

## COMMENTS

### BACK TO THE FUTURE: REDEFINING THE FOREIGN INVESTMENT AND NATIONAL SECURITY ACT'S CONCEPTION OF NATIONAL SECURITY

*Where we're going, we don't need [excessive restrictions on foreign investment].*<sup>1</sup>

#### INTRODUCTION

In an age of ever-widening globalization, national governments face an increasingly difficult balance between encouraging economically beneficial foreign investment and protecting industries seen as key to national security from foreign takeover. Governments often include economic factors in their definitions of national security, as the line between military and civilian industry is blurred by the globalization of dual-use technology. The perceived threat of terrorism after 9/11 as a result of acquisitions by Middle Eastern companies has only heightened American fear of foreign acquisitions. Yet as foreign direct investment in the United States accounted for over \$1.5 trillion cumulatively in 2004,<sup>2</sup> the stakes in the dispute over which foreign transactions should be allowed are higher than ever.

Since the 1988 passage of the Exon-Florio Amendment<sup>3</sup> to section 721 of the Defense Production Act,<sup>4</sup> the executive branch of the U.S. government has screened foreign investment, including mergers and acquisitions, that could

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<sup>1</sup> BACK TO THE FUTURE (Universal Pictures 1985) (quote *available at* <http://www.imdb.com/title/tt0088763/>) (“Where we’re going, we don’t need roads.”).

<sup>2</sup> See Jeffrey H. Lowe, *Foreign Direct Investment in the United States: Detail for Historical-Cost Position and Related Capital and Income Flows, 2004–2007*, SURV. CURRENT BUS., Sept. 2007, at 35, *available at* [http://www.bea.gov/scb/pdf/2007/09%20September/0907\\_fdiustext.pdf](http://www.bea.gov/scb/pdf/2007/09%20September/0907_fdiustext.pdf).

<sup>3</sup> Omnibus Trade and Competitiveness Act of 1988, § 5021, Pub. L. No. 100-418, 102 Stat. 1107, 1425–26 (Exon-Florio Amendment) (current version at 50 U.S.C. app. § 2170 (2006)).

<sup>4</sup> Defense Production Act of 1950, ch. 932, 64 Stat. 798 (1950) (current version at 50 U.S.C. app. §§ 2061–71 (2000)).

“threaten to impair the national security.”<sup>5</sup> President Reagan delegated the review of such transactions to the Committee on Foreign Investment in the United States (CFIUS), which was composed of the heads of several different federal departments, including Treasury, Defense and Commerce.<sup>6</sup> The amendment was passed in response to fears of Japanese takeovers of high-tech companies considered critical to the defense industrial base, most notably in the production of computer chips.<sup>7</sup> However, Exon-Florio did not define the term “national security.” Instead of a definition, the amendment suggested a few broad-based factors for the CFIUS to consider so that the amendment could apply to a wide variety of international transactions.<sup>8</sup> These factors included “the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the U.S. to meet the requirements of national security.”<sup>9</sup>

Following 9/11, the CFIUS scrutinized transactions at twice the rate it had during the pre-9/11 decade.<sup>10</sup> This trend culminated in the Dubai Ports controversy, in which there was a huge political outcry over the attempt by Dubai Ports World (Dubai Ports), a United Arab Emirates (U.A.E.) company, to purchase control of the major operations of six American ports.<sup>11</sup> Despite Dubai Ports passing all of the relevant CFIUS tests with flying colors, Congress responded with a vitriolic outburst against the sale, which ultimately

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<sup>5</sup> 50 U.S.C. app. § 2170(d). Section 2170(d) explains:

[T]he President may take such action for such time as the President considers appropriate to suspend or prohibit any acquisition, merger, or takeover, of a person engaged in interstate commerce in the United States proposed or pending on or after the date of enactment of this section [Aug. 23, 1988] by or with foreign persons so that such control will not threaten to impair the national security.

*Id.*

<sup>6</sup> Exec. Order No. 12,661, 3 C.F.R. 618, 620 (1989).

<sup>7</sup> EDWARD M. GRAHAM & DAVID MARCHICK, *US NATIONAL SECURITY AND FOREIGN DIRECT INVESTMENT* 41 (2006).

<sup>8</sup> *See id.* at 38.

<sup>9</sup> Omnibus Trade and Competitiveness Act of 1988, § 5021(e)(3), Pub. L. No. 100-418, 102 Stat. 1107, 1426 (Exon-Florio Amendment) (current version at 50 U.S.C. app. § 2170(f)(3) (2006)). For the full list of factors, see *infra* note 52.

<sup>10</sup> GRAHAM & MARCHICK, *supra* note 7, at 56–58. There were seven investigations between 1991 and 2001, and seven more between 2003 and 2005. *Id.* at 57. The CFIUS does not keep any direct data on companies discouraged from acquisitions, or on reviews that did not turn into full-scale investigations. *Id.*

<sup>11</sup> Jim VandeHei & Jonathan Weisman, *Republicans Split with Bush on Ports*, WASH. POST, Feb. 23, 2006, at A1.

resulted in the passage of the Foreign Investment and National Security Act (FINSA).<sup>12</sup>

FINSA broadened the Exon-Florio factors that determine whether a transaction threatens national security by adding foreign control of “critical infrastructure,” including “energy assets,” to a list of national security interests that the CFIUS must insure are not impaired by any transaction.<sup>13</sup> This legislation further muddied the already unclear waters regarding which foreign investments are permissible and what constitutes a national security interest.

The broad, open-ended definition of national security creates four concerns. First, the interpretation of national security is driven by xenophobic political concerns, and it can be expanded to encompass whatever foreign threat moves the most votes at the time.<sup>14</sup> Second, the broad interpretation of national security creates investor uncertainty, deterring what could be economically beneficial transactions, due to the fear of public backlash, as was the case with the Dubai Ports deal.<sup>15</sup> Third, a vague interpretation of national security could lead to retaliatory foreign restrictions of American investment abroad.<sup>16</sup> Fourth, a politicized reading of national security targeted against regions such as the Middle East, or rising powers such as China, could inhibit cooperation with the war on terror and other efforts, further contributing to the international isolation of the United States.<sup>17</sup>

This Comment will argue that the solution to these concerns is to amend FINSA to limit the factors that determine national security in order to exclude

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<sup>12</sup> Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246 (2007) (to be codified at 5 U.S.C. § 5313, 31 U.S.C. § 301, 50 U.S.C. app. §§ 2061, 2170); see GRAHAM & MARCHICK, *supra* note 7, at 136–41 (discussing congressional reaction to the Dubai Ports deal).

<sup>13</sup> Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246 (2007) (to be codified at 50 U.S.C. app. § 2170(f)). The added factors for the CFIUS to consider include the following:

- (6) the potential national security-related effects on United States critical infrastructure, including major energy assets;
- (7) the potential national security-related effects on United States critical technologies;
- ...
- (10) the long-term projection of United States requirements for sources of energy and other critical resources and material; and
- (11) such other factors as the President or the Committee may determine to be appropriate, generally or in connection with a specific review or investigation.

*Id.*

<sup>14</sup> See *infra* Part III.A.

<sup>15</sup> See *infra* Part III.B.

<sup>16</sup> See *infra* Part III.C.

<sup>17</sup> See *infra* Part III.D.

protectionist or xenophobic influences and add certainty and predictability to the CFIUS process. Part I of this Comment will consider the general pre-9/11 history of the regulation of foreign investment and the application of Exon-Florio, with special attention given to the various congressional and executive interpretations of national security and the motivations behind those interpretations. Part II will analyze the change in the application of Exon-Florio after 9/11, in particular the Unocal and Dubai Ports controversies and the passage of FINSA as a legislative response. Part III sets out the problems inherent in a broad set of factors determining national security and proposes a narrower set of national security factors for the President to consider.

## I. PRE-9/11 HISTORY OF REGULATION OF FOREIGN INVESTMENT

Before the 1980s, regulation of foreign direct investment was sporadic and largely driven by the First and Second World Wars.<sup>18</sup> However, in the 1980s, fears that Japan was purchasing large portions of the American economy led Congress to pass Exon-Florio, the first major systematic regulation of foreign direct investment in the United States.<sup>19</sup> President Reagan threatened to veto the original version of Exon-Florio, which would have restricted foreign investment on economic grounds.<sup>20</sup> As a result, Congress limited the criteria for determining what constituted a threat to national security in the final version of Exon-Florio to a set of national defense-related factors that was still quite broad.<sup>21</sup> Despite the broad scope of Exon-Florio, investigations were relatively rare during the 1990s.<sup>22</sup>

### A. *Legislative History of Restrictions on Foreign Direct Investment*

Antipathy toward foreign investment has a long history in the United States. During World War I, Congress passed the Trading with the Enemy Act (TWEA),<sup>23</sup> which allowed President Wilson to nationalize the assets of many German firms, especially those within the chemical industry, as well as their

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<sup>18</sup> See GRAHAM & MARCHICK, *supra* note 7, at 2–18.

<sup>19</sup> *Id.* at 1, 5.

<sup>20</sup> See *id.* at 43.

<sup>21</sup> See *id.* at 44–45.

<sup>22</sup> See *id.* at 57.

<sup>23</sup> Trading with the Enemy Act, ch. 106, 40 Stat. 411 (1917) (current version at 50 U.S.C. app. § 1 (2006)). This act gave President Wilson broad power to stop any transaction with a foreign country that he saw fit. See *id.*

American subsidiaries.<sup>24</sup> At the same time, the United States also seized control of all foreign-owned or controlled radio stations because of fears that Germans were using the radio to communicate the positions of U.S. ships.<sup>25</sup> After World War I had come to an end, foreign radio stations were legally outlawed in 1927, and German firms and patents were auctioned off to American companies.<sup>26</sup> German assets were seized again during World War II, but as a result of the previous seizures, there were relatively few German assets left within the United States.<sup>27</sup>

After World War II, concerns about foreign investment in the United States were relatively minimal, since nearly every other major economic power had been devastated by the war and lacked capital to invest abroad.<sup>28</sup> During the 1970s, foreign investment in the United States increased considerably, although a congressional investigation discovered that the investments were coming largely from Western allies, not from Middle Eastern countries as had been feared.<sup>29</sup> Against the backdrop of perceived abuses of presidential power by the Nixon administration, Congress decided to limit the peacetime presidential authority given in the TWEA to restrict foreign investment by passing the International Emergency Economic Powers Act (IEEPA).<sup>30</sup> This law allowed the president to seize foreign assets only when a state of national

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<sup>24</sup> GRAHAM & MARCHICK, *supra* note 7, at 5–6. These assets were then administered by the U.S. Government Office of the Custodian of Alien Properties until after the war when they were transferred to private U.S. companies, which benefited the U.S. chemical industry, *id.*, an early version of protectionist industrial policy. For a discussion of how the chemical industry benefited from this transfer, see GERARD COLBY ZILG, *DUPONT: BEHIND THE NYLON CURTAIN* (1974).

<sup>25</sup> GRAHAM & MARCHICK, *supra* note 7, at 10.

<sup>26</sup> *See id.* at 11–12.

<sup>27</sup> *See id.* at 16.

<sup>28</sup> *See id.* at 18.

<sup>29</sup> *See id.* at 20. Congressman Benjamin Rosenthal led the investigation. *Id.* Congress was concerned about foreign control of the economy, especially from “unfriendly sources,” and some members wanted to use the investigations as a bargaining chip to open foreign markets to American products abroad. *See* Mark Anspach, *Congress Eyes Investment Restrictions*, MULTINAT’L MONITOR, July 1980, at 10. For a more critical look at OPEC investment, see *OPEC’s Secrets*, TIME, Oct. 5, 1981, at 69.

<sup>30</sup> International Emergency Economic Powers Act, Pub. L. No. 95-223, title II §§ 202–07, 91 Stat. 1626 (1977) (current version at 50 U.S.C. §§ 1701–06 (2006)); *see also Executive Orders and Presidential Directives, Hearing Before the H. Subcomm. on Commerce and Admin. Law of the H. Comm. on the Judiciary*, 107th Cong. 61–65 (2001) (statement of Todd Gaziano) (discussing the historical context of the IEEPA compared to other restrictions of executive power).

emergency was declared and required that those assets had to be returned to the foreign companies after the state of emergency ended.<sup>31</sup>

During the mid-1980s, the dollar was relatively weak, and many Japanese companies were flush with cash and looking to purchase U.S. companies.<sup>32</sup> Many American commentators feared that the United States was becoming owned by Japan, as Japanese competition purchased or drove out of business many prominent American corporations.<sup>33</sup> Foreign direct investment skyrocketed from 1980 to 1990; its percentage of the net national wealth more than doubled from 1.2% to 2.7%.<sup>34</sup>

The rapid increase in foreign investment produced a strong regulatory response from Congress.<sup>35</sup> During the 1980s, congressional restriction of foreign investment was driven largely by populist, anti-foreign sentiment, rather than by special interest groups such as labor or domestic corporations.<sup>36</sup> Congressional backlash against foreign direct investment was especially potent in the districts that received the bulk of the new foreign investment.<sup>37</sup>

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<sup>31</sup> 50 U.S.C. § 1701(b). The Act states:

The authorities granted to the President by section 1702 of this title may only be exercised to deal with an unusual and extraordinary threat with respect to which a national emergency has been declared for purposes of this chapter and may not be exercised for any other purpose. Any exercise of such authorities to deal with any new threat shall be based on a new declaration of national emergency which must be with respect to such threat.

*Id.*

<sup>32</sup> GRAHAM & MARCHICK, *supra* note 7, at 34–35.

<sup>33</sup> *Id.*

<sup>34</sup> Lester Davis, *Foreign Direct Investment in the U. S. and Its Impact Are Highlighted in New Commerce Department Report*, BUS. AM., Aug. 23, 1993, at 11.

<sup>35</sup> See C. S. Eliot Kang, *U. S. Politics and Greater Regulation of Inward Foreign Direct Investment*, 51 INT'L ORG. 301, 302–05 (1997).

<sup>36</sup> *Id.* at 312–13, 314. For example, labor unions were at best ambivalent about restrictions on foreign direct investment, since they feared that such restrictions could result in lost jobs. *Id.* at 314.

<sup>37</sup> *Id.* at 312. For example, Representative James Florio, for whom Exon-Florio was named, represented New Jersey, where foreign direct investment skyrocketed in the late 1980s. John Dunning & Lorna Wallace, *New Jersey in a Globalising Economy*, in FOREIGN DIRECT INVESTMENT AND THE GLOBAL ECONOMY: CORPORATE AND INSTITUTIONAL DYNAMICS OF GLOBAL-LOCALISATION 253, 255–57 (Nicholas A. Phelps & Jeremy Alden eds., 1999). For more discussion on the general link between foreign investment and political backlash, see Judith Miller, *The Buying of America*, PROGRESSIVE, May 1974, at 42. Sensationalist depictions of Japanese investors in popular literature reflected such concerns. See MICHAEL CRICHTON, *THE RISING SUN* (1992) (centering on a Japanese corporation murdering a young American woman and purchasing several American senators). *The Rising Sun* plays on fears of an economic takeover and the unease that Americans feel when interacting with an unfamiliar culture, particularly that of a former military enemy.

In contrast, the executive branch supported foreign direct investment during this period.<sup>38</sup> The executive branch had access to economic data indicating that foreign direct investment was not nearly as dangerous as popular opinion believed.<sup>39</sup> Presidents were also understandably reluctant to cede power over foreign investment to Congress, as the executive branch felt that foreign direct investment benefited the U.S. economy and U.S. foreign policy goals.<sup>40</sup> The struggle between the two branches set the stage for political debates over regulation of foreign direct investment for the next two decades.

In the 1980s, Congress was particularly concerned with Japanese acquisition of high-tech companies, specifically an attempt by Fujitsu, a Japanese company, to acquire an 80% interest in Fairchild, a U.S. semiconductor manufacturer.<sup>41</sup> The Reagan administration, under congressional pressure, reviewed the Fairchild merger pursuant to the IEEPA and likely would have approved it.<sup>42</sup> But Fujitsu withdrew its offer due to the political pressure and negative publicity,<sup>43</sup> foreshadowing the future ramifications of Exon-Florio.<sup>44</sup> Blocking the sale under the IEEPA would have required a declaration of a state of emergency,<sup>45</sup> a step that Reagan likely was reluctant to take regarding a transaction with a Cold War ally like Japan. The wording of the IEEPA essentially made the presidential veto untenable for all but the most extreme transactions.<sup>46</sup> The reluctance of the Reagan administration to block the sale displeased Congress, and thus began the formulation of the Exon-Florio bill.

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<sup>38</sup> See Kang, *supra* note 35, at 313.

<sup>39</sup> See *id.* at 313 (noting that the White House had access to Treasury and Commerce data that was not available to Congress); BENJAMIN J. COHEN, IN WHOSE INTEREST? 134 (1986) (implying that the Executive, with access to unreleased statistics, did not express the same public apprehension as Congress toward foreign, and in particular Middle Eastern, investment).

<sup>40</sup> See Kang, *supra* note 35, at 313. Presidents were also reluctant as an institutional matter to cede power to Congress to engage in micro-management of foreign direct investment, and thus to affect foreign relations with other countries. See *id.*

<sup>41</sup> GRAHAM & MARCHICK, *supra* note 7, at 41.

<sup>42</sup> *Id.*

<sup>43</sup> *Id.*

<sup>44</sup> See *infra* Part II (discussing the Unocal and Dubai Ports incidents).

<sup>45</sup> 50 U.S.C. §§ 1701–02 (2006). The IEEPA requires an “emergency” in order to be invoked by the president, *id.* § 1701, which would arguably constitute a declaration of hostilities against the foreign power in question.

<sup>46</sup> GRAHAM & MARCHICK, *supra* note 7, at 40–41. Thus, in passing the IEEPA, Congress limited the president’s power to restrict foreign direct investment.

### B. *Legislative History of Exon-Florio*

The original House version of the Exon-Florio Amendment—aptly named the Foreign Investment, National Security, and Essential Commerce Act—included various economic factors, such as “economic security,” “substantial unemployment,” and the impact on individual industries, in the determination of a transaction’s effect upon national security.<sup>47</sup> Members of the House argued that the president should have the option to consider such economic factors, even if they were not mandated as part of the investigation.<sup>48</sup>

The Reagan administration rejected the inclusion of economic considerations in the bill on the grounds that such a broad definition of economic security would inhibit foreign investment in the United States, which the Reagan administration was on record as supporting as critical to growth.<sup>49</sup> In fact, Treasury Secretary James Baker hinted that such a broad definition of economic security would prompt a presidential veto: “[A]mendments of this nature could cause grave damage to the U.S. economy.”<sup>50</sup> Facing this veto threat, Congress stripped the provisions mentioning “economic welfare” or “essential commerce” from the bill.<sup>51</sup>

As a result, the final version of the bill only allowed the president to forbid a transaction that affects national security. The Exon-Florio Amendment laid out several factors to test whether a transaction related to national security, without defining the term itself:

- (1) domestic production needed for projected national defense requirements,
- (2) the capability and capacity of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services, and

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<sup>47</sup> GRAHAM & MARCHICK, *supra* note 7, at 42–44; Matthew R. Byrne, *Protecting National Security and Promoting Foreign Investment: Maintaining the Exon-Florio Balance*, 67 OHIO ST. L.J. 849, 858 (2006).

<sup>48</sup> GRAHAM & MARCHICK, *supra* note 7, at 42, 44.

<sup>49</sup> *Id.* at 42–43.

<sup>50</sup> *Id.* at 43 (quoting *Foreign Acquisitions of Domestic Companies: Hearing Before the S. Comm. on Commerce, Sci., and Transp.*, 100th Cong. 68 (1987) (letter of Hon. James A. Baker, III, Sec’y, Dep’t of the Treasury)).

<sup>51</sup> GRAHAM & MARCHICK, *supra* note 7, at 43.

- (3) the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the United States to meet the requirements of national security.<sup>52</sup>

The meaning of national security was purposely left open-ended to allow the president to interpret the term broadly and to apply it to any industry.<sup>53</sup> The regulations noted that any attempt to define national security “could improperly curtail the President’s broad authority to protect the national security, and, at the same time, not result in guidance sufficiently detailed to be helpful to parties.”<sup>54</sup> The Exon-Florio Amendment to the Defense Production Act passed in 1988.<sup>55</sup>

Despite the final text of the Exon-Florio Amendment, there was still strong support in Congress for using economic factors to regulate foreign transactions.<sup>56</sup> There were multiple attempts to amend Exon-Florio in order to include economic factors in the interpretation of national security. Senator Exon himself voiced these concerns when he noted that some industries are “so critical that they must remain under American control.”<sup>57</sup> House bill H.R. 2386 would have amended the language of FINSA to include “economic and national security,”<sup>58</sup> but it never made it out of committee.<sup>59</sup> Representative Dennis Kucinich proposed a more specific amendment in H.R. 2394 as a

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<sup>52</sup> Omnibus Trade and Competitiveness Act of 1988, § 5021(e)(1)–(3), Pub. L. No. 100-418, 102 Stat. 1107, 1426 (Exon-Florio Amendment) (current version at 50 U.S.C. app. § 2170(f)(1)–(3) (2006)). A later amendment to section 2170 added an additional two factors:

(4) the potential effects of the proposed or pending transaction on sales of military goods, equipment, or technology to any country—

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- (i) . . . that supports terrorism;
- (ii) . . . [is] a country of concern regarding missile proliferation; or
- (iii) . . . [is] a country of concern regarding the proliferation of chemical and biological weapons . . .

...

(5) the potential effects of the proposed or pending transaction on United States international technological leadership in areas affecting United States national security.

<sup>50</sup> U.S.C. app. § 2170(f)(4)–(5) (2006).

<sup>53</sup> 134 CONG. REC. H2118 (1988).

<sup>54</sup> Regulations Pertaining to Mergers, Acquisitions, and Takeovers by Foreign Persons, 31 C.F.R. § 800 app. A at 712 (2008).

<sup>55</sup> GRAHAM & MARCHICK, *supra* note 7, at 34.

<sup>56</sup> *Id.* at 47.

<sup>57</sup> 135 CONG. REC. 25,352 (1989) (statement of Sen. Exon).

<sup>58</sup> Foreign Investment and Economic Security Act of 1991, H.R. 2386, 102d Cong. (1st Sess. 1991).

<sup>59</sup> GRAHAM & MARCHICK, *supra* note 7, at 47.

response to a perceived crisis in the domestic steel industry.<sup>60</sup> This bill would have required a CFIUS investigation any time a foreign person or country attempted to acquire a domestic steel company.<sup>61</sup> H.R. 2394 also never made it out of committee.<sup>62</sup> More recently, in response to the proposed acquisition of Unocal by the Chinese National Offshore Oil Company (CNOOC), Senator James Inhofe unsuccessfully proposed a bill that would require the CFIUS to consider as a factor the effect of foreign acquisitions on “national economic security.”<sup>63</sup>

However, not every effort to broaden the definition of national security failed. The 1992 Byrd Amendment mandated an investigation

in any instance in which an entity controlled by or acting on behalf of a foreign government seeks to engage in any merger, acquisition, or takeover which could result in control of a person engaged in interstate commerce in the United States that *could affect* the national security of the United States.<sup>64</sup>

As such, under the Byrd Amendment, an acquisition by a foreign government-controlled entity is considerably more likely to be subject to review—the standard being “could affect the national security”<sup>65</sup>—than an acquisition by a foreign non-governmental entity—“threatens to impair the national security.”<sup>66</sup> Of course, it is still possible for the CFIUS to find that an acquisition by a foreign government-controlled entity will not affect national security,<sup>67</sup> but the Byrd Amendment set a higher bar.

Additionally, the Byrd Amendment requires a report to Congress at the conclusion of any investigation, thus “adding to the process an opportunity for

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<sup>60</sup> The Steel and National Security Act, H.R. 2394, 107th Cong. (1st Sess. 2001).

<sup>61</sup> *Id.*

<sup>62</sup> GRAHAM & MARCHICK, *supra* note 7, at 47–48.

<sup>63</sup> National Defense Authorization Act for Fiscal Year 2006, S. 1042, 109th Cong. § 1210(b)(2)(G) (2006).

<sup>64</sup> The National Defense Authorization Act for Fiscal Year 1993, Pub. L. No. 102-484, § 837, 106 Stat. 2315, 2464 (1992) (emphasis added).

<sup>65</sup> 50 U.S.C. app. § 2170(b) (2006) (as amended by The National Defense Authorization Act for Fiscal Year 1993, Pub. L. No. 102-484, § 837, 106 Stat. 2315, 2464 (1992)); *see also* GRAHAM & MARCHICK, *supra* note 7, at 37 (discussing greater scrutiny of transactions where a foreign government-controlled entity acquires a U.S. company).

<sup>66</sup> 50 U.S.C. app. § 2170(d).

<sup>67</sup> GRAHAM & MARCHICK, *supra* note 7, at 37. The Bush administration argued that the Dubai Ports acquisition would not affect national security; many congressional critics felt that as a legal matter, the acquisition “could” affect national security, since the requirement in the statute for affecting national security was not stringent. *Id.*

Congress to exert political pressure for more vigorous, stricter enforcement.”<sup>68</sup> As individual transactions became publicized, the impact of congressional involvement increased, stirring up popular opposition.<sup>69</sup>

### C. Pre-9/11 Application of Exon-Florio

As mentioned above, President Reagan delegated implementation of Exon-Florio to the CFIUS.<sup>70</sup> The Secretary of the Treasury chairs the CFIUS, and its membership includes the Secretaries of State, Defense, Commerce, and now Homeland Security, as well as the Attorney General and several other members.<sup>71</sup> The CFIUS can review a transaction to determine if it affects national security based upon either a voluntary notice filed by the parties to the transaction or upon an agency notice filed by one of the CFIUS members.<sup>72</sup> Due to its concern that increased investigations will deter foreign investment, the Treasury Department has traditionally taken a narrow view of national security threats.<sup>73</sup> Other departments, such as Defense and Homeland Security, have taken much broader views of national security that include concerns about foreign ownership affecting “critical infrastructure,” and the long-term future of American technological leadership.<sup>74</sup> This split between departments reflects the larger political debate between the narrow and broad interpretations of the term “national security” by the CFIUS.<sup>75</sup>

The CFIUS initiates a 30-day review as an initial step after receiving notice of the transaction, followed by an additional 45-day investigation if necessary.<sup>76</sup> After the 45-day investigation, the CFIUS files a formal report with the president, recommending a course of action regarding the transaction, and the law requires a presidential decision within 15 days of receiving the report.<sup>77</sup> At any point during the review process, the companies and the

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<sup>68</sup> Christopher F. Corr, *A Survey of United States Control on Foreign Investment Operations: How Much Is Enough?*, 9 AM. U. J. INT’L L. & POL’Y 417, 430–31 (1994).

<sup>69</sup> See *infra* Parts II.C–D (concerning the Dubai Ports incident and the subsequent legislative response, FINSA); VandeHei & Weisman, *supra* note 11.

<sup>70</sup> Exec. Order No. 12,661, 3 C.F.R. 618, 620 (1989).

<sup>71</sup> Exec. Order No. 11,858, 3 C.F.R. 990 (1971–1975), *codified as amended at* 50 U.S.C.A. app. § 2170(k) (West Supp. 2009).

<sup>72</sup> 31 C.F.R. § 800.401 (2008).

<sup>73</sup> GAO, ENHANCEMENTS TO THE IMPLEMENTATION OF EXON-FLORIO COULD STRENGTHEN THE LAW’S EFFECTIVENESS 12–13 (2005), *available at* <http://www.gao.gov/new.items/d05686.pdf>.

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

<sup>75</sup> *Id.*

<sup>76</sup> GRAHAM & MARCHICK, *supra* note 7, at 35.

<sup>77</sup> *Id.*

CFIUS may come to an agreement to “mitigate” the security consequences of the deal.<sup>78</sup> Since the CFIUS rejects very few deals, the most common outcome of the CFIUS process is a mitigation agreement.<sup>79</sup>

Through the end of 2001, there were 1,391 filings with the CFIUS, with nineteen 45-day investigations (twelve taking place in the first three years of the CFIUS).<sup>80</sup> While parties withdrew eight notices after the 45-day investigation during this period, the President has formally rejected only one transaction.<sup>81</sup> As such, even immediately after the passage of Exon-Florio, proponents of the legislation complained that the standards of review were not strict enough because the CFIUS investigated such a small percentage of all transactions submitted, and only one acquisition—a 1990 Chinese acquisition of a U.S. aerospace manufacturer—was vetoed by the President, due to concerns that the acquisition would allow China to circumvent export control laws.<sup>82</sup> However, parties withdrew a number of transactions following informal consultations with the CFIUS, and the CFIUS does not keep track of or publish data that indicates when transactions are withdrawn after a filing but before a formal investigation.<sup>83</sup>

The lack of complete transparency in the CFIUS process makes it difficult to evaluate the pre-9/11 impact of the Exon-Florio Amendment. Some have argued that even Exon-Florio as enforced during the 1990s had the potential to negatively affect foreign direct investment.<sup>84</sup> However, as the Japanese “threat” of foreign acquisitions faded in the 1990s, popular disapproval of foreign direct investment also abated; after twelve investigations during the first three years of the bill, there were only five more investigations during the rest of the 1990s.<sup>85</sup>

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<sup>78</sup> *Id.* at 58.

<sup>79</sup> *Id.* at 58–69. This mitigation agreement usually consists of the company agreeing to modify the deal in some way to satisfy the CFIUS security requirements. *See, e.g., id.* at 59–69.

<sup>80</sup> *Id.* at 56–57.

<sup>81</sup> *Id.*

<sup>82</sup> *See* JAMES K. JACKSON, THE EXON-FLORIO NATIONAL SECURITY TEST FOR FOREIGN INVESTMENT 4–5 (Congressional Research Service 2005); Kit Bond, *Evaluating the National Security Risk of Chinese Investment*, HAW. REP., Oct. 17, 2007, <http://www.hawaiireporter.com/story.aspx?a0d2f3e4-e51a-4369-af02-6d66e33c1a6d> (transcript of speech delivered at the Heritage Foundation, Oct. 16, 2007).

<sup>83</sup> GRAHAM & MARCHICK, *supra* note 7, at 57.

<sup>84</sup> This argument was especially popular immediately following the passage of the bill and then following the passage of the Byrd Amendment. *See* Corr, *supra* note 68, at 420–32; Patrick L. Schmidt, *The Exon-Florio Statute: How It Affects Foreign Investors and Lenders in the United States*, 27 INT’L LAW. 795, 800–02 (1993); Cecelia M. Waldeck, *Proposals for Limiting Foreign Investment Risk Under the Exon-Florio Amendment*, 42 HASTINGS L.J. 1175, 1221 (1991).

<sup>85</sup> GRAHAM & MARCHICK, *supra* note 7, at 57.

## II. POST 9/11 APPLICATION OF EXON-FLORIO

After 9/11, the CFIUS process shifted to focus more on threats from non-state actors, most noticeably by including the Department of Homeland Security (DHS) among the departments heading the CFIUS board. This shift in focus resulted in the scrutiny of several transactions that did not fit into the traditional military-based interpretation of national security, such as the Chinese purchase of an oil company and the purchase of the operation of ports by an Arab company. The change in the Exon-Florio process culminated in the passage of FINSA, which codified a much broader interpretation of national security that encompassed energy assets and other critical infrastructure.

### A. *A Shift in Foreign Policy Perspective*

Unsurprisingly, the terrorist attacks of 9/11 dramatically changed the American perspective on national security, including the scrutiny of foreign investment. When Exon-Florio passed, at the end of the Cold War, U.S. foreign policy was still focused on the realist, state-based model of international relations.<sup>86</sup> This realist model largely envisions foreign policy as a competition between states, in which states struggle to find the proper balance between deterrence and reassurance of other governments regarding their good intentions.<sup>87</sup> According to traditional conceptions of realism, non-governmental actors have little or no significant role to play in international relations.<sup>88</sup> The end of the Cold War and the widening web of globalization broadened the spectrum of foreign policy considerations somewhat, but it was not until after 9/11 that the U.S. national security apparatus really shifted to focus more on a range of non-state security threats.<sup>89</sup> The very nature of the 9/11 attacks made it clear that the instruments of globalization could be used to attack the international order itself, and there was a resultant effort on the part of the United States to secure various commercial facilities, such as airports,

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<sup>86</sup> See Charlie Papavizas, Op-Ed., *A Makeover for Foreign Investment*, FORBES, Mar. 3, 2006, [http://www.forbes.com/2006/03/03/foreign-investment-security-cx\\_cp\\_0303security.html](http://www.forbes.com/2006/03/03/foreign-investment-security-cx_cp_0303security.html). Papavizas argues that the original intent of the Exon-Florio factors did not take into account the risk of terrorist attacks. *Id.*

<sup>87</sup> Stephen M. Walt, *International Relations: One World, Many Theories*, 110 FOREIGN POL'Y 29, 31–32 (1998). There are many different forms and permutations of realism. *Id.* at 31. For the purpose of this Comment, it is enough to know that all forms of realism consider states to be the pre-eminent actors in international affairs. *Id.*

<sup>88</sup> *Id.* at 31–32, 36.

<sup>89</sup> Christopher R. Fenton, *U.S. Policy Towards Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security*, 41 COLUM. J. TRANSNAT'L L. 195, 215–19 (2002).

chemical factories, and ports<sup>90</sup>—exemplified in the formation of the DHS to coordinate domestic security measures against terrorism.

Consistent with the realist vision of foreign policy, Exon-Florio had focused on state-based acquisitions of defense-related technologies prior to 9/11, with an emphasis on the unique capabilities acquired by foreign governments or “lost” to the United States present in each transaction.<sup>91</sup> As part of the general paradigm change toward considering threats from non-state actors after 9/11, President Bush added the head of the DHS to the CFIUS board in February 2003.<sup>92</sup> Perhaps not coincidentally, “[b]etween January 2003 and December 2005, there were six [CFIUS] investigations, and five withdrawals, more than the previous ten years combined.”<sup>93</sup> In 2006, the CFIUS conducted seven investigations, the most ever in a single year.<sup>94</sup>

### *B. The Unocal Incident: Protectionism Run Amok*

The response to the attempt of CNOOC to purchase Unocal, an American oil company, exemplified the tighter CFIUS approach.<sup>95</sup> CNOOC, a Chinese state-owned oil company, regularly purchased foreign oil companies to create joint-ventures between itself and the foreign companies.<sup>96</sup> The Chinese government recognized that there would be a CFIUS review under the Byrd Amendment, since CNOOC was state-owned, but felt that ultimately there was no security risk and that the transaction would pass the CFIUS review.<sup>97</sup>

However, on June 24, 2005, 41 members of Congress from both parties wrote to President Bush urging a thorough CFIUS review of the sale.<sup>98</sup> The letter justified the review by raising questions about “whether CNOOC was using Chinese government funds to make the purchase and whether China

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<sup>90</sup> Charles Perrow, *The Disaster After 9/11: The Department of Homeland Security and the Intelligence Reorganization*, HOMELAND SECURITY AFF., Apr. 2006, <http://www.hsaj.org/?fullarticle=2.1.3>.

<sup>91</sup> Papavizas, *supra* note 86.

<sup>92</sup> GRAHAM & MARCHICK, *supra* note 7, at 58; *see also* 50 U.S.C.A. app. § 2170(k) (West Supp. 2009).

<sup>93</sup> *Id.* at 57–58.

<sup>94</sup> CIFIUS, ANNUAL REPORT TO CONGRESS PUBLIC VERSION 3 (Dec. 2008), *available at* <http://www.treas.gov/offices/international-affairs/cfius/docs/CFIUS-Annual-Rpt-2008.pdf>.

<sup>95</sup> Jonathan Weisman & Peter S. Goodman, *China's Oil Bid Riles Congress*, WASH. POST, June 24, 2005, at A1. The bid itself took place on June 23, 2005, and congressional reaction was immediate. *Id.*

<sup>96</sup> David Barboza & Andrew Ross Sorkin, *Chinese Company Drops Bid to Buy U.S. Oil Concern*, N.Y. TIMES, Aug. 3, 2005, at A1.

<sup>97</sup> *See id.* Chevron, which was also bidding for Unocal, may have subsidized some of the political opposition to the deal in order to drive out CNOOC as a competitor. *See id.*

<sup>98</sup> Evelyn Iritani, *Chinese Bid for Unocal Stirs Up Issues*, L.A. TIMES, June 25, 2005, at C1.

would be acquiring sensitive technology.”<sup>99</sup> Congress followed up this letter with the introduction of a resolution in the House on June 29, 2005, that recognized oil and natural gas as strategic national assets and argued that the purchase of Unocal would allow for the oil reserves to be preferentially sent to China—instead of purchasing them on the open market—thus opening up the possibility of China utilizing the “oil weapon” against the United States.<sup>100</sup>

China hawks<sup>101</sup> echoed these arguments, claiming that the deal would give China more leverage over the international oil market and that regardless of the facts of the transaction, the symbolic nature of giving into China’s resource goals should be prevented at all costs.<sup>102</sup> Unsurprisingly, hawkish arguments toward China played a large role in congressional opposition to the deal.<sup>103</sup>

The Bush administration kept relatively quiet during the Unocal controversy,<sup>104</sup> and eventually CNOOC withdrew their bid in the face of the negative publicity.<sup>105</sup> The most remarkable aspect of this episode was the congressional majority’s attempt to implicitly redefine national security. The definition of national security was no longer limited to technologies that were at least arguably related to the national defense industrial complex. Congressional opponents of the Unocal sale used public debate surrounding the deal to include energy assets in an expanded interpretation of national security and continued the long-running congressional struggle to use Exon-Florio and the CFIUS review process as a protectionist tool to prevent foreign investment in U.S. industry.<sup>106</sup> Previous CFIUS reviews focused on technological acquisitions that could allow foreign countries unique access to U.S. military capabilities,<sup>107</sup> in contrast to energy companies, which had no

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

<sup>100</sup> H.R. Res. 344, 109th Cong. (2005).

<sup>101</sup> These commentators are exemplified by Frank Gaffney, who has at various times predicted that conflict with China is inevitable, and that we should support Taiwanese independence. Conn Hallinan, *Cornering the Dragon*, FOREIGN POL’Y IN FOCUS, Feb. 22, 2005, <http://www.fpiif.org/fpiftxt/950>.

<sup>102</sup> Editorial, *National Security, China and the Unocal Deal*, WASH. TIMES, July 5, 2005, at A18; *National Security Implications of the Possible Merger Between the China National Offshore Oil Corporations with Unocal Corporation: Hearing Before the H. Comm. on Armed Servs.*, 109th Cong. 1 (2005) (statement of Frank J. Gaffney, Jr., President and CEO, Center for Security Policy). Opponents of the deal considered energy security to be a part of national security and argued that competition for resources was zero-sum. *Id.*

<sup>103</sup> David Barboza, *China Backs Away from Unocal Bid; U.S. Critics Created ‘Unacceptable Risk,’* INT’L HERALD TRIB., Aug. 3, 2005, at 1.

<sup>104</sup> Iritani, *supra* note 98.

<sup>105</sup> *Id.*

<sup>106</sup> See James A. Dorn, *U.S.-China Relations in the Wake of CNOOC*, POL’Y ANALYSIS NO. 553, at 2 (Cato Inst., 2005), available at <http://www.cato.org/pubs/pas/pa553.pdf>.

<sup>107</sup> See Papavizas, *supra* note 86.

direct connection to the military. If national security can also mean “important to the United States economy,” as energy assets no doubt are, then the definition of national security differs in no meaningful sense from the original “essential commerce” bill that Reagan threatened to veto in order to strip the economic security provisions.

### C. *The Dubai Ports Incident*

On December 15, 2005, Dubai Ports World, a U.A.E. ports company, filed formal notice with the CFIUS of a deal to purchase Peninsular and Oriental Steam Navigation Company (P&O), a British firm, which controlled the major operations of six American ports.<sup>108</sup> After 30 days, the CFIUS had not objected to the filing, and the transaction moved ahead uneventfully.<sup>109</sup>

On February 11, 2006, the Associated Press ran a story on the proposed acquisition, which noted that several of the 9/11 hijackers were from the U.A.E. and that U.S. ports were vulnerable to terrorism.<sup>110</sup> The news of the potential takeover of six U.S. ports by an Arab company prompted a political firestorm.<sup>111</sup> President Bush reversed course from the quiet stance he had taken during the Unocal deal and actively defended the CFIUS approval of the Dubai deal.<sup>112</sup> He threatened to veto any congressional action blocking the Dubai purchase, while admitting that he should have consulted with Congress prior to the CFIUS review process.<sup>113</sup> Still, the political pressure against allowing an Arab country to acquire managerial control of U.S. ports was so potent that one Republican congresswoman wrote a one-line letter to President Bush: “Dear Mr. President: In regards to selling American ports to the United Arab Emirates, not just NO but HELL NO!”<sup>114</sup> Critics voiced concerns that Dubai Ports World could be influenced by members of Al-Qaeda into

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<sup>108</sup> GRAHAM & MARCHICK, *supra* note 7, at 136–38.

<sup>109</sup> *Id.*

<sup>110</sup> Ted Bridis, *United Arab Emirates Firm May Oversee 6 U.S. Ports*, WASH. POST, Feb. 12, 2006, at A17. The article leads with the information that several citizens of the U.A.E. were hijackers in the 9/11 attacks and that the maritime industry is particularly vulnerable to terrorism, but later states that neither fact will affect port security, since the same American employees will run the ports under the new ownership. *Id.*

<sup>111</sup> *Id.* Even state-level politicians, such as Arkansas Governor Mike Huckabee, felt pressure from their constituents to block the deal. David Sanger, *Dubai Expected to Ask for Review of Port Deal*, N.Y. TIMES, Feb. 26, 2006, at A1.

<sup>112</sup> Bridis, *supra* note 110.

<sup>113</sup> *Id.* Congressional Republicans regarded Bush’s stance as a political error because it put him at loggerheads with the conservative base, which wanted to block the deal. *Id.*

<sup>114</sup> VandeHei & Weisman, *supra* note 11. Such a letter indicated Bush’s weakened political stance, as a lame-duck president. *Id.*

weakening the security of the ports, despite the fact that port security would remain in the hands of the same unionized workers after the purchase.<sup>115</sup> Congress also raised the argument that since Dubai Ports World was owned by the U.A.E., the Byrd Amendment's lower standard of review for purchases by entities controlled by foreign governments should have mandated a 45-day investigation and a report to Congress.<sup>116</sup> In response, the Bush administration insisted that the Dubai Ports controversy posed "no risk to national security."<sup>117</sup>

After three weeks of controversy, Dubai Ports World decided to drop its bid in the face of negative publicity,<sup>118</sup> just as CNOOC had done. This time, Congress was not satisfied with merely expanding the interpretation of national security. After the CFIUS review approved the Dubai acquisition without a 45-day investigation,<sup>119</sup> Congress apparently felt the CFIUS process itself was insufficient and began to prepare an amendment to Exon-Florio that would become the first successful legislative attempt to broaden the interpretation of national security.

#### *D. The Foreign Investment and National Security Act*

On July 26, 2007, President Bush signed FINSA into law.<sup>120</sup> The new legislation modified Exon-Florio in several aspects, most notably by broadening the definition of national security to encompass "homeland security," and also by including critical infrastructure, energy assets, and critical technologies under the umbrella of FINSA.<sup>121</sup> FINSA added the

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<sup>115</sup> *Id.*

<sup>116</sup> *Id.* Opponents of the deal used the language "could affect the national security" from the Byrd Amendment to argue their case that Exon-Florio required a 45-day review of the Dubai Ports deal, worrying that among other things, "Dubai Ports World could also offer a simple conduit for wire transfers to terrorist operatives in the Middle East." *Id.*

<sup>117</sup> *Id.* Robert Bonner, a former top U.S. Customs official pointed out that "[t]he reality is the major terminal operators are all foreign-owned . . . This one happens to be owned by Dubai . . ." *Id.*

<sup>118</sup> Bill Nichols & Andrea Stone, *Port Deal Off; Effect on Future Unclear*, USA TODAY, Mar. 9, 2006, at 1A.

<sup>119</sup> See VandeHei & Weisman, *supra* note 11.

<sup>120</sup> See *Bush Signs Foreign Investment Bill*, WASH. POST, July 26, 2007, <http://www.washingtonpost.com/wp-dyn/content/article/2007/07/26/AR2007072601573.html>. Bush fought with Congress to prevent FINSA from being more protectionist than it turned out to be, and he eventually signed the bill as a compromise measure. Michael A. Fletcher, *Bill on Foreign Investments in U.S. Makes Few Changes*, WASH. POST, July 30, 2007, at A13.

<sup>121</sup> FINSA, Pub. L. No. 110-49, 121 Stat. 246 (to be codified at 5 U.S.C. § 5313, 31 U.S.C. § 301, 50 U.S.C. app. §§ 2061, 2170).

Secretary of Energy as a voting member of the CFIUS<sup>122</sup> and made investigations mandatory when either an acquisition is made by an entity controlled by a foreign government or the transaction could result in the control of any critical infrastructure, including major energy assets, by a foreign business.<sup>123</sup> This requirement is excepted if the Secretary of the Treasury and the head of the lead agency jointly determine that the transaction will not impair national security.<sup>124</sup> Thus, the burden of proof to show that a controlling acquisition of “critical infrastructure” does not threaten national security has arguably shifted from the government to the companies.<sup>125</sup> FINSA does define critical infrastructure as “assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems or assets would have a debilitating impact on national security.”<sup>126</sup> But this definition still allows uncertainty, as the federal government has promulgated multiple evolving and expanding definitions of what constitutes critical infrastructure,<sup>127</sup> which could encompass more than a quarter of the national economy.<sup>128</sup> The Treasury regulations implementing FINSA do not attempt to define or limit the scope of critical infrastructure.<sup>129</sup> Such a broad

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<sup>122</sup> 50 U.S.C.A. app. § 2170(k)(2) (West Supp. 2009).

<sup>123</sup> *Id.* § 2170(b)(2)(A), (b)(2)(B)(i)(III). There is no clear definition in the Exon-Florio regulations of what constitutes control. *Id.* § 2170(a)(2). If the person or interest holds 10% or less of the outstanding voting securities in the company, then it would not constitute control. 31 C.F.R. § 800.302(b). However, Senators Evan Bayh and Jim Webb have urged stricter limits upon the definition of control and a broader regulation of foreign investment generally, with a particular focus on sovereign wealth funds. See Evan Bayh, Commentary, *Time for Sovereign Rules*, WALL ST. J., Feb. 13, 2008, at A26 (expressing concern that sovereign wealth funds can influence U.S. companies without meeting the 10% investment threshold); James Webb, *Remarks to the U.S.-China Economic and Security Review Commission*, Feb. 7, 2008, [http://www.uscc.gov/hearings/2008hearings/written\\_testimonies/08\\_02\\_07\\_wrts/08\\_02\\_07\\_webb\\_statement.php](http://www.uscc.gov/hearings/2008hearings/written_testimonies/08_02_07_wrts/08_02_07_webb_statement.php) (expressing concerns over Saudi Prince Walid Bin Talal’s influence at Citigroup, where he holds 3.9% of the shares, though he does not hold a seat on the board).

<sup>124</sup> 50 U.S.C.A. app. § 2170(b)(2)(D) (West Supp. 2009).

<sup>125</sup> Brijesh Dave & Peter Thomas, Simpson Thacher & Bartlett LLP, Reform of the CFIUS Process in the Wake of Dubai Ports World 3 (Aug. 10, 2007), <http://www.simpsonthacher.com/content/publications/pub624.pdf>.

<sup>126</sup> 50 U.S.C.A. app. § 2170(a)(6) (West Supp. 2009).

<sup>127</sup> *Foreign Ownership of Infrastructure, Hearing on H.R. 556 Before the Subcomm. on Transportation Security and Infrastructure Protection of the H. Comm. on Homeland Security*, 110th Cong. (2007) (statement of David Marchick, Covington Burling LLP) [hereinafter Marchick Testimony].

<sup>128</sup> See GRAHAM & MARCHICK, *supra* note 7, at 149 (stating that many sectors of the economy, including agriculture, transportation, and various parts of the communication industry, could fall under the definition of critical infrastructure).

<sup>129</sup> Edward L. Rubinoff, Tatman Ryder Savio & Christian C. Davis, *Treasury Issues Final CFIUS Regulations And Guidance On National Security Considerations*, METROPOLITAN CORPORATE COUNSEL, Jan. 2009, at 28, <http://www.metrocorpocounsel.com/pdf/2009/January/28.pdf>. The Treasury unhelpfully suggests that critical infrastructure determinations can be made on a “case-by-case” basis. *Id.*

grab of power for the CFIUS by Congress represents a major intervention into the economy with potentially negative consequences for foreign direct investment.<sup>130</sup> FINSA also includes a requirement that the CFIUS file a report with Congress at the completion of any 30-day review or 45-day investigation,<sup>131</sup> which increases transparency and the likelihood of congressional involvement.

Taken together, the FINSA reforms represent a victory for Congress in the long-running struggle between congressional attempts to broaden Exon-Florio to include economic factors, and the executive efforts to limit the review to issues directly relating to national defense.<sup>132</sup> While there is no explicit economic security factor added to the national security determination in FINSA, Congress achieved nearly the same end insofar as critical infrastructure is a broad enough term that practically any industry could be covered by it.<sup>133</sup>

Senator Charles Schumer's call to investigate the Borse Company's purchase of a 20% interest in Nasdaq demonstrates the broad nature of the FINSA review.<sup>134</sup> Although the Borse Company is a holding company owned by the Emir of Dubai,<sup>135</sup> at first glance, there appears to be no conceivable relation between a Nasdaq purchase and national security. Critics of the Unocal deal claimed that the United States military uses oil,<sup>136</sup> and critics of the Dubai Ports acquisition claimed that terrorists could infiltrate United States ports through the U.A.E. company.<sup>137</sup> Schumer does not seem to have proof of any plausible threat of terrorism due to the purchase, and Nasdaq has no apparent relationship to the defense industrial base. The only conceivable portion of Exon-Florio that a partial Nasdaq acquisition could fall under is the

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<sup>130</sup> See Marchick Testimony, *supra* note 127 (stating that nearly all foreign investment either sells products in areas covered under critical infrastructure, or is directly invested in critical infrastructure itself).

<sup>131</sup> 50 U.S.C.A. app. § 2170(b)(3) (West Supp. 2009).

<sup>132</sup> See Matthew R. Byrne, *Protecting National Security and Promoting Foreign Investment: Maintaining the Exon-Florio Balance*, 67 OHIO ST. L.J. 849, 889–90 (2006).

<sup>133</sup> The Treasury regulations support this claim by suggesting that acquisitions of firms in the “energy, transportation, or financial sectors” may threaten national security. Rubinoff, Savio & Davis, *supra* note 129 at 28; see also Marchick Testimony, *supra* note 127; Papavizas, *supra* note 86. While the Treasury notes that acquisition of firms with government contracts could threaten national security, the Treasury does not give any substantial guidance as to the possible limits of the term national security. Rubinoff, Savio & Davis, *supra* note 129, at 28.

<sup>134</sup> Stephanie Kirchgaessner, *Paulson Faces Test on Dubai's Nasdaq Offer*, FIN. TIMES, Sept. 26, 2007, at 11.

<sup>135</sup> *Id.*

<sup>136</sup> See *supra* notes 98–106 and accompanying text.

<sup>137</sup> See *supra* notes 110–16 and accompanying text.

critical infrastructure provision added in FINSA. Of course, if an electronic stock trading company can constitute critical infrastructure, then nearly any portion of the U.S. economy could qualify as such, and by extension, the vast majority of foreign direct investment within the United States would be potentially vulnerable to similar scrutiny.

### III. PROBLEMS WITH THE VAGUENESS OF NATIONAL SECURITY

The broad and vague interpretation of national security by the CFIUS creates four distinct problems. First, the open-ended interpretation of national security allows the term to be captured by critics of foreign investment. Second, the enormous and seemingly undefined economic sweep of CFIUS regulatory power creates business uncertainty and deters beneficial foreign direct investment. Third, the continual perceived use of the CFIUS as a tool of economic protectionism could lead to retaliation in the form of restriction of American foreign investment by other countries. Fourth, perception that CFIUS investigations are based upon political enmity could deter international cooperation with American foreign policy goals, just when such cooperation is essential to global peace.

#### A. *Xenophobic Politicization of the CFIUS Process*

Fear of foreign control has always politicized the Exon-Florio process. The tide of popular perception that the Japanese were purchasing large portions of the American economy largely drove the passage of the original Exon-Florio bill in 1988.<sup>138</sup> Similarly, economic competition from a rising China and acquisitions from oil-rich Middle Eastern states have driven Exon-Florio investigations in the 2000s.<sup>139</sup>

In the 1980s, the continual investigations of Japanese acquisitions hindered U.S. foreign policy goals of maintaining good relations with a crucial ally in the Cold War and major trading partner.<sup>140</sup> In the twenty-first century, maintaining good relations with China and cultivating ties to moderate Arab states are important elements of U.S. foreign policy.<sup>141</sup> Once again,

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<sup>138</sup> See GRAHAM & MARCHICK, *supra* note 7, at 40–41.

<sup>139</sup> See *id.* at 128–41.

<sup>140</sup> See David M. Marchick & Edward M. Graham, *How China Can Break Down America's Wall*, FAR E. ECON. REV., July–Aug. 2006, at 10, 10.

<sup>141</sup> See generally ZBIGNIEW BRZEZINSKI & BRENT SCOWCROFT, *AMERICA AND THE WORLD: CONVERSATIONS ON THE FUTURE OF AMERICAN FOREIGN POLICY* (2008).

protectionist forces are using Exon-Florio as a political tool and outlet of public unrest, regardless of diplomatic concerns.<sup>142</sup> The political pressures inherent in the Exon-Florio investigations prevent the CFIUS from accurately balancing security concerns because the definition of national security changes with the popular perception of threats.<sup>143</sup> Unease about high oil prices torpedoed a relatively innocuous Chinese acquisition of a U.S. oil company.<sup>144</sup> Just as in the 1980s and 90s, with the scare over Japanese acquisitions, many national security experts agree that there is no true threat in many of the recent proposed acquisitions.<sup>145</sup> Nevertheless, the vague interpretation of national security allows politicians to grandstand and manipulate the CFIUS process by appealing to public fears of high oil prices or Muslims.<sup>146</sup> Instead of a careful consideration of all of the different national security factors driving the CFIUS process, Exon-Florio investigations are driven by the political winds in Congress.<sup>147</sup>

After Dubai Ports, the political pressure for protectionism and the discomfort with globalization ran high.<sup>148</sup> But the responsibilities of politicians and the members of CFIUS are not to cave to popular opinion, but rather to make sober judgments about national security.<sup>149</sup> The lack of a limited statutory interpretation of national security creates the opportunity for popular opinion to define the term in opposition to whatever perceived foreign threat is currently in vogue.

### *B. National Security and Investor Uncertainty*

The uncertain interpretation of national security in Exon-Florio, combined with the broad sweep of terms like “energy assets” and “critical infrastructure” make the outcome of the CFIUS process nearly impossible to predict.<sup>150</sup> Continuing to construe the term national security broadly could have a chilling effect on all foreign investment within the United States, as it would send a

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<sup>142</sup> See Marchick & Graham, *supra* note 140, at 10, 12–13.

<sup>143</sup> See *infra* Part III.B.

<sup>144</sup> See Dorn, *supra* note 106, at 3–4.

<sup>145</sup> See, e.g., *id.*

<sup>146</sup> See Robert J. Samuelson, *Save Us from Our Politicians*, NEWSWEEK, Mar. 20, 2006, at 33.

<sup>147</sup> See Steven R. Weisman, *Brakes on a Foreign Deal: Security Concerns Block a Stake in 3Com for China*, N.Y. TIMES, Feb. 21, 2008, at B1.

<sup>148</sup> Samuelson, *supra* note 146.

<sup>149</sup> *Id.*

<sup>150</sup> See Marchick Testimony, *supra* note 127 (noting that the absence in guidance in these broad definitions is troubling from both a policy and market perspective).

signal that the age of openness to foreign direct investment is coming to a close.<sup>151</sup> Broadly defining national security creates costly uncertainty for foreign investors, as even the most sophisticated legal counsel cannot predict which investments will avoid a politicized CFIUS review.<sup>152</sup> According to Alan Greenspan, regulatory uncertainty deters business investment.<sup>153</sup> Defenders of the current process may point out that presidential vetoes are rare, as there have been none issued since 1990, and some controversial transactions, such as the Alcatel Lucent merger, have recently been approved.<sup>154</sup> Although presidential vetoes of transactions remain relatively scarce, the broad sweep of potential investigations can deter foreign direct investment without the president ever formally vetoing a transaction, as was done in the past to CNOOC and Dubai Ports.<sup>155</sup>

Even if the foreign enterprises do not touch upon defense technology, fear of an irrational regulatory regime may discourage deals on the margins.<sup>156</sup> As CFIUS reviews of foreign investment in critical infrastructure continue to be based upon mere political expediency, foreign countries may become wary of investing in the dollar if they see that Congress is willing to limit the amount of investment choices available to them.<sup>157</sup> While a wholesale dumping of American assets is unlikely, continual investigations of relatively innocuous foreign transactions like Unocal and Dubai Ports could lead foreigners to reconsider some of their investments.<sup>158</sup>

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<sup>151</sup> See Marchick Testimony, *supra* note 127; Papavizas, *supra* note 86.

<sup>152</sup> Marchick Testimony, *supra* note 127. Companies are also afraid that a failed CFIUS review will taint their reputation in future deal-making, and thus may avoid proposing some deals because of the uncertain nature of the CFIUS process. Nicholas Rummell, *Regulators Target Sovereign Wealth Funds*, FIN. WEEK, Feb. 11, 2008, <http://www.financialweek.com/apps/pbcs.dll/article?AID=/20080211/REG/445028497/1009/investments>.

<sup>153</sup> James Cooper & Kathleen Madigan, *What's Everyone So Rattled About?: Despite Record Wealth, Business and Consumers Remain Wary of the Future*, BUS. WK., Oct. 4, 2004, at 29. Greenspan has compared businesses dealing with regulatory uncertainty to a person "walking into an unlit room. Faced with darkness, the occupant tends to freeze up." *Id.*

<sup>154</sup> *Alcatel and Lucent Merger Receives CFIUS Approval*, M2 TELECOMWORLDWIRE, Nov. 20, 2006, available at [http://findarticles.com/p/articles/mi\\_m0ECZ/is\\_2006\\_Nov\\_20/ai\\_n16854357](http://findarticles.com/p/articles/mi_m0ECZ/is_2006_Nov_20/ai_n16854357).

<sup>155</sup> See Edward M. Graham & David M. Marchick, *A Misplaced Curb on Investment*, FIN. TIMES, Oct. 5, 2005, <http://www.ft.com/cms/s/0/300c8050-353c-11da-9e12-00000e2511c8.html>.

<sup>156</sup> See Brent Shearer, *Raising Barriers to Inbound Deals: Political Intervention Is Feared in Future Cross-Border M&A*, 41 MERGERS & ACQUISITIONS 22, 23–24 (2006).

<sup>157</sup> Samuelson, *supra* note 146, at 33.

<sup>158</sup> Axel Merk, *Protectionism May Hurt Dollar*, MERK INSIGHTS (Merk Investments LLC, Palo Alto, Cal.), Mar. 15, 2006, <http://www.merkfund.com/merk-perspective/insights/2006-03-15.html>.

Losing foreign investment in the United States could push the dollar down against other currencies, such as the rising euro.<sup>159</sup> A decline in the dollar fueled by investor pullout could cause interest rates to soar, possibly even worsening the current recession.<sup>160</sup> In an era when the dollar is falling in relation to other currencies, and the trade deficit is continuing to widen, the United States cannot afford to discourage foreign investment.<sup>161</sup>

Ironically, although foreign investment is one of the major factors maintaining economic growth, public backlash against such investment only deepens.<sup>162</sup> The housing crisis has exacerbated populist concern over the economy,<sup>163</sup> but while the housing crunch is ongoing, foreign investment is more vital than ever to provide liquidity to American markets.<sup>164</sup>

### C. *Economic Retaliation as a Result of CFIUS Protectionism*

Continued use of Exon-Florio to protect American economic security could also lead to retaliation by our trading partners.<sup>165</sup> The United States loses much of its credibility on global trade leadership when it caves to political pressure and blocks transactions that do not pose a clear threat to national

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<sup>159</sup> *Id.*

<sup>160</sup> Carl Steidtmann, Deloitte Research, Economist's Corner: Two Cheers for the Declining Dollar (Mar. 2005), <http://www.deloitte.com/dtt/article/0,1002,sid%253D15288%2526cid%253D77470,00.html>. During the mid-80s, when the growth of foreign investment declined somewhat, there was a rapid fall of the dollar, with a resultant recession. *Id.* Today, foreign investment has provided capital for domestic investment even as the dollar declines relative to other currencies. *Id.*

<sup>161</sup> Samuelson, *supra* note 146, at 33.

<sup>162</sup> Nina Easton, *America Sours on Free Trade*, FORTUNE, Feb. 4, 2008, at 104. In a 2008 poll, 68% of Americans said that free trade is no longer beneficial, and both of the leading Democratic candidates in the 2008 presidential election strongly criticized free trade, splitting with former President Bill Clinton, who signed NAFTA during his presidency. *Id.*

<sup>163</sup> Robin Toner, *A New Populism Spurs Democrats on the Economy*, N.Y. TIMES, July 16, 2007, at A1.

<sup>164</sup> Nora von Ingersleben & Braden Cox, Encouraging Foreign Investment by Limiting Political Influences (Feb. 22, 2008) (white paper, Association for Competitive Technology), *available at* <http://www.actonline.org/library/fdi-and-credit-crisis-act.pdf>. Foreign capital is especially essential for small start-up companies, which in the current capital crunch may not be able to get loans domestically. *Id.*

<sup>165</sup> Robert A. Mosbacher, *Trade is a Two Way Street*, WALL ST. J., Jul. 19, 2005, at A14 (arguing that CFIUS protectionism through the blocking of relatively innocuous deals such as Unocal could ignite retaliation against the United States from other countries, such as China); *see also* Alan P. Larson & David M. Marchick, *Foreign Investment and National Security: Getting the Balance Right*, in COUNCIL SPECIAL REPORT NO. 18, at 7–8 (Council on Foreign Relations, Bernard & Irene Schwartz Series on American Competitiveness, 2006) (noting that U.S. reform of the CFIUS is being carefully watched and replicated by Russia, China, and several European countries).

security, as it did during the Dubai Ports incident.<sup>166</sup> If the Exon-Florio power continues to widen to affect foreign investment outside of direct national defense concerns, then other countries will replicate such legislation, and protectionist trade wars will escalate.<sup>167</sup> In fact, France, Russia, India, and Canada have already passed, or are considering, more restrictions on foreign investment as a result of what is seen abroad as U.S. protectionism disguised as the CFIUS blocking deals for national security reasons.<sup>168</sup>

Russian legislators directly cited the U.S. example of the CFIUS when they debated the potential restrictions on foreign investment:

The government has decided to use [the] experience of the US . . . where there are stringent limitations for purchase of assets by foreign investors. . . . In the US if a foreign company is going to buy more than 5% of shares in a company that fulfills orders of the Department of Defense, [the] permit for such [a] deal is issued by the [P]resident.<sup>169</sup>

The Russian Economy Minister, German Gref, even made the case that the proposed Russian restrictions on foreign investment would be more liberal than the CFIUS process of the United States.<sup>170</sup>

Similarly, India retaliated against CFIUS restrictions on one of its telecom companies by placing similar restrictions on U.S. telecom firms that were attempting to enter the Indian market.<sup>171</sup> The Indian government felt that it needed to exclude U.S. companies as long as the United States was restricting Indian companies' transactions with American firms.<sup>172</sup> Both of these incidents are illustrative of a larger point: as long as the United States restricts

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<sup>166</sup> Paul Blustein, *Ports Debate Reawakens Foreign-Investment Jitters*, WASH. POST, Feb. 23, 2006, at D1 (quoting Secretary of the Treasury John Snow as saying that “[t]he implication of failing to approve this would be to tell the world that investments in the United States from certain parts of the world aren’t welcome”).

<sup>167</sup> Jean Eaglesham, *Free Trade “Is Not a One-Way Street” Says UK in Attack on US “Hypocrisy,”* FIN. TIMES, Mar. 31, 2006, at 9. British trade secretary Alan Johnson said of Dubai Ports and the CFIUS: “Such hypocrisy makes global progress impossible. How can the richest countries in the world lecture others about the gains from liberalisation whilst adding further barriers to entering their own markets?” *Id.*

<sup>168</sup> GRAHAM & MARCHICK, *supra* note 7, at 163.

<sup>169</sup> *Participation of Foreign Capital in Strategic Industries of Russia to Be Limited*, RUSSIAN BUS. MONITOR, May 18, 2005.

<sup>170</sup> *Russia Plans to Limit Foreign Investment in Move Seen as Threat to Trade Climate*, Int’l Trade Daily (BNA) (Mar. 10, 2006).

<sup>171</sup> GRAHAM & MARCHICK, *supra* note 7, at 164.

<sup>172</sup> *Id.*

foreign investment unnecessarily through the CFIUS process, other countries will do likewise, inhibiting global trade.<sup>173</sup>

Diagnosing the benefits of free trade goes beyond the scope of this Comment, but there is virtual unanimity among economists on both the benefits of foreign direct investment and free trade to the U.S. economy.<sup>174</sup> Without foreign direct investment, the U.S. economy would lose nearly ten million jobs.<sup>175</sup> A dynamic American economy is crucial to national security because without a strong economy, there would be insufficient revenue for the military and national defense.<sup>176</sup> If the U.S. economy were to contract even further, there could be isolationist pressure to reduce the defense budget and withdraw from international commitments.<sup>177</sup> Moreover, global free trade contributes to global stability by spreading democracy, integrating national economies, and dramatically raising the cost of war.<sup>178</sup>

Support for regulation of foreign direct investment centers around unsubstantiated fears that foreign direct investment creates economic instability.<sup>179</sup> According to this theory, foreign ownership of important U.S. assets gives other countries the power to destabilize the U.S. economy.<sup>180</sup> In reality, however, foreign direct investment aligns the interests of other

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<sup>173</sup> *Id.*

<sup>174</sup> See Dan Fuller & Doris Geide-Stevenson, *Consensus Among Economists: Revisited*, 34 J. ECON. EDUC., 369, 384–85 (2003). This consensus has been challenged somewhat in recent years but still remains the dominant view in the field of economics. *Id.* at 385.

<sup>175</sup> *Sovereign Wealth Funds Acquisitions and Other Foreign Government Investments in the U.S.: Assessing the Economic and National Security Implications: Hearing before the S. Comm. on Banking, Housing, and Urban Affairs*, 110th Cong. 30 (2007) (testimony of David H. McCormick, Under Sec’y for Int’l Affairs). Furthermore, workers employed by foreign investment are paid as much as 15% more than those employed by domestic firms. Ingersleben & Cox, *supra* note 164. Foreign investment is also crucial to small and start-up businesses, which drive innovation and growth. *Id.*

<sup>176</sup> GRAHAM & MARCHICK, *supra* note 7, at 173.

<sup>177</sup> Zalmay Khalilzad, *Losing the Moment? The United States and the World After the Cold War*, 18 WASH. Q. 87, 103–04 (Spring 1995). Khalilzad also argues that economic growth is necessary to maintain our technological base, which is crucial to the military aspect of national defense. *Id.*

<sup>178</sup> Jim Chen, *Pax Mercatoria: Globalization as a Second Chance for “Peace In Our Time,”* 24 FORDHAM INT’L L.J. 217, 226–28 (2000). While there is some dispute over the ability of free trade to prevent war, the consensus of international relations scholars is that free trade makes a positive contribution toward the goal of international peace. *Id.*

<sup>179</sup> GRAHAM & MARCHICK, *supra* note 7, at 118.

<sup>180</sup> *Id.* This theory is repeatedly hammered home in popular literature, with perhaps the most famous example being Tom Clancy’s novel, *Debt of Honor*, in which the Japanese government funds the purchase of a major U.S. investment firm and then uses that firm to tank the stock market and the American economy. Japan takes advantage of this economic downturn to launch an undeclared war against America. TOM CLANCY, *DEBT OF HONOR* (1994).

countries with the United States.<sup>181</sup> If another country owns substantial assets in the United States, its future is tied to the American economy, and that country would be going against its own interests to take any action that may destabilize the American economy.<sup>182</sup>

#### *D. Foreign Policy Consequences*

FINSA mandates that the CFIUS conduct a 45-day investigation any time the foreign investor is controlled by, or acting on behalf of, a foreign government, unless the Secretary of the Treasury and the head of the relevant agency both agree that there is no threat to national security and waive the investigation.<sup>183</sup> This provision shifts the burden of proof away from the U.S. government and to the foreign state-owned business in these transactions.<sup>184</sup> To foreign governments, however, FINSA may appear to discourage investment because of political enmity.<sup>185</sup> As such, continual politicized investigations of foreign direct investment in American infrastructure may alienate our allies and isolate America even further.<sup>186</sup>

For example, Dubai Ports World was not purchasing the operations of the ports from an American company; the ports were run by a British company, P&O.<sup>187</sup> The U.A.E. is perhaps the most moderate secular Arab regime in the Middle East, the central location for Middle Eastern banking, and a strong supporter of the war on terror, housing over a thousand U.S. soldiers and cooperating with initiatives to track down terrorist finances and insure container security.<sup>188</sup> Dubai's control of the ports would not have changed security in any measurable way—American unions would continue to unload the ships, and the Coast Guard and port authorities would still be responsible

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<sup>181</sup> GRAHAM & MARCHICK, *supra* note 7, at 118.

<sup>182</sup> *See id.*; Larson & Marchick, *supra* note 165, at 6–8. Allowing foreigners to invest in our markets gives them a stake in the success of our economy. *See id.*

<sup>183</sup> 50 U.S.C.A. app. § 2170(b)(2)(D) (West Supp. 2009).

<sup>184</sup> Dave & Thomas, *supra* note 125, at 3.

<sup>185</sup> *See 3Com's US Roadblock Seen Deterring China Investors*, REUTERS, Feb. 21, 2008, <http://www.reuters.com/article/idUKSHA236602008022>. China likely perceived the recent rejection of the 3Com deal as evidence of political enmity. *Id.*; *see also* Lawrence B. Lindsey, *Not for Sale to Foreigners*, WALL ST. J., Mar. 10, 2006, at A18. Lindsey relates a conversation he had with members of the Japanese parliament that was very critical of congressional backlash against the Dubai Ports deal, an attitude also prevalent in London. *Id.* He argues that if this is the attitude in the capitals of our allies, then the backlash against political restrictions on foreign direct investment will be far greater in Moscow, Beijing, and the Arab world. *Id.*

<sup>186</sup> Lindsey, *supra* note 185.

<sup>187</sup> GRAHAM & MARCHICK, *supra* note 7, at 137.

<sup>188</sup> *See generally* Samuelson, *supra* note 146; James Jay Carafano, *Port Security?*, NAT'L REV. ONLINE, Feb. 21, 2006, <http://www.nationalreview.com/symposium/symposium200602211008.asp>.

for picking which containers to scan.<sup>189</sup> Also, Dubai Ports World would have had a unique incentive to prevent any terrorist attacks, since any such attack would immediately put an end to all of their operations and investments in America.<sup>190</sup>

Given these facts, and the reality that other foreign port companies operate U.S. ports without political backlash, Arab businessmen may see the Dubai Ports controversy as a racially biased investigation.<sup>191</sup> If the CFIUS discourages the U.A.E. from investing in America after all of the favors that the U.A.E. has done for the United States, then what would be the incentive for other moderate Arab regimes to cooperate with American goals in the region?<sup>192</sup> The United States cannot afford to alienate moderate Arab states with the CFIUS process because their cooperation is crucial to the war on terror.<sup>193</sup>

Instead, integrating the moderate Arab regimes, such as the U.A.E., into the global financial order would minimize security risks. Encouraging investment in the American economy would give moderate Arab regimes a stake in preventing terrorist attacks upon American soil, since such attacks would devastate the value of their assets as well.<sup>194</sup> America should welcome foreign investment from the Middle East, not fear it as a security threat.

Similarly, CNOOC's purchase of Unocal did not threaten American access to oil.<sup>195</sup> Some advocates of vetoing the Unocal sale argued that if China was able to purchase Unocal, it would be able to corner a portion of the oil market

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<sup>189</sup> Rich Lowry, *Port Hysteria*, NAT'L REV. ONLINE, Feb. 24, 2006, <http://www.nationalreview.com/lowry/lowry200602240812.asp>.

<sup>190</sup> Bond, *supra* note 82.

<sup>191</sup> Lindsey, *supra* note 185 (arguing that the rejection of the Dubai Ports appears globally to be based on ethnic targeting); see also Jason Niss, *America Can't Afford to Alienate Its Arab Friends*, INDEP., Feb. 26, 2006, <http://www.independent.co.uk/news/business/comment/business-view-america-cant-afford-to-alienate-its-arab-friends-467701.html>.

<sup>192</sup> See Niss, *supra* note 191.

<sup>193</sup> *Id.* In an age of global media, and when images of U.S. torture are being circulated around the globe, the United States must be especially careful of its image in the Arab world. See *id.*

<sup>194</sup> Brink Lindsey, *The Trade Front: Combating Terrorism with Open Markets*, in TRADE POLICY ANALYSIS NO. 24, at 4-9 (Cato Inst. Ctr. for Trade Pol'y Stud., 2003), available at <http://www.freetrade.org/pubs/pas/tpa-024.pdf>. Free trade would also strengthen the moderates within those countries by creating a prosperous middle class that is friendly to the United States, upon whom their livelihoods depend. See *id.* at 6.

<sup>195</sup> See Paul Blustein, *Many Oil Experts Unconcerned over China Unocal Bid*, WASH. POST, July 1, 2005, at D1.

and prevent the United States from satisfying its own energy needs.<sup>196</sup> But the global market for oil is fluid, so the price is not affected by who owns it.<sup>197</sup> If China were to hoard oil from its own oil fields in an energy crisis, the price would still be determined by global supply and demand.<sup>198</sup> Thus, there is no basis for fear of Chinese ownership of energy resources.<sup>199</sup> China promised that the Unocal oil and gas produced in the United States would continue to be sold there, not shipped directly to China.<sup>200</sup> Even if CNOOC would divert Unocal's products to China, there would be no effect on the global oil markets; the United States would still be able to purchase the oil it needs.<sup>201</sup> Moreover, Unocal is only responsible for 0.23% of global oil production—hardly a devastating weapon.<sup>202</sup> Thus, CNOOC's purchase of Unocal did not remotely threaten American national security.

Ironically, by rejecting the Chinese purchase of Unocal for fear that it would threaten U.S. energy security, the United States drove China to invest in oil operations in various “pariah” states, including Iran and the Sudan.<sup>203</sup> China now depends on Sudan and Iran to satisfy domestic oil demand, and the Chinese leadership may become less willing to cooperate with international efforts to pressure Sudan or Iran to change their behavior.<sup>204</sup> China is profiting handsomely from its oil investments in Sudan and Iran, making it more difficult for the international community to take unified action to resolve the conflict in Sudan or pressure Iran to stop its nuclear programs.<sup>205</sup> If the United

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<sup>196</sup> *Id.* In 2005, Joe Barton, then-chairman of the House Committee on Energy and Commerce, and Ralph Hall, then-chairman of the Subcommittee on Energy and Air Quality, jointly wrote a letter to President Bush contending that the ability of the United States to obtain oil was “threatened by China’s aggressive tactics to lock up energy supplies around the world that are largely dedicated for their own use.” *Id.*

<sup>197</sup> *Id.*

<sup>198</sup> *Id.*

<sup>199</sup> *National Security Implications of the Possible Merger of the China National Offshore Oil Corporation with Unocal Corporation: Hearing Before the H. Comm. on Armed Servs.*, 109th Cong. (2005) (testimony of Jerry Taylor, Dir., Natural Res. Stud., Cato Inst.) [hereinafter Taylor Testimony].

<sup>200</sup> Dorn, *supra* note 106, at 4.

<sup>201</sup> Blustein, *supra* note 195.

<sup>202</sup> Taylor Testimony, *supra* note 199. During the first quarter of 2005, Unocal produced 169,000 barrels of gas and oil each day, while the global production during this period was 73.3 million barrels a day. *Id.* To put these numbers in perspective, the U.S. Geological Survey, considered the preeminent study in the field, found that there are about 1,634 billion barrels of recoverable oil still in the ground. Thomas S. Ahlbrandt et al., *Analysis of Assessment Results*, in U.S. GEOLOGICAL SURVEY WORLD PETROLEUM ASSESSMENT 2000, at AR-10 (2000), available at <http://energy.cr.usgs.gov/WEcont/chaps/AR.pdf>.

<sup>203</sup> See Erica S. Downs & Jeffrey A. Bader, *Oil-Hungry China Belongs at Big Table*, CALGARY HERALD, Sept. 8, 2006, at A24, available at [http://www.brookings.edu/opinions/2006/0908china\\_bader.aspx](http://www.brookings.edu/opinions/2006/0908china_bader.aspx).

<sup>204</sup> *Id.*

<sup>205</sup> See Barbara Slavin, *U.S. Explores New Strategies as Sudan, Iran Find Ways to Bypass Sanctions*, USA TODAY, June 11, 2007, at 10A (reporting that the growing economic power of China, and its incentive to

States wants to avoid China politicizing its oil deals with Sudan and Iran, then it should avoid politicizing China's oil deals with the United States by allowing China to acquire American's energy companies as it sees fit.<sup>206</sup>

China may view the United States' actions in the Unocal deal as a hostile attempt to prevent China's development by preventing its purchase of natural resources.<sup>207</sup> Should the Chinese take this viewpoint, it could lead to a cycle of conflicts between the United States and China.<sup>208</sup> Engaging China, by encouraging their investment within the United States and removing their fear that access to energy could be cut off, would greatly increase China's willingness to work within the international system and strengthen American national security.<sup>209</sup>

The Unocal and Dubai episodes illustrate the futility of a broad definition of the term national security. An open-ended approach by the CFIUS will encourage protectionism and alienate U.S. allies abroad.<sup>210</sup> FINSA's scrutiny of the Borse Company's proposed acquisition of an interest in Nasdaq indicates that FINSA has opened the floodgates for further scrutiny of foreign acquisitions.<sup>211</sup> Since it was enacted, FINSA has threatened several other major transactions. For instance, in 2008, Bain Capital, a U.S. private equity firm, and Huawei Technologies, a Chinese telecom firm, jointly proposed to purchase a minority stake in 3Com, a U.S. network equipment maker, for \$2.2 billion.<sup>212</sup> The deal collapsed in the face of the CFIUS's national security concerns.<sup>213</sup> Senator Christopher Dodd, chairman of the Senate Banking Committee, even threatened that more restrictive legislation might be necessary in order to prevent "potential pitfalls associated with" foreign investment.<sup>214</sup> Dodd explicitly conditioned his support for future foreign

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protect its oil investments in Sudan and Iran, makes it difficult to apply meaningful pressure on Sudan and Iran while China continues to trade with them).

<sup>206</sup> Downs & Bader, *supra* note 203.

<sup>207</sup> Dorn, *supra* note 106, at 9.

<sup>208</sup> *Id.* at 9–10.

<sup>209</sup> *See id.* at 11.

<sup>210</sup> GRAHAM & MARCHICK, *supra* note 7, at 175.

<sup>211</sup> *See supra* note 134 and accompanying text.

<sup>212</sup> Weisman, *supra* note 147.

<sup>213</sup> *Id.*

<sup>214</sup> *US Security Review of Bain-3Com Deal Scrutinized*, REUTERS, Jan. 23, 2008, <http://www.reuters.com/article/rbssTechMediaTelecomNews/idUSN2364561520080123>.

investment on it not “pos[ing] a threat to our economic stability,”<sup>215</sup> thus resurrecting the old economic security test in an even more blatant form.

Sovereign wealth funds pose another challenge to the new FINSA regulations. Governments have long pooled their money into funds with which to make purchases, and several U.S. states have their own sovereign wealth funds.<sup>216</sup> High oil prices coupled with several East Asian countries’ transfer of foreign reserves from government bonds to more aggressive investing strategies have driven the value of global sovereign wealth funds past \$2 trillion.<sup>217</sup> Yet under FINSA, each sovereign wealth fund acquisition would have to be automatically reviewed by the CFIUS, absent special approval from the Secretary of the Treasury or the relevant agency.<sup>218</sup> Such a rule opens the possibility of more Dubai Ports type incidents. Indeed, the 2008 World Economic Forum exposed the danger that sovereign wealth funds may ignite protectionist sentiment in the United States.<sup>219</sup> The United States would be wise to create transparent rules that limit the definition of national security as soon as possible, rather than reviewing every foreign governmental transaction and hoping to avoid an international incident.<sup>220</sup>

Considering recent events such as Unocal, Dubai Ports, and 3Com, it appears possible that xenophobic scrutiny of foreign investment will increase in the years ahead. Nevertheless, in the post-9/11 world, openness to foreign

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<sup>215</sup> *Dodd Eyes 3Com’s Stake Sale to Chinese*, DEAL, Jan. 23, 2008, [http://www.thedeal.com/dealscape/2008/01/dodd\\_may\\_block\\_3coms\\_stake\\_sal.php](http://www.thedeal.com/dealscape/2008/01/dodd_may_block_3coms_stake_sal.php).

<sup>216</sup> Stuart E. Eizenstat & Alan Larson, *The Sovereign Wealth Explosion*, WALL ST. J., Nov. 1, 2007, at A19. For example, “Alaska and Wyoming invest the proceeds of natural-resource income, and other states such as California and Alabama have prominent pension funds. Many of these funds have invested in other private equity, hedge and venture funds, as well as individual companies, for many years.” *Id.*

<sup>217</sup> *Id.* Norway has had a sovereign wealth fund, which it uses to pay operating expenses of its government, since 1967. *Id.* The Asian central banks hold more than \$3.1 trillion, and if even a fraction of that was used to invest in the American economy, the influx of foreign direct investment would dwarf any previous investment inflows. *See id.*

<sup>218</sup> 50 U.S.C.A. app. § 2170(b)(2)(D) (West Supp. 2009). There is, however, some ambiguity about whether sovereign wealth funds will be considered state actors. FINSA states, “The term ‘foreign government-controlled transaction’ means any covered transaction that could result in the control of any person engaged in interstate commerce in the United States by a foreign government or an entity controlled by or acting on behalf of a foreign government.” 50 U.S.C.A. app. § 2170(a)(4) (West Supp. 2009). Considering this definition, it seems likely that sovereign wealth funds will be found to act on behalf of foreign governments.

<sup>219</sup> Carter Dougherty & Katrin Bennhold, *Sovereign Funds on the Defensive; As Investments in the West Grow, Managers Want Respect*, INT’L. HERALD TRIB., Jan. 25, 2008, at 15. Some Europeans are afraid that Russia will use its sovereign wealth fund, which is not yet operational, to flex its strategic muscles, as it has attempted to use Gazprom, its national gas company, to intimidate the Ukraine. *Id.*

<sup>220</sup> *See Eizenstat & Larson, supra note 216.*

investment and cooperation with other governments is an absolute necessity.<sup>221</sup> National security must be clearly defined to encourage foreign direct investment.

## CONCLUSION

Exon-Florio should be amended to more narrowly define national security. The open-ended nature of the current definition has allowed the process to become politicized. Instead, national security should be specifically defined so as to prevent acquisition of industries that are critical to the military aspects of our national defense and that have capacities that are not duplicable by other market entities. The definition should also serve to ensure that export control laws are not circumvented by foreign acquisition of American companies. The following proposed definition would once again focus on preventing foreign governments from gaining unique military capabilities through private transactions that could threaten American national security:

*National Security shall be defined so as to consider the following factors in reviewing foreign acquisitions:*

*A. Potential effect upon assets essential to the military aspects of national defense, specifically those firms whose contributions to the national defense cannot be easily replaced by another domestic corporation;*

*B. Whether the acquisition poses a substantial risk of espionage or terrorism that can be certified by the relevant United States intelligence agencies;*

*C. Whether the acquisition would pose a unique risk of weapons proliferation of critical military assets that cannot be otherwise dealt with by United States laws, particularly to countries that are not allies of the United States;*

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<sup>221</sup> See Thomas Friedman, Op-Ed., *9/11 is Over*, N.Y. TIMES, Sept. 30, 2007, § 4, at 12. This does not mean, however, that foreign countries should hold a veto over U.S. foreign or domestic policies, particularly policies that are not directly related to their national survival. Allowing foreign countries or international institutions to veto or modify unrelated U.S. policies would make a mockery of our foreign policy and destroy the credibility of American leadership. International cooperation does not require making our policy subservient to the whims of other nations. See generally THE ALLIES AND ARMS CONTROL (F.O. Hampson et al. eds., 1992). See also Khalilzad, *supra* note 177.

*D. Economic security, or any other factor not mentioned in this section, shall not be considered by the CFIUS process.*<sup>222</sup>

Such an interpretation of national security would heavily scrutinize acquisition of, or joint ventures with, Lockheed Martin or any other company that makes a large contribution to the defense industrial base. Certain high-tech companies that produce computer chips that give the U.S. armed forces technological advantages over other countries might also fall under this definition. China should not be allowed to acquire a controlling interest in the present-day equivalent of Fairchild Semiconductor.

This proposed definition of national security would be even more limited than the original Exon-Florio signed by President Reagan, as Exon-Florio was designed to apply mainly to defense-based technological acquisitions.<sup>223</sup> The main difference between this definition of national security and the original Exon-Florio legislation is that this definition would codify national security to explicitly prevent protectionist use of the CFIUS for political ends. Any consideration of economic security or protection of energy assets from foreign acquisition would be excluded from this definition, as inclusion of such economic factors can only encourage protectionism and politicization of the CFIUS process.<sup>224</sup>

The narrower definition of national security would eliminate the mandatory reviews of every foreign-government-controlled transaction as required by FINSAs.<sup>225</sup> Instead, the CFIUS would be given flexibility to decide which transactions truly threaten national security, without being bound to review every governmental acquisition. Narrowing the definition of national security in this manner would allow the CFIUS to focus its resources on real national security threats, rather than waste resources analyzing nearly every transaction involving a foreign governmental takeover.<sup>226</sup>

The CFIUS should certainly consider the prospect of terrorism and take every step possible to safeguard against such a risk. In many cases, safeguards such as extra scans on containers should be put in place to minimize the risk of

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<sup>222</sup> The form of this definition is modeled somewhat loosely off of the structure of 50 U.S.C.A. app. §2170(F) (West Supp. 2009). Of course, all portions of this definition could be satisfied by appropriate mitigation procedures, if possible.

<sup>223</sup> Papavizas, *supra* note 86.

<sup>224</sup> GRAHAM & MARCHICK, *supra* note 7, at 172.

<sup>225</sup> See 50 U.S.C.A. app. § 2170(b)(2)(B) (West Supp. 2009).

<sup>226</sup> See GRAHAM & MARCHICK, *supra* note 7, at 168.

terrorism. These safeguards should be applied regardless of whether the ownership is foreign or domestic.<sup>227</sup> Protectionism cannot replace the Department of Homeland Security when it comes to defending critical infrastructure.<sup>228</sup> Besides, the terrorists who struck on 9/11 did not own substantial property within the United States. Nor would the CFIUS regulations have stopped the subsequent terrorist incidents, such as Richard Reid's attempted shoe bomb or the anthrax shipments. In fact, there is no evidence that any company has been used as a front for a terrorist plot.<sup>229</sup>

However, transactions should be blocked by the CFIUS on the basis of homeland security only when there is evidence of a clear and present threat of terrorism, or perhaps of espionage or sabotage. If the term "critical infrastructure" must be kept in FINSA, then members of Congress and the CFIUS must do a better job articulating what exactly constitutes critical infrastructure and what they consider the link between foreign ownership of critical infrastructure and threats to national security.<sup>230</sup> Explicitly laying out such guidelines will illustrate the boundaries to foreign investors and will make CFIUS decisions seem less arbitrary and political.<sup>231</sup> Additionally, screening employees of foreign corporations that purchase critical infrastructure can often identify potential security vulnerabilities without taking the drastic step of vetoing a transaction.<sup>232</sup>

Limiting the Exon-Florio definition of national security only to military threats may seem odd and reactionary in the post-9/11 world, where unconventional threats abound. However, counter-terrorism requires appropriate tools, and regulating foreign direct investment simply falls short of being a cost-effective method of ensuring homeland security.<sup>233</sup> Focusing on the nationality of a company's ownership in a globalized world only distracts us from real security threats posed by non-state actors.<sup>234</sup> Many terrorist threats do not exist as a result of primary support from any nation, but rather as tactics in service of an ideology.<sup>235</sup> As José Padilla, John Walker Lindh, and

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<sup>227</sup> See Lowry, *supra* note 189.

<sup>228</sup> See *id.*

<sup>229</sup> Larson & Marchick, *supra* note 165, at 19–20.

<sup>230</sup> Papavizas, *supra* note 86.

<sup>231</sup> See *id.*

<sup>232</sup> GRAHAM & MARCHICK, *supra* note 7, at 150.

<sup>233</sup> Larry Kudlow, *Opposition to Port Deal Misguided*, KAN. CITY STAR, Mar. 2, 2006, at C3.

<sup>234</sup> Larson & Marchick, *supra* note 165, at 10; see also Lowry, *supra* note 189.

<sup>235</sup> See generally Fiona Adamson, Center for International Security and Cooperation (CISAC), Stanford University, International Terrorism, Non-State Actors and the Logic of Transnational Mobilization: A

many others have illustrated, no one ethnic group has a monopoly on Al-Qaeda membership or support. Instead of penalizing investments from various Arab states simply because terrorists draw support from that region, homeland security policy should focus on thwarting the terrorists themselves. The CFIUS must return to a focus on state military capabilities *because* the terrorist threats are from non-state actors, and restricting economic investment from certain nations does not, per se, deal with the threat of terrorism. Just because terrorism is a serious threat does not mean that the CFIUS is the best tool to protect critical infrastructure.

In conclusion, 9/11 did radically change the world, and Exon-Florio should change to fit the new realities of homeland security. However, the most effective reform of Exon-Florio is not expansion of the definition of national security to include economic protectionism, but rather a narrowing of the definition to guard against real threats to American security while encouraging beneficial foreign investment. The security challenges of the twenty-first century cannot be met by protectionism. Only by embracing globalization and cooperation can the United States truly achieve national security.

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Perspective from International Relations, Memo for Social Science Research Council Workshop: International Law, International Relations, and Terrorism (Nov. 14, 2002), *available at* [http://programs.ssrc.org/gsc/gsc\\_activities/adamson/](http://programs.ssrc.org/gsc/gsc_activities/adamson/).

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