

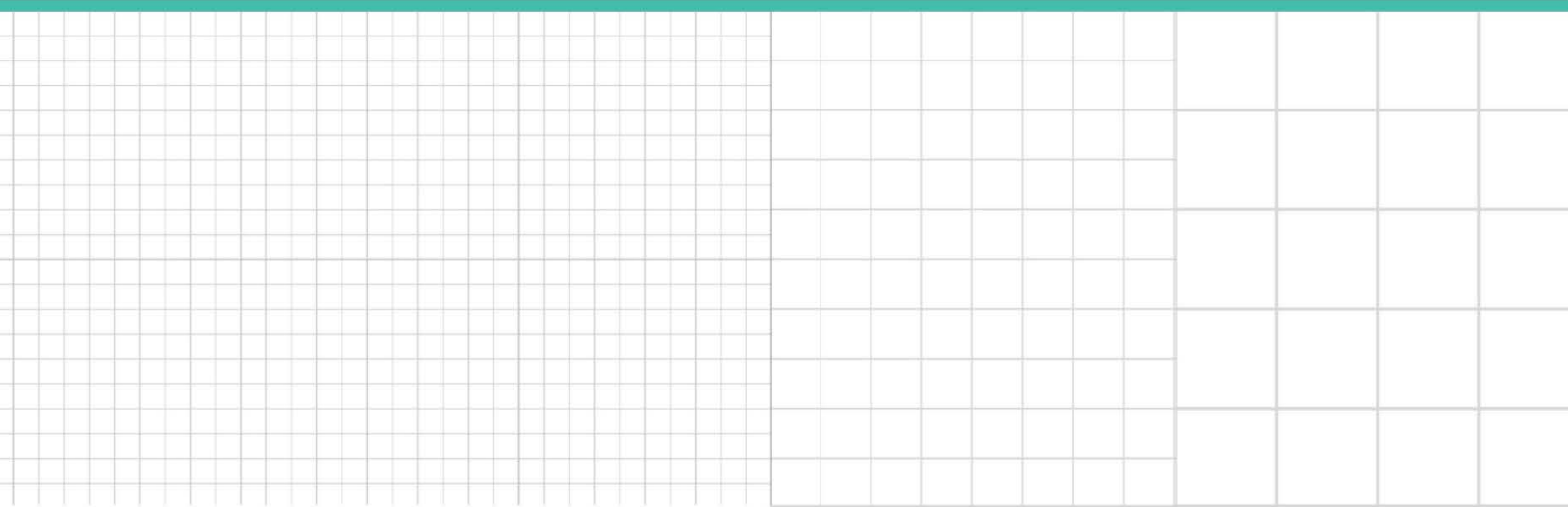


Professional Perspective

# CFIUS and Real Estate Transactions Under FIRRMA

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# CFIUS and Real Estate Transactions Under FIRRMA

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On Jan. 13, 2020, the U.S. Department of the Treasury issued final regulations that implement most of the Foreign Investment Risk Review Modernization Act of 2018. The purpose of this article is to call attention to how the application of these rules may trigger the need for more significant Committee on Foreign Investment in the U.S. reviews for real estate and real estate related transactions that do not intuitively fit into our historical understanding of CFIUS's role in this space.

The rules were issued in two parts: Part 802, addressing Real Estate, and Part 800, primarily addressing business acquisitions potentially implicating national security concerns. The rules expand the authority of CFIUS in the U.S. in a number of significant ways, including the right to review non-controlling investments and introducing categories of investments (e.g., businesses that maintain or collect sensitive personal data) that were not previously viewed as raising national security concerns subject to CFIUS review.

In the not too distant past, CFIUS was not a significant issue for real estate transactions, and only came up on very rare occasions. However, CFIUS became more of a concern given the delay and increased scrutiny (in some cases leading to the withdrawal) of numerous transactions involving businesses with real estate in close proximity to sensitive U.S. government facilities. The rules provide some clarity around what would typically be considered sensitive U.S. government facilities, and provide more structured rules concerning the review of real estate focused transactions.

The rules define a universe of transactions that are considered covered real estate transactions and subject to CFIUS review. These involve transactions through which a foreign person gains, by itself or shared with others, at least three of the four following rights with respect to real estate that is located in or in close proximity to ports or certain U.S. government facilities: access, the right to exclude other's access, the right to improve or develop the real estate, or the right to attach fixed or immovable structures or assets to the real estate. Real estate transactions are not subject to mandatory filing. The fact that a transaction is a "covered real estate transaction" does not mean that it is forbidden, just that it is subject to CFIUS review and approval.

While providing some clarification and structure, the rules have expanded the jurisdiction of CFIUS with respect to real estate and real estate related transactions in a number of ways that are not obvious.

## Contingent Ownership/Loans

The rules specifically address contingent ownership rights and loans. While these would not by themselves trigger a CFIUS review, the conversion of these rights or acquisition of control of the real estate through foreclosure could be considered a covered transaction. Transactions that are being funded by foreign lenders should be reviewed to make sure that lenders have an effective way to exercise any conversion or foreclosure rights. This would apply not only at the property level, but at any level of the corporate structure that would give the new owner at least three of the four property rights listed above. Even if the original holder/lender is not someone who could trigger such a review, subsequent holders/lenders may be.

## TID U.S. Business

When acquiring real estate, investors must also consider if the contemplated transaction involves the acquisition of a controlling or non-controlling interest in a U.S. business implicating critical technology, critical infrastructure, or sensitive personal data of U.S. citizens (a TID U.S. Business) that would afford the investor access to "material non-public technical information"; membership or observer rights or the right to nominate an individual to the board, or rights to involvement, other than through voting of shares, in the "substantive decision-making" with respect to the critical technology, critical infrastructure, or sensitive personal data. Such transactions are considered "excepted real estate transactions" and will be governed by Part 800 rather than Part 802.

"Substantive decision-making" under the rules is defined as the process through which decisions regarding significant matters affecting an entity are undertaken. The rules provide a non-exhaustive list of the types of significant matters that are covered (that are focused on the level of authority and access to information/systems), and clarify that strictly administrative decisions do not constitute substantive decision-making.

“Sensitive personal data” includes 10 different categories of information collected about 1,000,000 or more persons, including, for instance:

- Data that relates to a person's physical, mental, or psychological well-being (i.e., health information)
- Non-public electronic communications, including email messaging or chat communications between or among users of a U.S. business's products or services (if the U.S. business is providing communications platforms used by third parties)
- Geolocation data collected using positioning systems, cell phone towers, or Wi-Fi access points such as via a mobile application, vehicle GPS, other onboard mapping tool, or wearable electronic device (e.g., location data on customers collected and maintained for customer marketing or customer experience purposes); or for mobile mapping services

Therefore, if the transaction involves the acquisition of a controlling or non-controlling interest in real estate that incorporates any of the above or of an operating business that is real estate intensive (whether or not the business acquires the relevant real estate), the investor will need to analyze not only the proximity to government installations, but also whether the substantive business triggers any of these other rules. Some examples include:

- Businesses in the broader health-care space
- Hospitality operating companies that may be tracking guest locations for marketing and other purposes, or biometric data for access privileges
- Data centers storing non-public electronic communications

Investors should pay particular attention to businesses collecting geolocation data positioning information, as this feature is becoming a more and more prevalent part of loyalty or other service offering programs, primarily through various smartphone applications.

## Secondary Transactions

The application of the rules to non-control investments requires a review of any investor's ownership structure, including direct and indirect shareholders, members, limited partners, and the like. The rules also apply to any future secondary (direct or indirect) acquisitions of equity interests. Therefore, to the extent relevant, an investor would want to create restrictions and procedures governing any purchases of direct or indirect interests of its equity, to minimize the risk of a CFIUS review at a later stage.

## Sovereign Funds

If the potential investor is a foreign person in which the national or subnational governments of a single foreign state have a substantial interest (e.g., sovereign wealth funds), an investment in a TID U.S. Business would not only trigger a review but would also trigger a mandatory filing.

Note that in the case of either a voluntary or mandatory filing, all filers—without regard to government ownership—will generally disclose government ownership in the foreign person's ownership structure, including nationality and percentage of ownership, board management personnel, and any rights that a foreign government holds, directly or indirectly, with respect to the foreign person; along with information related to financing or other sources of funds for the investment, and summaries of the business activities of the foreign person and any of its parent entities. This may not be comfortable or permissible for some investors or their owners.

The CFIUS rules have changed the regulatory landscape and have expanded CFIUS's jurisdiction to additional transactions. The structure, the nature of securities purchased, the business purchased, and the type of investor may affect the obligation to make mandatory filings or whether or not the contemplated transactions are covered by CFIUS. Particular attention should be afforded when the real estate transaction involves the acquisition of an operating business that would be considered a TID U.S. Business. In addition, rules governing secondary transactions and loans/contingent equity mean that reviews may also be triggered by subsequent transfers of interests, an issue that should be addressed upfront to avoid a messy situation down the road.