

CFIUS Real Estate Transaction Review Fees Demand Caution

By **Paul Nash and Andrew Demirchyan** (July 9, 2020, 6:14 PM EDT)

Effective as of May 1, real estate transactions subject to the federal government's review by the Committee on Foreign Investment in the United States, including those involving foreign participation through investment, acquisition or management of U.S. real property or businesses, are subject to filing fees.

U.S. real estate organizations seeking debt or equity financing, investment or other participation from foreign sources in U.S. real estate transactions should determine whether their transaction falls under CFIUS review, and if so, take note of the current filing fees payable in connection with any such review.

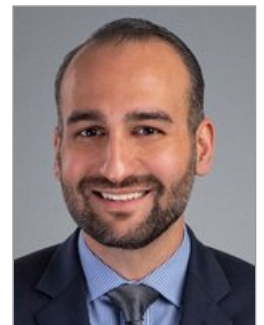


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What is the Committee on Foreign Investment in the United States?

CFIUS is a federal interagency committee comprised of the heads of various federal government agencies and offices, and is chaired by the secretary of the U.S. Treasury, and is responsible for analyzing and investigating foreign investment in the U.S., with the primary purpose of identifying and neutralizing potential threats to national security, primarily to the nation's critical infrastructure.

CFIUS does not issue public decisions or publish public reports on its specific investigations or findings, and operates confidentially. Pursuant to the Foreign Investment Risk Review Modernization Act, the president of the U.S. is authorized to take any action that the president deems appropriate to either suspend or prohibit a covered transaction that would be a potential threat to national security. The president has delegated the assessment of covered transactions to CFIUS.



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What is a covered transaction under CFIUS?

The act broadly defines a "covered transaction" to be any transaction that would be a potential threat to U.S. national security or critical infrastructure, including mergers, acquisitions or takeovers by or with any foreign person that could result in foreign control of a U.S. business, including a noncontrolling foreign investment in critical U.S. businesses involved in technology, data and infrastructure.

Since "foreign control" is generally defined as a foreign person having the ability, after the covered transaction is consummated, to cause the U.S. business to either take an action, or refrain from taking an action, related to the management, operations or disposition of business assets, certain real estate transactions including acquisition of undeveloped land involving foreign participation are subject to CFIUS review.

What fees are required in connection with CFIUS review?

The U.S. Department of the Treasury issued an interim rule^[1] on April 27, establishing filing fees for certain transactions filing any formal written notice for CFIUS review. These filing fees cover all

transactions filing for voluntary CFIUS review and are used to offset associated costs.

Effective as of May 1, an applicant seeking CFIUS review of a covered transaction is required to pay a fee in connection with the filing. Previously, no filing fees were required. The amount of the filing fee is calculated based on the transaction value, as follows:

Transaction Value	CFIUS Filing Fee
\$0 to \$499,999.99	\$0
\$500,000 to \$4,999,999.99	\$750.00
\$5,000,000 to \$49,999,999.99	\$7,500.00
\$50,000,000 to \$249,999,999.99	\$75,000.00
\$250,000,000 to \$749,999,999.99	\$150,000.00
\$750,000,000 +	\$300,000.00

The filing fees apply to any formal written notice of a covered transaction or covered real estate transaction seeking CFIUS review, and are generally due concurrently with the filing. In certain limited circumstances, CFIUS may waive the filing fees or issue refunds.

The Treasury has specified that, for purposes of determining the amount of the fee, the value of a transaction will be the total value of all consideration paid by or on behalf of the foreign person that is a party to the transaction (e.g., cash, shares or other in-kind consideration).

Payments must be made at the time that a notice is formally filed with CFIUS, unless a waiver has been issued, and CFIUS generally will not commence its review unless and until the filing fee has been paid.

What does the CFIUS review process involve?

To avoid a potential challenge to a covered transaction, parties can file a voluntary notice with CFIUS to clear the transaction. This helps to mitigate the risk that CFIUS will block the closing of a real property asset or order that the asset be divested or a transaction unwound following the closing.

Given the extent of CFIUS authority and its demonstrated willingness to affect a transaction post-closing, if a party feels its transaction may be subject to CFIUS review it is highly recommended for the party to file a voluntary notice prior to closing its transaction.

CFIUS may also place greater scrutiny on foreign purchasers from countries with which the U.S. has sensitive or strained diplomatic relations. While a party's notification to CFIUS is largely voluntary, mandatory filing is required in certain instances (for example, if a foreign government acquires a critical U.S. business that is involved in technology, data or infrastructure).

The review process begins with a party filing a draft notice with CFIUS explaining the transaction. After reviewing the draft notice, CFIUS informs the party whether or not the party should formally file a voluntary notice.

Title 31 of the Code of Federal Regulations, Section 800.502 describes the type of information that a party is required to provide in its voluntary notice, including:

- A detailed description of the transaction;
- Detailed corporate identification information for the transaction parties;
- Detailed personal identification information for the transaction parties;
- Information on all entities in the proposed ownership/organizational structure;
- The foreign entity's plans for the U.S. business it is acquiring;

- the value of the transaction;
- the location of the assets in relation to U.S. government facilities; and
- the nature of the foreign purchaser (e.g., foreign government, private party or hybrid).

What are the risks of not voluntarily seeking CFIUS review?

If CFIUS determines that a potential covered transaction poses a threat, it may require that the parties to the transaction take certain actions to mitigate any risks or dangers identified. These actions may include, but are not limited to the divestment of specific assets, a restructuring, the elimination of particular requirements (e.g., board seats), and/or a recommendation to the president that the covered transaction be prohibited entirely.

CFIUS may also recommend that the president order a purchaser of real estate to divest the asset after the closing has occurred if CFIUS determines that the purchase of the asset poses a threat to the national security interests of the U.S. Further, the act allows for CFIUS to impose civil penalties on parties that fail to file.

Historically, CFIUS has scrutinized transactions in which a foreign purchaser sought to acquire real estate that is leased by tenants who may have access to classified information or are federal government contractors, thereby posing a potential risk to national security.

However, the U.S. has a longstanding practice to leave the term "national security" undefined, which provides the president, through CFIUS, with maximum flexibility to assert jurisdiction over foreign acquisitions of various U.S. businesses. A recent example involved CFIUS ordering a Chinese conglomerate to sell its majority stake in a Manhattan skyscraper whose tenants include a New York City police precinct tasked with protecting Trump Tower.

Recommendations

Given the significant risks involved, real estate organizations seeking financing, investment or other participation of foreign sources in U.S. real estate transactions should determine whether their transaction could fall under CFIUS review, and if so, be prepared to pay the filing fee in connection with any such review. Though not exhaustive, we recommend implementing the strategies discussed below to achieve this objective.

Negotiate matters related to CFIUS review into the purchase agreement.

When negotiating a real property acquisition, disposition or investment, the parties should consider negotiating, among other things:

- Allocation of the payment of any required CFIUS filing fee and the related increase in overall additional costs, such as legal or consulting fees;
- Recalibration of the closing timeline of a transaction if CFIUS review is necessary;
- Structuring of certain responsibilities among the parties in the event of CFIUS review;
- Expansion of conditions precedent to closing;
- Negotiation of specific extension options tailored to CFIUS review; and

- Consideration of how CFIUS review will affect the interest of each party in the larger scope of the transaction (e.g., delay from CFIUS review may lead a party to miss a 1031 tax deferred exchange deadline).

In addition, an increasing number of lenders are adding CFIUS review provisions to their real estate finance documents and underwriting process, considerations that the parties must analyze and plan for in their negotiations.

Understand the nature of foreign participation in the transaction.

CFIUS review involves a detailed understanding of foreign control over the acquired U.S. real property asset. Thus, it is imperative to understand the role of the foreign participant and the level of control they will have in the transaction. The following examples highlight common scenarios faced by real estate organizations:

Financing

Though it is standard to obtain lender approval for certain material or threshold matters that affect an asset post-closing, even a routine approval by a foreign lender of something such as a major lease may be problematic if the tenant is a critical U.S. business and the lease contains descriptions of certain buildouts and tenant improvement plans.

Joint Ventures

In a typical joint venture scenario, one party is the operator of the asset and the other party is the capital investor (i.e., the silent partner). Significant issues may arise if the operating party is a foreign entity, as the joint venture documents typically provide the operating party with broad control and management rights.

In this scenario, the joint venture could be structured to reallocate certain tasks between the parties in order to limit or eliminate the sharing of sensitive information with the foreign party, or to eliminate the ability of a representative of the foreign party to vote on certain matters that would control certain key outcomes in the direction of the business.

Leasing

CFIUS analysis requires review of the type of tenants leasing premises in an asset and the nature of the tenants' business. If the foreign participant becomes the successor landlord of a lease with a tenant that is a critical U.S. business involved in technology, data or infrastructure, certain protocols should be built into the asset and property management procedures in order to limit or eliminate the foreign party's direct involvement with the tenant.

Perform CFIUS due diligence prior to the execution of a purchase agreement.

CFIUS concerns are often flagged when an asset is leased by tenants that (1) maintain government offices in the asset, (2) are parties to certain government or defense contracts, or (3) are broadly involved in technology, data or infrastructure.

Since a buyer typically does not begin its review of a property's diligence materials and related leases until after a negotiated purchase agreement has been signed, if the buyer has CFIUS concerns it should consider entering into an early access agreement with the seller to gain earlier access to certain due diligence materials prior to entering into the purchase agreement. During this early review period, the buyer can analyze underlying leases and tenant business profiles to properly assess potential CFIUS concerns.

Overall, because of the lack of precedent and rapidly evolving guidelines and regulations, it would be prudent for a party to file a draft notice with CFIUS framing any potential issues in the applicant's favor, while at the same time establishing some goodwill with the committee. The foregoing recommendations provide for a general framework in the broader CFIUS review and analysis process. The specifics of each transaction and its foreign participation should be individually evaluated by legal

counsel.

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[1] 31 C.F.R. parts 800 and 202.

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