

Understanding the Role of CFIUS in Real Estate Transactions with Foreign Buyers and Lenders

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The authors of this article discuss the role of the Committee on Foreign Investment in the United States in real estate transactions.

The Committee on Foreign Investment in the United States (“CFIUS”) is an interagency committee, chaired by the Department of the Treasury, authorized to review and investigate foreign investments in the United States to evaluate potential threats to national security posed by such transactions. CFIUS has authority to initiate review of any foreign investment in the U.S. that results in control of a U.S. company and that may negatively affect the national security of the United States.

Key national security concerns historically considered by CFIUS include whether the transaction involves secured facilities, government facilities, export-controlled information, U.S. government contracts, critical infrastructure, a foreign government purchaser, the opportunity for surveillance or sabotage, the acquirer’s prior dealings with governments or entities unfriendly to the United States, and the post-acquisition plans for the acquired

business. Chinese investments in the United States continue to be the leading source of most cases filed with CFIUS, followed by investments from the United Kingdom, Canada, Japan, and France. In 2014, notices from Germany, Israel, the Netherlands, South Korea, Switzerland, and the United Kingdom doubled from the prior year levels.

While notification to CFIUS of a contemplated transaction is voluntary, notification can be critical to protect the expectations and investments of all parties involved. If CFIUS finds that a transaction presents national security risks, it may impose conditions on the parties to mitigate such risks or recommend that the president block the transaction entirely, including the unwinding of a closed transaction. Most recently, on December 2, 2016, President Obama issued an Order blocking the proposed purchase by a Chinese company of the U.S. subsidiary of a German

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semiconductor equipment maker due to national security concerns. The Chinese company could proceed to purchase the German company without the U.S. subsidiary. CFIUS' authority to review a transaction is not time-barred; therefore, a transaction not submitted to CFIUS for review may be subject to scrutiny and potential unwinding at any time if it is determined that the transaction threatens or impairs national security. On the other hand, once CFIUS completes review of a transaction, the parties receive a "safe harbor" from subsequent review with respect to that transaction.

National Security Considerations: Critical Infrastructure and Proximity

CFIUS has jurisdiction to review a "covered transaction," defined as "any transaction . . . by or with any foreign person, which could result in control of a U.S. business by a foreign person."¹ "Control" is defined expansively to include direct or indirect control, whether or not exercised, through a majority ownership interest, a dominant minority ownership interest, board representation, or "other means, to determine, direct, or decide important matters affecting" the U.S. business.²

Recent transactions reviewed by CFIUS demonstrate that CFIUS' interest extends far beyond those involving the traditional defense industrial base to include real estate located in proximity to critical infrastructure or sensitive government installations. For example, in 2009, CFIUS reviewed a Chinese company's acquisition of a U.S. mining company and raised concerns about the proximity of the properties to sensitive military facilities, including the TOPGUN flight training school. CFIUS reportedly intended to recommend that the

president block the transaction. As a result, that deal collapsed. In 2012, a Chinese-owned company was forced to divest its interest in a wind farm located in proximity to a naval base after President Obama ordered the divestment based on CFIUS' recommendation. In 2015, CFIUS reviewed a Chinese-based company's purchase of the Waldorf Astoria hotel in New York City. Although CFIUS ultimately determined to take no action with respect to that transaction, CFIUS' review of the acquisition further demonstrates the expansive scope of CFIUS' authority and interest in reviewing real estate transactions involving foreign parties.

Lending Transactions

While a loan or similar financing by a foreign person to a U.S. business does not generally, by itself, constitute a covered transaction, a loan or similar financing arrangement through which a foreign person obtains an interest in profits of the U.S. business, the right to appoint directors of the U.S. business, or other rights typically characteristic of an equity investment rather than a loan, may constitute a covered transaction.³ Similarly, where a foreign lender obtains the right to control the U.S. business upon default or another event, CFIUS may review the transaction once there is a significant possibility that the foreign person will obtain control of the U.S. business due to the imminent or actual default of the loan or financing arrangement.⁴

The Process

The CFIUS process is initiated by a written notice submitted jointly by the buyer and seller. The notice must include detailed information about the proposed equity structure, as well as detailed corporate and personal identifier

information for all entities in the proposed chain of ownership and their officers and directors or other key management personnel. Pre-filing of a draft notice at least five business days prior to the filing of the formal notice is highly recommended but not mandatory. After the formal filing is made, CFIUS will confirm that the filing is complete and has been accepted, after which it has a statutory requirement to advise the parties within 30 days as to whether it intends to conduct a further investigation or, alternatively, that it has determined that there are no issues of national security to warrant such further investigation. If no investigation is required, the matter will be closed and the parties may proceed with the transaction. If a further investigation proceeds, it must be concluded within 45 days. If CFIUS determines that the transaction creates a risk to national security, then it may require that the parties take certain steps to mitigate such risk (e.g., restructure the transaction so that the foreign party does not have control over certain assets or business). If the parties refuse to implement the mitigation steps required by CFIUS, the matter may be referred to the president for a determination as to whether the transaction should be blocked or unwound. The president is required to make such a determination within 15 days of the referral from CFIUS.

Conclusion

Prudent buyers and sellers of U.S. real estate involving foreign interests must carefully analyze transactions for potential national security implications and plan to submit a CFIUS notice, where appropriate. Similarly, foreign lenders that obtain the right to control a U.S. business (whether exercised or not) through a loan or similar financing arrangement should consider the national security implications of the contemplated transaction and require the parties to seek CFIUS approval where appropriate in order to protect their investment. A CFIUS filing is detailed and time-consuming. Parties to real estate transactions involving foreign acquirers or lenders are therefore well-advised to analyze the national security implications of the transaction early in the due diligence process to determine whether submitting a CFIUS notice is warranted, and, if so, to plan at least four months to draft and submit the notice as well as receive a final determination from CFIUS.

NOTES:

¹31 U.S.C.A. § 800.207.

²31 U.S.C.A. § 800.204.

³31 U.S.C.A. § 800.303(b).

⁴31 U.S.C.A. § 800.303(a)(2)