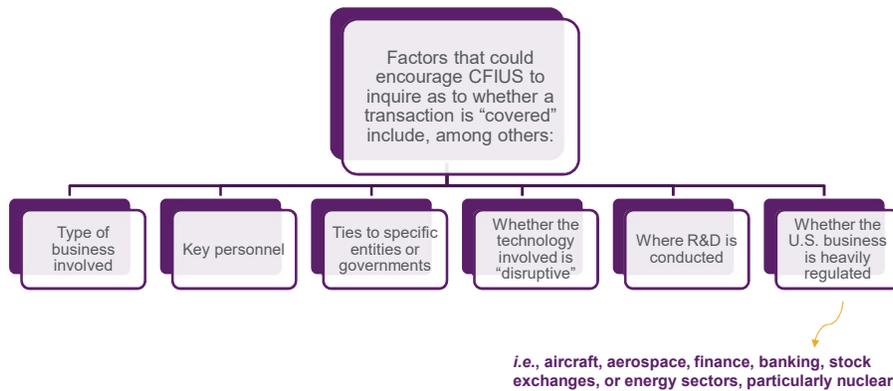
Pro rata stock dividend (as long as it does not result in a change in control)

Securities underwriter acquisition in the “ordinary course of business”

Insurance contract acquisition if made in the “ordinary course of business”

CFIUS Review Jurisdiction: “Covered Transactions”

CFIUS can seek information on non-noticed transactions, typically beginning with an assessment whether a transaction is covered and thus subject to review.



CFIUS Review Jurisdiction: “Covered Transactions”

Covered Control Transactions



CFIUS Review Jurisdiction: “Covered Transactions”

Covered Non-Controlling Investments

CFIUS jurisdiction over foreign investments that give foreign persons:

Access to any material nonpublic technical information in the possession of the U.S. business

Membership or observer rights on or the right to nominate an individual to the U.S. business's board of directors or governing body

Any involvement, other than through voting of shares, in substantive decision-making of TID U.S. businesses regarding:

- The use, development, acquisition, safekeeping, or release of sensitive personal data of U.S. citizens maintained or collected by the U.S. business;
- The use, development, acquisition, or release of critical technologies; or
- The management, operation, manufacture, or supply of critical infrastructure

Certain foreign persons and/or investors are excepted

- Based on their ties to foreign states - currently Canada, U.K., and Australia
- Certain indirect investments by foreign persons through an investment fund are not covered investments

CFIUS Review Jurisdiction: “Covered Transactions”

Covered Real Estate Transactions

Real estate that is within, or will function as part of an air or maritime port

Real estate that is within “close proximity” (defined as one mile) of certain specified U.S. military installations;

Real estate that is within the “extended range” (defined as between one mile and 100 miles) of certain military installations; and

Real estate that is within certain geographic areas associated with missile fields and offshore ranges.

Exceptions:

- Certain “excepted real estate investors” based on their ties to certain countries identified as “excepted real estate foreign states,” and their compliance with certain laws, orders, and regulations

CFIUS ISSUES

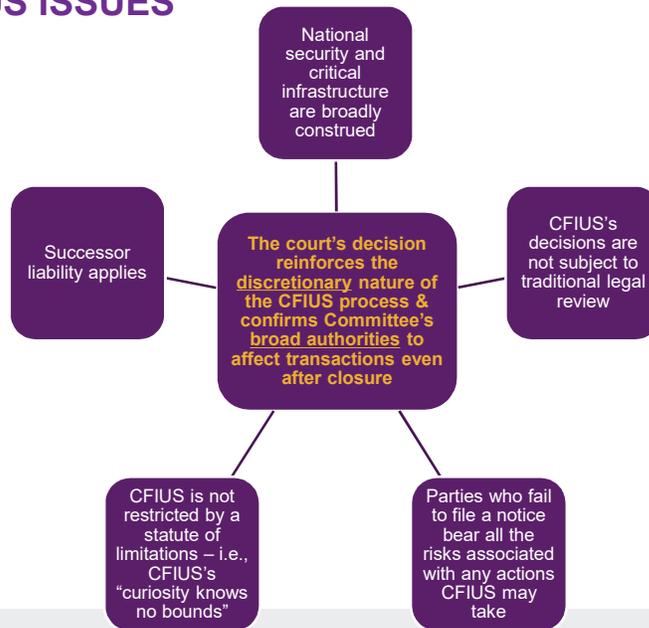
Court cases have highlighted the scope of CFIUS' discretion and affected the risks associated with CFIUS filings

When voluntary, companies sometimes choose not to file, but wait for CFIUS to reach out and request a filing

This approach may be appropriate in some contexts, but the decision in *Ralls v. CFIUS* (October 9, 2013) affects the analysis regarding whether to file a CFIUS notice or not

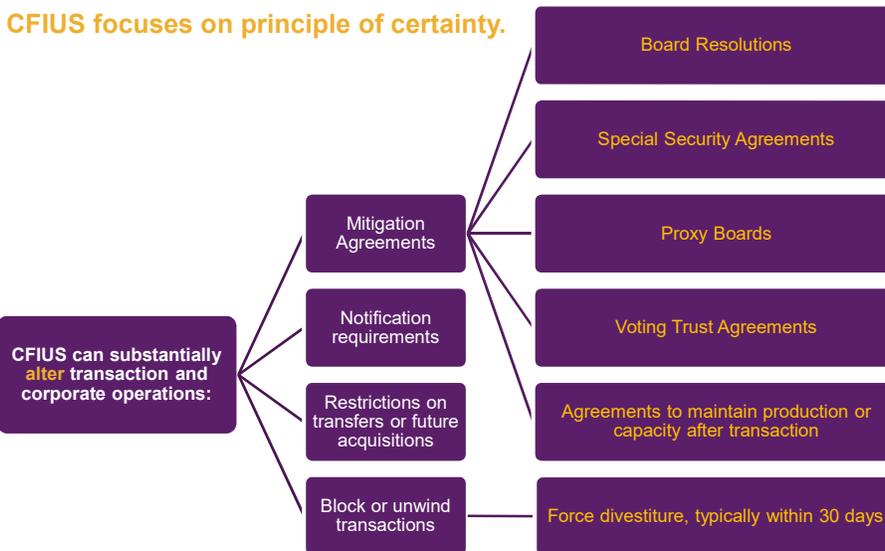
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CFIUS ISSUES



CFIUS Authority

CFIUS focuses on principle of certainty.



RISK AND RISK MITIGATION

Risk calculus is predicated on the degree and depth of due diligence conducted

Due diligence is generally affected by deal timing, seller cooperation, number of potential purchasers, technology/products/customers at issue and skill of the purchaser's advisors (both counsel and consultants)

Even within a *caveat emptor* environment, risks can be mitigated through baseline due diligence requirements that apply in all transactions

Baseline due diligence should include an analysis of those elements necessary to ensure a "file/no file" CFIUS decision is well supported and reasonable

RISK AND RISK MITIGATION

Determine the drivers: "investment banker v. counsel"

Determine the purchase/investment driver: "one purchaser v. many purchaser" candidates

Assess and verify the seller's counsel's/consultant's CFIUS and regulatory experience and expertise

Analyze seller responses to due diligence questionnaires:

- E.g., export compliance program, export classifications, CAGE Codes, NAICS Codes, and DPAS ratings

WHAT TO LOOK FOR DURING DUE DILIGENCE

Security clearances	Secure facilities	Classified work
Reseller and/or distributor agreements	Methods of distribution	Proximity to U.S. government facilities in relation to the target – whether in the U.S. or abroad
Nondisclosure agreements – whether customer or evaluative	Export classifications	Evaluation of TID U.S. Business Factors

WHAT TO LOOK FOR DURING DUE DILIGENCE

Compliance programs – whether formal or informal:

- Export
- Human resources
- FCPA or anti-corruption
- Fees and commissions under export laws
- IT and cybersecurity

Employee base:

- Visa holders, wherever located and employed if tied to the United States business

List of all countries in which the business conducts any activities, has any resources, or where customers do business:

- Sales, marketing, manufacturing, development, IP ownership, R&D, technology or software development

New TikTok Executive Order

Requires ByteDance to divest from Musical.ly on national security grounds

The EO gives ByteDance, the Chinese owner of TikTok, 90 days to divest from its American assets that enable its operation of TikTok in the United States and any data that ByteDance has obtained or derived from U.S. users.

The EO rests on a finding that the acquisition of Musical.ly, which ByteDance then merged with TikTok, threatens to impair U.S. national security.

- Specifically, the concern is over the collection of information from Musical.ly / TikTok users, which, according to the U.S., threatens to allow the Chinese Communist Party access to Americans' personal and proprietary information.

CFIUS will have control and monitoring power over the divestment process.

The Case of Beijing Kunlun Technology Company Ltd./Grindr

BKTC purchased a 60 percent interest in Grindr in 2016; BKTC completed the acquisition in 2018 for ~ \$250 million

Both steps were "covered transactions" under CFIUS

BKTC decided to make no CFIUS filing at either step

By not making a CFIUS filing, CFIUS retained jurisdiction indefinitely to review the transaction

Post-closing reviews usually start with a request by CFIUS to make the filing previously not made

CFIUS then reviews the parties, the assets, the technology to determine if any "national security" risks exist

The Case of Beijing Kunlun Technology Company Ltd./Grindr

Parties then work with and negotiate with CFIUS to determine if divestiture or other mitigation measures are needed

Whether the U.S. business has personal identifier information of United States citizens is considered in the national security evaluation

CFIUS has ordered the divestiture of Grindr, as Grindr was preparing for an IPO

BKTC can certainly sell Grindr

Takeaways:

- Do risk assessment before the deal is closed
- If a decision not to file is made, understand that CFIUS retains jurisdiction indefinitely to require a review and plan for a negative result
- CFIUS has multiple ways to determine deals in the offing or that have closed, so be prepared

Thank you!



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QUESTIONS?