An Overview of CFIUS Authority and Process

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The Committee on Foreign Investment in the U.S. (CFIUS) is the federal interagency committee consisting of representatives from 16 U.S. government agencies, chaired by the U.S. Department of the Treasury (the "Treasury Department"). CFIUS reviews the U.S. national security implications of certain transactions (referred to as "covered transactions") involving U.S. businesses or real property made directly or indirectly by foreign persons to determine the effect of such transactions on the national security of the U.S. This overview summarizes key aspects of the CFIUS process as relevant to the transaction context, covering the following topics:

Authority

CFIUS's authority is limited to "covered transactions," which fall within two types of transactions: (A) transactions involving "U.S. business"1 (see points 1 and 2 below); and (B) transactions involving "covered real estate" (certain U.S. real property, in point 3 below).

> Practice Note: the term "U.S. business" is broadly defined by CFIUS and could apply to entities or assets that are not conducting commercial operations, are dormant or idle, or are in the planning stages of a start-up. CFIUS's authority relating to transactions involving U.S. businesses is by far the most common type of authority exercised by CFIUS, representing approximately 95-98% of recent filings.

Transactions involving U.S. businesses (Part 800 Authority)

1. Covered control transaction – Any transaction that could result in "control"2 of a "U.S. business" directly or indirectly by a foreign person.

> Practice Note: "Control" is a broad concept under the CFIUS laws and can exist even with a minority shareholding – see definition in footnote 2.

2. Covered investment – Any non-controlling "investment"3 directly/indirectly by a foreign person that meets the following criteria:

- The investment is in a "Technology, Infrastructure and Data (TID) U.S. business,"4 which means it has certain defined involvement with "critical technology," "covered investment critical infrastructure" or the collection and maintaining of US citizen "sensitive personal data."
- The subject investment provides the foreign person, directly or indirectly, with any of the following access, *governance or involvement* rights:
  - Access to any "material nonpublic technical information" in the possession of the TID U.S. business that relates to any applicable critical technology or covered investment critical infrastructure
  - Membership or observer rights on, or the right to nominate an individual to a position on, the board of directors or equivalent governing body of the TID U.S. business
  - "Involvement,"5 other than through voting of shares, in substantive decision-making of the TID U.S. business.

> Practice Note: "Involvement" is a broad concept under the CFIUS laws and captures a broad range of actions typical of non-passive investors – see definition in footnote 5.

Transactions Involving U.S. Covered Real Estate (Part 802 Authority)

3. Covered real estate transactions – Any transaction resulting in the direct or indirect acquisition of defined "real property rights"6 by a foreign person in covered real estate, which consists of real property located within enumerated strategic airports and maritime ports, or within defined proximities to enumerated military installations in the regulations.

> Practice Note: Assessing covered real estate transaction authority requires running diligence on the location of any real property investments to assess whether the location falls within the location or proximity thresholds.

1 The term "U.S. business" means any entity or assets "engaged in interstate commerce in the U.S." See § 800.252.

2 Control means "the power, direct or indirect, whether or not exercised . . . to determine, direct or decide important matters affecting an entity." Control can be through ownership or any "other means" that would give a foreign person the ability to direct or decide important matters. See § 800.208

3 An "Investment" is defined as an acquisition of any amount of equity or contingent equity interest. See § 800.211.

4 "TID U.S. business" means any U.S. business that: (i) produces, designs, tests, manufactures, fabricates, or develops one or more critical technologies; (ii) performs the functions as set forth in the regulations with respect to covered investment critical infrastructure; or (iii) maintains or collects, directly or indirectly, sensitive personal data of U.S. citizens. See § 800.248(a)–(c).

5 "Involvement" means (i) the use, development, acquisition, safekeeping, or release of sensitive personal data of U.S. citizens maintained or collected by the TID U.S. business; (ii) the use, development, acquisition, or release of critical technologies; or (iii) the management, operation, manufacture, or supply of covered investment critical infrastructure. See § 800.211(b)(3).

6 "Property Rights," with respect to real estate, means any of the following rights or abilities: (i) to physically access the real estate; (ii) to exclude others from physically accessing the real estate; (iii) to improve or develop the real estate; and (iv) to attach fixed or immovable structures or objects to the real estate. See § 802.233.

Understanding Voluntary and Mandatory Filings

CFIUS has authority to review any covered transaction, but only a small subset of those covered transactions requires a mandatory filing prior to closing. A filing is mandatory if it meets one of two filing tests summarized below. Even if a filing is not mandatory, parties can decide to voluntarily file with CFIUS for any covered transaction. The majority of filings to CFIUS are voluntary submissions, representing 80% or more of all filings any given year. CFIUS is effectively a voluntary based system, combining aggressive monitoring of non-notified transactions with safe-harbor incentives for filing. Voluntarily filing with CFIUS, and obtaining a CFIUS clearance over a transaction, gives parties a safe harbor from future CFIUS authority, as explained further below.

Mandatory Filing Tests

Unless an exception applies (see following section), any transaction that meets one of following tests must submit a mandatory CFIUS filing (either a full notice or short-form declaration filing – two types of filing options discussed further below). Parties cannot close the transaction until 30 days after filing with CFIUS – but note, the CFIUS review will take longer than 30 days.

1. U.S. Critical Technology Business Test

- A covered control or covered investment transaction in a U.S. business that is a TID U.S. business as a result of "critical technology."
- The subject critical technology would require a "U.S. regulatory authorization"7 to be exported to the foreign person investor, the investor's "parent"8 entities and any of their 25% or greater shareholders.

> Practice Note: An existing investment can become a US Critical Technology Business, at which point any changes which result in more rights to a foreign investor could trigger a mandatory CFIUS filing under this US Critical Technology Business test.

2. Substantial Interest Test

- A covered control or covered investment transaction in a TID U.S. business;
- The transaction involves a 25% or greater interest acquisition in a TID US business; and
- A foreign government (that is not an "excepted state" – see definition in the following section) holds a direct or indirect interest of greater than 49% in the foreign investor.

> Practice Note: For purposes of determining the percentage of interest held indirectly, any interest of a parent will be deemed to be 100% in any entity of which the foreign government is a parent.[9]

Common Exceptions to Mandatory Filings

The regulations provide for certain exceptions to the mandatory filing requirements. If an exception applies, CFIUS still retains authority over the transaction, but filing is no longer mandatory. The parties still retain the option of submitting a voluntary filing. The following are three common exceptions. Note – others may apply depending on the deal structure, and characteristics of the parties.10

1. Exception to U.S. critical technology business test based on TSU, STA or ENC license exceptions under the EAR

A mandatory filing under the US Critical Technology Business test is not required where the sole reason for being a mandatory filing is because the U.S. business produces, designs, tests, manufactures, fabricates or develops one or more critical technologies that is/are eligible for export, reexport or transfer (in country) pursuant to at least one of the following license exceptions under the EAR:

- **Technology and Software (TSU) (15 CFR 740.13)** – Unrestricted, authorizing exports and reexports of operation technology and software; sales technology and software; software updates (bug fixes); "mass market" software subject to the General Software Note; and release of technology and source code in the U.S. by U.S. universities to their bona fide and full time regular employees.
- **ENC (15 CFR 740.17)(b)** – Authorizing export, reexport and transfer (in-country) of systems, equipment, commodities and components that are classified under ECCN 5A002, 5B002, equivalent or related software and technology.
- **STA (15 CFR 740.20) (c)(1)** – Covering exports, reexports and transfers (in-country), including releases within a single country of software source code and technology of foreign nationals.

7 "U.S. regulatory authorization" means: (i) a license or other approval issued by the Department of State under the International Traffic in Arms Regulations (ITAR); (ii) a license from the Department of Commerce under the Export Administration Regulations (EAR); (iii) a specific or general authorization from the Department of Energy under the regulations governing assistance to foreign atomic energy activities at 10 CFR part 810, other than the general authorization described in 10 CFR 810.6(a); or (iv) a specific license from the Nuclear Regulatory Commission under the regulations governing the export or import of nuclear equipment and material at 10 CFR part 110. See § 800.254.

8 "Parent" means, with respect to an entity, a person who or which directly or indirectly: (i) holds or will hold at least 50 percent of the outstanding voting interest in the entity; (ii) holds or will hold the right to at least 50 percent of the profits of the entity, or has or will have the right in the event of dissolution to at least 50 percent of the assets of the entity; or is the general partner, managing member, or equivalent of the entity. Any entity that meets these conditions with respect to another entity (i.e., an intermediate parent) is also a parent of any other entity of which the intermediate parent is a parent. See § 800.235.

9 § 800.244

10 Please see § 800.401 (e) for the full list of exceptions to the mandatory filings (e.g., relating to acquisitions by foreign person owned FOCI cleared entities operating under an agreement with the U.S. Government.)

To be "eligible" for a license exception refers to any requirements imposed by the EAR that must be satisfied prior to export even if no export is to occur. This requires an understanding of the application export controls and export classifications related to the target's U.S. operations.

2. Exception for "Excepted Investors"

A mandatory filing under either test is not required for "excepted investors," which applies to certain investors from Australia, Canada, New Zealand and the UK (each an "excepted state"). Furthermore, CFIUS covered investment and covered real estate transaction authority does not apply to excepted investors.

Excepted investor status is afforded to foreign companies that meet each of the following conditions with respect to itself and each of its parents (if any).11

- Is organized under the laws of an either Australia, Canada, UK, New Zealand or the U.S. (together, "Excepted State");
- Has its principal place of business in an Excepted State;
- 75% or more of the members and 75% or more of the observers of the board of directors or equivalent governing body of such entity are nationals of only one or more Excepted States (if an individual is also a citizen of a state that is not an Excepted State, then that individual cannot be counted to meet the 75% threshold);
- Any shareholder that individually, and or as part of a formal or informal group, holds 10% or more of the outstanding voting interest; holds the right to 10% or more of the profits; holds the right in the event of dissolution to 10 percent or more of the assets or otherwise could exercise control, is either an individual that is a national of only one or more Excepted States, or is an entity that has its principle place of business in, and is organized under the laws of, only one or more Excepted States;
- "The minimum excepted ownership"12 is held by one or more persons who: is either an individual that is a national of only one or more Excepted States, or is an entity that has its principle place of business in, and is organized under the laws of, only one or more Excepted States; and
- Having none of the enumerated violations or adverse actions under U.S. laws in the prior five years, such as for violating a CFIUS mitigation agreement or falsifying a certification to CFIUS.13

11 § 800.219(a)(3)(i)-(v).

12 For the purposes of this criteria, "Minimum excepted ownership" means: (i) with respect to an entity whose equity securities are primarily traded on an exchange in an excepted foreign state or the United States, a majority of its voting interest, the right to a majority of its profits, and the right in the event of dissolution to a majority of its assets; or (ii) with respect to an entity whose equity securities are not primarily traded on an exchange in an excepted foreign state or the United States, 80 percent or more of its voting interest, the right to 80 percent or more of its profits, and the right in the event of dissolution to 80 percent or more of its assets. See § 800.220

13 § 800.219(c)(1) a foreign person is not an excepted investor with respect to a transaction if in the five years prior to the completion date of the transaction, the foreign person, any of its parents, or any entity of which it is a parent has been a subject to any of the listed instances in the provision.

3. Investment Fund Exception

A mandatory filing under either test is not required with respect to a covered transaction by an investment fund if:14

- The fund is managed exclusively by a general partner, a managing member, or an equivalent
- The general partner, managing member or equivalent is:
  - Ultimately controlled exclusively by U.S. nationals
  - Not a foreign person
- With respect to any foreign person with membership as a limited partner on an advisory board or a committee of the fund, such entity does not have the ability to approve, disapprove or otherwise control investment decisions and decisions made by a general partner, a managing member or equivalent. The foreign person does not otherwise have the ability to control investment fund.

Voluntary Filing & "Safe Harbor" Benefit of CFIUS Clearance

Parties to any covered transaction have the option of submitting a voluntary filing to CFIUS, which subjects the covered transaction to CFIUS review. Voluntary filings constitute the majority of CFIUS filings. If CFIUS clears a transaction following its review, the transaction15 enters a safe harbor and cannot be reviewed again by CFIUS absent material misrepresentations or omissions by the parties during the filing and review process. The safe harbor covers what was reported to CFIUS: the acquisition by the buyer and each of its parent entities that were reported in the CFIUS filing.16 Other entities, even if wholly owned by the same ultimate parent, are not included in that CFIUS safe harbor. Without the safe harbor, CFIUS has authority to review the national security implications of the transaction after closing, even years later.

14 See § 800.307(a)(3)-(4).

15 Although a clearance provides a safe harbor, that safe harbor is only applicable to the transaction structure that was cleared by CFIUS to acquire the relevant US business. Thus, any changes to that ownership and control structure, such as reorganizations that would give a new foreign entity control over the acquired US business, could re-trigger CFIUS authority, even if the new foreign entity is wholly owned by the same ultimate controlling entity.

16`The parent entities covered include the buyer and all non-U.S. persons that were reported as having a controlling interest in the CFIUS filing.

Process and Timeline for Filings

Parties to any covered transaction have the option of submitting either a long-form notice filing, or a shortform declaration filing. While the latter reduces the cost and time associated with the filing, the former may provide for better timing certainty and is often preferred for that reason. Under either process, if there is a lapse in U.S. appropriations (aka, U.S. Government shutdown) that impacts a member agency of CFIUS, the time limits under the regulations are tolled, which can significantly prolong the process.

Long-form Notice Filings

Filing a notice to CFIUS is typically a joint filing made by buyer and seller prior to consummating a transaction. Prior to submitting the notice, parties consult with CFIUS and submit a draft notice (called a "prefiling") to ensure that all information will be timely available to CFIUS. CFIUS will then provide comments to this prefiling that the parties must address in a "formal" filing. The timing requirements for this prefiling process can take up to multiple weeks, depending on the scope of the filing and CFIUS's case load at the time of filing. After parties address CFIUS's comments during the prefiling process, parties must submit a formal notice and pay a filing fee, which can range from US$750 to US$300,000 depending on the size of the transaction.

Once CFIUS "accepts" the formal filing, CFIUS is required to complete an initial review within 45 days from the date of acceptance. At the close of this initial review period, CFIUS may elect to clear the transaction with a letter (stating all action under Section 721 has been concluded), or commence a 45-day "investigation," essentially extending the review period, to further assess any possible adverse impact on U.S. national security interests. At any time during the review or investigation period, parties must respond to CFIUS' follow-up requests for information within three business days of the request, or within a longer time frame if the parties make request in writing and the staff chairperson grants that request in writing. If, at the end of the 45-day investigation period, CFIUS has concerns that have not been mitigated, the parties can withdraw and potentially refile to allow for more time to work with CFIUS. Alternatively, CFIUS will send a recommendation to the president to prevent the transaction at the end of the investigation period. The president has 15 days to decide whether to follow CFIUS's approach.

See accompanying chart summarizing the tasks necessary to move through the CFIUS notice process (excluding the unlikely 15-day presidential review period).

Task Description	Duration
• Gather information and draft notice	2-3 weeks
• Pre-filing of notice with CFIUS • CFIUS conducts review of completeness and to identify any information needed for CFIUS review • Address questions and revise notice	2-3 weeks
• Formally submit notice to CFIUS • CFIUS confirms that changes are complete and initiates review	1 week
• 45-day CFIUS review	45 days
• 45-day CFIUS investigation (if no decision in review) ending in CFIUS decision (assuming no Presidential review)	45 days
Total duration without investigation	~3 months
Total duration with investigation	~4.5 months

Short-form Declaration Filings

Short-form, i.e. abbreviated declaration filings usually do not have a "prefiling" (CFIUS may issue comments in some cases, such as when it seeks to delay acceptance or the filing is materially lacking information), and declarations do not require a filing fee. These filings are normally accepted by CFIUS within one week of filing, depending on the workload of CFIUS at that time. Declaration filings must be reviewed by CFIUS within 30 days after "accepting" a completed declaration. After CFIUS's 30-day review of a declaration filing, CFIUS can take one of four actions: (1) request that the parties file a full joint notice; (2) inform the parties that it is not able to clear the transaction on the basis of the declaration and that the parties may file a joint notice if they seek to obtain clearance; (3) initiate a unilateral review of the transaction or (4) clear the transaction.

Because of the uncertainty associated with the review of a declaration filing (i.e., CFIUS is not required to come to a determination as it is for notice filings), parties choose to file a declaration filing in only the most straightforward cases that CFIUS can review quickly. Even if a transaction may ultimately clear after a full 45-day notice review, CFIUS will often not have enough time to complete its diligence during a 30-day declaration review. For example, in cases where the foreign investor has filed repeatedly with CFIUS, so it is known to the agencies and where the U.S. business presents little to no evidence of national security risks, a declaration can be appropriate.

See accompanying chart summarizing the tasks necessary to move through the CFIUS declaration process.

Task Description	Duration
Gather information and draft declaration	1–2 weeks
Filing of declaration with CFIUS CFIUS confirms and accepts declaration (assuming no comments are issued by CFIUS)	1–2 weeks
CFIUS review ending in CFIUS decision	30 days
Total Duration	~2 months

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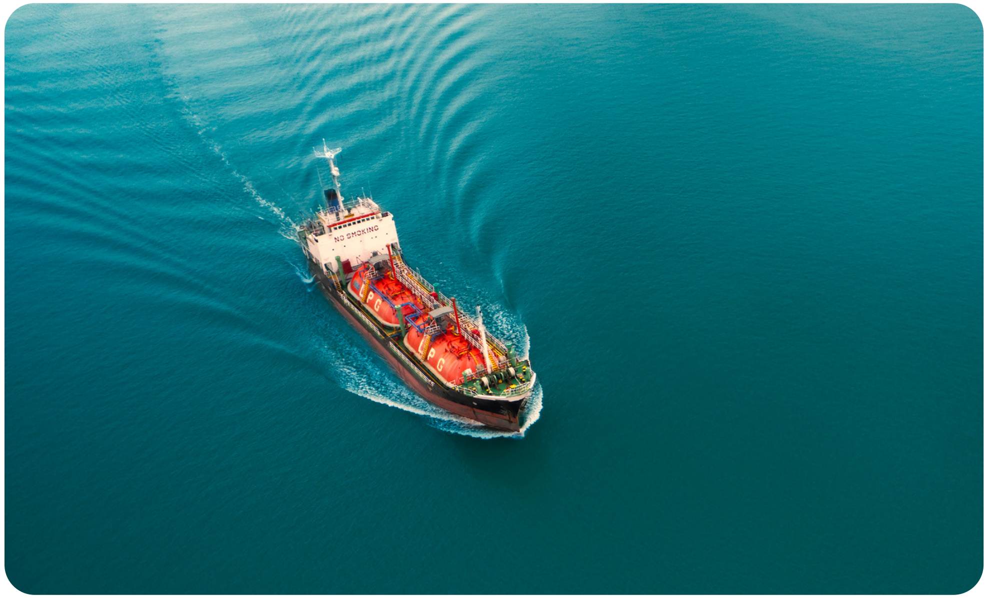

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