

Report from Washington

Key Takeaways From CFIUS's Annual Report Covering The 2014 Calendar Year

February 22, 2016

Introduction

On February 19, 2016, the Committee on Foreign Investment in the United States (“CFIUS” or the “Committee”), the inter-agency committee charged with reviewing foreign investments in U.S. businesses for potential national security implications, released its Annual Report to Congress detailing the Committee’s activity during calendar year 2014. The report offers an overview of the deals that came before the Committee during 2014 and provides insight into trends and touchpoints that may be helpful for parties to consider in making cross-border investments into the United States. Although the data are more than a year old, the increasing number of covered transactions involving Chinese investors, which is a major and controversial topic in the media today, is a trend clearly described in the Annual Report.

The Number of Notices Deemed Covered Transactions Approached a Record High

The annual number of CFIUS notices deemed covered transactions had increased year over year since the end of the financial recession in 2009 through 2012, increasing from 65 filings to 114. That trend ended in 2013 when just 97 notices were reviewed during the year. 2013 proved to be an aberration, however, as 2014 saw a significant jump with 147 notices determined to be covered transactions by the Committee. The 2014 total was just shy of the record high of 155 notices reviewed in 2008. All indications are that the trend will continue and that 2015 was a very active year for CFIUS.

Covered Transactions Involving East Asian Buyers Continue to Outpace the Rest of the World

2012 was the first year in which the number of reviewed transactions involving Chinese investors exceeded the individual total of any other country. The latest report shows that trend continues. In 2014, the number of covered transactions involving Chinese investors

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increased to an all-time high of 24. Between 2012 and 2014, investors from China were involved in 68 covered transactions, which is 23 transactions more than the next highest country over the same period.

Following behind China, Japanese investors were involved in 10 covered transactions in 2014, South Korean investors another seven, and investors from Hong Kong and Singapore were involved in six covered transactions each during the year. While the number of covered transactions involving Japanese investors was down from 2013, the number of transactions involving investors based in South Korea, Singapore, and Hong Kong all increased sharply in 2014.

The Percentage of Filings That Entered the Investigation Stage Has Regressed to the Historical Norm

The percentage of covered transactions proceeding from the initial 30-day review period to the 45-day investigation stage had remained stable between 2009 and 2012, falling within a few percentage points of 38% of covered transactions entering the investigation stage each year. In 2013, however, approximately 50% of notices deemed covered transactions entered the investigation stage. The 2014 data now shows that, similar to the sharp decrease in notified transactions, the percentage increase in investigations appears to have been anomalous. In 2014, CFIUS conducted an investigation in 52 of the 147 instances of notified covered transactions, which is approximately 35%. Although there was a large decline in the percentage of transactions that reached the investigation stage, the absolute number of 52 investigations in 2014 is very close to the 48 investigations conducted in 2013.

The Number of Notices Withdrawn During the Investigation Phase Increases

In 2014, nine of the 52 investigated covered transactions resulted in withdrawn notices, or about 17%. While the 2014 data indicates noticeably more withdrawn notices than 2013 when approximately 10% of notices were voluntarily withdrawn during the investigation stage, the percentage does remain considerably lower than 2012 where nearly 50% of investigations resulted in withdrawn notifications.

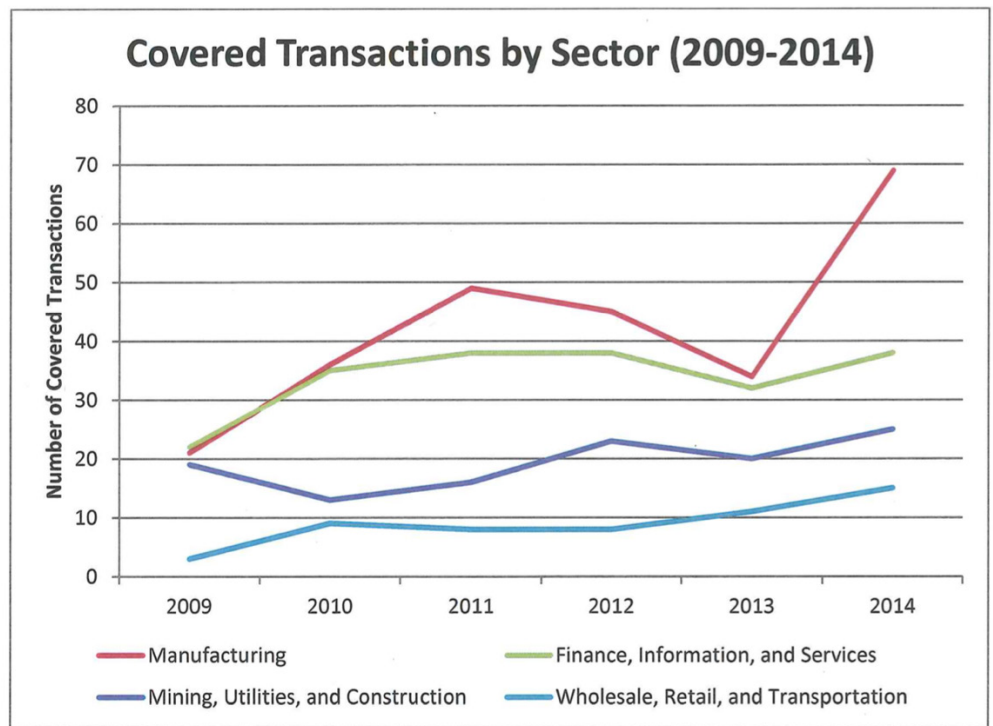
As in previous years, the latest Annual Report does not disclose the transaction-specific circumstances of withdrawals, but does acknowledge that some notices were withdrawn and refiled with approval of CFIUS to allow the Committee more time to consider national security concerns. Other notices were withdrawn and never refiled because the underlying transactions were abandoned either entirely or at least with respect to the involvement of the foreign party that prompted the notice.

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The Margin By Which Manufacturers Continue to be the Most Frequent Targets in Covered Transactions Widens

Each year, the Annual Report categorizes the sector of the U.S. target as either manufacturing; finance, information, and services; mining, utilities, and construction; or wholesale, retail, and transportation. In 2014, 69 of 147, or approximately 47%, of notices involved targets that were categorized as manufacturers. This is up from 36% in 2013.

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Covered Transactions by Sector 2009-2014

Computer and electronic product manufacturers continue to represent the largest share of the manufacturer sector targets, but 2014 was not an exceptionally high year for that subsegment. Rather, the widened margin is attributable to an uptick in chemical manufacturers and plastics and rubber manufacturers, both of which were targeted at notably higher levels in notified covered transactions in 2014.

The Committee Continues to Request Mitigation Measures to Address National Security Concerns

In 2014, nine transactions were approved only after the Committee negotiated legally binding mitigation measures. Those transactions involved U.S. companies involved in

telecommunications, software, services, and technology industries. Mitigation measures negotiated and adopted in 2014 included:

- Ensuring that only authorized persons have access to certain technology and information;
- Establishing a Corporate Security Committee and other mechanisms to ensure compliance with all required actions, including the appointment of a U.S. Government-approved member of the board of directors;
- Establishing guidelines and terms for handling existing or future U.S. Government contracts, U.S. Government customer information, and other sensitive information;
- Ensuring that only U.S. citizens handle certain products and services, and ensuring that certain activities and products are located only in the United States;
- Notifying relevant U.S. Government parties of any awareness of any vulnerability or security incidents; and
- Providing relevant U.S. Government parties with the right to review certain business decisions and object if they raise national security concerns.

The U.S. Intelligence Community's Conclusion of a Likely Coordinated Foreign Strategy to Acquire Critical Technology Companies is Restated

Based on its assessment of transactions identified by CFIUS in its report for the 2014 calendar year, the U.S. Intelligence Community concluded that there may be an effort among foreign governments or companies to acquire U.S. companies involved in research, development, or production of critical technologies for which the United States is a leading producer.

This finding is consistent with the annual report for 2013, but contrasts with the conclusion contained in the 2012 report in which the Intelligence Community found it unlikely that such a coordinated strategy existed. The unclassified version of the report available to the public does not discuss the underlying reasons for this conclusion.

Although some commentators have criticized the CFIUS review process for its lack of transparency, the Committee continues to clear an overwhelming majority of the transactions it reviews. That said, the number of transactions subject to investigations and the increased number of withdrawn notices in 2014 are clear indications that parties to transactions with a nexus to U.S. national security are well-advised to conduct a pre-transaction CFIUS risk analysis.

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