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The Committee on Foreign Investment in the United States (CFIUS)

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Summary

The Committee on Foreign Investment in the United States (CFIUS) is comprised of 12 members representing major departments and agencies within the federal Executive Branch. While the group generally operates in relative obscurity, the proposed acquisition of commercial operations at six U.S. ports by Dubai Ports World in 2006 placed the group's operations under intense scrutiny by Members of Congress and the public. Prompted by this case, some Members are questioning the ability of Congress to exercise its oversight responsibilities given the general view that CFIUS's operations lack transparency. Other Members are revisiting concerns about the linkage between national security and the role of foreign investment in the U.S. economy. Some Members of Congress and others argue that the nation's security and economic concerns have changed since the September 11, 2001 terrorist attacks and that these concerns are not being reflected sufficiently in the Committee's deliberations. In addition, anecdotal evidence seems to indicate that the CFIUS process may not be market neutral, instead a CFIUS investigation of an investment transaction may be perceived by some firms and by some in the financial markets as a negative factor that adds to uncertainty and may spur firms to engage in behavior that is not optimal for the economy as a whole.

Since some Members of Congress focused attention on the Dubai Ports World transaction, more than two dozen measures on foreign investment have been introduced. These measures reflect various levels of unease with the broad discretionary authority Congress has granted CFIUS. As a result, most measures would place new reporting requirements on CFIUS and strengthen Congress's ability to exercise oversight over CFIUS through the federal agencies that comprise the Committee. Such measures as **H.R. 4813** and **H.R. 4917** would place new reporting requirements on CFIUS to inform Congress when it initiates an investigation of a proposed acquisition, merger, or takeover. Other measures would seek to reduce CFIUS's discretion in deciding whether to investigate a foreign investment transaction. **H.R. 4929** would limit CFIUS's discretion by mandating that an investigation must occur for any proposed or pending merger, acquisition, or takeover. **S. 1797** would increase requirements for reporting to Congress, allow specified congressional leaders to request an investigation of certain investments, and would require CFIUS to consider the long-term projections of the United States requirements for sources of energy and other critical resources and materials and for economic security. **S. 2380** would add a new national security review to the CFIUS process and add the Secretary of Homeland Security and the Secretary of Defense as vice chairs of the Committee.

This report will be updated as events warrant.

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Background

The Committee on Foreign Investment in the United States (CFIUS) is an interagency committee that serves the President in overseeing the national security implications of foreign investment in the economy. Since it was established by an Executive Order of President Ford in 1975, the committee has operated in relative obscurity.[1] According to a Treasury Department memorandum, the Committee originally was established in order to placate Congress, which had grown concerned over the rapid increase in Organization of the Petroleum Exporting Countries (OPEC) investments in American portfolio assets (Treasury securities, corporate stocks and bonds), and to respond to concerns of some that much of the OPEC investments were being driven by political, rather than by economic, motives.[2] Thirty years later, public and congressional concerns about the proposed purchase of commercial port operations of the British-owned Peninsular and Oriental Steam Navigation Company (P&O)[3] in six U.S. ports by Dubai Ports World (DP World)[4] sparked a firestorm of criticism and congressional activity concerning CFIUS and the manner in which it operates. Some Members of Congress and the public argue that the nation's economic and national security concerns have been fundamentally altered as a result of the September 11, 2001 terrorist attacks on the United States and that these changes require a reassessment of the role of foreign investment in the economy and in the nation's security.

Members of Congress have so far introduced more than 25 bills in the 2nd Session of the 109th Congress that would address various aspects of foreign investment since the proposed DP World transaction These measures can be grouped

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[1] Executive Order 11858 (b), May 7, 1975, 40 F.R. 20263.

[2] U.S. Congress. House. Committee on Government Operations. Subcommittee on Commerce, Consumer, and Monetary Affairs. *The Operations of Federal Agencies in Monitoring, Reporting on, and Analyzing Foreign Investments in the United States*. Hearings. 96th Cong., 1st Sess., Part 3, July 30, 1979. Washington, U.S. Govt. Print. Off., 1979. p. 334-335. (Hereafter cited as, *The Operations of Federal Agencies*, part 3.)

[3] Peninsular and Oriental Steam Company is a leading ports operator and transport company with operations in ports, ferries, and property development. It operates container terminals and logistics operations in over 100 ports and has a presence in 18 countries.

[4] Dubai Ports World was created in November 2005 by integrating Dubai Ports Authority and Dubai Ports International. It is one of the largest commercial port operators in the world with operations in the Middle East, India, Europe, Asia, Latin America, the Carribean, and North America.

into four major areas: those that deal specifically with the proposed DP World acquisition; those that focus more generally on foreign ownership of U.S. ports, especially if the foreign entity is owned or controlled by a foreign government; those that would amend the CFIUS process; and those that would amend the Exon-Florio process (explained below). Six bills focus primarily on CFIUS and display a range of responses by some Members of Congress. These bills are examined in more depth later in this report. The measures seem to indicate that some Members are concerned over the way in which CFIUS operates and the lack of transparency in the process that some Members believe has hampered Congress's ability to exercise its oversight responsibilities.

Establishment of CFIUS

President Ford's 1975 Executive Order established the basic structure of CFIUS, and directed that the "representative"[5] of the Secretary of the Treasury be the chairman of the Committee. The Executive Order also stipulated that the Committee would have "the primary continuing responsibility within the Executive Branch for monitoring the impact of foreign investment in the United States, both direct and portfolio, and for coordinating the implementation of United States policy on such investment." In particular, CFIUS was directed to: (1) arrange for the preparation of analyses of trends and significant developments in foreign investments in the United States; (2) provide guidance on arrangements with foreign governments for advance consultations on prospective major foreign governmental investments in the United States; (3) review investments in the United States which, in the judgement of the Committee, might have major implications for United States national interests; and (4) consider proposals for new legislation or regulations relating to foreign investment as may appear necessary.[6]

President Ford's Executive Order also stipulated that information submitted "in confidence shall not be publicly disclosed" and that information submitted to CFIUS be used "only for the purpose of carrying out the functions and activities" of the order. In addition, the Secretary of Commerce was directed to perform a number of activities, including:

(1) obtaining, consolidating, and analyzing information on foreign investment in the United States;

(2) improving the procedures for the collection and dissemination of information on such foreign investment;

(3) the close observing of foreign investment in the United States;

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[5] The term "representative" was dropped by Executive Order 12661, December 27, 1988, 54 FR 780.

[6] Executive Order 11858 (b), May 7, 1975, 40 F.R. 20263.

(4) preparing reports and analyses of trends and of significant developments in appropriate categories of such investment;

(5) compiling data and preparing evaluation of significant transactions; and

(6) submitting to the Committee on Foreign Investment in the United States appropriate reports, analyses, data, and recommendations as to how information on foreign investment can be kept current.

The Executive Order, however, raised questions among various observers and government officials who doubted that federal agencies had the legal authority to collect the types of data that were required by the order. As a result, Congress and the President sought to clarify this issue, and in the following year President Ford signed the International Investment Survey Act of 1976.[7] The Act gave the President clear and unambiguous authority" to collect information on "international investment." In addition, the Act authorized "the collection and use of information on direct investments owned or controlled directly or indirectly by foreign governments or persons, and to provide analyses of such information to the Congress, the executive agencies, and the general public."[8]

By 1980, some Members of Congress had come to believe that CFIUS was not fulfilling its mandate. Between 1975 and 1980, for instance, the Committee had met only ten times and seemed unable to decide whether it should respond to the political or the economic aspects of foreign direct investment in the United States.[9] One critic of the Committee argued in a congressional hearing in 1979 that, "the Committee has been reduced over the last four years to a body that only responds to the political aspects or the political questions that foreign investment in the United States poses and not with what we really want to know about foreign investments in the United States, that is: Is it good for the economy?"[10]

From 1980 to 1987, CFIUS investigated a number of foreign investments, mostly at the request of the Department of Defense In 1983, for instance, a Japanese firm sought to acquire a U.S. specialty steel producer. The Department of Defense subsequently classified the metals produced by the firm because they were used in the production of military aircraft, which caused the Japanese firm to withdraw its offer. Another Japanese company attempted to acquire a U.S. firm in 1985 that manufactured specialized ball bearings for the military. The acquisition was completed after the Japanese firm agreed that production would be maintained in the United States. In a similar case in 1987, the Defense Department objected to a proposed acquisition of the computer division of a U.S. multinational company by

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[7] P.L. 94-472, Oct 11, 1976; 22 USC 3101.

[8] P.L. 94-472, Oct 11, 1976; 22 USC Sec. 3101(b).

[9] U.S. Congress. House. Committee on Government Operations. *The Adequacy of the Federal Response to Foreign Investment in the United States*. Report by the Committee on Government Operations. House Report No. 96-1216, 96th Cong., 2d Sess. Washington, U.S. Govt. Print. Off., 1980. 166-184.

[10] *The Operations of Federal Agencies*, part 3, p. 5.

a French firm because of classified work engaged in by the computer division. The acquisition proceeded after the classified contracts were reassigned to the U.S. parent company.[11]

The "Exon-Florio" Provision

In 1988, amid concerns over foreign acquisition of certain types of U.S. firms, particularly by Japanese firms, Congress approved the Exon-Florio provision. This statute grants the President the authority to block proposed or pending foreign acquisitions of "persons engaged in interstate commerce in the United States"that threaten to impair the national security. Congress directed, however, that before this authority can be invoked the President is expected to believe that other U.S. laws are inadequate or inappropriate to protect the national security, and that he must have "credible evidence" that the foreign investment will impair the national security.

By the late 1980s, Congress and the public had grown increasingly concerned about the sharp increase in foreign investment in the United States and the potential impact such investment might have on the U.S. economy. In particular, the proposed sale in 1987 of Fairchild Semiconductor Co. by Schlumberger Ltd. of France to Fujitsu Ltd. of Japan touched off strong opposition in Congress and provided much of the impetus behind the passage of the Exon-Florio provision. The proposed Fairchild acquisition generated intense concern in Congress in part because of general difficulties in trade relations with Japan at that time and because some Americans felt that the United States was declining as an international economic power as well as a world power. The Defense Department opposed the acquisition because some officials believed that the deal would give Japan control over a major supplier of computer chips for the military and would make U.S. defense industries more dependent on foreign suppliers for sophisticated high-technology products.[12]

Although Commerce Secretary Malcolm Baldridge and Defense Secretary Casper Weinberger failed in their attempt to have President Reagan block the Fujitsu acquisition, Fujitsu and Schlumberger called off the proposed sale of Fairchild.[13] While Fairchild was acquired some months later by National Semiconductor Corp. for a discount,[14] the Fujitsu-Fairchild incident marked an important shift in the Reagan Administration's support for unlimited foreign direct investment in U.S.

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[11] U.S. Congress. House. Committee on Energy and Commerce. Subcommittee on Commerce, Consumer Protection, and Competitiveness. *Foreign Takeovers and National Security*. Hearings on Section 905 of H.R. 3. 100th Cong., 1st. Sess., October 20, 1987. Testimony of David C. Mulford. Washington, U.S. Govt., Print., Off., 1988. p. 21-22.

[12] Auerbach, Stuart. Cabinet to Weigh Sale of Chip Firm. *The Washington Post*, March 12, 1987. p. E1.

[13] Sanger, David E. Japanese Purchase of Chip Maker Canceled After Objections in U.S. *The New York Times*, March 17, 1987. p. 1.

[14] Pollack, Andrew. Schlumberger Accepts Offer. *The New York Times*, September 1, 1987. p. D1.

businesses and boosted support within the Administration for fixed guidelines for blocking foreign takeovers of companies in national security-sensitive industries.[15]

In 1988, after three years of often contentious negotiations between Congress and the Reagan Administration, Congress passed and President Reagan signed the Omnibus Trade and Competitiveness Act of 1988.[16] The Exon-Florio provision, which was included as section 5021 of that Act, fundamentally transformed CFIUS. The provision originated in bills reported by the Commerce Committee in the Senate and the Energy and Commerce Committee in the House, but the measure was transferred to the Banking Committee as a result of a dispute over jurisdictional responsibilities.[17]

Part of Congress's motivation in adopting the Exon-Florio provision apparently arose from concerns that foreign takeovers of U.S. firms could not be stopped unless the President declared a national emergency or regulators invoked federal antitrust, environmental, or securities laws. Through the Exon-Florio provision, Congress attempted to strengthen the President's hand in conducting foreign investment policy, while providing a cursory role for itself as a means of emphasizing that, as much as possible, the commercial nature of investment transactions should be free from political considerations. Congress also attempted to balance public concerns about the economic impact of certain types of foreign investment with the nation's long-standing international commitment to maintain an open and receptive environment for foreign investment

Furthermore, Congress did not intend to have the Exon-Florio provision alter the generally open foreign investment climate of the country or to have it inhibit foreign direct investments in industries that could not be considered to be of national security interest. At the time, some analysts believed the provision could potentially widen the scope of industries that fell under the national security rubric. CFIUS, however, is not free to establish an independent approach to reviewing foreign investment transactions, but operates under the authority of the President and reflects his attitudes and policies. As a result, the discretion CFIUS uses to review and to investigate foreign investment cases reflects policy guidance from the President. Foreign investors are also constrained by legislation that bars foreign direct investment in such industries as maritime, aircraft, banking, resources and power.[18] Generally, these sectors were closed to foreign investors prior to passage of the Exon-Florio provision in order to prevent public services and public interest activities from falling under foreign control, primarily for national defense purposes.

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[15] Kilborn, Peter T. Curb Asked On Foreign Takeovers. *The New York Times*, March 18, 1987. p. D1.

[16] P.L. 100-418.

[17] Testimony of Patrick A. Mulloy before the Committee on Banking, Housing, & Urban Affairs, October 20, 2005.

[18] CRS Report RL33103, *Foreign Investment in the United States: Major Federal Restrictions,* by Michael V. Seitzinger.

Through Executive Order 12661, President Reagan implemented provisions of the Omnibus Trade Act. In the Executive Order, President Reagan delegated his authority to administer the Exon-Florio provision to CFIUS,[19] particularly to conduct reviews, to undertake investigations, and to make recommendations, although the statute itself does not specifically mention CFIUS. As a result of President Reagan's action, CFIUS was transformed from a purely administrative body with limited authority to review and analyze data on foreign investment to one with a broad mandate and significant authority to advise the President on foreign investment transactions and to recommend that some transactions be blocked. Presently, the Committee consists of twelve members, including the Secretaries of State, the Treasury, Defense, Homeland Security, and Commerce; the United States Trade Representative; the Chairman of the Council of Economic Advisers; the Attorney General; the Director of the Office of Management and Budget; the Director of the Office of Science and Technology Policy; the Assistant to the President for National Security Affairs; and the Assistant to the President for Economic Policy.[20]

Procedures

According to the Exon-Florio provision, CFIUS has 30 days to decide after it receives the initial formal notification by the parties to a merger, acquisition, or a takeover, whether to investigate a case as a result of its determination that the investment "threatens to impair the national security of the United States." If during this 30 day period all of the members of CFIUS conclude that the investment does not threaten to impair the national security, the review is terminated. If, however, at least one member of the Committee determines that the investment does threaten to impair the national security CFIUS can proceed to a 45-day investigation. At the conclusion of the investigation or the 45-day review period, whichever comes first, the Committee can decide to offer no recommendation or it can recommend that the President suspend or prohibit the investment. The President is under no obligation to follow the recommendation of the Committee to suspend or prohibit an investment.

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[19] Executive Order 12661 of December 27, 1988, 54 F.R. 779.

[20] Executive Order 11858 of May 7, 1975, 40 F.R. 20263 established the Committee with six members: the Secretaries of State, the Treasury, Defense, Commerce, and the Assistant to the President for Economic Affairs, and the Executive Director of the Council on International Economic Policy. Executive Order 12188, January 2, 1980, 45 F.R. 969, added the United States Trade Representative and substituted the Chairman of the Council of Economic Advisors for the Executive Director of the Council on International Economic Policy. Executive Order 12661, December 27, 1988, 54 F.R. 779, added the Attorney General and the Director of the Office of Management and Budget. Executive Order 12860, September 3, 1993, 58 F.R. 47201, added the Director of the Office of Science and Technology Policy, the Assistant to the President for National Security Affairs, and the Assistant to the President for Economic Policy. Executive Order 13286, Section 57, February 28, 2003 added the Secretary of Homeland Security.

Factors for Consideration

The Exon-Florio provision includes a short list of factors the President *may* consider in deciding to block a foreign acquisition. These factors are also considered by the individual members of CFIUS as part of their own review process to determine if a particular transaction threatens to impair the national security. This list includes the following elements:

(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;

(3) 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;

(4) the potential effects of the transactions on the sales of military goods, equipment, or technology to a country that supports terrorism or proliferates missile technology or chemical and biological weapons; and

(5) the potential effects of the transaction on U.S. technological leadership in areas affecting U.S. national security.

The first two factors emphasize the national defense aspects of foreign acquisitions, while the other three factors highlight national security implications of such investment. No clear definition is provided in the legislation for what constitutes "national security" or foreign "control," but CFIUS' regulations state that control is, "the power, whether or not exercised, to formulate, determine, direct, or decide important matters relating to the entity."[21] While national security might be interpreted broadly to include a range of economic issues, neither Congress nor the Administration attempted to define the term. Treasury Department officials have indicated that during an Exon-Florio review or investigation each CFIUS member is expected to apply that definition of national security that is consistent with the representative agency's specific legislative mandate.[22]

The Treasury Department has provided some guidance to firms deciding whether they should notify CFIUS of a proposed or pending merger, acquisition, or takeover. The guidance states that proposed acquisitions that need to notify CFIUS are those that involve "products or key technologies essential to the U.S. defense industrial base." This notice is not intended for firms that produce goods or services with no special relation to national security, especially toys and games, food

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[21] Regulations Pertaining to Mergers, Acquisitions, and Takeover by Foreign Persons. 31 CFR Sec. 800.

[22] Senate Armed Services Committee, Briefing on the Dubai Ports World Ports Deal, February 23, 2006.

products, hotels and restaurants, or legal services. CFIUS has indicated that in order to assure an unimpeded inflow of foreign investment it would implement the statute "only insofar as necessary to protect the national security," and "in a manner fully consistent with the international obligations of the United States."[23]

As originally drafted, the Exon-Florio provision also would have applied to joint ventures and licensing agreements in addition to mergers, acquisitions, and takeovers. Joint ventures and licensing agreements subsequently were dropped from the proposal because the Administration and various industry groups argued that such business practices are generally beneficial arrangements for U.S. companies. In addition, they argued that any potential threat to national security could be addressed by the Export Administration Act[24] and the Arms Control Export Act.[25]

Confidentiality Requirements

The Exon-Florio provision also codified confidentiality requirements that are similar to those that appeared in Executive Order 11858 by stating that any information or documentary material filed under the provision may not be made public "except as may be relevant to any administrative or judicial action or proceeding."[26] The provision does state, however, that this confidentiality provision "shall not be construed to prevent disclosure to either House of Congress or to any duly authorized committee or subcommittee of the Congress." The Exon-Florio provision requires the President to provide a written report to the Secretary of the Senate and the Clerk of the House detailing his decision and his actions relevant to any transaction that was subject to a 45-day investigation.[27] As presently written, there is no requirement for CFIUS or the President to notify or otherwise inform Congress of cases it reviews or of the outcome of any investigation.

Treasury Department Regulations

After extensive public comment, the Treasury Department issued its final regulations in November 1991 implementing the Exon-Florio provision.[28] These regulations created an essentially voluntary system of notification by the parties to an acquisition and they allow for notices of acquisitions by agencies that are members of CFIUS. Despite the voluntary nature of the notification, firms largely comply with the provision because the regulations stipulate that foreign acquisitions that are governed by the Exon-Florio review process that do not notify the Committee

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[23] Ibid.

[24] 50 U.S.C. App. Sec. 2401, as amended.

[25] 22 U.S.C. App. 2778 et seq.

[26] 50 U.S.C. Appendix Sec. 2170(c)

[27] 50 U.S.C. Appendix Sec. 2170(g).

[28] Regulations Pertaining to Mergers, Acquisitions, and Takeovers by Foreign Persons. 31 C.F.R. Part 800.

remain subject indefinitely to divestment or other appropriate actions by the President. Under most circumstances, notice of a proposed acquisition that is given to the Committee by a third party, including shareholders, is not considered by the Committee to constitute an official notification. The regulations also indicate that notifications provided to the Committee are considered to be confidential and the information is not released by the Committee to the press or commented on publicly.

The "Byrd Amendment"

In 1992, Congress amended the Exon-Florio statute through section 837(a) of the National Defense Authorization Act for Fiscal Year 1993 (P.L. 102-484). Known as the "Byrd" amendment after the amendment's sponsor, the provision requires CFIUS to investigate proposed mergers, acquisitions, or takeovers in cases where two criterion are met:

(1) the acquirer is controlled by or acting on behalf of a foreign government; and

(2) the acquisition results in control of a person engaged in interstate commerce in the United States that could affect the national security of the United States.[29]

This amendment has come under intense scrutiny by the 109th Congress as a result of the DP World transaction. Many Members of Congress and others believed that this amendment required CFIUS to undertake a full 45-day investigation of the transaction because DP World was "controlled by or acting on behalf of a foreign government." The DP World acquisition, however, exposed a sharp rift between what some Members apparently believed the amendment directed CFIUS to do and how the members of CFIUS were interpreting the amendment. In particular, some Members of Congress apparently interpreted the amendment to direct CFIUS to conduct a mandatory 45-day investigation if the foreign firm involved in a transaction is owned or controlled by a foreign government. Representatives of CFIUS argued that they interpret the amendment to mean that a 45-day investigation is discretionary and not mandatory. In the case of the DP World acquisition, CFIUS representatives argued that they had concluded as a result of an extensive review of the proposed acquisition prior to the case being formally filed with CFIUS and during the 30-day review that the DP World case did not warrant a full 45-day investigation. They conceded that the case met the first criterion under the Byrd amendment, because DP World was controlled by a foreign government, but that it did not meet the second part of the requirement, because CFIUS had concluded during the 30-day review that the transaction "could not affect the national security."[30]

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[29] P.L. 102-484, Oct. 23, 1992.

[30] Briefing on the Dubai Ports World Deal before the Senate Armed Services Committee, February 23, 2006.

CFIUS Since Exon-Florio

Recent information indicates that the number of cases reviewed by CFIUS has declined since the late 1990s. In part, the decline reflects the slowdown in foreign investment activity in the United States generally that occurred between 1998 and 2003, as indicated in **Table 1**. Based on the number of transactions per year, acquisitions of U.S. firms by other U.S. firms has accounted for the largest share of all merger and acquisition (M&A) transactions over the past ten years. This share fell from 76% of all U.S. M&A transactions in 1996 to 72% in 2005, but that was up from a low of 68% recorded in 2001. The share of M&A activity attributed to foreign firms acquiring U.S. firms in 2005 accounts for 13% of all such transactions, up from 9% in 1996.

In addition to a lower overall level of investment activity, the lower case load experienced by CFIUS may reflect the impact of an informal CFIUS review process that has developed over time. This process gives firms the opportunity to reconsider their investments if they believe they could face a difficult CFIUS review or if they believe the transaction could be subjected to a formal 45-day investigation with its potentially negative connotations regarding national security concerns. In addition, some observers argue that the case load diminished following the September 11th, 2001terrorists attacks on the United States due to the organization of the Department of Homeland Security (DHS), which has participated actively in the CFIUS process and has raised security concerns. These concerns may have caused some firms to reconsider their investment transactions before they had progressed very far in the formal CFIUS process in order to avoid a long and involved investigation by DHS.[31]

Table 1. Merger and Acquisition Activity in the United States, 1996-2005

	Total Number of Mergers and Acquisitions	U.S. Firms Acquiring U.S. Firms	Non-U.S. Firms Acquiring U.S. Firms	U.S. Firms Acquiring Non-U.S. Firms
1996	7,347	5,585	628	1,134
1997	8,479	6,317	775	1,387
1998	10,193	7,575	971	1,647
1999	9,173	6,449	1,148	1,576
2000	8,853	6,032	1,264	1,557
2001	6,296	4,269	923	1,104
2002	5,497	3,989	700	808
2003	5,959	4,357	722	880
2004	7,031	5,084	813	1,134
2005	7,298	5,274	936	1,088

Source: *Mergers & Acquisitions*, February 2006.

[31] Marchick, David. Testimony Before the House Financial Services Committee, March 1, 2006.

As a consequence of the confidential nature of the CFIUS review of any proposed transaction, there are few official sources of information concerning the Committee's work to date. For the most part, information concerning individual transactions that have been reviewed by CFIUS or any final recommendations that have been issued by CFIUS have come from announcements released by the companies involved in a transaction and not by CFIUS. According to one source,[32] CFIUS has received more than 1,500 notifications since 1988, of which it conducted a full investigation of 25 cases. Of these 25 cases, thirteen transactions were withdrawn upon notice that CFIUS would conduct a full review and twelve of the remaining transactions cases were sent to the President. Of these twelve transactions, one was prohibited.[33]

Impact of the Exon-Florio Process on CFIUS

The DP World case has exposed a number of important aspects of CFIUS' operations that apparently were not well known or understood by the public in general. As already indicated, the Exon-Florio provision stipulates a three-step process: the formal notification to CFIUS and a 30-day review; a 45-day investigation for those transactions that raised national security concerns during the 30-day review and for those in which the concerns were not resolved during the review period; and a 15-day Presidential determination stage for those transactions that were determined after the 45-day review to pose an impairment to national security. Over time, however, this process apparently has evolved to include an informal fourth stage of unspecified length of time that consists of an unofficial CFIUS determination prior to the formal filing with CFIUS. This type of informal review has developed because it likely serves the interests of both CFIUS and the firms involved in an investment transaction. According to Treasury Department officials, this informal contact enables "CFIUS staff to identify potential issues before the review process formally begins."[34]

Firms that are party to a transaction apparently benefit from this informal review in a number of ways. For one, it allows firms additional time to work out any national security concerns privately with individual CFIUS members. Secondly, and perhaps more importantly, it provides a process for firms to avoid risking the potentially negative publicity that could arise if a transaction were to be blocked or otherwise labeled as impairing U.S. national security interests. For some firms, public knowledge of a CFIUS investigation has had a negative effect on the value of the firm's stock price.

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[32] CFIUS, *The Washington Post*, July 3, 2005. p. F3.

[33] Auerbach, Stuart. "President Tells China to Sell Seattle Firm." *The Washington Post*, February 3, 1990. p. A1; and Benham, Barbara. "Blocked Takeover Fuels Foreign Policy Flap." *Investor's Daily*, February 8, 1990. p. 1.

[34] Testimony of Robert Kimmett, Briefing on the Dubai Ports World Deal before the Senate Armed Services Committee, February 23, 2006.

After a lengthy review by CFIUS in 2000 of Verio, Inc., a U.S. firm that operates websites for businesses and provides internet services, was acquired by NTT Communications of Japan. Verio's stock price reportedly fell during the CFIUS investigation as a result of uncertainty in the market about prospects for the transaction. The CFIUS review was instigated by the FBI, which had expressed concerns during the initial review stage that the majority interest of the Japanese government in NTT could give it access to information regarding wiretaps that were being conducted on email and other Web-based traffic crossing Verio's computer system. After completing its investigation, however, CFIUS did not recommend that President Clinton block the transaction.

The potentially negative publicity that can be associated with a CFIUS investigation of a transaction apparently has had a major impact on the transactions CFIUS has investigated. Since 1990, nearly half of the transactions CFIUS investigated were terminated by the firms involved, because the firms decided to withdraw from the transaction rather than face a negative determination by CFIUS. In 2006, for instance, the prospects of a CFIUS investigation apparently was the major reason the Israeli firm Check Point Software Technologies decided to call off its proposed $225 million acquisition of Sourcefire, a U.S. firm specializing in security appliances for protecting a corporation's internal computer networks. In addition, the decision by the China National Offshore Oil Company (CNOOC) to drop its proposed acquisition of Unocal oil company in 2005 was partly due to concerns by CNOOC about an impending CFIUS investigation of the transaction.

For CFIUS members, the informal process is beneficial because it gives them as much time as they feel is necessary to review a transaction without facing the time constraints that arise under the formal CFIUS review process. This informal review likely also gives the CFIUS members added time to negotiate with the firms involved in a transaction to restructure the transaction in ways that address any potential security concerns or to develop other types of conditions that members of CFIUS feel are appropriate in order to remove security concerns.

The DP World acquisition demonstrates how this informal CFIUS process can operate in reviewing a proposed foreign investment transaction. According to officials involved in the review, DP World officials contacted the Treasury Department in early October 2005 to informally discuss their proposed transaction. Treasury officials directed DP World to consult with the Department of Homeland Security and in November the Treasury officials requested an intelligence assessment from the Director of National Intelligence. Staff representatives from all of the CFIUS members met on December 6, 2005 to discuss the transaction, apparently to determine if there were any security concerns that had not been addressed and resolved during the two-month long informal review of the proposed transaction.

Ten days after that meeting, DP World filed its official notification with CFIUS, which distributed the notification to all of the CFIUS members and to the Departments of Energy and Transportation. During this process, the Department of Homeland Security apparently negotiated a letter of assurances with DP World that addressed some outstanding concerns about port security. On the basis of this letter and the lack of any remaining concerns expressed by any member of CFIUS or other agencies that were consulted, CFIUS completed its review of the transaction on

January 17, 2006 and concluded that the transaction did not threaten to impair the national security and therefore that it did not warrant a 45-day investigation.[35]

Actions in the 109th Congress

Following the public attention that focused on the DP World transaction in mid-February 2006, Members of Congress introduced more than two dozen bills that related directly or closely to the proposed transaction. The bills range in focus from blocking the DP World transaction to revamping the CFIUS process. These measures can be grouped into four major areas: those that deal specifically with the proposed Dubai Ports World acquisition; those that focus more generally on foreign ownership of U.S. ports, especially if the foreign entity is owned or controlled by a foreign government; those that would amend the CFIUS process; and those that would amend the Exon-Florio process. On the whole, a broad range of measures would increase reporting requirements on CFIUS to keep key congressional leaders apprised of the Committee's actions. In some measures, Congress would have the authority to intercede in a transaction that had been approved by CFIUS, to override the CFIUS action, and to block a transaction.

The first measures that were introduced were directed at stopping the DP World acquisition from occurring and at requesting CFIUS to undertake a full 45-day investigation of the transaction. For instance, **S.J.Res. 32**, introduced February 27, 2006 and **H.J.Res. 79**, introduced February 28, 2006 express congressional disapproval of the proposed acquisition and direct CFIUS to conduct a full 45-day review of the transaction and to brief Members of Congress on the results of the investigation.

On March 8, 2006, the House Appropriations Committee attached an amendment (**H.Amdt. 702**) to a supplemental appropriations bill for defense activities in Afghanistan and Iraq and emergency relief for the victims of hurricane Katrina (**H.R. 4939**) that effectively would have nullified the actions of CFIUS regarding the DP World transaction. The amendment would have withheld the use of any funds to approve or "otherwise allow the acquisition of leases, contracts, rights, or other obligations of P&O Ports by Dubai Ports World." In addition, the amendment would have prohibited Dubai Ports World from acquiring any leases, contracts, rights, or other obligations in the United States of P&O Ports by Dubai Ports World or "any other legal entity affiliated with or controlled by Dubai Ports World." The measure passed by a vote of 62 to 2 in the Committee.[36] The following day, DP World officials announced that they will sell off the newly-acquired U.S. port operations to an American owner.[37]

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[35] *Ibid*.

[36] Hulse, Carl, "In Break with While House, House Panel Rejects Port Deal," *The New York Times*, March 9, 2006. p. A1.

[37] Weisman, Jonathan, and Bradley Graham, "Dubai Firm to Sell U.S. Port Operations," *The Washington Post*, March 10, 2006. p. A1.

On March 16, 2006, the measure passed the full House by a margin of 348 to 71 after an attempt the previous day failed by a vote of 377 to 38 to remove the ban on Dubai Ports World from the measure.[38] The measure is now awaiting Senate action.

Such other measures as **H.R. 4813** and **H.R. 4917** would place new reporting requirements on CFIUS to inform Congress when it initiates a 45-day investigation of a proposed acquisition, merger, or takeover. **H.R. 4917** also would express a sense of Congress that CFIUS be moved from operating out of the Treasury Department to the Department of Homeland Security. Since CFIUS is entirely a creation of Executive Order and operates exclusively for and on behalf of the President, it is unclear how much of an impact this measure would have on the President.

Other measures attempt to address various concerns some Members of Congress have expressed with the current CFIUS process. In particular, some Members have voiced their dissatisfaction with the broad discretion CFIUS has to determine which transactions it will subject to a 45-day investigation. Also, some Members apparently are dissatisfied with the discretion CFIUS uses to interpret the Byrd Amendment. Other measures have been introduced to shift the leadership of CFIUS from the Treasury Department to the Department of Homeland Security and to limit CFIUS's discretion in investigating certain kinds of transactions, because some Members argue that the Treasury Department has acted to limit the number of transactions CFIUS investigates in order to promote the Department's traditional position of supporting an open and unobstructed investment process. Other measures would leave unchanged the basic structure of CFIUS, but would institute CFIUS as a matter of statute to strengthen Congressional oversight of the Committee's operations.

The following measures focus most specifically on the Committee on Foreign Investment in the United States and propose various changes to the existing CFIUs process.

H.R. 4929. H.R. 4929 was introduced by Representative Sabo on March 9, 2006. This measure would amend the Exon-Florio process to limit CFIUS' discretion to investigate foreign investment transactions by mandating that an investigation must occur for any proposed or pending merger, acquisition, or takeover by any foreign person that could result in foreign control of any person engaged in interstate commerce in the United States. This measure would establish the Committee on Foreign Investment in the United States in statute and formally make it responsible for conducting an investigation within 75 days of receipt of a written notification of a proposed or pending merger, acquisition, or takeover. The Committee would remain as presently constituted with 12 members and with the Secretary of the Treasury as the Chairperson of the Committee. The Director of National Intelligence would provide appropriate intelligence analysis and briefings to the Committee.

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[38] *Washington Trade Daily*, March 17, 2006. p. 3.

The measure also attempts to prod the administration into investigating more investment cases by requiring that the President must find that a transaction "will not threaten" to impair the national security of the United States in order for any proposed or pending merger, acquisition, or takeover of a person engage in interstate commerce in the United States by a foreign person to occur. The measure would limit somewhat the President's discretion by amending the existing Exon-Florio statute. Presently, the statute states that "the President may exercise the authority ...only if he finds that..." The measure would change the statute to indicate that the President's ability to act is based on findings that "shall be based on credible evidence" that leads the President to believe that a) the foreign interest "might" take action that threatens to impair the national security, and b) other provisions of law are appropriate to protect the national security. During an investigation, the measure would require that those factors that the President is required to consider in investigating a proposed or pending transactions would be the same as those that currently are specified in the Exon-Florio provision.

The measure also would increase reporting requirements on the CFIUS process by requiring the President to transmit immediately a written notification to the Secretary of the Senate and the Clerk of the House of Representatives containing a detailed explanation of any determination by the President to approve or disapprove of any merger, acquisition, or takeover by or with any foreign person which could result in foreign control of any person engaged in interstate commerce in the United States. Congress would have 30 days to enact a joint resolution of disapproval of a transaction, which, if adopted, would then have the President " take such action...as is necessary to prohibit the merger, acquisition, or takeover." The measure would also require the President to provide a report to the Congress that evaluates whether there is "credible evidence of a coordinated strategy by one or more countries or companies to acquire U.S. companies that are involved in research, development, or production of critical technologies for which the United states is a leading producer." The report would also be required to evaluate whether there are industrial espionage activities that are directed or directly assisted by foreign governments against private U.S. companies.

S. 1797. S. 1797 was introduced by Senator Inhofe on September 29, 2005. This measure reflects long-standing displeasure with CFIUS that pre-dates the Dubai Ports World transactions. The measure would amend the Exon-Florio process by giving CFIUS 60 days instead of the present 30 days to decide if a pending investment requires a mandatory 45-day investigation. In addition, the measure increases reporting requirements by directing that the findings and recommendations from any 45-day investigation would be sent immediately to the President and to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House. This measure would provide for a congressional role in the CFIUS process by allowing the Chairman and Ranking Member of the Senate Banking Committee and the House Financial Services Committee to request a full 45-day investigation of investments that fall under the Byrd Amendment and would provide that the results of any such investigation be sent to the President and the Senate Banking Committee and the House Financial Services Committee.

This measure also attempts to limit CFIUS' discretion by changing from optional (may) to mandatory (shall) the factors that CFIUS considers in determining if a transaction threatens to impair national security. It would also add a new factor by requiring that CFIUS consider "the long-term projections of the United States requirements for sources of energy and other critical resources and materials and for economic security." The measure also would require the Secretary of the Treasury to provide a report quarterly to the Senate Banking Committee and the House Financial Services Committee that contains a detailed summary and analysis of each transaction that is being reviewed or was reviewed during the quarter. In further broadening Congress' role in the CFIUS process, a transaction that the President has chosen not to suspend or prohibit would not be finalized for 10 legislative days after the President notifies Congress during which if either House of Congress introduced a joint resolution of disapproval, the transaction would be stopped for 30 legislative days. If such a joint resolution were to be enacted into law, the transaction would be blocked.

S. 2380. On March 7, 2006, Senator Dodd introduced **S. 2380**, which would attempt to address concerns among some Members who argue that CFIUS has not been viewing national security concerns broadly enough when reviewing and investigating proposed investment transactions. As a result of these concerns, this measure would restrict CFIUS's discretion in investigating proposed investment transactions by adding a new national security review. The measure would replace the present leadership model with the Secretary of the Treasury as the lead official with a troika leadership that would include the Secretary of Homeland Security and the Secretary of Defense as vice chairs of the Committee. In addition, CFIUS membership would expand to include the Directors of National Intelligence and Central Intelligence. The measure would have the President establish a Subcommittee on Intelligence within the CFIUS structure that would be chaired by the Director of National Intelligence and would include the head of each member of the intelligence community. The measure would amend the Exon-Florio process to provide for a pre-investigation review by the Subcommittee on Intelligence of CFIUS during a 15-day period that would begin following the receipt by the Committee of any proposed merger, acquisitions, or takeover and before the commencement of any 45-day investigation and provide written comments on that review.

The measure would also amend the Exon-Florio process to require that only the President or the Secretary of the Treasury, with the concurrence of the Secretary of Homeland Security and the Secretary of Defense acting on the President's behalf, can determine that a proposed merger, acquisition, or takeover does not threaten to impair the national security and, therefore, would not require a 45-day investigation. In such cases, either the President or members of CFIUS acting on his behalf would be required to certify this conclusion in writing. In addition, any person controlled by or acting on behalf of a foreign government that is a party to a proposed merger, acquisition, or takeover of any U.S. critical infrastructure (as defined in 42 U.S.C. 5195c(e)) would be required to notify the President or his designee. The Exon-Florio provision would also be amended to require the President or his designee to notify Congress not later than 15 days after he receives a written notification of a proposed merger, acquisition, or takeover that could proceed to the 45-day investigation. The measure would amend the Exon-Florio provision to specify that the President's

designee named under the provision is the Committee on Foreign Investment in the United States.

S. 2400. On March 13, 2006, Senator Collins introduced S. 2400 that would appreciably alter the current Exon-Florio process and expand the current national security review to include "homeland security." Most importantly, the measure would repeal that section of the Defense Production Act that is known as the Exon-Florio provision and transfer the function for reviewing mergers, acquisitions and takeovers to the Secretary of Homeland Security. The measure would establish the Committee for Secure Commerce, which would be comprised of the heads of those executive departments, agencies, and offices that the President determines to be appropriate and would include the Director of National Intelligence. The chairperson of the Committee would be able to seek information and assistance from any other department, agency, or office of the Federal Government as the chairperson determines is necessary or appropriate to carry out the duties of the Committee.

The Committee would be charged with conducting a review of proposed or pending mergers, acquisitions, or takeovers within 30 days of being notified of such a transaction, and could undertake an investigation of proposed or pending mergers, acquisitions, or takeovers "to determine the effects on national security and homeland security." Such an investigation would need to be completed within 45 days of its commencement. Any investigation would require the Director of National Intelligence to create a report that consolidates the intelligence findings, assessments, and concerns of each of the relevant members of the intelligence community. The intelligence report would be provided to all members of the Committee and would be included as part of any recommendation by the President. An investigation would be mandated in any instance in which an entity that is controlled by or acting on behalf of a foreign government seeks to engage in any merger, acquisition, or takeover which would result in the control of a person (entity) engaged in interstate commerce in the United States.

The chairperson of the Committee would be responsible for establishing written processes and procedures to be used by the Committee in conducting reviews and investigations. In addition, the chairperson would be responsible for describing the role and responsibilities of each member of the departments, agencies, and offices that are involved in the investigation of foreign investment in the United States. The head of each department, agency, or office that serves as a member of the Committee would be required to establish written internal processes and procedures in conducting reviews and investigations. Congress would be able to review such written procedures as part of its oversight responsibilities.

Under the measure, the President would have the authority to "take such action for such time as the President considers appropriate to suspend or prohibit any acquisition, merger, or takeover." The President would be required to announce his decision within 15 days after the completion of the investigation by the Committee. The President would be allowed to exercise his authority under this provision "only if the President finds:" that there is credible evidence that leads the President to believe that the foreign interest exercising control might take action that threatens to impair the national security or homeland security; or that other provisions of law do

not provide adequate and appropriate authority for the President to protect the national security or homeland security. In making his decision, the President would be required (shall) to take into account the requirements of national security and homeland security and consider among other factors the same set of factors that currently exist under the Exon-Florio provision.

The measure also would require the President or his designee to report immediately upon completion of an investigation to the Congress. This reporting would comprise a written report of the results of the investigation and would include a detailed explanation of the findings that were made; details of any legally binding assurances that were provided by the foreign entity that were negotiated as a condition for approval; and the factors that were considered in reaching the determination. The President would also be required to transmit to certain Members of Congress a report in both classified and unclassified form on a quarterly basis that provides a detailed summary and analysis of each merger, acquisition, or takeover that would be under review or investigation at the time of the report. In addition, the measure would require the President to furnish to Congress on a quadrennial basis a report that a) evaluates whether there is credible evidence of a coordinated strategy by 1 or more countries or companies to acquire critical infrastructure within the United States or U.S. companies involved in research, development, or production of critical technologies for which the United States is a leading producer; and b) evaluates whether there are industrial espionage activities directed or directly assisted by foreign governments against private U.S. companies aimed at obtaining commercial secrets related to critical technologies or critical infrastructure.

Conclusions

The proposed DP World acquisition of P&O, while of arguably little economic impact on the U.S. economy, could affect public policy on foreign investment that relates to issues of corporate ownership, foreign investment, and national security in the U.S. economy. The transaction revealed significant differences between Congress and the Administration over the operations of CFIUS and over the objectives the Committee should be pursuing. In addition, the transaction demonstrated that neither Congress nor the Administration has been able so far to define clearly the national security implications of foreign direct investment. This issue likely reflects differing assessments of the economic impact of foreign investment on the U.S. economy and differing political and philosophical convictions among Members and between the Congress and the Administration.

The incident also focused attention on the informal process firms use to have their investment transactions reviewed by CFIUS prior to a formal review. According to anecdotal evidence, some firms apparently believe that the CFIUS process is not market neutral, but that it adds to market uncertainty that can negatively affect a firm's stock price and lead to economic behavior by some firms that is not optimal for the economy as a whole. Such behavior might involve firms expending a considerable amount of resources to avoid a CFIUS investigation, or deciding to terminate a transaction that would improve the optimal performance of the economy in order to avoid a CFIUS investigation. While such anecdotal evidence

does not provide enough evidence to serve as the basis for developing public policy, it does raise a number of concerns about the possible impact of the CFIUS process on the market and the potential costs of redefining the concept of national security relative to foreign investment.

The recent focus by Congress on the Committee has also shown that the DP World transaction, in combination with other recent unpopular foreign investment transactions, has exacerbated dissatisfaction among some Members of Congress over the operations of CFIUS. In particular, some Members are displeased with the way the Committee uses its discretionary authority under the Exon-Florio provision to investigate certain foreign investment transactions. As a result, Congress could make significant changes to the CFIUS process through legislation that has been proposed in the 2nd Session of the 109th Congress. The changes could mandate more frequent contact between the Committee, which generally operates without much public or congressional attention, and the Congress. Other measures would enhance Congress's oversight role over the Committee. Other measures would give Congress some form of a veto over aspects of the Committee's investigations of foreign investment transactions.

The DP World transaction also revealed that the September 11, 2001 terrorist attacks may have fundamentally altered the viewpoint of some Members of Congress regarding the role of foreign investment in the economy and over the impact of such investment on the national security framework. These observers argue that this change requires a reassessment of the role of foreign investment in the economy and of the implications of corporate ownership of activities that fall under the rubric of critical infrastructure. As a result, some Members of Congress are looking to amend the CFIUS process to enhance Congress's oversight role while reducing somewhat the discretion of CFIUS to review and investigate foreign investment transactions in order to have CFIUS investigate a larger number of foreign investment cases. In addition, the DP World transaction has focused attention on long-unresolved issues concerning the role of foreign investment in the nation's overall security framework and the methods that are being used to assess the impact of foreign investment on the nation's defense industrial base and homeland security.

Most economists agree that there is little economic evidence to conclude that foreign ownership, whether by a private entity or by an entity that is owned or controlled by a foreign government, has a measurable impact on the U.S. economy. Others may argue that such firms pose a risk to national security or to homeland security, but such concerns are not within the purview of this report. Similar issues concerning corporate ownership were raised during the late 1980s and early 1990s when foreign investment in the U.S. economy increased rapidly. There are little new data, however, to alter the conclusion reached at that time that there is no definitive way to assess the economic impact of foreign ownership or of foreign investment on the economy. Although some observers have expressed concerns about foreign investors who are owned or controlled by foreign governments acquiring U.S. firms, there is little confirmed evidence that such a distinction in corporate ownership has any effect on the economy as whole.

For most economists, the distinction between domestic- and foreign-owned firms, whether the foreign firms are privately owned or controlled by a foreign

government, is sufficiently small that they would argue that it does not warrant placing restrictions on the inflow of foreign investment. Nevertheless, foreign direct investment does entail various economic costs and benefits. On the benefit side, such investments bring added capital into the economy and potentially could add to productivity growth and innovation. Such investment also represents one repercussion of the U.S. trade deficit. The deficit transfers dollar-denominated assets to foreign investors, who then decide how to hold those assets by choosing among various investment vehicles, including direct investment. Foreign investment also removes a stream of monetary benefits from the economy in the form of repatriated capital and profits that reduces the total amount of capital in the economy. Such costs and benefits likely occur whether the foreign owner is a private entity or a foreign government.