

Treasury proposes new CFIUS rules on enforcement and mitigation

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MAY 2, 2024

Introduction

On April 11, 2024, the U.S. Department of the Treasury (“Treasury”) proposed significant changes to the rules governing the Committee on Foreign Investment in the United States (“CFIUS” or the “Committee”) concerning enforcement and procedural aspects of its authorities.

The new rules will obligate transaction parties to respond to any mitigation proposal presented by the Committee within three business days unless a formal request for extension is granted.

As detailed below, the proposed rules (i) compress the timeline for parties to negotiate mitigation agreements; (ii) expand the Committee’s ability to investigate compliance and demand a broader scope of information from parties to the transaction and third parties not directly involved in a transaction; and (iii) increase the range of penalties for certain violations.

As may be relevant for dealmakers, asset managers, and other institutional investors, the proposed rules do not modify or expand the Committee’s jurisdiction or the types of transactions that are notifiable. Nevertheless, these changes and the overall tone of the proposed rules exhibit a continued focus and priority by the Committee under the current Administration on investigation, enforcement, and mitigation.

We expect these proposed rules to broaden existing administrative practices around investigations concerning non-notified transactions, increase the scope and distribution of information demands from the Committee, and accelerate the Committee’s ability to impose mitigation on parties in a variety of contexts.

CFIUS compliance has long been a focus for the global investment community, and we expect these rules to underscore the institutional importance of staying within the good graces of the Committee.

The proposed rules are subject to public review and comment for thirty days. We expect final rules to be announced and promulgated later this calendar year.

(I) Compressed timeline to negotiate mitigation

The new rules will obligate transaction parties to respond to any mitigation proposal presented by the Committee within three business days unless a formal request for extension is granted. The proposal is intended to expedite the mitigation negotiation process so that CFIUS may conclude its review within the statutorily required timeframe.

Under the current procedures, there is no specific timeframe by which parties must respond to a mitigation proposal. As CFIUS will often propose conditions relatively late in its investigation period, parties sometimes seek permission to “pull and refile” their CFIUS Notice, which restarts the statutory clock for a new review cycle, in order to provide additional time to evaluate and negotiate proposed mitigation terms.

The proposed rules will allow the Committee to require from parties a broader range of information when investigating non-notified transactions.

The proposed rule change could make it harder for clients to respond. Based on our experience, clients may find it difficult to negotiate these agreements with the Committee on an expedited basis, particularly where conditions require technical or business-level input on the practical feasibility of the proposed terms. Compressing the timeline by which a party must review, evaluate, and revert may prove challenging in certain circumstances.

While the rules afford the Committee with the flexibility to grant extensions and parties can still seek permission to pull and refile their CFIUS Notice, the practical implications of a hurried approach may result in agreements that carry unexpected burdens or challenges to the underlying business upon completion.

The proposed change highlights the need for transaction parties to consider with CFIUS counsel what potential mitigation the Committee may request early in the deal process so that they may assess the feasibility of standard conditions and be ready to negotiate if non-standard terms are requested by the Committee.

(II) Expanded ability to investigate and inquire

The proposed rules will allow the Committee to require from parties a broader range of information when investigating non-notified transactions. Currently, the Committee may demand certain information from transaction parties to evaluate whether CFIUS would have jurisdiction over a particular investment.

The proposed rules will increase the maximum penalty per violation in certain instances from the greater of \$250,000 or the value of the transaction, to \$5 million or the value of the transaction.

While in practice CFIUS has often asked parties during non-notified inquiries to provide additional details on the underlying nature of the U.S. business, the proposed rules will stipulate that parties must also respond to questions to determine if a mandatory filing was required, as well as questions concerning the national security sensitivities of the business that may suggest that a filing was otherwise warranted.

The stated purpose of these proposed changes to the rules is that these requirements will afford the Committee with greater flexibility to determine as a threshold matter whether a formal filing to evaluate the non-notified transaction is necessary. While these changes largely codify some of the existing practices that have developed at the Committee with respect to non-notified investigations, we see this as another example that demonstrates an ever-growing focus by the Committee on non-notified inquiries.

As we have discussed in prior publications, the Committee's 2023 annual report documented an increase in the number of non-notified transactions for which the Committee sought a post-closing filing in 2022, notwithstanding a downturn in overall M&A activity that year.

Separately, the proposed rules afford the Committee with the ability to solicit information from transaction parties for other reasons, such as compliance with existing mitigation agreements, conditions, or orders.

In addition, the proposed rules would permit the Committee to require relevant information, including through subpoena, from any "other person" — even if not a party to a transaction. It remains to be determined how CFIUS will utilize this broad expansion of their investigative abilities in practice, but the consequence of this change is that unrelated third-parties may be the recipient of information demand letters from CFIUS.

(III) Increased penalties

CFIUS leadership continues to place an increased focus on enforcement and penalties with respect to the CFIUS process. The proposed rules will increase the maximum penalty per violation in certain instances from the greater of \$250,000 or the value of the transaction, to \$5 million or the value of the transaction.

While it is unlikely that this increase in penalty authorization will have a material impact on the broader investment community, it does reflect the Committee's focus on ensuring they have the tools they believe necessary to handle non-compliance.

Conclusion

The proposed rules represent another step in the Committee's continued prioritization and messaging around mitigation and enforcement, including as reflected in the Enforcement and Penalty Guidelines (the "Guidelines") that Treasury issued in October 2022. The Guidelines laid out the Committee's enforcement framework aimed at incentivizing compliance with the CFIUS regulations, and the new rules proposed today build on those principles.

In addition, given the extensive ongoing collaboration among CFIUS and other U.S. national security policymakers with their foreign counterparts responsible for implementing and enforcing foreign direct investment ("FDI") regimes globally, we expect similar trends and more proactive regulators emerging in many other countries around the world.

In the long run, the national security-focused investment requirements and enforcement led by CFIUS will require increased attention and education early in the investment cycle.

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This article was published on Westlaw Today on May 2, 2024.

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