



PHILLIPS LYTLE LLP CLIENT ALERT INTERNATIONAL



JANUARY 2020

Treasury Publishes New Cross-Border Real Estate Investment Rules

On January 13, 2020, the U.S. Department of the Treasury issued its final rules (following publication last September of proposed regulations) pursuant to 2018's Foreign Investment Risk Review Modernization Act (FIRRMA), which governs foreign investment in the United States subject to review by the Committee on Foreign Investment in the United States (CFIUS or "Committee"). A set of these pertains specifically to cross-border investment in U.S. real estate. Due to close and long-standing security relationships with the U.S., under these rules, Canada, Australia and the United Kingdom are designated as "excepted real estate foreign state(s)," rendering their nationals eligible to be "excepted real estate investors" exempt from certain CFIUS review and filing requirements. This status and exemption is not automatic, however, and is subject to qualifying requirements and continuing review (see below).

New Regulations

FIRRMA significantly broadened the scope of cross-border investments – in U.S. companies, assets, technology and real estate – subject to review by CFIUS. The Treasury Department's proposed implementing regulations detailing the application of these new authorities will become final by **February 12, 2020**.

When these rules become final, virtually any investment, including most noncontrolling investments, by a non-U.S. person (not otherwise "excepted") in a U.S. business involved in critical technology, infrastructure, personal data or certain real estate that in any way implicates U.S. national security (broadly defined) concerns will be subject to review and to CFIUS' authority to block or even force unwinding of the transaction. Additionally, CFIUS will be authorized to impose significant civil penalties on both sides of the deal up

to the total value of the transaction should the required notices not be filed in a timely manner.

Real Estate

Until now, noncontrolling investments in real estate have largely been insulated from national security review. The proposed rules add to current CFIUS regulations at 31 C.F.R. Part 800 a new Part 802 covering certain real estate transactions.

Covered transactions include any investment that gives a foreign investor the direct or indirect right to any three of the following four: (a) physical access; (b) exclude others from; (c) improve or develop; or (d) attach fixed structures to "covered real estate." "Covered real estate" includes land or buildings that are:

- Within or will function as part of a maritime port or airport, including "joint use (military and civilian) airports";
- Within any of 57 specified counties, areas or offshore (within 12 nautical miles) military zones;
- Within a mile of any of 164 specified military installations; or
- Within 100 miles of 32 enumerated military facilities.

Exemptions are possible for single-family housing units, certain types of urbanized areas (as defined by the Census Bureau), some types of commercial office space, and for certain retail trade or food service establishments.

"Excepted" Real Estate Foreign States/Investors

The regulations published in September broke new ground by proposing the identification of "excepted" foreign states



PHILLIPS LYTLE LLP CLIENT ALERT

INTERNATIONAL



JANUARY 2020

and investors, whose noncontrolling investments would be conditionally exempt from CFIUS review. The Committee noted that due to national security implications, this “white list” would be kept very limited, especially at the outset. The eligibility criteria were two-pronged:

- (a) National security interests closely aligned with those of the U.S., with a record of close cooperation in security matters; and
- (b) Within two years, demonstrable establishment of an internal national security investment review process similar to CFIUS regarding investment in their own countries, which would share information with U.S. authorities.

Unsurprisingly, then, the first named to this list are the United Kingdom, Australia and Canada, which the Committee identified due to “aspects of their robust intelligence-sharing and defense industrial base integration mechanisms with the United States.”

Note that this “excepted” status is subject to review after a mandatory two-year period.

To be eligible as an “excepted real estate investor” under Part 802, a person or entity must not be otherwise disqualified and must have a robust connection with an excepted foreign state, so that:

- The entity must be incorporated in the excepted foreign state or in the U.S., with its principal place of business in one or the other, or if a natural person, be a national of the excepted state;
- Any board of directors must be comprised of no more than 25 percent representation by foreign nationals of non-excepted states;

- Such foreign nationals may hold no more than a 10 percent voting interest in the entity; and
- Such investors must not have in the past violated any CFIUS requirements or U.S. laws or regulations.

Any change in the above factors may risk “excepted status” and prompt CFIUS review.

Filing

Part 802 provides investors with greater clarity as to which investments may be “covered.” Filing with CFIUS regarding a noncontrolling investment *remains voluntary*; the decision to file rests with the parties to a deal. However, note that even without a filing, CFIUS retains the authority on its own to initiate a review and impose conditions upon, block or unwind covered transactions.

Takeaway

These new rules clearly indicate that investors will face heightened scrutiny and new regulatory hurdles even for noncontrolling cross-border real estate transactions. Parties would be well advised to consult with counsel early in evaluating such transactions to assess, notwithstanding “excepted” origin, whether the excepted foreign state investment provisions apply, and plan (if appropriate) for the risks and costs associated with CFIUS review.

Additional Assistance

For more information on this topic, please contact James Kevin Wholey at jwholey@phillipslytle.com or (202) 617-2714. ■



PHILLIPS LYTLE LLP CLIENT ALERT

INTERNATIONAL

JANUARY 2020



Phillips Lytle LLP

Albany Omni Plaza 30 South Pearl Street Albany, NY 12207-1537 (518) 472-1224

Buffalo One Canalside 125 Main Street Buffalo, NY 14203-2887 (716) 847-8400

Chautauqua 201 West Third Street Suite 205 Jamestown, NY 14701-4907 (716) 664-3906

Garden City 1205 Franklin Avenue Plaza Suite 390 Garden City, NY 11530-1629 (516) 742-5201

New York City 340 Madison Ave 17th Floor New York, NY 10173-1922 (212) 759-4888

Rochester 28 East Main Street Suite 1400 Rochester, NY 14614-1935 (585) 238-2000

Cleveland, OH One Cleveland Center 1375 E. 9th Street 30th Floor Cleveland, OH 44114-1797 (216) 928-3474

Washington, DC 1101 Pennsylvania Avenue NW Suite 300 Washington, DC 20004-2514 (202) 617-2700

Canada The Communitel Hub 151 Charles Street West Suite 100 The Tannery Kitchener, Ontario N2G 1H6 Canada (519) 570-4800

Prior results do not guarantee a future or similar outcome. The foregoing is for informational and advertising purposes only. The information provided is not legal advice for any specific matter and does not create an attorney-client relationship. The recipient of this publication cannot rely on its contents. If legal advice is required for any specific matter, please consult with qualified legal counsel. We would be pleased to assist you.

©2020 Phillips Lytle LLP
Attorney Advertising
PHILLIPSLYTLE.COM