



U.S. Treasury Department seal

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## CFIUS Reviews of M&A Deals Get Broader, Deeper, and More Detailed

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*Reviews of foreign direct investment transactions by the Committee on Foreign Investment in the U.S. are broader, deeper, and more inclusive in the current geopolitical environment, says Giovanna M. Cinelli, international trade and national security partner at Morgan, Lewis & Bockius. Investors should increase their due diligence, starting with expanding export controls and sanctions compliance checklists, and “know your customer” research when parties deal with sanctioned countries, she says.*

Regardless of ongoing geopolitical turmoil, foreign direct investment (FDI) continues and, in some sectors, has increased in scope and size. In the last three years, investments in biotech, pharmaceutical, big data, real estate and several tiers of the supply chain have drawn CFIUS’ active interest.

Although the committee had jurisdiction over these industries and investments more generally under legislation prior to the Foreign Investment Risk Review Modernization Act of 2018 (FIRRMA), shifting geostrategic conditions raised their profiles. The importance of maintaining open supply chains, guaranteeing access to markets, and keeping financial engagements flowing has resulted in robust cross-border transactions.

In conjunction with this backdrop, national security reviews of FDI continue both in the U.S. and abroad. The Committee on Foreign Investment in the U.S. (CFIUS) is managing mandatory and voluntary submissions with enhanced resources and is incorporating the ever-broadening scope of national security into its analysis of the implications of security interests across industry sectors.

Although much remains the same for FDI, we have seen trends in the last five years that—along with underlying shifts in geopolitical circumstances, such as instability and conflict between a number of countries, including China, Taiwan, Russia and Ukraine—point to an existing information deficit.

This combination of factors is creating a need for enhanced due diligence and further risk mitigation and potentially indicates a foundational shift in how parties determine what may or may not raise a national security concern that warrants CFIUS review.

The following three trends indicate what may portend for the remainder of 2022 and beyond:

- An increase in more detailed questions during the CFIUS review process;
- An increase in non-notified outreach from the committee; and
- An increase in the need to confirm regulatory requirements, whether export controls, sanctions, or government contracts/subcontracts

## **A More Detailed CFIUS Review Process**

Recent CFIUS engagements during the review process reflect a higher degree of sophistication by the committee both in understanding the nuances of deal structure and in identifying pinpoint areas of concern such as supply chain, cyber risks, export control misclassifications, and “hidden in plain sight” government issues.

The need to ask for more detailed information stems from the following, among other things:

- [The CFIUS regulations](#) may not include all the questions or topics that should be included in a filing, thereby leaving the committee to collect the information during the review process; and/or:
- Parties may not be identifying and gathering the more nuanced information during the diligence process, thereby making the filing less than complete. Although parties cannot drive the regulatory changes, they can adjust their diligence process to minimize some of the more extensive exchanges between parties and the committee that can extend the timelines for CFIUS review.

## **More Non-Notified Outreach**

CFIUS always has had the authority to maintain a list of cross-border investments that have not been notified to the committee. Past resourcing limitations may have impacted how many and which non-notified transactions merited an outreach. Recent budget and personnel increases, however, provide the committee with the ability to communicate more often in this area.

Apart from resources and budgets, increased non-notified outreach may also be based on at least the following circumstances:

- The definition of “national security” has expanded. The definition now includes corruption, climate change, and other policy-oriented issues. This broadened definition creates exigencies for reviews that may not have existed earlier.
- The diligence process does not always account for this broadened definition. As a result, therefore, parties have been led to decide that an investment is not subject to CFIUS jurisdiction, or would not be of interest to the committee—or, even if the investment would be of interest—submission to CFIUS for review for CFIUS review would not be required.
- The committee evaluates more closely the impact of cumulative investments. While investors seek synergies or common threads when making investments, including when to consolidate within industry sectors, the committee now appears attentive to those same threads. Consolidation of industry sectors, at any level, represents a national security risk based on the leverage that can be created through the limits on diverse sources of supply.
- Regulatory compliance takes on more importance. Increased sanctions across industries, multilateral sanctions, and tightening of export controls create more touch points for national security concerns. This impacts the diligence process for both the seller and the investor, as the Foreign Investment Risk Review Modernization Act highlighted the need for parties to understand the compliance posture of the foreign investor as well as of the seller.

## **Increased Need to Confirm Regulatory Requirements**

Regulatory compliance has been part of the CFIUS review process since 1975. Sellers and investors determine how to manage the diligence process, what questions to ask and answer, and how to allocate risk based on the information shared.

While these diligence engagements continue, the risk calculus has changed shifted—e.g., the risks of not filing a notice, especially where miscalculations occur on whether a mandatory notice is required, include potential fines, enforcement, and litigation among the parties.

Weak diligence and gaps in independent verification of information provided during the diligence process magnifies the risks. This may also have a downstream impact on representations made to the committee should parties decide to make a voluntary filing.

CFIUS's ability to unwind a transaction—an authority the committee has had since its statutory inception in 1988—becomes more of an issue if the parties miscalculate on whether a deal is subject to mandatory or voluntary review.

The mandatory submission process is focused primarily on critical technologies, as defined under U.S. export laws, therefore weak diligence takes on makes a greater impact. CFIUS has shown an increased interest in underlying classification information, export licensing requirements, and sanctions compliance. This interest affects information collected during the diligence process since sellers sometimes hesitate to provide details about their business operations.

Therefore, investors may need to consider whether a seller's hesitancy in providing this information changes the risk that a transaction would be subject to CFIUS jurisdiction, or of interest to the committee, as well as whether a transaction requires a mandatory submission. Given the current environment of robust cross-border transactions that have emerged, investors can enhance their diligence processes to identify, analyze, and manage risks more robustly.

Investors can start by expanding their export controls and sanctions compliance diligence checklists, and request documentation such as export licenses and end user statements, as well as background "know your customer" research when parties work or provide services in sanctioned countries or with sanctioned entities.

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## **Author Information**

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