Corporate Counsel

How U.S. Companies Can Prepare for New Foreign Investment Rules

By **Priya R. Aiyar** | June 19, 2018

Increased concerns about Chinese investment in U.S. companies, as well as Chinese government policies that result in technology transfers from U.S. companies, have fueled bipartisan support for legislative reform of the foreign investment review process. Statutory changes to the jurisdiction and procedures of the Committee on Foreign Investment in the United States (CFIUS) appear likely this year. On May 22, the Senate Banking Committee and the House Financial Services Committee unanimously approved versions of the most prominent CFIUS reform bill, the Foreign Investment Risk Review Modernization Act (FIRRMA). The bill has now passed the full Senate and would significantly expand the number and types of transactions subject to national security review, as well as establish new controls on the export of technology.

FIRRMA as Introduced and as Amended

While FIRRMA would make a number of changes to the CFIUS process, its most salient feature is the expansion of CFIUS's jurisdiction to review transactions. As originally introduced, FIRRMA would have extended that jurisdiction to, among other categories of transactions, purchases or leases of real estate located near military installations or other sensitive government facilities by a foreign person; nonpassive investments by a foreign person in any U.S. "critical technology company" or "critical infrastructure company," with "passive" investments strictly defined; and contributions of intellectual property by a U.S. critical technology company to a foreign person, with an exclusion for ordinary customer relationships. The latter two provisions drew significant criticism, with representatives of the business and investor communities noting that the definition of "critical technology" was vague, and that the expansion of jurisdiction to any outbound transfer of intellectual property, including through joint ventures, was duplicative of export control regimes.

Legislators were responsive to those concerns, and the versions of FIRRMA advanced in the House and Senate address them in different ways. The Senate version eliminates the provision regarding contributions of intellectual property by U.S. critical technology companies, and instead would establish an interagency process to identify emerging and foundational technologies and authorize the Secretary of Commerce to establish controls on the export of those technologies. he House version does the same, and also replaces the provision relating

to investment in critical technology or critical infrastructure with one giving CFIUS jurisdiction to review "sensitive transactions involving countries of special concern." That term includes investments in a U.S. business that could result in a foreign entity's obtaining sensitive personal data of U.S. citizens, or its influencing of the decision-making of the U.S. business with regard to the use or release of sensitive personal data or critical technologies.

The House bill also incorporates the text of the Export Control Reform Act of 2018, which had been introduced as a separate piece of legislation in February. That legislation would both establish a permanent statutory basis for the Export Administration Regulations and expand the current export control regime, including by broadly defining technology to include "foundational information" and "know-how items." Notably, the House bill does not include the most controversial provision of the Export Control Reform Act of 2018 as originally introduced, which would have subjected transactions between U.S. companies to export controls if one of the U.S. companies had a foreign parent or majority shareholder.

FIRRMA's Likely Path

The bipartisan, unanimous votes in the House and Senate committees demonstrate the momentum behind tightening foreign investment and export regulations with respect to technology in particular. Moreover, the removal of the most sweeping and problematic provisions of the original FIRRMA and Export Control Act of 2018 make it substantially more likely that one of the modified versions of the legislation will pass. The Senate has attached its version of FIRRMA to its version of the National Defense Authorization Act for 2019 (NDAA), a piece of legislation that Congress must pass annually and that passed the full Senate by an 83 to 10 vote on June 18. Differences between the House and Senate bills could be resolved as part of the conference process on the NDAA, or through a separate conference process if FIRRMA is removed from the NDAA and proceeds as a separate piece of legislation.

Even if no legislation passes, the Trump administration has the authority to accomplish similar changes to foreign investment policy administratively, at least as that policy pertains to China. The administration stated on May 29 that, as part of its response to its investigation of China's trade practices, it would "implement specific investment restrictions and enhanced export controls for Chinese persons and entities related to the acquisition of industrially significant technology," to be announced by June 30. Progress in ongoing U.S.-China trade negotiations may result in changes to the administration's policy or intent, but for now companies should assume that such restrictions may be implemented as soon as this summer.

What Companies Can Do to Prepare

CFIUS reform legislation is more likely than not to pass and to include provisions that allow for national security review and the potential blocking of noncontrolling minority investments by foreign persons in U.S. companies that possess or operate critical technologies, critical infrastructure, and/or sensitive data of U.S. persons. To the extent that companies expect to receive or make such investments in 2018 or 2019, they should consider whether it is possible to structure the investments to fall within the draft legislation's definition of "passive."

Companies that are involved in outbound technology transfers should similarly expect that they may be subject to new export controls, and should be prepared to participate in a rulemaking process led by the Department of Commerce to establish the contours of that

regime. Although both the House and Senate versions of FIRRMA attempt to streamline the CFIUS process in various ways and provide more resources to CFIUS, companies should expect the current trend of longer timelines for CFIUS approvals to continue, given the increased volume of cases and the substantial workload involved in issuing new regulations under a new statute.

Finally, companies should be prepared for restrictions on Chinese investment and export of technology to Chinese persons to come into force prior to or alongside the passage of any legislation as part of the administration's response to China on trade issues. The administration has not yet indicated what specific investment restrictions and controls it envisions, other than through its reference to "industrially significant technology." Companies should be prepared to engage with the Departments of Treasury and Commerce with respect to the scope of those restrictions and controls.

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