
Treasury Department Issues Proposed CFIUS Regulations

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On April 21, the Treasury Department made public new proposed regulations governing the process for review of transactions by the Committee on Foreign Investment in the United States (CFIUS). See http://www.treas.gov/press/releases/reports/proposed_regulations42108.pdf. Comments on the proposed regulations are permitted for 45 days from publication in the *Federal Register*, which will likely occur on or about Wednesday, April 23. If so, comments will be accepted until June 9. The Treasury Department will be holding a public meeting on May 2 to hear comments in person. Those who would like to attend the public meeting must register by April 25.

We expect that much of the focus in coming days will be on the provisions in the proposed regulations that deal with the definition of a "foreign entity" and standards for foreign "control." We have provided a brief synopsis of key provisions below. If you have questions regarding specific provisions or would like to request a more detailed analysis, feel free to contact any of the individuals on our CFIUS team.

Process:

1. Pre-filing consultation. The proposed regulations make express what

we have counseled for years--that parties should contact the CFIUS Committee in advance of filing a formal notice of a transaction. Pre-filing submissions are required to be made at least five days before the actual filing of the voluntary notice. 31 CFR 800.401(f).

2. Certification and penalties. The proposed regulations require all parties to a transaction to certify the accuracy of information provided. 31 CFR 800.701(c). Civil penalties of up to \$250,000 per violation are provided for any "material misstatement or omission," whether made "intentionally or through gross negligence." 31 CFR 800.801(a). The same penalties may apply to violations of a mitigation agreement separate and apart from any damages sought pursuant to the terms of the mitigation agreement itself. 31 CFR 800.801(b). Parties that receive a notice of the imposition of penalties may appeal for relief to CFIUS. 31 CFR 800.801(e).

3. Data required. The proposed regulations impose more detailed requirements for the information that must be included in a voluntary notice. The required information includes more information on parent companies and their shareholders; the identity of all financial institutions involved in the transaction; whether a foreign government or a person controlled by or acting on behalf of a foreign government has "any affirmative or negative rights or powers that could be relevant to" CFIUS review; and biographical and personal identifier information on the board members, senior management, and ultimate beneficial owners of five percent or more of the foreign person involved in the transaction, and of its immediate and ultimate parents. 31 CFR 800.402.

4. Lead agency. The proposed regulations authorize the CFIUS Chairperson to designate one or more agencies as a lead agency for all or a portion of a review, investigation, negotiation, or mitigation agreement

monitoring assignment. This may increase the level of transparency associated with the CFIUS process in terms of identifying key stakeholders, but could also add further levels of complexity as entities and their advisors seek to navigate the CFIUS process with the interests of multiple agencies in mind. 31 CFR 800.218.

Substantive Provisions:

1. **Control.** The proposed regulations adopt a functional definition of "control," and avoid a categorical bright line test. "Control" is *not* defined in terms of specific percentages of shares (such as 51 percent) or a certain number of board seats, but rather by the ability of a foreign person/entity to determine, direct, or decide "important matters affecting an entity." The "control" standard is not triggered by the mere acquisition of "influence" over "important matters." See Overview Discussion at 12. The proposed regulations include a list of 10 "important matters affecting an entity," as well as a list of five minority shareholder protections that are not generally considered to confer "control." While the lists clearly expand upon the existing regulations, most of the new provisions simply codify guidance previously gleaned from the results of particular cases to come before CFIUS. Common minority shareholder protections, such as the power to prevent the sale or pledge of all or substantially all of the assets of an entity and the power to purchase additional shares to prevent dilution, are among the rights that will *not*, in and of themselves, be deemed to confer "control." On the other hand, the ability to select new business lines or ventures that an entity will pursue, and the power to appoint or dismiss officers or senior managers, *are* deemed to be indicia of "control." Section 800.302(c) reaffirms existing guidance that a transaction that results in a foreign person holding 10 percent or less of the voting shares of a US entity is not a covered transaction subject to CFIUS review if the transaction is "solely for the

purpose of investment." Examples following section 800.302(c) appear to suggest, however, that this provision is applicable only when a foreign person or entity does not obtain any indicia of "control," such as the right to a Board seat or special contractual rights relating to the US entity's business. 31 CFR 800.203, 800.223, 800.302.

2. Foreign person/Foreign entity. The proposed regulations broaden the definition of "foreign person" to include "foreign entities," which are defined to mean public companies organized under the laws of a foreign country "whose equity securities are primarily traded on one or more foreign exchanges" and "any other entity" organized under the laws of a foreign country "in which foreign nationals hold, directly or indirectly, at least 50 percent of the outstanding ownership interest." The latter part of the definitions sweeps in entities where the combined ownership of foreign nationals exceeds 50 percent regardless of whether the owners are of different foreign nationalities. 31 CFR 800.212, 800.216.

3. Critical infrastructure/Critical technologies. The proposed regulations track the statutory definition of "critical infrastructure" as "systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of the particular systems or assets of the entity over which control is acquired pursuant to [the] covered transaction would have a debilitating impact on national security," while making clear that this determination is to be made on a case-by-case basis with reference to the particular assets at issue in the proposed transaction. The statutory definition of "critical technologies," however, is expanded upon to incorporate by reference the definitions from various existing regulatory regimes that deal with the export, trade, or handling of sensitive goods, technologies, and services. Specifically, the proposed regulations define "critical technologies" to include, among other things, "[d]efense articles or

defense services covered by the United States Munitions List ... in the International Traffic in Arms Regulations," "[t]hose items specified on the Commerce Control List ... that are controlled pursuant to multilateral regimes (i.e., for reasons of national security, chemical and biological weapons proliferation, nuclear nonproliferation, or missile technology), as well as those that are controlled for reasons of regional stability or surreptitious listening," certain "nuclear equipment, parts and components, materials software and technology specified in the Assistance to Foreign Energy Activities regulations," and "[s]elect agents and toxins specified in the Export and Import of Select Agents and Toxins regulations." The proposed regulations state that voluntary notices filed with CFIUS shall identify, among other things, any "critical technologies" produced or traded by the US business that is the subject of the covered transaction.

Authors



Jamie Gorelick

PARTNER

Chair, Regulatory and
Government Affairs Department

✉ jamie.gorelick@wilmerhale.com

☎ +1 202 663 6500