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## Treasury Issues New CFIUS Interim Rules

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On October 10, 2018, the U.S. Department of the Treasury, acting in its role as chair of the Committee on Foreign Investment in the United States (“CFIUS”), issued two interim rules to implement certain provisions of the Foreign Investment Risk Review Modernization Act of 2018 (“FIRRMA”).

Enacted in August 2018, FIRRMA broadened CFIUS' authority to review a wider range of foreign investments in U.S. businesses, including certain noncontrolling investments. The interim rules:

1. amend the CFIUS regulations to implement those provisions of FIRRMA that took effect immediately upon enactment; and
2. establish a pilot program – which requires the submission to CFIUS of a *mandatory* declaration for certain transactions – to implement certain provisions that did not take effect upon FIRRMA's enactment.

### A. Amendment of CFIUS Regulations to Implement Certain FIRRMA Provisions

Upon FIRRMA's enactment, a number of provisions of the statute took effect immediately on August 13, 2018, including the expansion of the CFIUS review period from 30 days to 45 days. Effective October 11, 2018, the interim rules amend the CFIUS regulations to implement those provisions and update the existing regulations to resolve inconsistencies with FIRRMA.

### B. Pilot Program

FIRRMA authorizes CFIUS to conduct one or more pilot programs to implement any provisions of the statute that did not immediately take effect upon enactment. The newly announced pilot program expands the scope of “covered transactions” subject to CFIUS review to include certain noncontrolling investments made by foreign nationals in U.S. businesses. For an investment to be covered under the pilot program, the investment must give the foreign investor:

- Access to any nonpublic “critical technology” in the possession of the target U.S. business;
- Membership or observer rights on the board of directors or equivalent governing body of the U.S. business, or the right to nominate an individual to a position on the board of directors or equivalent governing body of the U.S. business; or
- Any involvement, other than through voting of shares, in substantive decision making of the U.S. business regarding the

use, development, acquisition, or release of critical technology.

The pilot program applies to any U.S. business that produces, designs, tests, manufactures, fabricates, or develops a “critical technology” that is either: (1) utilized in connection with the U.S. business's activity in one or more of the “pilot program industries”; or (2) designed by the U.S. business specifically for use in one or more “pilot program industries.” The interim rules refer to such U.S. businesses as “pilot program U.S. businesses.”

“Critical technologies” generally include (1) military technologies subject to the International Traffic in Arms Regulations of the U.S. State Department; (2) certain military/civilian dual-use technologies subject to the Export Administration Regulations of the U.S. Commerce Department and controlled (a) pursuant to multilateral regimes addressing national security, chemical and biological weapons proliferation, nuclear nonproliferation or missile technology, or (b) for purposes of regional stability or surreptitious listening; (3) certain specially designed and prepared nuclear technologies governed by rules relating to foreign atomic energy development; (4) select agents and toxins; and (5) certain yet-to-be-determined “emerging and foundational technologies” controlled pursuant to the Export Control Reform Act of 2018. The mandatory disclosure requirement under the FIRRMA regulations will require a U.S. business to know precisely, to the extent not already so determined, the export control regulations governing its products, services, and technology. One also may reasonably anticipate that lenders involved with the U.S. business may soon, to the extent not already done, require information or certifications from the U.S. business upon any foreign investment regarding the applicability of the mandatory CFIUS disclosure rule.

The interim rules identify 27 total “pilot program industries” by their respective North American Industry Classification System (“NAICS”) code which we have listed below in Appendix A.

**Mandatory Disclosure to CFIUS:** As noted above, the pilot program requires mandatory declarations for transactions that fall within the pilot program's scope. This is revolutionary for the CFIUS process which to date has been a voluntary process. Although such mandatory declarations are to be no more than five pages in length, the interim rules require the parties to provide a lengthy list of information in the declarations including: (1) information about the foreign investor and its ownership; (2) a description of the transaction; (3) a description of the U.S. business, including information regarding its business activities; (4) a description of any critical technology that the U.S. business produces, designs, tests, manufactures, fabricates, or develops; (5) information about the U.S. business' government contracts, grants, and funding; (6) the addresses or geographic coordinates of all locations of the U.S. business; and (7) a statement as to whether one or more of the parties to the transaction stipulate that the transaction is covered within the purview of the pilot program, among other items. Parties may elect to submit a full written notification to CFIUS in lieu of the declaration. Parties required to file with CFIUS that do not do so can be assessed a civil monetary penalty up to the value of the transaction.

The new mandatory declarations may have far reaching impacts on transactions that, even only marginally, implicate ITAR technology. Under the interim rules, for example, an acquisition in which a foreign investor acquires a minority interest (including membership on the board of directors and the ability to influence general policies of the U.S. business) in a pilot program U.S. business that produces an ITAR controlled technology which represents only 5% of the U.S. business' sales would fall within the pilot program's scope and be subject to the mandatory declaration process. Although the ITAR already imposes a pre-deal requirement to notify the U.S. State Department, the parties to such foreign investments were not previously subject to mandatory CFIUS submission requirements. Under the new CFIUS disclosure process, the parties must now also make the disclosure pre-deal in the CFIUS context where more active or probing eyes within the U.S. Government appear trained on the transaction.

The word “pilot” may be slightly misleading to the extent that it suggests the pilot program is not applicable uniformly to a potentially broad range of merger, acquisition, and investment circumstances. The pilot program takes effect on November 10, 2018 and is expected to continue and become permanent, with appropriate minor revisions, upon implementation of the final regulations implementing FIRRMA which become effective in early 2020. That said, the pilot program does not apply (1) to transactions that have closed prior to November 10, 2018, or (2) where prior to October 11, 2018 (a) the parties have executed a binding agreement establishing the deal terms, (b) a foreign party has made a public offer to buy shares of the U.S. business, (c) a foreign party has solicited proxies in connection with the election of the U.S. business's board of directors or has requested the conversion of convertible voting securities.

The interim rules reflect the first step in the roll out of the regulations to implement FIRRMA and mandatory notifications to the U.S. Government for many “covered transactions” even where no obvious national security threats appear from the foreign investment in the U.S. business. With the changing CFIUS regulatory and national security oversight landscape, it is increasingly important for parties to transactions involving foreign investment in a U.S. business to identify the precise export control regulations governing a U.S. business' goods, services, and technology and to conduct careful due diligence early to identify factors in the deal that may require CFIUS disclosure or raise CFIUS concerns. Such proactive measures may minimize costly delays in the transaction's closing, or potential CFIUS-ordered post-closing divestment, down the line.

## Appendix A

### Pilot Program Industries

Industry	NAICS Code
Aircraft Manufacturing	336411

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

Storage Battery Manufacturing	335911
Telephone Apparatus Manufacturing	334210
Turbine and Turbine Generator Set Units Manufacturing	333611