

Self-Disclosure In Light Of New CFIUS Penalty Guidelines

By **Scott Jansen, Barbara Linney and Melissa Mannino** (October 31, 2022)

On Oct. 20, the U.S. Department of the Treasury issued its first-ever enforcement and penalty guidelines for the Committee on Foreign Investment in the United States.[1]

Publishing of the guidelines reinforces CFIUS' recent statements about the need for penalties to ensure compliance with statutory and regulatory requirements, and strongly suggests that CFIUS is likely to begin taking enforcement actions in the coming months.

Assistant Secretary of the Treasury for Investment Security Paul Rosen stated,

[T]he guidelines send a clear message: Compliance with CFIUS mitigation agreements is not optional, and the Committee will not hesitate to use all of its tools and take enforcement action to ensure prompt compliance and remediation, including through the use of civil monetary penalties and other remedies.[2]

Increased Enforcement — Including Financial Penalties — on the Horizon

The passage of the Foreign Risk Review Modernization Act, or FIRRMA, allowed CFIUS to stand up a robust enforcement and mitigation division that is actively reaching out to U.S. businesses on non-notified transactions, and monitoring CFIUS mitigation agreements for compliance.

In recent years, however, only two CFIUS enforcement actions have resulted in penalties: a \$750,000 penalty was imposed in 2019 for failure to restrict and adequately monitor access to protected data defined in the interim CFIUS order,[3] and a \$1 million penalty was levied in 2018 for repeated breaches of a 2016 mitigation agreement, failure to establish required security policies and failure to provide adequate reports to CFIUS.[4]

Depending upon the seriousness and frequency of the violation, potential penalties and other remedial measures mentioned in Title 31 of the Code of Federal Regulations, Sections 800.901 and 800.902 include:

- Civil penalties not to exceed \$250,000 or, in certain cases, up to the value of the transaction, whichever is higher;
- A drafting of a plan of action or new/amended CFIUS mitigation agreement (with failure to comply with plan of action being grounds for a new penalty); and



Scott Jansen



Barbara Linney



Melissa Mannino

- The possibility of CFIUS initiating a new review of certain transactions.

The new guidelines will apply to enforcement in the context of these provisions, as well as the enforcement provisions of Title 31 of the Code of Federal Regulations, Parts 801 and 802.

Types of Conduct That May Constitute a Violation

The guidelines identify three types of conduct that may constitute a violation.

- Material misstatements or omissions in filings with CFIUS, or false or materially incomplete certifications delivered to CFIUS;
- Failure to file a mandatory declaration or notice; and
- Noncompliance with CFIUS mitigation agreements, conditions or orders.

Four-Step Penalty Process

In the event that CFIUS decides a penalty is warranted, the new guidelines contemplate a four-step process.

Step 1

CFIUS sends written notice of penalty to the alleged violator — a company or an individual — that includes a description of the conduct to be penalized, the legal reasons why a penalty is being sought and the amount of the financial penalty. The notice may include aggravating and mitigating factors that CFIUS considered in reaching its penalty decision.

Step 2

The recipient has 15 business days to submit a written petition for reconsideration — unless extended by the Treasury — that may include evidence in defense, justification or mitigation, or explanatory information.

Step 3

If no written response is filed, CFIUS ordinarily will issue a final penalty — likely to be the same as proposed in the notice of penalty. If a written response is received, CFIUS will consider the written submission before making a final decision within 15 business days — subject to extension by agreement with CFIUS.

It is possible, but not clearly signaled in the guidelines, that at this stage there may be negotiations with CFIUS over penalty terms and conditions.

Step 4

CFIUS issues its final written penalty determination. Given the considerable deference typically granted to CFIUS and other national security agency decisions by U.S. courts, lawsuits challenging CFIUS decisions are rare.

The time frames contemplated by the guidelines come as no surprise, as they essentially mirror the timeframes set out in the regulations.

Aggravating and Mitigating Factor Considerations

The guidelines lay out factors that CFIUS may consider as aggravating or mitigating, but emphasize that the list is nonexhaustive, and that factors relevant to one case may not be relevant to another. The various factors are categorized in the guidelines, as follows:

- **Accountability and future compliance:** This factor attempts to balance the need to hold violators accountable with the need to incentivize compliance and cooperation — self-reporting is evaluated as part of this factor;
- **Harm:** the degree of harm to U.S. national security because of the violation;
- **Negligence, awareness and intent:** an evaluation of the role of simple negligence, gross negligence, intentional action or willfulness that led to the violation, along with any efforts to conceal or delay, and the seniority of the personnel in an entity who knew or should have known of the conduct;
- **Persistence and timing:** frequency and duration of conduct, and how long it took to report the violation to CFIUS; the length of time between a beginning of a CFIUS mitigation agreement and the occurrence of a violation of the agreement, and, in the case of a failure to file, the date the transaction occurred;
- **Response and remediation:** whether there was self-disclosure, and how timely and complete was the disclosure; whether the company cooperated with CFIUS by providing timely and detailed information; whether there was complete remediation; and whether the company performs a detailed internal review of the violation to prevent future violations; and
- **Sophistication and record of compliance:** an evaluation of history and familiarity with CFIUS and record of compliance in previous or ongoing CFIUS cases; whether the violator has adequate internal and external compliance resources, including legal counsel, consultants, auditors and monitors; the adequacy of policies and procedures in place and whether they are communicated and complied with across the business;

whether there is a general culture of compliance within the company; and whether the CFIUS security officer — if applicable — had appropriate authority, access and independence.

None of these factors are surprising. In fact, most are already commonly in use by CFIUS and other federal agencies — such as the export control agencies and the Office of Foreign Assets Control.

Common Ways CFIUS Discovers Violations

The guidelines make clear that CFIUS strongly encourages the filing of timely self-disclosures of conduct that may constitute a violation. As noted above, a timely and detailed voluntary disclosure may be weighed as a mitigating factor in CFIUS' decision whether to impose a penalty, and if so, the appropriate amount for the penalty.

Significantly, however, it should be noted that CFIUS enjoys a number of other means of obtaining information about violations, including:

- Tips from the public, members of Congress, the media, and public interest groups — CFIUS has a tips line on its website for public citizen comment;
- Answers and information provided by a company during an ongoing CFIUS review concerning a company's mitigation agreement compliance;
- Third-party audits and third-party monitor reports — particularly relevant for mitigation agreements with third-party oversight requirements;
- Federal and state agency reports to CFIUS, such as Federal Bureau of Investigation and other intelligence agency reports — reports may come from both CFIUS-member agencies and non-CFIUS-member agencies);
- Transaction and filing parties;
- Publicly available information; and
- Responses to the exercise of CFIUS subpoena authority under Title 50 of the U.S. Code, Section 4555(a).

It is likely that issuance of the enforcement and penalty guidelines is just the first step toward a ramp-up of CFIUS enforcement activity in the coming months.

Given the large number of potential sources of information, persons who may have been involved in a violation should carefully consider the potential benefits of self-disclosure.

Scott Jansen is counsel, and Barbara Linney and Melissa Mannino are partners, at BakerHostetler.

BakerHostetler associate Orga Cadet contributed to this article.

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[1] <https://home.treasury.gov/policy-issues/international/the-committee-on-foreign-investment-in-the-united-states-cfius/cfius-enforcement-and-penalty-guidelines>.

[2] <https://home.treasury.gov/news/press-releases/jy1037>.

[3] <https://home.treasury.gov/system/files/206/Actions-Taken-by-the-Committee-to-Impose-Penalties-and-Unilateral-Reviews-Initiated-2019.pdf>.

[4] <https://home.treasury.gov/system/files/206/Penalties-Imposed-and-Unilateral-Reviews-Initiated-2018.pdf>.