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# National Security or Xenophobia: The Impact of the Foreign Investment and National Security Act ("FINSA") in Foreign Investment in the U.S.

Maira Goes de Moraes Gavioli

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# The William Mitchell Law Raza Journal

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**National Security or Xenophobia: The Impact of the Foreign Investment and National Security Act (“FINSAs”) in Foreign Investment in the U.S.**

*Maira Goes de Moraes Gavioli*

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## I. INTRODUCTION

“International investment in the United States promotes economic growth, productivity, competitiveness, and job creation. It is the policy of the United States to support unequivocally such investment, consistent with the protection of the national security.”<sup>1</sup>

Foreign investment is vital to the continued growth and vitality of the U.S. economy. According to the U.S. Department of Commerce’s Bureau of Economic Analysis, foreigners invested an impressive \$260.4 billion in the U.S. in 2008, amid a slow national economy and despite a worldwide decrease in merger and acquisition activities.<sup>2</sup> Foreign investment is a vital source of job creation, innovation, development and critical to the U.S. manufacturing industry.<sup>3</sup> As of 2006, foreign investors employed more than 5 million Americans and were responsible for roughly 20% of the U.S. manufacturing GDP.<sup>4</sup> Even though foreign investment is necessary to the U.S. economy, some critics perceive foreign imports as a threat to the U.S. economy, sovereignty and national security. Congress enacted the Foreign Investment and National

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<sup>1</sup> Exec. Order No. 13,456, 73 Fed. Reg. 4677 (Jan. 23, 2008) (amending Exec. Order 11,858 and stating the U.S. foreign investment policy).

<sup>2</sup> See generally, THOMAS ANDERSON, BUREAU OF ECONOMIC ANALYSIS, FOREIGN DIRECT INVESTMENT IN THE UNITED STATES 54 (2009), available at [http://www.bea.gov/scb/pdf/2009/06June/0609\\_fdius.pdf](http://www.bea.gov/scb/pdf/2009/06June/0609_fdius.pdf).

<sup>3</sup> David Marchick, *Remarks Before Senator Baucus Trade and Security Forum 1* (Apr. 3, 2006), available at <https://finance.senate.gov/press/Bpress/2005press/prb040306dm.pdf> [hereinafter Marchick’s Remarks] (noting that “in some sectors in which the U.S. leads the world, such as the chemicals sector, foreign affiliates are responsible for almost 30% of the total value created in the U.S. The stock of foreign direct investment in the U.S. has grown from \$185 billion in 1985 to more than \$1.5 trillion today.” Marchick argues that “actions to restrict foreign investment in the United States could lead to retaliation against, or imitation that hurts, U.S. investors abroad. Nevertheless, the levels of foreign investment in the United States remain relatively low compared to other major industrialized countries.” According to Marchick, due to the current account deficit the U.S. needs more foreign investment, not less. In order to eliminate the deficit, “the United States must import more than \$2 billion of capital per day. If the investment environment in the United States is hostile for foreign investment, investors will put their money, jobs and technology in other economies.” See also, Press Release, U.S. Census Bureau, Foreign Trade Statistics: Exhibit 5 – Exports, Imports and Trade Balance of Goods (April 2008), available at [http://www.census.gov/foreign-trade/Press-Release/current\\_press\\_release/exh5.pdf](http://www.census.gov/foreign-trade/Press-Release/current_press_release/exh5.pdf) (indicating that from Jan. to April 2008, the U.S. exported \$110,338 million and imported \$180,912 million in goods) [hereinafter Foreign Trade Statistics].

<sup>4</sup> See generally Marchick, *supra* 2.

Security Act (“FINSA”)<sup>5</sup> to address national security threats involved in certain foreign investment transactions.

National security concerns justify governmental intervention in certain foreign investment transactions, but the U.S. must balance that concern with maintaining an open foreign investment policy. The fear that foreign entities could control American “strategic” industries triggered many legislative attempts to prevent such control.<sup>6</sup> These attempts started to shape up more clearly in the 1970’s and 1980’s amidst fears of “the Japanese dominance” and investments from OPEC countries.<sup>7</sup> The September 11, 2001, attacks most recently made the U.S. suspicious of the outside world, and fearful for its homeland security. The risk of an unsafe homeland became too real in 2005 when the Dubai World Port, a United Arab Emirates government company, acquired the rights to manage six main ports in the U.S. Congress reacted almost immediately and not long after the deal fell through it enacted FINSA. FINSA is a federal statute that allows the President to block or suspend transactions involving foreign investors when the transaction imposes a national security risk. From the U.S. perspective, FINSA provides the framework to ensure that foreign companies do not divest the U.S. of its critical infrastructure, technology, and defense industry through investment in the U.S. From the foreign investors’ perspectives, FINSA burdens foreign investment transactions and allows political pressure to obstruct economically efficient and beneficial transactions.

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<sup>5</sup> Pub. L. No. 110-49, §§ 2-7(b), 8-10, 121 Stat. 246, 259 (2007) (codified as amended at 50 U.S.C. app. § 2170 (2000)).

<sup>6</sup> *See generally*, EDWARD M. GRAHAM & PAUL R. KRUGMAN, FOREIGN DIRECT INVESTMENT IN THE UNITED STATES 53-54 (Institute for International Economics 1995).

<sup>7</sup> *See infra* notes 9-13 (noting that until 1988 the main U.S. legislation regarding foreign investment was the 1917 Trading with the Enemy Act, the 1975 Executive Order 11,858 creating the CFIUS, and the 1977 International Emergency Economic Powers Act).

This article argues that FINSA’s framework allows political and protectionist considerations to interfere with and potentially erode the U.S. free foreign investment policy. Part II of this article provides relevant historical and legislative background about FINSA and the policy underlying it. Next, it provides information about post-9/11 enforcement of foreign investment regulations and how these regulations have been strengthening up to FINSA. Finally, Part II analyzes FINSA’s key terms and the risks associated with its broad scope and lack of clear guidance on how to assess national security threats. Part III argues that FINSA’s lack of guidance regarding the national security analysis allows protectionist concerns and political influences to undermine free investment and principals of laissez-faire economics. Secondly, Part III argues that although national security is a paramount concern, U.S. politicians unjustly rely on it for political reasons when no national security threat exists. Finally, Part III suggests that Congress can improve FINSA by focusing on real national security risks, limiting congressional involvement, and creating a “fast-track” analysis for passive investment.

## **II. BACKGROUND**

### **A. The Exon-Florio Regulatory Framework**

#### **1. Where it all began: Creating the CFIUS**

Throughout U.S. history, policymakers have manifested concern about foreign investments’ potential adverse effects on national security.<sup>8</sup> This history dates back to World War I when the U.S. passed legislation restricting foreign ownership of strategic industry sectors

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<sup>8</sup> See, e.g., Brendan J. Reed, *Sovereign Wealth Funds: the New Barbarians at the Gate? An Analysis of the Legal and Business Implications of their Ascendancy*, 4 VA. L. & BUS. REV. 97, 107-08 (2009) (discussing the historical public concern on foreign investment’s effect on national security).

such as shipping and civil aviation.<sup>9</sup> Concerned with investments from OPEC countries in the 1970's Congress enacted the International Economic Emergency Powers Act ("IEEPA").<sup>10</sup> IEEPA allows the president to seize foreign assets only when he or she declares a state of national emergency.<sup>11</sup> Thus, the President may regulate foreign acquisition of U.S. companies through IEEPA, but doing so requires the declaration of a national emergency against the foreign investor's government. Historically, U.S. presidents have been reluctant to invoke IEEPA because the national emergency declaration is akin to a declaration of hostilities against the investor's country.<sup>12</sup> Thus, the national emergency requirement made IEEPA applicable only to extreme situations, but inadequate to regulate the great majority of foreign investment operations (even when national security might be involved). Due to IEEPA's diplomatic and political drawbacks, the president and Congress sought alternative mechanisms to regulate foreign investment in the U.S.

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<sup>9</sup> See generally MIRA WILKINS, THE HISTORY OF FOREIGN INVESTMENT IN THE UNITED STATES 1914-1945 634 (Harvard Studies in Business History 2004) (listing the principal legislation affecting foreign investment in the U.S. from 1914-1945, including: the 1914/1916 Shipping Act; 1917 Espionage Act, and the Trading with the Enemy Act). For further discussions on World War I legislation regarding foreign assets in the United States see James F. F. Carroll, *Back to the Future: Redefining the Foreign Investment and National Security Act's Conception of National Security*, 23 EMORY INT'L L. REV. 167, 170-72 (2009) (discussing the Trading with the Enemy Act (TWEA) passed in 1917 during World War I. The TWEA authorized the President to nationalize the assets of U.S. subsidiaries of German firms and gave the president broad power to stop any transaction with a foreign country as he saw fit. The TWEA's current version is codified at 50 U.S.C. app. § 1 (2006)).

<sup>10</sup> Pub. L. No. 95-223, title II §§ 202-07, 91 Stat. 1626 (1977), *reprinted as amended in* 50 U.S.C. §§ 1701-06 (2006) [hereinafter IEEPA].

<sup>11</sup> IEEPA § 1701(a)-(b) (stating in relevant part: "[a]ny authority granted to the President [herein] may be exercised to deal with an unusual and extraordinary threat [ ] to the [U.S.] national security, foreign policy, or economy if the President declares a national emergency with respect to such threat") (emphasis added). Furthermore, IEEPA authorizes the president to investigate, regulate, or prohibit any acquisition of any property in which a foreign country or national has any interest. See IEEPA § 1702(a)(1)(B).

<sup>12</sup> See Jonathan C. Stagg, *Scrutinizing Foreign Investment: How Much Congressional Involvement Is Too Much?*, 93 IOWA L. REV. 325, 334 (2007) (noting that presidents have been reluctant to invoke IEEPA in the great majority of transactions because doing so would be akin to "a declaration of hostilities against the government of the acquirer company" (quoting Jose E. Alvarez, *Political Protectionism and United States International Investments Obligations in Conflict: The Hazards of Exon-Florio*, 30 VA. J. INT'L L. 1, 69 (1989))). Stagg further points out that the declaration of national emergency requirement made IEEPA inadequate to meet the demands on the president to regulate foreign investments that affect national security.

In the 1980's Congress feared "the Japanese dominance" and was apprehensive about the inadequate mechanisms to review foreign transactions<sup>13</sup> in the U.S.<sup>14</sup> In response to this political pressure President Gerald Ford issued Executive Order 11,858, creating the Committee on Foreign Investment in the United States ("CFIUS").<sup>15</sup> The CFIUS is an inter-agency body within the Executive Branch, initially responsible for monitoring the impact of foreign investment in the United States and implementing foreign investment policies.<sup>16</sup> The Department of Treasury is the CFIUS' chair. The Committee consisted originally of six members, but today it is composed of fourteen member-agencies and departments, including the Departments of Justice, Homeland Security, Defense, and the Office of the U.S. Trade Representative.<sup>17</sup>

Executive Order 11,858 did not grant the President or CFIUS authority to block or suspend any foreign investment transactions. The agency's role was merely to review transactions involving the takeover of U.S. companies by foreign individuals<sup>18</sup> and to evaluate whether the transaction generally would impose any threat to national security.<sup>19</sup> Ultimately, CFIUS' served the limited role to alert the government of potential problems with certain transactions. Any decision regarding government intervention in individual transactions was left to Congress (political process), or solved by the application of antitrust or alternative laws.<sup>20</sup>

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<sup>13</sup> For purposes of this article the term "transaction" refers collectively to an acquisition, merger, or takeover of a U.S. company by a foreign company or individual.

<sup>14</sup> See Joanna Rubin Travalini, Comment, *Foreign Direct Investment in the United States: Achieving a Balance Between National Economy Benefits and National Security Interests*, 29 NW. J. INT'L L. & BUS. 779, 783 (2009) (commenting on U.S. history in regulating foreign investment).

<sup>15</sup> Executive Order No. 11,858, 3 C.F.R. 990 (1971-1975) [*hereinafter* Executive Order 11,858], (codified at 50 U.S.C. app. § 2170 (2006)).

<sup>16</sup> Executive Order 11,858 § 1.

<sup>17</sup> CFIUS Home Page, <http://www.treasury.gov/resource-center/international/Pages/Committee-on-Foreign-Investment-in-US.aspx> (follow "Composition of CFIUS" hyperlink) (last visited Jan. 27, 2010).

<sup>18</sup> For purposes of this article the term "individual" refers to both natural persons and legal entities.

<sup>19</sup> Executive Order 11,858 § 1(b), (c).

<sup>20</sup> See Matthew R. Byrne, *Protecting National Security and Promoting Foreign Investment: Maintaining the Exon-Floixio Balance*, 67 OHIO ST. L. J. 849, 857 (2006).

This initial CFIUS role was sufficient to make Congress comfortable that at least some mechanism monitored foreign investment. However, the change in the political-economic context since Executive Order 11,858 and heightened fear of foreign dominance of U.S. assets led to legislative initiatives to increase the CFIUS' powers and Congress' oversight. Three Congressional bills have affected the CFIUS's operation: (1) the Exon-Florio Amendment; (2) the Byrd Amendment; and (3) FINSA. This article focuses on FINSA, however a background on the Exon-Florio is particularly important to understanding FINSA.

## 2. The Exon-Florio Amendment to the Defense Production Act

The Exon-Florio Amendment was passed as part of the Omnibus Trade and Competitiveness Act of 1988<sup>21</sup> ("Exon-Florio") to amend § 721 of the Defense Production Act of 1950.<sup>22</sup> Exon-Florio expanded CFIUS's role by authorizing the President to suspend or prohibit any transactions leading to the control of U.S. companies by foreign persons when: (1) there *is credible evidence* of national security threats and; (2) when other legislation cannot provide "adequate and appropriate authority for the President to protect national security."<sup>23</sup> The dramatic increase of foreign ownership of U.S. assets in the mid 1980's yielded anti-foreign sentiments, which reflect the socio-political context of Exon-Florio's passage.<sup>24</sup> At that time the

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<sup>21</sup> Pub. L. No. 100-418, § 5021, 102 Stat. 1107, 1425 (1988). Congress named Exon-Florio after its primary sponsors, Sen. John James Exon (D-NE) and Rep. James J. Florio (D-N.J.). For more information on Sen. Exon *see* Associated Press, *Former Senator J. James Exon, 83, Dies*, N.Y. TIMES, June 13, 2005, available at [http://www.nytimes.com/2005/06/13/politics/13exon.html?\\_r=1&scp=1&sq=Senator%20James%20Exon&st=cse](http://www.nytimes.com/2005/06/13/politics/13exon.html?_r=1&scp=1&sq=Senator%20James%20Exon&st=cse).

<sup>22</sup> 50 U.S.C. app. § 2170 (2006).

<sup>23</sup> Pub. L. No. 100-418, § 5021(d)(1)(2), 102 Stat. 1107, 1425-26 (1988) (noting that the literal language of the statute allows the president to act under Exon-Florio upon credible evidence of national security threat and when "provisions of law, other than this section and the *International Emergency Economic Powers Act* do not [ ] provide adequate and appropriate authority for the President to protect national security").

<sup>24</sup> *See* Carroll, *supra* note 9, at 172-73.

public opinion discussed the potential negative impacts of foreign investment, such as adverse effects on domestic employment and trade, political process, and national security.<sup>25</sup>

Japan attracted special attention from Congress because of its growing presence as a successful investor in the U.S. automobile and banking sectors.<sup>26</sup> This background set the stage for the case that provided the principal impetus for the Exon-Florio's passage: the 1987 proposed sale of the U.S.-based chip maker Fairchild Semiconductor Company ("Fairchild") to the Japanese-based computer maker Fujitsu Corporation ("Fujitsu").<sup>27</sup> As a major supplier of chips to the U.S. military, Fairchild was a strategic company to the U.S. defense industry. The potential Japanese control over such a strategic U.S. company raised several national security concerns.<sup>28</sup> Congress disliked the deal and vociferated national security concerns and political pressure to terminate the transaction.<sup>29</sup> Due to the political pressure and negative publicity over the deal, Fujitsu withdrew its bid for Fairchild.<sup>30</sup> President Reagan could have blocked the transaction under the IEEPA, but he was reluctant to declare a state of emergency against Japan, a Cold War ally.<sup>31</sup>

Even though the Fujitsu-Fairchild deal fell through, Congress was displeased with President Reagan's reluctance to block the deal. Congress wanted a stronger mechanism to

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<sup>25</sup> See Graham & Krugman, *supra* note 6, at 3-5.

<sup>26</sup> *Id.* at 53-54 (noting that Honda Motor Company and five other Japanese manufacturers yielded 21.8% of the automobile production in the U.S. in 1992. The Japanese presence in the banking sector exceeded this percentage).

<sup>27</sup> THEODORE H. MORAN, THREE THREATS: AN ANALYTICAL FRAMEWORK FOR THE CFIUS PROCESS 9 (Peter G. Peterson Institute for International Economics 2009).

<sup>28</sup> *Id.*

<sup>29</sup> See Carroll, *supra* note 9, at 173.

<sup>30</sup> See Donna K. H. Walters, *Deal to Sell Fairchild Semiconductor to Fujitsu Canceled*, L.A. TIMES, March 17, 1987, available at [http://articles.latimes.com/1987-03-17/business/fi-12290\\_1\\_fairchild-semiconductor](http://articles.latimes.com/1987-03-17/business/fi-12290_1_fairchild-semiconductor) (last visited Nov. 12, 2010).

<sup>31</sup> See Carroll, *supra* note 9, at 173 (noting that IEEPA's wording – requiring a state of emergency declaration – essentially made the presidential veto untenable for all but the most extreme transactions).

oversee similar transactions, and as a result it proposed the Exon-Florio bill.<sup>32</sup> The early Congressional discussions about the Exon-Florio show Congress' "long-range concerns regarding economic and political independence, [as well as national security]."<sup>33</sup> The House Committee Report regarding House Bill 3 and section 907 (one of the early versions of the Exon-Florio Amendment) pointed to the proposed takeover of Fairchild by Fujitsu as an example of a transaction detrimental to national security.<sup>34</sup>

When the bill reached the Senate some Senators ardently supported it, but others criticized the inclusion of broad economic factors, such as "economic security" and "national unemployment" in the determination of a transaction's effect on national security.<sup>35</sup> The Executive branch and others who opposed the original bill feared that it could impede beneficial foreign investment.<sup>36</sup> After long debates and President Reagan's threat to veto the bill, Congress passed a final version that excluded the broad commercial regulation provisions.<sup>37</sup> Congress attached the Exon-Florio to the Defense Production Act of 1950 to limit it to the national security context.<sup>38</sup> Following the enactment of Exon-Florio<sup>39</sup> President Reagan issued Executive Order

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<sup>32</sup> *Id.*

<sup>33</sup> H.R. REP. NO. 100-40, pt.2, at 47 (1987).

<sup>34</sup> H.R. REP. NO. 100-40, pt.2, at 48 (1987) (the Committee argued that semiconductors were essential to national defense, and its loss to a foreign country would be disastrous).

<sup>35</sup> *See id.* at pt. 2 at 25 (statement of Sen. James J. Exon). *See also* Federal Collection of Information on Foreign Investment in the U.S.: Hearing Before the S. Comm. on Commerce, Sci. and Transp., 100th Cong. 10 (1988) (statement of John W. Bryant, Rep. from Texas); Byrne, *supra* note 20, at 862-63 (discussing the broad "essential commerce" and "economic welfare" goals that were proposed as part of the CFIUS's review process, but which were ultimately rejected); Carroll, *supra* note 9, at 174.

<sup>36</sup> *See* Howard E. O'Leary & Judy Parker Jenkins, "Exon-Florio": *An Impediment to Foreign Investment in the United States?*, 69 MICH. B. J. 680, 681 (1990) (criticizing Exon-Florio).

<sup>37</sup> Omnibus Trade and Competitiveness Act of 1988, S. 1420, 100th Cong. § 1401 (1987); *see also* 19 U.S.C. § 2901 (1988).

<sup>38</sup> Omnibus Trade and Competitiveness Act of 1988, S. 1420, 100th Cong. § 1401.

<sup>39</sup> 50 U.S.C. app. § 2170 (2006).

12,661 delegating to CFIUS his authority to examine transactions for national security concerns and retaining the power to suspend or prohibit a transaction.<sup>40</sup>

The U.S. had its first major systematic regulation of foreign investment. For the first time Congress expressly authorized the President to block specific private transactions on national security grounds, without having to declare emergency or hostilities against the investor's country. Under Exon-Florio, the President or his designee-CFIUS has broad authority to investigate the national security effects of transactions by or with foreign individuals that could result in foreign control of U.S. companies.<sup>41</sup> Not surprisingly "control" includes any type of arrangement that would allow the foreign investor to direct the decisions of the acquired American entity,<sup>42</sup> which illustrates the broad sweep of the statute.

#### **a. Exon-Florio's CFIUS Review Process in a Nutshell**

The Exon-Florio review process starts with the filing of a voluntary notice to CFIUS by the parties to a covered transaction.<sup>43</sup> The filing must contain a description of the transaction, appropriate timelines, a list of target assets, and the parties' detailed background.<sup>44</sup> The CFIUS has thirty days to determine whether to conduct an investigation.<sup>45</sup> Each CFIUS member (agencies and departments) conducts its own internal analysis and presents its conclusions to the Committee. If the CFIUS finds at this point that the transaction does not pose any national security threat, it will not conduct any further investigation and the parties may consummate the deal without U.S. interference on the grounds of national security. However, if the CFIUS

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<sup>40</sup> Exec. Order No. 12,661, 3 C.F.R. 618 (1988), reprinted as amended in 50 U.S.C. app. § 2170 (2006).

<sup>41</sup> 50 U.S.C.A. app. § 2170 (West 1991 & Supp. 2009).

<sup>42</sup> See 31 C.F.R. § 800.204 (2005).

<sup>43</sup> 50 U.S.C.A. app. § 2170(a)(3) (West 1991 & Supp. 2009) (defining "covered transaction" as a merger, acquisition, or takeover by or with foreign persons, which could result in foreign control of persons engaged in interstate commerce).

<sup>44</sup> See Travalini, *supra* note 14, at 785.

<sup>45</sup> 50 U.S.C.A. app. § 2170(b)(1)(E).

determines that an investigation is warranted, then it must investigate the deal and reach a conclusion within forty-five days.<sup>46</sup> Within fifteen days after completion of the investigation, the President must announce whether or not to block the transaction.<sup>47</sup> In order to block a transaction the President must find credible evidence that the transaction would impair national security and that no other provision of law provides the necessary relief to ameliorate the national security threat.<sup>48</sup>

Although the Exon-Florio language does not *mandate* the CFIUS notification filing, failure to do so allows the President to take the extreme measure of post-consummation divestiture.<sup>49</sup> The practical result is that most parties to a proposed foreign acquisition file notifications expecting to obtain CFIUS clearance to avoid, or at least minimize, future risks of divestiture.<sup>50</sup> This is illustrated by the two hundred notifications filed in 1989 compared to just fourteen notifications in filed in 1988, the year of Exon-Florio's enactment.<sup>51</sup>

### **b. Exon-Florio's National Security and Confidentiality Provisions**

The Exon-Florio does not define the term "national security," nor did the regulations that followed the Amendment.<sup>52</sup> Congress did this intentionally so that national security remained a broad and flexible concept so the law did not stifle the President's ability to affirmatively act.<sup>53</sup> The government anticipated that any definition of national security would give foreign entities

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<sup>46</sup> *Id.* at §2170(b)(2)(C).

<sup>47</sup> 50 U.S.C.A. app. § 2170(d)(2) (West 1991 & Supp. 2010).

<sup>48</sup> *Id.* § 2170(d).

<sup>49</sup> *Id.*

<sup>50</sup> See UNITED STATES GENERAL ACCOUNTING OFFICE, FOREIGN INVESTMENT – IMPLEMENTATION OF EXON-FLORIO & RELATED AMENDMENTS 3 (1995), available at <http://www.gao.gov/archive/1996/ns96012.pdf> [hereinafter GAO 1995 Report].

<sup>51</sup> *Id.* at 4.

<sup>52</sup> 31 C.F.R. § 800 app. A, § II (2005)

<sup>53</sup> *Id.*

and sophisticated attorneys the opportunity to structure transactions to get around the definition thereby creating a loophole.<sup>54</sup>

The Exon-Florio laid out several factors to test whether a transaction related to national security. The factors assess whether: (1) the deal affects domestic production needed for projected national defense; (2) the transaction affects the capability and capacity of domestic industries to meet national defense; and (3) whether foreign citizens' control of domestic industries affects the United States' capability to meet national security requirements.<sup>55</sup>

It is unclear how the CFIUS weighs and analyzes each factor because Exon-Florio has a confidentiality provision, which prevents public release of detailed information on CFIUS-reviewed transactions.<sup>56</sup> Thus, most of CFIUS' review process information is not publicly available, and much of the information that becomes available is often provided by the very companies involved in the transactions. The 1995 Exon-Florio report to Congress suggests that an important factor the Committee takes into consideration is the possibility that foreign countries gain control over key industries critical to national security.<sup>57</sup> Consequently, the government focuses on the preservation and promotion of its leadership in technologies that are crucial to the U.S. defense system.<sup>58</sup> Even though these factors are helpful in identifying CFIUS' issues based on the industry sector targeted by the investor, they still do not provide very clear guidelines. Thus the analysis of two landmark Exon-Florio transactions helps to shed some light into how the government enforces the Amendment.

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<sup>54</sup> Byrne, *supra* note 20, at 867.

<sup>55</sup> 50 U.S.C.A. app. § 2170 (e)(1)-(3) (West 1991 & Supp. 2010).

<sup>56</sup> 50 U.S.C.A. app. § 2170(c) (2006) (stating in relevant part: “[a]ny information or documentary material filed with [the CFIUS] pursuant to this section shall be exempt from disclosure...and no such information or documentary material may be made public, except as may be relevant to any administrative or judicial action or proceeding”).

<sup>57</sup> See GAO 1995 Report, *supra* note 50, at 2.

<sup>58</sup> *Id.*

### c. The CATIC-MAMCO Transaction

On November 3, 1989 MAMCO Manufacturing Inc. (“MAMCO”) filed a voluntary notification to CFIUS about its proposed sale to China National Aero-Technology Import & Export Corporation’s (“CATIC”).<sup>59</sup> MAMCO was a Seattle based U.S. aircraft parts manufacturer, which had never exported any of its products. CATIC was a People’s Republic of China government-related manufacturer of civilian and military aircrafts, aircraft engines, and missiles.<sup>60</sup> During the 30-day review process, CFIUS raised national security issues because it was concerned that sensitive technology held by MAMCO would be transferred to CATIC absent export controls.<sup>61</sup> Before the CFIUS completed the takeover review, CATIC purchased all MAMCO’s voting securities, completing the transaction.<sup>62</sup>

Shortly after the transaction’s closing, the CFIUS unanimously concluded that it posed national security threats. The Committee reasoned that: (1) CATIC had ties to the Chinese military; (2) the transaction would give CATIC “unique access” to U.S. aerospace companies; and (3) some of the technology produced by MAMCO was export-controlled.<sup>63</sup> On February 3, 1990 the New York Times reported that “Bush, Citing Security Law, Voids Sale of Aviation Concern to China.”<sup>64</sup> Based on CFIUS’ unanimous recommendations President George H. W. Bush ordered the divestiture of MAMCO by CATIC. Some speculated that CATIC’s past actions

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<sup>59</sup> UNITED STATES GENERAL ACCOUNTING OFFICE, STATEMENT OF ALLAN I. MENDELOWITZ DIRECTOR INT’L TRADE, ENERGY, AND FIN. ISSUES BEFORE THE SUBCOMM. ON COMMERCE, CONSUMER PROT. AND COMPETITIVENESS 4 (1990) [*hereinafter* Allan Mendelowitz’s Statement], <http://archive.gao.gov/t2pbat11/140886.pdf>.

<sup>60</sup> Nuclear Threat Initiative - CATIC’s profile, <http://www.nti.org/e-research/profiles/China/index.html> (*last visited* on Nov. 12, 2010).

<sup>61</sup> Allan Mendelowitz’s Statement, *supra* note 59, at 5.

<sup>62</sup> *Id.* at 4.

<sup>63</sup> Byrne, *supra* note 20, at 872.

<sup>64</sup> Andrew Rosenthal, *Bush, Citing Security Law, Voids Sale of Aviation Concern to China*, N.Y. TIMES, Feb. 3, 1990, at 1.

and connections to the Chinese government motivated the President's decision.<sup>65</sup> Because of the Exon-Florio's confidentiality provision the public will never ascertain Bush's actual motivation. The CATIC-MAMCO deal was the first and only transaction that a president has ever formally blocked after a negative recommendation from CFIUS.<sup>66</sup>

#### **d. The Thomson-CSF and LTV Corporation Transaction**

In 1992 Congress and the national media paid close attention to another extremely controversial CFIUS transaction. Thomson-CSF, Inc. ("Thomson"), a French government-owned company participated in a complex bidding process to acquire LTV Corporation ("LTV"), a U.S. company that owned an aerospace division. The LTV missile division's primary customer was the U.S. government and LTV held classified Department of Defense ("DOD") contracts.<sup>67</sup> LTV filed for bankruptcy and needed to raise cash. In order to obtain liquidity, the Bankruptcy Court in New York approved the sale of LTV's missile division and considered proposals from Thomson, Martin Marietta (a U.S. Aerospace company), and Lockheed (a U.S.-owned company).<sup>68</sup> The Court hesitated to consider Thomson's bid because of the risk that CFIUS would not approve the transaction.<sup>69</sup> However, Thomson was confident that it would secure CFIUS clearance and it made an offer to pay LTV a \$20 million "reverse break-up fee" in the event it failed to close the transaction due to inability to obtain U.S. approval.<sup>70</sup>

Thomson's bid won and the company filed a CFIUS notice regarding the takeover. Meanwhile Congress and the Pentagon expressed concerns about the potential leakage of LTV's

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<sup>65</sup> *Id.*

<sup>66</sup> See COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES, ANNUAL REPORT TO CONGRESS – PUBLIC VERSION 2 (2008), <http://www.treasury.gov/resource-center/international/foreign-investment/Documents/CFIUS-Annual-Rpt-2008.pdf> [*hereinafter* CFIUS 2008 report](last visited on Jan. 8, 2011).

<sup>67</sup> *In Re Chateaugay*, 198 B.R. 848, 850-51 (S.D.N.Y. 1996).

<sup>68</sup> See Moran, *supra* note 27, at 16.

<sup>69</sup> *In Re Chateaugay*, 198 B.R. at 852.

<sup>70</sup> *Id.*

classified information and defense technology to Thomson's parent company in France.<sup>71</sup>

Numerous members of Congress strongly objected to the acquisition and proposed at least a few bills designed to block the deal.<sup>72</sup>

Martin Marietta (Thomson's U.S. competitor) used the national security argument to fight Thomson's takeover and to try to get back into the bidding process.<sup>73</sup> Marietta argued that Thomson had sold military equipment to Iraq in the past, and could easily sell LTV's technology to a U.S. enemy again following consummation of the deal.<sup>74</sup> Congress held multiple hearings about the Thomson-LTV deal and continued to pressure both the CFIUS and Thomson. The DOD conducted extensive negotiations with Thomson regarding potential mitigation agreements. To prevent Thomson's access to LTV's export-controlled information, "the DOD conducted extensive negotiations with Thomson regarding potential mitigation agreements." However, they failed to reach an agreement.<sup>75</sup> Ultimately the DOD strongly opposed the transaction because Thomson had provided radar equipment to Iraq during the Gulf War, implicating what the DOD deemed a national security risk.<sup>76</sup>

Thompson finally accepted the defeat in its attempt to acquire LTV and withdrew from the CFIUS process. CFIUS never issued a formal opinion disapproving the Thomson-LTV deal. However, Congress' pressure, the public opinion, and the political context strongly support the inference that CFIUS would issue a negative recommendation. As a final defeat to Thomson, the Bankruptcy court enforced the "reverse break-up fee" provision of the bid and forced Thomson

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<sup>71</sup> Moran, *supra* note 27, at 16.

<sup>72</sup> See Eric Schmitt, *G.A.O. Investigator Opposes LTV Unit Sale*, N.Y. TIMES, June 26, 1992 at D4.

<sup>73</sup> Byrne, *supra* note 20, at 873.

<sup>74</sup> *Id.*

<sup>75</sup> *Id.* at 873-874.

<sup>76</sup> *Id.* at 874.

to pay \$20 million to LTV.<sup>77</sup> This outcome undoubtedly defeated Thomson and sent a clear message to foreign investors interested in purchasing U.S. defense industry companies.

Nevertheless Congress remained dissatisfied and anticipated that other transactions involving a foreign government could occur without appropriate review mechanisms. Thus, it decided to strengthen the Exon-Florio.

### e. The Byrd Amendment

In immediate response to the Thomson-LTV landmark case, Congress passed the Byrd Amendment (“Byrd Amendment”) to section 721 of the *Defense Production Act*. This Amendment mandates CFIUS investigation of: (1) any transaction involving an entity controlled or acting on behalf of a foreign government; (2) seeking to acquire control of an American company; (3) which “could affect” U.S. national security.<sup>78</sup> This section lowered the standard that would trigger a review of an acquisition from a “threat to national security” standard used for private business to the “could affect” national security standard for foreign-government related transactions. The loosening of this provision indicates a high likelihood that CFIUS will review any foreign-government transaction involving a U.S. business.<sup>79</sup> It also suggests that CFIUS could easily classify any transaction by, with, or involving a foreign government as a national security threat.

Additionally, the Byrd Amendment added two more factors to the Exon-Florio’s original list of national security assessment factors. Under the Byrd Amendment, CFIUS can consider the

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<sup>77</sup> See *In Re Chateaugay Corp.*, No. 96-5110, 1997 WL 138384, at \*1 (2d Cir. Mar. 25, 1997) (upholding the enforcement of the reverse break up fee and finding it irrelevant, for purposes of the purchase contract (bid), that Thomson used its best efforts to try to reach a deal with, and obtain approval from the government). Thomson challenged the enforceability of the reserve breakup fee, since it was unable to perform its purchasing obligations due to governmental opposition to the deal. *Id.* However, the court affirmed the imposition of the contractual fee. *Id.*

<sup>78</sup> National Defense Authorization Act for the Fiscal Year 1993, Pub. L. No. 102-484, §837, 106 Stat. 2315, 2463-65 (1992) (codified as amended at 50 U.S.C. app. § 2170 (2006)).

<sup>79</sup> See Carroll, *supra* note 9, at 176.

transaction's potential effect on various military sales to foreign countries and its potential effect on the U.S.'s technological leadership role in the area.<sup>80</sup> The "potential effect" language makes it easier for CFIUS to reject transactions that might eventually affect military sales or the U.S. technological leadership, without the need to assess the actual likelihood that it could occur.

Finally, the Byrd Amendment requires that CFIUS send a report to Congress at the conclusion of any investigation<sup>81</sup> to allow Congress to exert political pressure in the CFIUS' Exon-Florio implementation. The Byrd Amendment also requires the President to report to Congress as to whether credible evidence of a foreign coordinated strategy to acquire U.S. critical technology companies, or industrial espionage exists.<sup>82</sup> The higher scrutiny levels and the Congressional notification provisions sent a clear message to CFIUS that Congress would carefully observe and review CFIUS' recommendations and decisions.

### **B. Post 9/11 Application of Exon-Florio: Finding the Balance Between National Security and Open Foreign Investment**

Following the September 11, 2001 terrorist attacks, the U.S. government has heightened national security standards and has reviewed foreign-related transactions with greater scrutiny.<sup>83</sup> A primary theme in recent U.S. government practices includes a stronger defensive position and broader security measures.<sup>84</sup> The 9/11 attacks changed the paradigm of state-actors' security threats to non-state actors' security threats. As described by Travalini, "the CFIUS responded to the threat of terrorism by tightening the requirements for approval of foreign acquisitions and

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<sup>80</sup> 50 U.S.C. app. § 2170(f)(4)-(5).

<sup>81</sup> *See id.* § 2170(b)(3)(A).

<sup>82</sup> *Id.* § 2170(m)(3)(A)(ii).

<sup>83</sup> Travalini, *supra* note 14, at 787.

<sup>84</sup> Gregory W. Bowman, *Thinking Outside the Border: Homeland Security and the Forward Deployment of the U.S. Border*, 44 HOUS. L. REV. 189, 200-01 (2007).

adding the Department of Homeland Security to its membership in 2003.”<sup>85</sup> Despite this higher standard of scrutiny, the official statistics show that most transactions are likely to obtain CFIUS approval, which has been a point of criticism to the CFIUS.<sup>86</sup> However, many of these approvals have been conditioned to the foreign investor’s willingness to enter into mitigation agreements. Mitigation agreements involve a broad range of measures to restrict or limit the foreign investor’s control over the acquire business. Such agreement can require the purchaser to provide representations and assurances to the CFIUS, as well as voting control mechanisms (to limit or eliminate control of the U.S. entity by the foreign investor).<sup>87</sup> From 1997 to 2008 the government entered into fifty-two mitigation agreements.<sup>88</sup>

Since the 9/11 attacks, the U.S. government has fought to achieve a balance between increasing national security protection through foreign investment regulation and maintaining investment freedom.<sup>89</sup> Many post 9/11 transactions have raised Congressional concerns over the quality of the CFIUS and Exon-Florio’s analytical scheme. It seems that national security is not only a legitimate concern of the highest order, but also a reason for the government to intervene in private transactions involving unpopular foreign investors.

Selective involvement in such transactions may have occurred in 2005 when the China National Offshore Oil Corporation (“CNOOC”) made an \$18.5 billion cash bid for the California-based oil company Unocal Corporation (“Unocal”).<sup>90</sup> When CNOOC publicly

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<sup>85</sup> Travalini, *supra* note 14, at 787.

<sup>86</sup> See GAO 1995 Report, *supra* note 50, at 4. CFIUS 2008 Report, *supra* note 66, at 15.

<sup>87</sup> See CFIUS 2008 Report, *supra* note 66, at 15.

<sup>88</sup> *Id.*

<sup>89</sup> Travalini, *supra* note 14, at 787.

<sup>90</sup> See Moran, *supra* note 27, at 18-19 (analyzing the CNOOC proposed purchase of Unocal and concluding that a less superficial analysis would have led to the conclusion that there was no real national security threat related to the transaction). Moran points out that oil supply sources were not tightly concentrated and switching costs were not high. Thus even if the deal went through, the U.S. would have had 21 countries (including 15 non-OPEC countries)

announced the bid, Congress was outraged and expressed serious concerns regarding the possibility that a foreign investor could take control of a domestic energy company. It urged strict CFIUS review of the deal and expressed its concern “about China’s ongoing and proposed acquisition of energy assets around the world, including those in the United States.”<sup>91</sup> According to Congress introduced various bills that could have prevented the transaction and it conducted hearings regarding potential changes to the Exon-Florio.<sup>92</sup> CNOOC ultimately withdrew its bid due to the “political environment in the United States.”<sup>93</sup> Instead of the deal receiving an objective evaluation into the possible risks, the political climate thwarted the purchaser from pursuing the deal. The American Chevron Corporation took advantage of the negative publicity and security concerns and purchased Unocal.<sup>94</sup> The termination of this deal sent another clear message to foreign investors that they would incur significant political opposition if they attempt to invest in the U.S. energy industry.

### 1. The Dubai Ports World and P&O Steam Navigation Transaction

“Don’t let them tell you this is just the transfer of title.  
Baloney. We wouldn’t transfer title to the Devil;

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that would have immediate availability of oil to export to the U.S. Such alternative supply sources were greater than Unocal’s entire U.S. production. Additionally, six more countries could be called on to make up for large portion of Unocal’s U.S. output. The result is that U.S. buyers would simply replace Unocal’s “minuscule” production with extra imports without a great economic impact. Finally Moran argues that the U.S. energy needs would have been better served by energy policies that promote efficiency and stimulate new energy sources rather than focusing on blocking deals of this kind). *Id.*

<sup>91</sup> See Travalini, *supra* note 14, at 788 (citing Joseph Mamounas, *Controlling Foreign Ownership of U.S. Strategic Assets: The Challenge of Maintaining National Security in a Globalized and Oil Dependent World*, 13 LAW & BUS. REV. AM. 381, 382 (2007).

<sup>92</sup> Byrne, *supra* note 20, at 876.

<sup>93</sup> See Travalini, *supra* note 14, at 789 (citing Gauray Sud, *From Takeovers to Vetting CFIUS: Finding a Balance in U.S. Policy Regarding Foreign Acquisitions of Domestic Assets*, 39 VAND. J. TRANSN’L L. 1303, 1306 (2006); Carroll, *supra* note 9, at 181-82 (pointing out that the opponents to the CNOOC-Unocal deal’s main argument was that the purchase would “give China more leverage over the international oil market, and regardless of the facts to this specific transaction, the symbolic nature of giving in to China’s resource goals should be prevented at all costs.” “Unsurprisingly, hawkish arguments toward China played a large role in congressional opposition to the deal.” *Id.* at 181. He further points out that energy companies have no direct connection to the military, and could not impose any direct threat to the U.S. economy or national security). *Id.* at 181-182.

<sup>94</sup> See Travalini, *supra* note 14, at 789.*Id.*

we're not going to transfer title to Dubai.”<sup>95</sup>

Not long after the CNOOC-Unocal transaction fell through, Congress faced another challenge in balancing national security concerns with foreign investment. Dubai Ports World (“DPW”), a United Arab Emirates (“UAE”) government-owned company entered into an agreement to purchase London-based Peninsular & Oriental Steam Navigation Company (“P&O”). The British-P&O managed the operation of six major U.S. ports, including New York, Baltimore and Miami.<sup>96</sup> In October 2005 the two companies informally informed CFIUS that they would seek review of the transaction.<sup>97</sup> The CFIUS then requested an intelligence assessment of DPW, which showed that DPW had neither the intention nor the capability to threaten U.S. national security.<sup>98</sup> CFIUS did not identify national security issues in this transaction because DPW would neither be in charge of the ports themselves nor port security. Rather, it would manage terminal port operations without acquiring the ports themselves.<sup>99</sup> Moreover, the Coast Guard and the U.S. Customs and Border Protection would remain in charge of port security. Based on this previous assessment, DPW and P&O filed their formal notices with the CFIUS requesting review of the transaction on December 16, 2005.<sup>100</sup>

On January 17, 2006 the CFIUS announced its approval of the transaction, and on February 24 it issued a press release in a public acknowledgment of the transaction’s approval.<sup>101</sup> This was very unusual considering the Exon-Florio’s confidentiality provision requiring all

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<sup>95</sup> Moran, *supra* note 27, at 24 (citing Senator Frank Lautenberg’s (D-NJ) statement about the DPW-P&O deal).

<sup>96</sup> Jonathan Weisman & Bradley Graham, *Dubai Firm to Sell U.S. Port Operation*, WASH. POST, Mar. 10, 2006, available at <http://www.washingtonpost.com/wp-dyn/content/article/2006/03/09/AR2006030901124.html>.

<sup>97</sup> Travalini, *supra* note 14, at 789.

<sup>98</sup> Press Release, Dep’t of the Treasury, CFIUS and the Protection of the National Security in the Dubai Ports World Bid for Ports Operations (Feb. 24, 2006), available at <http://www.treasury.gov/press-center/press-releases/js4071.aspx> [*hereinafter* Treasury Press Release Feb. 24, 2006](last visited Jan. 8, 2011).

<sup>99</sup> *Id.*

<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

investigations to remain unavailable to the public. Congress voiced strong concerns that the CFIUS review neglected national security considerations.<sup>102</sup> Critics to the transaction argued that UAE had a history as an operational and financial base for hijackers who carried out the 9/11 attacks.<sup>103</sup> They further argued that DPW could be influenced by Al-Qaeda into weakening ports' security.<sup>104</sup> Even though DPW offered assurances that its key employees in the U.S. would be American citizens, and it committed to the additional 45-day CFIUS review period, the transaction simply could not overcome Congress' opposition.<sup>105</sup> Some members of Congress proposed emergency legislation with antiterrorism appeal.<sup>106</sup> President George W. Bush supported the deal and threatened to veto any congressional action blocking it. However, after several weeks of controversy, political pressure and negative publicity, DPW decided to drop its bid. It sold P&O's American port operations to American International Group ("AIG").<sup>107</sup>

After the DPW incident Congress deemed the CFIUS review under Exon-Florio inadequate to protect national security under the current state of affairs of terrorist threats. In an attempt to expand the scope of foreign investment regulation Congress prepared another amendment to Exon-Florio, broadening the interpretation of national security.

### **C. The Foreign Investment and National Security Act of 2007**

“Unless the United States continues to welcome foreign investment, [it] could find [itself] more and more isolated in an increasingly interdependent world. Maintaining an open environment for investment is, in itself, deeply in the national security interest of the

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<sup>102</sup> See Deborah M. Mostaghel, *Dubai Ports World Under Exon-Florio: A Threat to National Security or a Tempest in a Seaport?*, 70 ALB. L. REV. 583, 606 (2007).

<sup>103</sup> *Id.*

<sup>104</sup> See Carroll, *supra* note 9, at 184.

<sup>105</sup> Mostaghel, *supra* note 102, at 609-10.

<sup>106</sup> *Id.* at 612 (discussing the legislation proposed to prohibit the DPW-P&O transaction, and prevent sales of U.S. port operations to companies with foreign ownership).

<sup>107</sup> See Joan Gralla, *AIG NY-NJ OK Pact with DP World for Newark Port*, REUTERS, Feb. 16, 2007, available at <http://www.reuters.com/article/ousiv/idUSN1665883120070218>.

United States.”<sup>108</sup>

On July 26, 2007 President Bush signed the FINSA into law.<sup>109</sup> FINSA amends the Defense Production Act of 1950 and replaces many of Exon-Florio’s provisions. FINSA represents a victory for Congress in the long-running struggle to expand the covered transactions, broaden the national security concept and increase congressional oversight. FINSA keeps the Exon-Florio basic structure in place and expressly reaffirms CFIUS’s role in reviewing foreign investment transactions.<sup>110</sup>

The main additions brought in by FINSA can be summarized as follows: (1) it expands the concept of national security to include issues relating to “homeland security”;<sup>111</sup> (2) expands ‘covered transactions’ to include transactions involving ‘critical infrastructure’;<sup>112</sup> (3) includes additional factors that CFIUS might consider in its assessment of national security threats;<sup>113</sup> (4) expressly authorizes CFIUS to require mitigation agreements and monitor compliance;<sup>114</sup> (5) prohibits notice withdrawals without CFIUS prior approval;<sup>115</sup> (7) expands Congressional access to CFIUS transactions’ specific information;<sup>116</sup> and (8) provides for civil penalties if parties to a

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<sup>108</sup> Marchick’s Remarks, *supra* note 3, at 3.

<sup>109</sup> Pub. L. No. 110-49, §§ 2-7(b), 8-10, 121 Stat. 246, 259 (2007) (amending 50 U.S.C. app. § 2170 (2000)).

<sup>110</sup> 50 U.S.C. app. § 2170(k) (codifying the CFIUS, establishing its membership, role, and authority in the implementation of Exon-Florio); *See also* Stagg, *supra* note 12, at 351 (arguing that CFIUS’s statutory establishment strengthened its authority and “prompted companies to be more receptive to its requirement”).

<sup>111</sup> 50 U.S.C. app. § 2170(a)(5).

<sup>112</sup> *See Id.* at § 2170(b)(2)(B)(i)(III).

<sup>113</sup> *Id.* § 2170(f)(6)-(10).

<sup>114</sup> *See Id.* §§ 2170(l), 2170(l)(3)(B)(ii).

<sup>115</sup> 50 U.S.C. app. § 2170(b)(1)(C)(ii).

<sup>116</sup> 50 U.S.C. app. §§ 2170(b)(3)(A)-(C), 2170(m)(1)-(2) (subsection 2 states the content requirements of the annual reports that CFIUS shall issue to Congress, which include, *inter alia*: a list of all notices filed and all reviews or investigations completed in the period; a detailed discussion of all perceived adverse effects of covered transactions on the national security or critical infrastructure of the United States; specific cumulative and, as appropriate, trend information on the business sectors involved and the countries from which the investments have been made).

transaction violate FINSA and/or mitigation agreements.<sup>117</sup> The additional factors that CFIUS can consider in its national security analysis under FINSA specifically target, *inter alia*, situations that involve terrorist-related parties or countries. For example, the statute allows the CFIUS to consider whether the foreign government involved in the transaction has adhered to non-proliferation regimes, as well as that country's relationship with the U.S. (specifically in regards to "cooperating in counter-terrorism efforts").<sup>118</sup>

FINSA maintains the Exon-Florio provision that precludes judicial review of any findings regarding national security, and actions blocking or suspending reviewed transactions.<sup>119</sup> The obvious result is that foreign investors cannot seek relief from CFIUS or Presidential decisions in U.S. Courts. FINSA also requires CFIUS to issue guidance on the types of reviewed transactions that presented national security and critical infrastructure concerns.<sup>120</sup> This is a positive change from the previous statute because it increases transparency and advances foreign investors' awareness about the threshold of risk deemed acceptable by CFIUS.

### 1. Interpreting FINSA's Key Terms

On January 23, 2008, President Bush issued Executive Order 13,456 implementing FINSA and directing the CFIUS to issue additional regulations.<sup>121</sup> On November 14, 2008, the CFIUS issued the required regulations, which focused heavily in defining "covered transaction"

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<sup>117</sup> *Id.* § 2170(h)(3)(A); 31 C.F.R. § 800.801 (a)-(g)(2008) (establishing civil penalties not to exceed \$ 250,000 for intentional or negligent submission of material misstatements, omissions, false certifications and violation of mitigation agreements).

<sup>118</sup> *Id.* § 2170(f)(9)(A)-(B).

<sup>119</sup> *Id.* § 2170(e).

<sup>120</sup> *Id.* §2170(b)(2)(E).

<sup>121</sup> Exec. Order No. 13,456, 73 Fed. Reg. 4677 (Jan. 23, 2008) (amending Exec. Order 11,858).

and “control” under FINSA.<sup>122</sup> However, the key concept of “national security” remained undefined. The following subsections discuss key FINSA terms according to the CFIUS’ 2008 regulations.

**a. “National Security”**

Like the situation with Exon-Florio, neither FINSA nor the regulations define the term “national security” or the phrase “threatens to impair the national security.”<sup>123</sup> However, FINSA does expand the concept of national security to include “issues relating to ‘homeland security, including its application to critical infrastructure.’”<sup>124</sup> Furthermore, the statute defines critical infrastructure as a “system or asset, whether physical or virtual, so vital to the [U.S.] that [its] incapacity or destruction... *would have a debilitating impact on national security*” (emphasis added).<sup>125</sup> But this is as far as FINSA and the regulations go into defining national security. FINSA instead provides a list of illustrative factors for CFIUS and the President to consider in assessing whether the transaction poses national security risks.<sup>126</sup>

The Exon-Florio and Byrd amendments already covered some of these factors, however FINSA added some key factors. Under FINSA, the CFIUS may also consider: (1) the potential national security related effects on U.S. critical technologies; (2) the potential effects on the long-term projection of U.S. requirements for sources of energy and other critical resources and

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<sup>122</sup> See THE DEP’T OF THE TREASURY, CFIUS REFORM: FINAL REGULATIONS ISSUED ON NOVEMBER 14 1-2 (2008), available at <http://www.treasury.gov/resource-center/international/foreign-investment/Documents/CFIUS-Final-Regulations-new.pdf> [hereinafter CFIUS Regulations].

<sup>123</sup> See 50 U.S.C. app. §2170(b)(2)(B)(i)(I).

<sup>124</sup> *Id.* at §2170(a)(5); See also Moran, *supra* note 27, at 5 (explaining that “critical” and “essential” are introduced by FINSA without qualification, leaving the potential for protectionist mischief. Under the current unqualified standard the door is open for assertions that every “critical” and “essential” industry sector should be kept in the hands of home-country citizens or business.).

<sup>125</sup> See U.S.C. app. §2170(a)(6); see also 31 C.F.R. § 800.208 (2008).

<sup>126</sup> See Guidance Concerning the Nat’l Sec. Review Conducted by the Comm. on Foreign Inv. in the United States, 73 Fed. Reg. 74,569 (Dec. 8, 2008).

materials; (3) the potential national security related effects on critical infrastructure including major energy assets; (4) the potential effects of the transaction on the sales of military goods, equipment, or technology to countries that present concerns related to terrorism and missile proliferation; and (5) the potential for transshipment or diversion of technologies with military applications, including the relevant country's export control system.<sup>127</sup>

These additional factors clearly provide more information to foreign investors, which prior to FINSA, lacked information given the confidential nature of the investigation process.<sup>128</sup> Nevertheless, the president retains broad discretion to determine if the transaction presents any national security considerations. The CFIUS 2008 Guidance suggests that national security risk is a result of the interaction between threat and vulnerability of a particular industry sector, and the potential consequences of such interaction to national security.<sup>129</sup> But there is no simple or "CFIUS-proof" standard.

The intention remains to keep "national security" a broad and flexible concept so that the President to can act in his or her discretion whenever necessary to protect the nation. The downside of this flexibility is that national security might in many cases turn out to mean whatever the President decides it to be under the circumstances, to the detriment of the necessary freedom of foreign investment.

#### **b. "Covered Transaction" and "Control"**

FINSA defines "covered transaction" as any "merger, acquisition, or takeover... by or with any foreign person, which *could result in foreign control* of any person engaged in interstate

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<sup>127</sup> *Id.* at 74,469-70.

<sup>128</sup> See Stagg, *supra* note 12, at 348.

<sup>129</sup> *Id.*

commerce in the United States” (emphasis added).<sup>130</sup> Control is a key threshold concept of FINSA because both the CFIUS authority to review a transaction and the president’s power to block it are predicated on foreign control of an American company engaged in interstate commerce.

The regulations define “control” in a very broad manner. Control includes any form of direct or indirect power, through ownership of voting interests, or any formal or informal contractual arrangement that would otherwise allow the acquiring company to decide important matters affecting the target entity.<sup>131</sup> “Important matters affecting the target entity” relate, but are not limited to, its sale, transfer of assets, reorganization, closing, alteration of production, entry into, and termination of contracts.<sup>132</sup> This means that not only mergers and acquisitions are subject to analysis, but also the acquisition of stock interests with voting rights, forming a joint venture, and the conversion of convertible voting securities.<sup>133</sup> Control is a case-by-case analysis, and neither FINSA nor the regulations specify a certain percentage of shares or number of board seats that a foreign investor has to hold in order to have “control” of the U.S. entity.

On the other hand, an important exception to the covered transactions is the “passive investment” scenario. Under the regulations a foreign person does not control an entity if it satisfies a two-pronged test. First the CFIUS assess whether a foreign person holds ten percent or less of the outstanding voting interest in the entity, second, whether it holds its investment solely

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<sup>130</sup> 50 U.S.C. app. § 2170(a)(3) (emphasis added). *See also* 31 C.F.R. at § 800.212 (2008) (defining “foreign entity” as any entity, group or subdivision thereof, in whatever form organized, with “its principal place of business outside the United States or its equity securities primarily traded on one or more foreign exchanges”).

<sup>131</sup> *See* 31 C.F.R. §800.204 (a)(1)-(10).

<sup>132</sup> *Id.* (listing all the important matters affecting the target entity, which the CFIUS will consider when assessing control).

<sup>133</sup> *See also Id.* at § 800.204(c)(1)-(6) (excluding from “control” certain minority shareholder protections, i.e., the power to prevent an entity from entering into contracts with majority investors); *See also* §800.204(d) (clarifying that the CFIUS will consider on a case-by-case basis whether other non-listed minority shareholder protections do not confer control over an entity).

for the purpose of passive investment.<sup>134</sup> Passive investment occurs when the foreign investor has no plan or intent to control the entity, or ever develops or possesses any purpose other than passive investment.<sup>135</sup> Even though such passive investment is not a ‘covered transaction’ this is a determination that the CFIUS will make, not the parties themselves. Thus, the parties to such a transaction still must file a CFIUS notification and obtain an official holding that the deal is not a ‘covered transaction.’<sup>136</sup>

Finally, foreign investors should be aware that the CFIUS’s analysis focuses on substance over form. This means that the CFIUS will disregard legal devices or other arrangements entered into for the purpose of avoiding FINSA. Instead, the CFIUS will analyze the substance of the transaction regardless of its legal form.<sup>137</sup>

### c. “Certifications to Congress”

FINSA has significantly increased Congress’ ability to access confidential information relating to transactions that have undergone CFIUS review. FINSA provides that upon completion of CFIUS investigations, the Secretary of Treasury shall transmit a certified notice and subsequent written report to Congress on the results of the investigation.<sup>138</sup> Each certified notice and report shall contain a description of the actions taken by CFIUS with respect to the transaction, and the factors that were determinative in the transaction analysis.<sup>139</sup> Furthermore,

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<sup>134</sup> 31 C.F.R. § 800.302(b) (2005).

<sup>135</sup> 31 C.F.R. § 800.223 (2005). The regulations expressly indicate that this rule applies to all types of investors equally, rather than assuming that certain types of institutions are passive investors. *Id.*

<sup>136</sup> 31 C.F.R. § 800.403(c) (2005).

<sup>137</sup> 31 C.F.R. § 800.104 (2005) (providing an example of a transaction that the CFIUS would consider a device to avoid FINSA).

<sup>138</sup> 50 U.S.C. app. § 2170(b)(3)(A)-(B).

<sup>139</sup> *Id.* at § 2170(b)(3)(C).

each certified notice and report shall state that there are no unresolved national security concerns with the reported transaction.<sup>140</sup>

This certification requirement allows Congress to access to confidential information that was not otherwise available to it under the Exon-Florio structure. However, the main concern about this information-sharing is that FINSA does not prevent Congress from releasing the contents of the reports to the public.<sup>141</sup> For example, FINSA allows the Majority and Minority Leaders of the Senate, the Speaker and Minority Leader of the House, the House Committee on Financial Services, as well as the staff of any authorized Congressmen to gain access to CFIUS information.<sup>142</sup> State senators may even access confidential information about transactions involving critical infrastructure and companies that have a principal place of business in their state.<sup>143</sup>

### III. ANALYSIS

The CFIUS process under Exon-Florio allowed for great political pressure and considerations other than national security to play a role in foreign investment transactions in the U.S. FINSA's broad national security concept and lack of clear guidance's as to how the U.S. government will access national security risks will likely perpetuate the same problems of political pressure, persecution of unpopular investors, and protectionism concerns that occurred under the previous regulations. Under this regulatory scheme, foreign investors carry the risk of having their transaction blocked under the proxy of national security when such threat may not

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<sup>140</sup> *Id.* at § 2170(b)(3)(C)(ii).

<sup>141</sup> *See* Stagg, *supra* note 12, at 353 (discussing the negative effects of the CFIUS's release of information to Congress without any guarantee that FINSA's confidentiality provision will be respected).

<sup>142</sup> *See* 50 U.S.C. app. § 2170 (g)(1) (requiring the CFIUS to provide briefings on a covered transaction upon request of any Member of Congress, which may also be provided to the *congressional staff* of the requesting Congressman having appropriate security clearance). *See also id.* at § 2170(b)(3)(C)(iii).

<sup>143</sup> *Id.* at § 2170(b)(3)(C)(iii)(V).

actually be present. While the nation's security is a concern of the highest order, past cases reveal that even in the absence of national security risks, Congress has used political pressure to delay and prevent unpopular foreign investors' deals to further protectionist concerns. This result erodes the U.S. free foreign investment policy and principals of laissez-faire economics, and has the potential to stifle U.S. economic growth by driving away efficient investment.

**A. FINSA's Lack of Analytical Guidance for National Security Risks has the Potential to Turn FINSA into an Instrument for Protectionism**

Fear of foreign control of U.S. industries has politicized the CFIUS review process under Exon-Florio, and FINSA perpetuates this model. The CFIUS's unchecked interpretation of national security concerns permit the U.S. government to use FINSA as a tool to perpetuate protectionism and threaten efficient economic investment that has made the United States a global economic leader.

First, FINSA's broad national security concept fails to provide analytical guidance to distinguish between serious and implausible national security threats. The terms "critical," as applied to technology and infrastructure, is introduced without qualification, leaving the potential for protectionist abuse.<sup>144</sup> For example, FINSA fails to provide guidance regarding when the CFIUS should consider the fact that the existence of a multiplicity of alternative supplies to the critical infrastructure would render any attempt to delay, deny, or place conditions on supply access entirely non-credible. This lack of Congressional guidance to the CFIUS is problematic because it permits the government to assume that every "critical" sector of the U.S. industry

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<sup>144</sup> See *supra* note 124 and accompanying text.

should be kept in the hands of home-country citizens or business when little or not security issue is at risk.<sup>145</sup>

That same problem related to critical infrastructure also exists in regards to military goods. For instance, FINSA and the CFIUS regulations fail to consider whether alternative sources for the sale of military goods are easily available.<sup>146</sup> Instead, the CFIUS identifies that a defense related or critical infrastructure industry will be under foreign control, and that fact alone becomes determinative to the deal.<sup>147</sup> For example, in the CNOOC-Unocal deal, political pressure resulted in CNOOC's withdrawal prior to the conclusion of the CFIUS analysis.<sup>148</sup> However, nothing indicated that either CFIUS or Congress considered the fact that twenty one countries, (including fifteen non-OPEC countries) had oil for export greater than Unocal's entire U.S. production, and that six more could supplement a large portion of Unocal's U.S. output.<sup>149</sup>

The conclusion that CNOOC's acquisition of Unocal would have affected the U.S. national energy interests was far out from reality. Congressional and the public opinion reaction, driven by protectionist sentiments, failed to consider the true economic reality behind the proposed transaction.<sup>150</sup> The U.S. government used national security as a proxy to drive away an unpopular investor. Under FINSA's broad national security and critical infrastructure umbrella, the government has set a dangerous precedent that permits it to terminate future deals similarly to the CNOOC-Unocal case. The risk remains high that Congress and other governmental agencies will use FINSA as a protectionist tool given that CFIUS's analysis does not take into

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<sup>145</sup> See *supra* notes 6 at 53-54, 124 and accompanying text.

<sup>146</sup> See Graham & Krugman, *supra* note 6 at 53-54; see *supra* note 124 and accompanying text.

<sup>147</sup> See Travalini, *supra* note 14; see Bowman, *supra* note 84.

<sup>148</sup> See *supra* note 93 and accompanying text (suggesting that no real national security threat was present in the CNOOC-Unocal deal).

<sup>149</sup> See *supra* note 90 and accompanying text (analyzing the transaction and suggesting that extra imports of oil to make up for Unocal production would not have a significant economic impact).

<sup>150</sup> See *supra* notes 90, 93 and accompanying text.

account the availability of alternative supply sources at no great additional costs to the economy.<sup>151</sup>

Second, the definition of national security changes with the popular perception of threats, which allows the political pressures inherent in the Exon Florio/FINSA investigations to prevent CFIUS from accurately balancing security concerns. That was the case when the public and Congressional unease about high oil prices terminated a relatively innocuous Chinese acquisition of a U.S. oil company.<sup>152</sup> Protectionist practices are even more evident after the 9/11 attacks when the public opinion's perception of foreign threat and Congressional discomfort with globalization ran high like in the DPW deal.<sup>153</sup>

Although the CFIUS announced its approval of the DPW deal, Congress exercised political pressure to the extent that DPW could not feasibly move forward with the recently acquired port management business. As has been the case since the "fears of the Japanese dominance" in the 1950's up to the more recent DPW case, Congress and the public opinion have taken advantage of the unclear standards of FINSA (then Exon-Florio) to create xenophobic political pressure on foreign investment strategies and acquisitions. Fairchild, Thomson-LTV, CNOOC –Unocal, and the DPW deal all represent situations when political pressure and bad publicity resulted in voluntary withdrawal from a transaction.<sup>154</sup> These transactions demonstrate that unclear statutory terms permit the public opinion to define the term as a means of opposing any perceived foreign threat that may not have anything to do with national security.

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<sup>151</sup> See *supra* notes 90,93 and accompanying text.

<sup>152</sup> See *supra* text accompanying note 91 (describing the political pressure over the CNOOC-Unocal proposed deal and the reasons beyond national security that caused the termination of the deal).

<sup>153</sup> See *supra* text accompanying notes 103-06 (noting the post 9/11-fear surrounding the DPW deal and the U.S. policy of strengthening foreign investment controls).

<sup>154</sup> See *supra* text accompanying notes 26-28, 72, 98; See *also* note 93 and accompanying text.

Finally, FINSA has unjustly expanded the “national security” concept with the unqualified inclusion of “homeland security.” The homeland security term is so broad that it has the potential to turn unrelated issues that impose little or no threat to national security into national security threats. The risk is that the “homeland security” concept will provide those opposing an open foreign investment policy an additional argument to define national security as related to whatever foreign threat is currently in vogue, in a manner does not really involve national security and instead thwart beneficial foreign investment.

According to the CFIUS’ 2008 Annual Report to Congress, in the years 2005 to 2007, companies filed 313 notices of transactions. Roughly eight percent of such notices were withdrawn during the review stage, five percent resulted in an investigation (45 day review process), and less than one percent resulted in a Presidential decision.<sup>155</sup> If the U.S. government can deem the transactions that resulted in presidential action (less than one percent of the total transactions in a two year period) as legitimate national security threats, then CFIUS must be reviewing too many transactions that are otherwise outside of its scope of authority. The result is that the lack of clear guidance regarding the CFIUS review of national security-related transactions creates additional administrative burdens on the government as well.

Additionally, the CFIUS 2008 report showed that there was no credible evidence of a widespread coordinated strategy among foreign governments or corporations to acquire critical U.S. technologies through the use of foreign direct investment.<sup>156</sup> If the CFIUS itself has observed, analyzed, and found that foreign investment has not been used as a national security threat in the vast majority of transactions that were reviewed between 2006-2008, the

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<sup>155</sup> See CFIUS 2008 report, *supra* note 66, at 3.

<sup>156</sup> See *id.*

government should create filters that allow it to focus in transactions that really relate to national security.

Although a broad national security concept provides the President the necessary flexibility to deal with real threats not readily fit in any specific category listed in FINSAs, the lack of more specific guidance leaves the government without appropriate filters to discern truly troublesome cases from nonthreatening ones. The result is an unnecessary burden or inefficiency on foreign investors, the U.S. government, and the U.S. economy.

### **B. FINSAs's expanded Congressional Oversight Has The Potential To Unduly Politicize Foreign Investment**

FINSAs has significantly increased Congress' ability to politicize foreign investment transactions, even when no real national-security threat exists. It allows members of Congress (including their staff) to access confidential information regarding CFIUS transactions, which will likely result in more congressional pressure over certain unpopular transactions.<sup>157</sup>

By allowing so many members of Congress (including their staff) to view CFIUS's confidential information, FINSAs significantly increases the probability that politicians will thwart foreign investment deals through political rhetoric, instead of via objective analyses.<sup>158</sup> Another problematic point is that FINSAs fails to clarify who decides which information should remain classified. It is important to note that most of the information being disclosed to Congress

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<sup>157</sup> See *supra* notes 141-42 and accompanying text.

<sup>158</sup> See Stagg, *supra* note 12, at 353.

under FINSA is corporate confidential information. The main concern about this information sharing is that contents of the reports might leak to the public.<sup>159</sup>

In weighing the risks of investing in the United States, foreign investors consider the consequences of compromising sensitive proprietary information through the CFIUS review process. Companies are generally unwilling to risk the disclosure of strategic competitive information during the CFIUS review process if they believe such disclosure could lead to compromising business objectives and proprietary information.<sup>160</sup> This will likely disincentive foreign investors and heighten the political nature of foreign investment in the United States when no risk of national security is at stake. The history of transactions that have been cancelled as a result of political pressure and negative publicity is long.<sup>161</sup> Even before FINSA, Congress has intervened effectively (although indirectly) to prevent many transactions from being concluded.<sup>162</sup> That was the case with the Fujitsu-Fairchild proposed deal, CNOOC-Unocal, Thomson-LTV and DPW. In each instance, Congress exercised political pressure by threatening to pass legislation specifically banning the transaction.<sup>163</sup> Even when CFIUS approval looked certain, the parties would abandon the transaction at the prospect of a battle with Congress. This is illustrated in the DPW case, where despite the CFIUS's announcement of approval, DPW could not feasibly fight Congress. Congressional pressure alone has been a highly effective tool, if not the most effective one, in preventing undesired deals.<sup>164</sup> Under FINSA, Congress has statutory authority to access confidential information relating to CFIUS transactions. The risk is

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<sup>159</sup> See *supra* notes 141-42 and accompanying text (discussing the negative effects of CFIUS's release of information to Congress without any guarantee that FINSA's confidentiality provision will be respected).

<sup>160</sup> See Stagg, *supra* note 12, at 357.

<sup>161</sup> See *supra* text accompanying notes 30, 64-65, 100-106.

<sup>162</sup> *Id.*

<sup>163</sup> *Id.*

<sup>164</sup> See *supra* text accompanying notes 92-93, 102-04.

high that this information sharing will give Congress even more leverage to intervene in foreign investment transactions.

FINSA should not allow the CFIUS to provide Congress with detailed reports of specific transactions. It is important that Congress be informed about foreign investment transactions and their effect upon the nation's economy and national security. However, FINSA already requires detailed annual reports to Congress, which are appropriate for such an assessment. For example, the CFIUS 2008 report to Congress contains specific findings about potential espionage activities and foreign intelligence threats.<sup>165</sup> By providing the additional briefing and disclosure requirements (beyond what is provided in the annual reports) FINSA exaggerates transparency to the detriment of foreign investors.

Additionally, when foreign investors disclose corporate confidential information to CFIUS they rely on FINSA's confidentiality provision and the guarantee of privacy.<sup>166</sup> Without assurances that corporate sensitive data will be protected, investors might withdraw given the fear that U.S. competitors or lobbying groups related to specific industry sectors might acquire access to such information. Domestic competitors could seek to win a bidding war with a foreign investor by exerting influence on the CFIUS process through lobbying Congress as exemplified in the Thomson-LTV case, when Thomson's American competitor, Martin Marietta, used national security as a proxy to argue against Thomson's bid to acquire LTV.<sup>167</sup> In that case, Congressional pressure was so intense that Thomson gave up the bid, and Martin Marietta

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<sup>165</sup> See *supra* text accompanying note 82; 50 U.S.C. app. §§ 2170(b)(3)(A)-(C); 50 U.S.C. app. §§ 2170(m)(1)-(2); see *supra* text accompanying note 116.

<sup>166</sup> See 50 U.S.C. app. § 2170(c)(2006) and accompanying text (explaining FINSA's confidentiality provision).

<sup>167</sup> See *supra* text accompanying notes 73-74.

eventually acquired LTV.<sup>168</sup> Similarly to the Thomson-Marietta situation, there is also the possibility that special interest groups will likely gain influence in the CFIUS process as a result of information disclosed to congress. Thus, the potential for political abuse is high.

The U.S. has been a leading example of free market ideas, as well as of policies favoring foreign investment. However, FINSA's allowance of such a close congressional oversight over CFIUS transactions can negatively impact the free market. Congress has acted in xenophobic ways as illustrated in the DPW transaction.<sup>169</sup> The risk remains that emotionally-charged messages and arguments aimed at guaranteeing votes during upcoming elections will disrupt the freedom in private transactions and foreign investment despite the lack of actual national security risks.

Finally, the continual perceived use of CFIUS as a tool of economic protectionism could lead to retaliation in the form of restrictions of American foreign investment by other countries. Perception that CFIUS investigations are based upon political enmity could deter international cooperation with American foreign policy goals at a time when such cooperation is essential to global stability and cooperation.

### **C. FINSA's Broad Coverage Has the Potential to Burden Foreign Investors and Negatively Impact Foreign Investment**

Foreign investment in the United States has the potential to benefit the domestic economy,<sup>170</sup> even though "national security concerns over the increased opportunities for espionage and technology disruptions are paramount."<sup>171</sup> Although national security justifies

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<sup>168</sup> *Id.*

<sup>169</sup> See *supra* text accompanying notes 95, 102-106.

<sup>170</sup> See *supra* notes 1, 3-4 and accompanying text.

<sup>171</sup> See Travalini, *supra* note 14, at 795 (discussing FINSA's potential effects on foreign investment transactions).

governmental monitoring and intervention in cross-border deals taking place in the U.S., FINSA's broad coverage will likely have a negative impact in foreign investment.

From the foreign investors' perspective, FINSA's new CFIUS review process has several implications. First, it adds time and risk to the investment due to the CFIUS reviews. Second, it increases the costs and burdens to involved parties related to the transaction. Third, it adds the risk that the investor might have to make concessions and enter into mitigation agreements, in which the government holds more leverage and significantly more bargaining power than the foreign investor. Fourth, it adds the potential risk that competing domestic bidders may use the CFIUS review process to manipulate the system and make unsolicited or hostile bids.<sup>172</sup> The additional time, risk and cost implications will likely serve as a deterrent to some potential investors who might not welcome the intense scrutiny and lengthy process necessary for the transaction to proceed. Additionally, the investor must therefore consider additional costs regarding attorney's fees, CFIUS filing fees, production of documents, data, among other logistical costs associated with approval. These costs exist even when the transaction poses no national security threat because the CFIUS review is mandatory. Even when investors properly determine that the transaction will not impose national security threats, such an assessment has to come from CFIUS itself.<sup>173</sup> Although the CFIUS filing is *voluntary*, it is also the only way to avoid risks of divestiture.

Similarly, the risks associated with potential concessions or mitigation agreements are likely to be a deterrent. Concessions have generally included divesting from subsidiaries with sensitive technology, and entering into agreements concerning network security, government

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<sup>172</sup> *See id.*

<sup>173</sup> *See supra* notes 135-37 and accompanying text.

access to critical infrastructure, and voting arrangements.<sup>174</sup> Some foreign investors might be willing to enter into mitigation agreements when the agreement does not significantly affect the business' management. However, it seems obvious that in many instances the investor will have to make a difficult and potentially costly decision regardless of the situation. This is aggravated by the fact that the government holds a significantly stronger bargaining position than any foreign investor, and is mostly free to impose "take it or leave it" deals. Mitigation agreements are appropriate when real national security threats are involved, but they should not be used as a means to disincentive "undesired" transactions or to interfere in the free market.

Competing bidders for domestic acquisitions may use the CFIUS process to their advantage by manipulating the system thereby making unsolicited hostile bids as exemplified in the Thomson-LTV and CNOOC-Unocal deals. In the latter case, the American Chevron Corporation acquired Unocal despite the lack of a real national security threat in Unocal's proposed acquisition by CNOOC.<sup>175</sup> This is merely another factor, or potential barrier, that a foreign investor must consider when investing in the U.S, especially when it is in a sensitive industry such as critical infrastructure.

In addition to the implications on foreign investors, multiple implications threaten domestic companies. The U.S. economy welcomes foreign investment because it depends on it for economic stability.<sup>176</sup> In a globalized and integrated world, economic isolationism can be disastrous. Given its relatively low savings rate and the global economic crisis, the U.S. depends heavily on foreign capital inflows to help promote growth and to fund the federal budget

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<sup>174</sup> See *supra* text accompanying notes 87-88.

<sup>175</sup> See *supra* text accompanying note 87.

<sup>176</sup> See *supra* notes 3-4 and accompanying text (noting that as of 2006 foreign investors employed more than 5 million Americans, and were responsible for close to 20% of U.S. manufacturing GDP).

deficit.<sup>177</sup> This is also true at the microeconomic level, where many U.S.-based businesses depend on doing business abroad. Innumerable U.S. businesses depend on foreign markets to buy their products and services, as well as to sell to the U.S. companies raw materials, manufactured goods, commodities, etc.<sup>178</sup> Due to this dependence, it is in the best interests of U.S. national security that other countries provide an efficient and safe investment environment for U.S. businesses. U.S. businesses could possibly suffer a negative effect when other countries enact laws similar to FINSA in an effort to retaliate against U.S. isolationism. For example, “Canada, China and Thailand have all passed legislation creating new rules for foreign investment, including new screening requirements and reporting regimes.”<sup>179</sup>

Despite the undisputed need for foreign investment regulation and national security protection, FINSA’s current structure is unbalanced. The broad and undefined national security concept has created additional burdens on foreign investors even when no real national security threat exists. This structure is likely to disrupt the U.S. free foreign investment policy, the country’s domestic economy, and U.S. investment in other markets.

#### **D. Congress Can Improve FINSA by Providing Clear Guidance to Real National Security Risks, Limiting Congressional Involvement, and Providing a “Fast Track” Analysis for Passive Investment**

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<sup>177</sup> See generally WAINE M. MORRISON & MARC LABONTE, CHINA’S HOLDINGS OF U.S. SECURITIES: IMPLICATIONS FOR THE U.S. ECONOMY 1 (Congressional Research Service 2009), <http://www.fas.org/sgp/crs/row/RL34314.pdf> (arguing that “given its relatively low savings rate, the U.S. economy depends heavily on foreign capital inflows from countries with high savings rates (such as China) to help promote growth and to fund the federal budget deficit.” Morrison & Labonte point out that from June 2002 to June 2008, China’s holdings of U.S. securities increased by over \$1 trillion. Of the public debt that is privately held, foreigners hold roughly more than half. They also note that the current global financial crisis has raised considerable concern in the U.S. over the willingness of foreigners, including China, to continue to invest in U.S. securities).

<sup>178</sup> See Foreign Trade Statistics, *supra* note 3.

<sup>179</sup> See Travalini, *supra* note 14, at 797.

Congress can improve FINSA's regulatory scheme by limiting direct congressional involvement and providing clear analytical guidance to national security risks. FINSA's current structure allows Congress to unduly politicize foreign investment and erode the free foreign investment policy.<sup>180</sup> Under the U.S. Constitutional system of checks and balances it is important that Congress has some information relating to foreign investment, but Congress should not have unbridled access to specific business information and corporate data. The CFIUS annual reports to Congress suffice for this purpose and contain significant findings and aggregate information that preserves confidential information.<sup>181</sup>

Congress should amend FINSA and direct the CFIUS to issue more specific guidelines discerning truly troublesome national security risks from nonthreatening ones. Defining national security is not necessarily the solution, since this is a complex term and involves several considerations. But limiting FINSA's broad and ambiguous national security concept is necessary.<sup>182</sup> The best option is to require the CFIUS to establish and consider factors that would render a more thorough analysis of the alleged national security risk to avoid repeats of the Unocal deal.<sup>183</sup> For example, CFIUS should take into consideration whether a multiplicity of alternative supplies to the domestic critical infrastructure would mitigate or terminate risks of supply shortage. This consideration should take into account national and international alternative sources. If the domestic "critical infrastructure" company supplies a practically insignificant amount of the national demand, this should indicate that the acquisition of such company by a foreign entity creates no national security threat. Implementation of such a standard would have

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<sup>180</sup> See *supra* Part III.A-B.

<sup>181</sup> See *supra* text accompanying note 82 (stating that FINSA requires CFIUS to state in its annual report to Congress whether there is credible evidence of a foreign coordinated strategy to acquire U.S. critical technology companies, and whether there is industrial espionage).

<sup>182</sup> See *supra* text accompanying notes 124, 127 (explaining the breadth of FINSA's national security factors).

<sup>183</sup> See *supra* note 90 and accompanying text.

permitted the parties to conclude the Unocal deal and perhaps many other similar non-threatening ones.<sup>184</sup>

CFIUS should also analyze the additional costs involved with alternative supply sources. If the costs of obtaining the same good or commodity abroad are relatively similar, and the alternative source is in a U.S. trade partner, this should indicate (at least in most situations) that no real risk of domestic shortage exists.<sup>185</sup> In today's global market it is not unreasonable to acquire critical infrastructure goods or commodities abroad.<sup>186</sup> In many situations this method might be more economically efficient than developing and keeping local industries that cannot compete with foreign companies that make a better product. Congress should also require that CFIUS disclose which factors it considered assessing transactions with national security implications. Congress should require the CFIUS to provide this information in an aggregate basis, so as to protect the confidentiality of foreign investors' information. This method would enhance transparency in the review process and would save the government and foreign investors time and investment resources.

Finally, Congress should amend FINSAs to provide a simplified and faster ("fast-track") analysis for passive investment situations, since they generally do not involve foreign control of U.S. business.<sup>187</sup> This would significantly decrease the time and costs involved in the CFIUS review process (for the investor and the government), and would likely incentive passive investors to report each transaction. In addition, a "fast-track" analysis for passive investment

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<sup>184</sup> *Id.*

<sup>185</sup> *Id.*

<sup>186</sup> See Foreign Trade Statistics, *supra* note 3.

<sup>187</sup> See *supra* notes 134-36 and accompanying text (explaining passive investment situations, as well as other investment situations that might not involve control, but must be submitted to the CFIUS review for clearance).

situations would allow the CFIUS to focus on transactions that could actually affect national security without spending time and resources on non-threatening and beneficial deals.

#### IV. CONCLUSION

Protecting national security when actual threats exist is undisputedly necessary. The question of how far the concept of national security should go to the detriment of a free foreign investment policy is a more difficult issue to assess. When balancing the competing interests of national security and foreign investment policy, Congress should be mindful of the impacts of excessive regulation. When President Ford created the CFIUS over thirty years ago to monitor foreign investment in the U.S, the world socio-economical context was very different. As foreign investment intensified over the years, so did Congressional concern of foreign ownership of U.S. assets.

Congress has significantly amended the CFIUS process to increase the scrutiny of review. Not surprisingly, the latest amendment (FINSAs) came after the 9/11 attacks as an immediate response to a UAE government-owned company's attempt to acquire U.S.-based ports management. FINSAs's broad sweeping concept of national security, and expanded congressional oversight provisions has the potential to perpetuate the historical political interference with foreign investment, and disrupt the U.S. free foreign investment policy. Many pre-FINSAs transactions illustrate these concerns, when protectionist and political considerations interfered with, and ultimately prevented the conclusion of such transactions. Congress should amend FINSAs to provide clearer analytical guidance to real national security risks (including analysis of the availability and cost of alternative supply sources), and allow non-threatening transactions to go on without additional burdens and delays. A simplified "fast-track" review process for passive

investment would also benefit many foreign investors and decrease FINSA's impact in these types of investment.

Foreign investment is a vital source of job creation, development and employment of more than 5 million Americans. In a globalized economy where countries are interdependent, FINSA's lenient structure towards protectionist actions has the potential to negatively impact the free market. Considering that many sectors of the U.S. economy depend on foreign investment, FINSA's ambiguity about national security could be detrimental to the national economy. In the current state of global economic interdependence it is within the United States' best national security interests to keep a favorable policy towards foreign investment.