

Fall 2012

CFIUS Now Made in China: Dueling National Security Review Frameworks as a Countermeasure to Economic Espionage in the Age of Globalization

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Souvik Saha, *CFIUS Now Made in China: Dueling National Security Review Frameworks as a Countermeasure to Economic Espionage in the Age of Globalization*, 33 *Nw. J. INT'L L. & BUS.* 199 (2012).
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CFIUS Now Made in China: Dueling National Security Review Frameworks as a Countermeasure to Economic Espionage in the Age of Globalization

*By Souvik Saha**

Abstract: The era of globalization has produced previously unimaginable economic benefits by spurring linkages between countries through trade and foreign investment. This newfound interconnectivity, however, also raises national security concerns for countries, such as the United States, that welcome foreign investment in the form of mergers, acquisitions, and takeovers. Part II highlights one such threat stemming from the rise of China and its aggressive foreign investment strategy to acquire American companies in industries critical to national security. In response to the growing threat of economic espionage from foreign investors, the United States created the Committee on Foreign Investment in the United States (CFIUS)—a national security review process for foreign mergers and acquisitions. Part III analyzes the evolution of CFIUS, while Part IV introduces China's freshly minted model for analogous national security reviews. Given the rise of these dueling frameworks in the world's two largest economies, critics contend that such national security reviews inject non-transparency, uncertainty, and politics into viable investment opportunities. Part V addresses these concerns and demonstrates that such criticisms are either overblown or outweighed in the post-9/11 world.

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I. INTRODUCTION

When asked whether the United States or China were perpetrators of industrial espionage, Julian Assange declared, “The U.S. is one of the victims.”¹ The disclosure smacks of irony given its source, a man dedicated to proliferating corporate and governmental secrets in the name of freedom of information. Yet, the United States’ vulnerability to espionage—military or economic—is hardly a secret. While many believe that spy games are a relic of the Cold War, the United States, and presumably all developed economies, remain on high alert. Those operating on the frontlines of American counter-intelligence efforts echo the sentiment: “The Cold War is not over, it has merely moved into a new arena: the global marketplace.”²

Indeed, the critically acclaimed “Age of Globalization” is upon us, and it features rapidly developing economies linked together in a mounting global market. The promise of globalization is well-documented as a force that is “enlarg[ing] the world economy, promot[ing] technological

¹ Andy Greenberg, *An Interview with WikiLeaks’ Julian Assange*, FORBES (Nov. 29, 2010, 5:02 PM), <http://www.forbes.com/sites/andygreenberg/2010/11/29/an-interview-with-wikileaks-julian-assange/>.

² *Economic Espionage*, FED. BUREAU OF INVESTIGATION, <http://www.fbi.gov/about-us/investigate/counterintelligence/economic-espionage> (last visited Mar. 25, 2012).

innovations, foster[ing] universal political participation, and enhanc[ing] international cooperation.”³ Unlike the rhetoric of the Cold War, the new vernacular emphasizes mutual economic development rather than mutually assured destruction. In the process of “integrat[ing] markets, transportation systems, and communication systems,” globalization renders “national boundaries immaterial.”⁴ In light of these previously unimaginable economic benefits, it is unsurprising that the initial reviews of globalization are overwhelmingly positive.⁵

While the United States has benefited greatly from this global transformation, the remarkable and unprecedented expansion of China’s global presence is one of the principal narratives of globalization.⁶ A key ingredient in China’s grand strategy of expansion—foreign direct investment (FDI)—continues to raise serious concerns in the United States. Simply stated, “Foreign ownership of an American corporation provides a presence for that parent company’s country in the United States.”⁷ This creates a potential conduit for leaking American technology, intellectual property, and sensitive information pertaining to critical infrastructure. Repeated Chinese attempts to purchase American companies, particularly in markets deemed essential to national security, are alarming to policymakers given China’s challenge to American economic leadership.⁸

In response to this potential threat, the United States has crafted an elaborate legislative framework to review foreign mergers and acquisitions for national security implications. Pursuant to the Defense Production Act of 1950, the Committee on Foreign Investment in the United States (CFIUS)⁹ is now charged with implementing the review process. Seen as an impediment to trade liberalization, however, some argue that CFIUS threatens economic productivity, potentially in an arbitrary and capricious manner.¹⁰ They argue that such discrimination not only threatens future FDI in American markets, but also could lead to retaliatory measures by rebuffed investors, such as China, to the detriment of American investors attempting to enter into markets abroad.¹¹

³ Arthur C. Helton & Dessie P. Zagorcheva, *Globalization, Terror, and the Movements of People*, 36 INT’L LAW. 91, 92 (2002).

⁴ Joseph Mamounas, *Controlling Foreign Ownership of U.S. Strategic Assets: The Challenge of Maintaining National Security in a Globalized and Oil Dependent World*, 13 L. & BUS. REV. AM. 381, 382 (2007).

⁵ *E.g.*, *id.* at 383.

⁶ *See infra* Part II.B.

⁷ Mamounas, *supra* note 4, at 384.

⁸ *See infra* Part II.A.

⁹ Defense Production Act of 1950 §721, 50 U.S.C. app. § 2170 (2012).

¹⁰ Mamounas, *supra* note 4, at 393.

¹¹ Gaurav Sud, Note, *From Fretting Takeovers to Vetting CFIUS: Finding a Balance in U.S. Policy Regarding Foreign Acquisitions of Domestic Assets*, 39 VAND. J. TRANSNAT’L L.

That fear of Chinese retaliation recently proved prescient. In early 2011, China codified its own national security review framework that mirrors the functionality of CFIUS.¹² In light of this recent development, there is a renewed debate concerning the necessity, scope, and wisdom of the current national security review process, which potentially impedes trade and free market economics. This Comment seeks to address the rise of these dueling national security review frameworks in the United States and China.

In Part II, this Comment contextualizes the potential Chinese threat via FDI. This includes a snapshot of the current U.S.-China trade relationship, as well as the most recent threat analysis according to the U.S. intelligence community. Part III provides a detailed glimpse of the U.S. national security review process for foreign mergers and acquisitions, including recent developments involving CFIUS. As a juxtaposition, Part IV introduces the Chinese counterpart to CFIUS, and provides a comparison of the two national security review frameworks. Part V proceeds to respond to the common criticisms of CFIUS through a case study approach. This Comment contends that the alleged economic costs of CFIUS are both exaggerated and outweighed by the threat of economic espionage. Finally, Part VI concludes that CFIUS, through its various iterations, strikes the proper balance between national security and economic interests.

II. THE TWO FACES OF GLOBALIZATION AND THE THREAT FROM CHINA

Despite the many benefits of globalization, there also exists a darker underside that is becoming exceedingly apparent. While globalization expands economies, it also amplifies the inequalities that are inherent within market capitalism, often at the expense of the poor.¹³ However, the negative externalities of globalization are not confined to the underdogs; its effects are also felt in developed countries. Just as globalization re-directs human capital into higher-skilled positions, U.S. workers lacking requisite qualifications are left vulnerable to the cold, profit-maximizing calculus of outsourcing.¹⁴ Coupled with the global recession, “millions of citizens have lost steady work . . . and a race to the bottom has been ignited abroad.”¹⁵ The recent “Occupy Movement” is a testament to these social and economic ills.

1303, 1325 (2006).

¹² Lester Ross & Kenneth Zhou, *China Adopts its Own ‘CFIUS’ Regulations*, WILMERHALE (Feb. 28, 2011), <http://www.wilmerhale.com/publications/whPubsDetail.aspx?publication=9726>.

¹³ Helton & Zagorcheva, *supra* note 3.

¹⁴ Mamounas, *supra* note 4, at 383–84.

¹⁵ *Id.* at 384.

Furthermore, the era of globalization cannot be understood through the lens of an economic narrative alone. Rather, a tale of two simultaneous transformations—one economic, the other political—more accurately describes our rapidly-changing world. The free flow of people, ideas, and technologies—the trademark features of globalization—enables stagnant markets to flourish, but also de-stabilizes political institutions.¹⁶ The growing influence of transnational actors is not limited to multinational corporations; it also facilitates global crime syndicates and international terrorists.¹⁷ The tragic events of September 11, 2001 provide a dramatic lesson in the destructive potential of such stateless groups. Yet, the ensuing “Age of Terror” is ultimately couched within the broader meta-narrative of globalization, and thus, is both a subset and a byproduct of the changing landscape of international relations.¹⁸ Such unintended consequences present detrimental challenges to both U.S. leadership and national security.

A. Globalization as a Challenge to American Hegemony

Since the fall of the Soviet Union, the United States has enjoyed sole superpower status.¹⁹ However, one of the more recent, principal storylines within the narrative of globalization has been the meteoric rise of China, both economically and militarily, as a threat to U.S. hegemony. In the face of a lingering recession in the United States, China has continued its strong economic expansion with yearly double-digit GDP growth.²⁰ As the United States’ “unipolar moment” inevitably gives way to a bipolar world marked by China’s ascendancy, some predict a violent transition in the global world order.²¹ Whether China intends for a peaceful rise to superpower status vis-à-vis the United States remains to be seen.

However, one thing is fairly certain: China intends to harness the full scope of economic opportunities within the international marketplace in its quest for regional and global dominance. “The most farsighted Chinese leaders understand that globalization has changed the game and that China accordingly needs strong, prosperous partners around the world.”²² Indeed,

¹⁶ Helton & Zagorcheva, *supra* note 3, at 92–93.

¹⁷ Mamounas, *supra* note 4, at 384.

¹⁸ See generally PHILIP BOBBITT, *TERROR AND CONSENT* (2008).

¹⁹ See Stephen G. Brooks & William C. Wohlforth, *Reshaping the World Order: How Washington Should Reform International Institutions*, FOREIGN AFFAIRS, Mar.–Apr. 2009; G. John Ikenberry, *The Rise of China and the Future of the West: Can the Liberal System Survive*, FOREIGN AFFAIRS, Jan.–Feb. 2008.

²⁰ *Statement for the Record on the Worldwide Threat Assessment of the U.S. Intelligence Community: Hearing Before the H. Permanent Select Comm. on Intelligence*, 112th Cong. 12 (2011) [hereinafter *Intelligence Hearings*] (statement of James R. Clapper, Dir. of Nat’l Intelligence).

²¹ Ikenberry, *supra* note 19, at 26.

²² *Id.* at 30.

the recipe for China's dramatic economic growth features an aggressive combination of an unparalleled supply of cheap labor, increased foreign investment, and its comparative advantage in trade.²³

The remarkable and unprecedented expansion of China's global presence is well-documented. Indeed, three decades of near double-digit economic expansion has provided ample time for the world to take notice.²⁴ While the Soviet Union's policy of militarization as a means of expanding its sphere of influence ultimately proved unsustainable, China has instead focused on harnessing the opportunities of globalization. "China's embrace of foreign investment and trade has helped drive its transformation into a global economic powerhouse."²⁵ Despite China's fairly recent economic liberalization, foreign capital has provided an integral boost to its growth as well. In particular, the inflow of foreign capital has allowed for the transfer of "advanced technology" that has propelled its economy, as well as its "military and intelligence communities and, as a result, national security."²⁶

This sensational economic growth, coupled with China's formidable military prowess, seemingly places it on a collision course with the United States. However, the implications of this growing challenge to U.S. hegemony remain hotly contested.²⁷ Some are hopeful that the United States can accommodate China's rise within the architecture of global, liberal institutions, thereby avoiding a "volcanic struggle" that promises catastrophe in light of their respective military capabilities.²⁸ In fact, U.S. policymakers seemingly agreed with this proposition, given the United States' critical role in paving the way for China's accession into the World Trade Organization (WTO) in 2001.²⁹

However, the past decade of China's involvement in the WTO has generated mixed results, tempering such hopeful projections. On one hand, the United States and China have certainly engaged one another in a deeply entrenched economic relationship. By 2010, "China was the second-largest

²³ *The Chinese Economy*, ECONOMY WATCH, (June 30, 2010), http://www.economywatch.com/world_economy/china/?page=full.

²⁴ U.S.-CHINA ECON. & SEC. REVIEW COMM'N, 111TH CONG., ANN. REP. ON U.S.-CHINA TRADE RELATIONSHIP 17 (Comm. Print 2010).

²⁵ Eric Jensen, *Balancing Security and Growth: Defining National Security Review of Foreign Investment in China*, 19 PAC. RIM. L. & POL'Y J. 161, 164 (2010).

²⁶ *Id.*

²⁷ *See generally* Ikenberry, *supra* note 21.

²⁸ *Id.* at 33–34.

²⁹ WAYNE M. MORRISON, CONG. RESEARCH SERV., RL33536, CHINA-U.S. TRADE ISSUES 24 (2011) ("Many U.S. policymakers at the time maintained that China's WTO membership would encourage the Chinese government to deepen market reforms, promote the rule of law, reduce the government's role in the economy, further integrate China into the world economy, and enable the United States to use the WTO's dispute resolution mechanism to address major trade issues.").

U.S. trading partner (after Canada), the third-largest U.S. export market (after Canada and Mexico), and the largest source of U.S. imports.”³⁰ On the other hand, the trade relationship with China has perpetuated deep-seated asymmetries that threaten U.S. interests. Trade with China has led to a dramatically lop-sided trade deficit,³¹ and China’s aggressive policy of investing in U.S. debt provides political leverage, especially during tough economic times in the United States.³²

B. China as a Threat to U.S. National Security

A more direct threat stems from China’s current FDI policy in advanced economies, such as the United States. Not only do foreign mergers and acquisitions provide a foothold for the parent company’s country in the United States, they enable opportunities for unwanted proliferation of valuable intellectual property to foreign powers.³³ Arguably, “such investment is done largely to transfer technology and know-how to Chinese firms, but do little to help the U.S. economy.”³⁴ This becomes problematic where Chinese multinational companies, some of which are government-sponsored, attempt to acquire American companies that deal with strategic assets or critical infrastructures. This fear played a central role in forcing Lenovo, a company primarily owned by the Chinese government, to restructure its 2004 bid to acquire IBM’s personal computer business.³⁵ “[T]he Departments of Justice and Homeland Security were especially concerned about Chinese infiltration of computer systems.”³⁶ Ultimately, the U.S. government demanded that both companies overcome national security concerns by physically sealing off the buildings that Lenovo and IBM would occupy in a shared complex in North Carolina.³⁷

Alternatively, the presence of Chinese companies in certain markets might directly corrupt manufacturing and distribution processes that cater to U.S. governmental use.³⁸ The notion that domestic products or services could be compromised to enable foreign powers to eavesdrop, copy, or steal

³⁰ *Id.* at 1.

³¹ *Id.* (“The U.S. trade deficit with China has surged over the past two decades, as U.S. imports from China have grown much faster than U.S. exports to China.”).

³² *Id.* at 10–14.

³³ Robert Gray Blacknell, *Trust Not Their Presents, Nor Admit the Horse: Countering the Technically-Based Espionage Threat*, 12 ROGER WILLIAMS U.L. REV. 832, 856 (2007).

³⁴ Morrison, *supra* note 29, at 17.

³⁵ *Id.* at 17–18.

³⁶ Anthony Michael Sabino, *Transactions That Imperil National Security: A Look at the Government’s Power to Say “No”*, N.Y. ST. B.A.J., January 2005, at 20, 22.

³⁷ *Id.*

³⁸ Blacknell, *supra* note 33, at 838–39 (referencing the computer chip, telecommunication, and information systems as U.S. industries that are vulnerable to corruption in the manufacturing phase).

sensitive data or technology is not Hollywood fiction; it is a legitimate threat. For example, the U.S. national security review process recently scuttled Bain Capital's buyout of 3Com because it would have provided the Chinese company Huawei a minority stake in 3Com. "The specific concern was that Huawei would gain access to the equipment maker's technology which is used by the [U.S.] Defense Department."³⁹ Accordingly, investment policies must consider the risk of economic espionage through foreign acquisition of U.S. companies whose products may ultimately affect consumers within the U.S. national security apparatus.⁴⁰

The threat of economic espionage emanating from China is increasingly a concern for U.S. national security interests. While China has focused heavily on economic growth through trade partnerships, its success has translated into a dramatic increase in its power potential relative to other countries. In particular, the United States' lop-sided trade deficit with China endows China with the upper hand in the economic sector, which subsequently provides China financial capital and technical expertise to expand its military capability and political clout.⁴¹

This newfound power potential has shifted Chinese behavior toward its trading partners, as well as its traditional regional foes. The most recent threat assessments from the U.S. intelligence community suggest a growing assertiveness within China's international policies.⁴² China seemingly perceives that its economic success translates into increased clout to pursue its diplomatic and foreign policy objectives.⁴³ For example, in addition to its outright support for North Korea's recent military aggression toward South Korea, China has also advanced its efforts to expand territorial claims in the South China Sea, and has adopted intimidation tactics against Japan over fishing rights near disputed island territories.⁴⁴

³⁹ Steven Gliberman & Daniel Shapiro, *Economic and Strategic Considerations Surrounding Chinese FDI in the United States*, 26 ASIA PAC. J. MGMT. 163, 174 (2009).

⁴⁰ Blacknell, *supra* note 33, at 841 ("Prudent counterespionage policy also requires a failsafe process on the U.S. end of the transaction to verify the efforts of the supplying companies, by assessing risk posed by foreign acquisitions of domestic business organizations and by detecting the existence of technically-based espionage devices or apparatus that slip through the company's processes, in order to manage and apportion risk.").

⁴¹ U.S.-CHINA ECON. & SEC. REVIEW COMM'N, *supra* note 24, at 14.

⁴² *Intelligence Hearings*, *supra* note 20 (statement of James R. Clapper, Dir. of Nat'l Intelligence) ("China's rise drew increased international attention over the past year, as several episodes of assertive Chinese behavior fueled perceptions of Beijing as a more imposing and potentially difficult international actor.").

⁴³ *Id.*

⁴⁴ U.S.-CHINA ECON. & SEC. REVIEW COMM'N, *supra* note 24, at 15 ("China has undermined the progress it had made over the past decade in promoting its peaceful rise with a renewed assertiveness in advancing its sovereignty claims to large areas in the East and South China Seas.").

Moreover, China's increasing aggressiveness has spilled over into its economic policies. China has not concealed its desire to acquire trade secrets, sensitive information, and advanced technology through its investment policy. "[S]ome businesses have publicly declared that they gradually are being squeezed out of Chinese markets by government policies that first demand technology transfer in exchange for market access."⁴⁵ Recently, the chairman of BASF Corporation criticized China's policy of requiring disclosure of intellectual property as a precondition to conduct business in China.⁴⁶ Thus, China's thirst for advanced technology and access to intellectual property from foreign companies is quite apparent.

In addition to its aggressive economic policies, China has allegedly resorted to economic espionage through cyberspace.⁴⁷ The Office of the National Counterintelligence Executive warns that China has been at the forefront of accelerating efforts of "foreign economic collection and industrial espionage activities against major [U.S.] corporations."⁴⁸ The modes of economic espionage vary from the use of corporate insiders to sophisticated online hacking. For example, "China's intelligence services, as well as private companies and other entities, frequently seek to exploit Chinese citizens or persons with family ties to China who can use their insider access to corporate networks to steal trade secrets."⁴⁹ While this Comment will sidestep an in-depth discussion of the threat of cyber espionage, recent high-profile attempts to hack into major U.S. corporations, such as Google, offer significant anecdotal evidence of the rising threat of economic espionage emanating from China.⁵⁰

U.S. intelligence reports corroborate the fears of China's desire to acquire sensitive economic information from U.S. corporations through illicit means. Given this threat, the Federal Bureau of Investigation (FBI) unsurprisingly places counter-intelligence as its number two priority, only behind countering the more direct physical threat of terrorism.⁵¹ While calculating the exact cost of such economic espionage is difficult, the FBI estimates that "every year billions of U.S. dollars are lost to foreign and domestic competitors who deliberately target economic intelligence in

⁴⁵ *Id.* at 20.

⁴⁶ *Id.*

⁴⁷ *Id.* at 15.

⁴⁸ OFFICE OF THE NAT'L COUNTERINTELLIGENCE EXEC., FOREIGN SPIES STEALING US ECONOMIC SECRETS IN CYBERSPACE, 112TH CONG., REP. TO CONG. ON FOREIGN ECON. COLLECTION & INDUS. ESPIONAGE 1 (Comm. Print. 2011).

⁴⁹ *Id.* at 5. This intelligence report also states that "[o]f the seven cases that were adjudicated under the Economic Espionage Act . . . in fiscal year 2010, six involved a link to China." *Id.*

⁵⁰ Morrison, *supra* note 29, at 18.

⁵¹ *Economic Espionage*, *supra* note 2.

flourishing U.S. industries and technologies.”⁵² Yet, the “knowledge of cyber-enabled economic espionage threats to the U.S. private sector remains limited.”⁵³ This reality highlights the importance of vetting foreign mergers and acquisitions into critical U.S. markets that implicate national security. The threat of economic espionage is real, and national security reviews of proposed FDIs are an invaluable tool to curb the potential transfer of American trade secrets and critical technologies.

III. THE AMERICAN APPROACH TO NATIONAL SECURITY

Since World War II, the United States has been at the forefront of promoting economic liberalization in the international system.⁵⁴ The United States has not only invested in various economies around the world, but its own economy has remained one of the key destinations for foreign capital. Accordingly, the United States has “negotiate[d] internationally for reduced restrictions on foreign direct investment, for greater rules on incentives offered to foreign investors, and for equal treatment under law of foreign and domestic investors.”⁵⁵ The United States’ commitment to an open investment policy has arguably served as one of the hallmarks of U.S. diplomatic policy.⁵⁶

Nonetheless, national security considerations have always been recognized as a caveat to any investment policy. Accordingly, “Most governments also have some form of statutory review process for foreign mergers and acquisitions in the domestic economy that look at a myriad of issues, including national security.”⁵⁷ The challenge, however, lies in balancing two oft-competing interests: promoting an economy that is open to foreign investment and protecting national security from foreign threats. The U.S. national security review framework for foreign investment has faced this challenge at every stage of its evolution.

A. Historical Development of the U.S. Model

The need for a national security review process in the United States became apparent in the 1970s as a result of the devaluation of the U.S.

⁵² *Id.*

⁵³ OFFICE OF THE NAT’L COUNTERINTELLIGENCE EXEC., *supra* note 48, at A-1.

⁵⁴ Jonathan C. Stagg, *Scrutinizing Foreign Investment: How Much Congressional Involvement is Too Much?*, 93 IOWA L. REV. 325, 327 (2007).

⁵⁵ JAMES K. JACKSON, CONG. RESEARCH SERV., RL34561, FOREIGN INVESTMENT AND NATIONAL SECURITY: ECONOMIC CONSIDERATIONS 7 (2010).

⁵⁶ Sud, *supra* note 11, at 1314.

⁵⁷ Stephen Sothmann, *Let He Who is Without Sin Cast the First Stone: Foreign Direct Investment and National Security Regulation in China*, 19 IND. INT’L & COMP. L. REV. 203, 205 (2009).

dollar, which led to an influx of FDI.⁵⁸ In response, Congress passed the Foreign Investment Study Act of 1974, which directed the Secretaries of Treasury and Commerce to review all foreign direct and portfolio investments.⁵⁹ That comprehensive review demonstrated that Congress lacked an effective mechanism to examine the potential security implications of FDI. As a result, President Ford established the Committee on Foreign Investment in the United States (CFIUS) in 1975.⁶⁰

The purpose of this body was to observe “the impact of foreign investment in the [United States] . . . and coordinat[e] the implementation of United States Policy on such investment.”⁶¹ Yet initially, “CFIUS’s only power was to monitor investments and request foreign governments to file preliminary reports regarding their foreign investment activities.”⁶² Thus, CFIUS was conceived as a paper tiger with little to no enforcement power of its own.

This glaring limitation surfaced most notably in 1987 with the attempted acquisition of Fairchild Semiconductor Co. by Japanese computer company Fujitsu Ltd. The proposed sale sparked vehement congressional opposition because “officials believed that the deal would give Japan control over a major supplier of computer chips for the military,” thereby “mak[ing] U.S. defense industries more dependent on foreign suppliers for sophisticated high-technology products.”⁶³ Congress felt helpless given CFIUS’s impotency in blocking foreign mergers and acquisitions that might threaten national security. Congress believed 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.”⁶⁴

In response to these growing concerns, Congress passed the Omnibus Trade and Competitiveness Act of 1988, which included the Exon-Florio provision endowing CFIUS with much of its present authority.⁶⁵ Relying on its power to regulate interstate commerce, Congress empowered the President to block proposed foreign mergers, acquisitions, and takeovers

⁵⁸ Joanna Rubin Travalini, *Foreign Direct Investment in the United States: Achieving a Balance Between National Economic Benefits and National Security Interests*, 29 NW. J. INT’L L. & BUS. 779, 783 (2009).

⁵⁹ Foreign Investment Study Act of 1974, Pub. L. No. 93-479, 88 Stat. 1450.

⁶⁰ Travalini, *supra* note 58.

⁶¹ Deborah M. Mostaghel, *Dubai Ports World Under Exon-Florio: A Threat to National Security or a Tempest in a Seaport?*, 70 ALB. L. REV. 583, 589 (2007).

⁶² Travalini, *supra* note 58.

⁶³ JAMES K. JACKSON, CONG. RESEARCH SERV., RL33388, THE COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES (CFIUS) 4 (2009).

⁶⁴ *Id.*

⁶⁵ Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418, § 5021, 102 Stat. 1107, 1425–26 (codified at 50 USC app. § 2170 (2012)).

that “threaten to impair the national security” of the United States.⁶⁶ However, the President could invoke this authority to block proposed FDI only if two conditions were met: first, that no other law could adequately or appropriately protect the national security interest, and second, that credible evidence exists to believe that the proposed foreign investment will actually threaten national security.⁶⁷ Nonetheless, President Reagan issued Executive Order 12661, which delegated his Exon-Florio authority to CFIUS.⁶⁸ This newfound ability to conduct investigations and make presidential recommendations regarding proposed or completed foreign mergers and acquisitions transformed CFIUS from a toothless administrative body into a real consideration for foreign investors.⁶⁹

While CFIUS provides an additional layer of review to guard against potential national security threats, Congress did not intend to undercut its commitment to an open investment policy.⁷⁰ In a liberal economic system, where “private ordering is favored and a trust of market forces is preached to generate the most economically sound outcome,” the persistent challenge is to broker a tenable balance between national security goals and economic interests.⁷¹ Yet, the terrorist attacks of September 11, 2001 raised the stakes, rendering a heightened security environment. Given the transnational composition and sophisticated financing mechanisms of global terrorism, Congress has sought to secure the borders.⁷² In 2003, CFIUS not only created more stringent preconditions for approving foreign acquisitions but also added the Department of Homeland Security (DHS) to its membership.⁷³ Accordingly, the DHS provided a clear national security advocate in the foreign investment review process.

However, two developments in the global market triggered concerns over the sufficiency of the CFIUS process during the late 2000s. First, much like the 1980s, the depreciation of the dollar increased the attractiveness of foreign investment in U.S. markets. Bracing for another wave of FDI, Congress again sought to ensure that CFIUS was up to the task of reviewing proposed foreign mergers in critical industries linked to the U.S. national security apparatus.⁷⁴ Second, the advent of sovereign wealth funds, which are tied to foreign national governments, projected new

⁶⁶ JACKSON, *supra* note 63, at 3.

⁶⁷ *Id.* at 3–4.

⁶⁸ Exec. Order No. 12,661, 54 Fed. Reg. 779 (Dec. 27, 1988).

⁶⁹ JACKSON, *supra* note 63, at 5.

⁷⁰ *Id.*

⁷¹ Sud, *supra* note 11, at 1325.

⁷² Travalini, *supra* note 58, at 787.

⁷³ *Id.*

⁷⁴ George Stephanov Georgiev, *The Reformed CFIUS Regulatory Framework: Mediating Between Continued Openness to Foreign Investment and National Security*, 25 YALE J. ON REG. 125, 130 (2008).

threats to American markets.⁷⁵ Accordingly, the “prototypical new purchasers of major assets . . . are government-controlled Chinese companies and the sovereign investment funds of petrol-rich Gulf states.”⁷⁶

For example, CFIUS became the focal point of criticism following the botched national security review of an attempt by Dubai Ports World, a company owned by the United Arab Emirates (UAE), to acquire several U.S. ports.⁷⁷ In its regular review process, CFIUS actually approved the deal, finding no credible evidence of an actual national security threat.⁷⁸ However, Congress, whose role in the review process was not clearly delineated, rejected CFIUS’s findings regarding the proposed transaction. Opponents of the acquisition feared foreign influence over U.S. port operations given “UAE’s history as an operational and financial base for the hijackers who carried out the September 11, 2001 attack.”⁷⁹ Ultimately, Congress voted to block the transaction, which sparked a new round of concerns regarding the uncertainty of the CFIUS review process and renewed the call for additional legislation that would “clarify the CFIUS’s roles and powers.”⁸⁰

Ultimately, Congress passed the Foreign Investment and National Security Act of 2007 (FINSAs)⁸¹ in order to address growing uncertainty that followed Congress’s decision to block the Dubai Ports World deal after CFIUS had already approved it. In order to avoid post-CFIUS interventions in the future, Congress expanded its oversight role in the review process.⁸² Also, FINSAs provided statutory grounding for CFIUS, which previously had relied solely on authority flowing from President Ford’s Executive Order in 1975. By imposing heightened congressional reporting requirements on CFIUS, the new law attempts to increase transparency in the process by ensuring investors that each deal is thoroughly reviewed for national security implications prior to approval.⁸³ Concurrently, FINSAs establishes additional factors that CFIUS may consider in evaluating a proposed transaction’s impact on national security.⁸⁴ Finally, FINSAs formalizes the role of the intelligence agencies in the review process.⁸⁵

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ Travalini, *supra* note 58, at 789–90.

⁷⁸ Georgiev, *supra* note 74, at 131.

⁷⁹ Mostaghel, *supra* note 61, at 606.

⁸⁰ Travalini, *supra* note 58, at 790.

⁸¹ Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246.

⁸² JACKSON, *supra* note 63, at 1.

⁸³ Travalini, *supra* note 58, at 793.

⁸⁴ Georgiev, *supra* note 74, at 133. For a more detailed discussion of the additional factors for consideration in the CFIUS review process, see *infra* Part III(B).

⁸⁵ *Id.* See *infra* Part III.B for a list of U.S. intelligence agencies that participate in the

Thus, FINSA attempts to strike an appropriate balance between protecting U.S. national security interests and promoting FDI in U.S. markets.⁸⁶

B. Key Features of the U.S. Model

In addition to the legislative expansion of its investigative and advisory powers, CFIUS has also undergone structural transformations since its inception in 1975.⁸⁷ In its current form, the Secretary of Treasury serves as the chairperson for the review body, which spans sixteen governmental departments and offices.⁸⁸ As membership in CFIUS has expanded over the years, the Departments of Treasury, Commerce, Justice, and Homeland Security have continued to play the most active roles.⁸⁹ Unsurprisingly, the Department of Defense has also played an influential role in CFIUS's national security assessments of foreign investment deals.⁹⁰

Procedurally, only "covered transactions" are subject to CFIUS review, though parties to a proposed foreign investment will usually provide voluntary notice to CFIUS along with necessary information related to the deal if it likely implicates national security.⁹¹ Under CFIUS regulations, "covered transactions" are defined as "any merger, acquisition, or takeover which results in 'foreign control of any person engaged in interstate commerce in the United States.'"⁹² The Exon-Florio provision permits members of CFIUS to independently trigger a review of a proposed covered transaction.⁹³ However, most filings are voluntary, because parties to a foreign investment scheme understand that a failure to provide notice to CFIUS may later subject the transaction to indefinite Executive review.⁹⁴

CFIUS review process.

⁸⁶ *Id.* at 131.

⁸⁷ Mamounas, *supra* note 4, at 391.

⁸⁸ *Composition of CFIUS*, U.S. DEPT. OF THE TREASURY, <http://www.treasury.gov/resource-center/international/foreign-investment/Pages/cfius-members.aspx> (last visited Nov. 30, 2012). The website lists the following members of CFIUS: Department of Treasury, Department of Justice, Department of Homeland Security, Department of Commerce, Department of Defense, Department of State, Department of Energy, Office of the U.S. Trade Representative, Office of Science & Technology Policy. The Director of National Intelligence and the Secretary of Labor are non-voting *ex-officio* members. In addition, the following offices are observer members: Office of Management & Budget, Council of Economic Advisors, National Security Council, National Economic Council, Homeland Security Council. *Id.*

⁸⁹ Travalini, *supra* note 58, at 783.

⁹⁰ *Id.* at 784.

⁹¹ Ilene Knable Gotts et al., *Is Your Cross-Border Deal the Next National Security Lightning Rod?*, *BUS. L. TODAY*, July–Aug. 2007, at 33.

⁹² JACKSON, *supra* note 63, at 9.

⁹³ Gotts et al., *supra* note 91.

⁹⁴ Sud, *supra* note 11, at 1316 (citing Department of the Treasury, Deputy Secretary Robert M. Kimmitt Testimony Before the United States Senate Committee Banking,

Following a proper filing, the Staff Chairperson will circulate the portfolio to CFIUS members for a maximum thirty-day review.

If CFIUS harbors concerns that a proposed transaction might affect national security interests within that initial thirty-day review, then it must conduct a secondary forty-five-day investigation to clear the deal or recommend it for suspension or rejection.⁹⁵ During this heightened stage, the President, *vis-à-vis* CFIUS, must conduct a national security investigation if one of the following three conditions is present:

- (1) as a result of a review of the transaction, CFIUS determines that the transactions threaten to impair the national security of the United States and that the threat had not been mitigated during or prior to a review of the transaction;
- (2) the foreign person is controlled by a foreign government; or
- (3) the transactions would result in the control of any critical infrastructure by a foreign person, the transactions could impair the national security, and that such impairment had not been mitigated.⁹⁶

At any point during the review process, parties are entitled to voluntarily withdraw from the review by nixing the deal, though they are subject to continuing notification requirements if the parties decide to re-file or pursue the transaction at a later date.⁹⁷

During the forty-five-day investigation, three outcomes are possible. First, CFIUS may clear the deal if it finds no national security threat.⁹⁸ On the other hand, if CFIUS does find a valid threat, it could still clear the deal if another law can address the concern.⁹⁹ Second, if CFIUS does find a national security threat, then it may work with the parties to the transaction to modify its terms to mitigate the national security concerns.¹⁰⁰ Finally, CFIUS may file a non-binding recommendation to the President to suspend or reject the proposed transaction.¹⁰¹

Once a recommendation is made to the President, he or she will have fifteen days to render a final decision as to the viability of the foreign investment.¹⁰² Where a transaction has already been completed prior to the

Housing, and Urban Affairs (Oct. 20, 2005)).

⁹⁵ *Id.*

⁹⁶ JACKSON, *supra* note 63, at 12 (bracketed numbers in original).

⁹⁷ *Process Overview*, U.S. DEPT. OF THE TREASURY, <http://www.treasury.gov/resource-center/international/foreign-investment/Pages/cfius-members.aspx> (last visited Dec. 26, 2012).

⁹⁸ *Id.*

⁹⁹ *Id.*

¹⁰⁰ Gotts et al., *supra* note 91, at 33.

¹⁰¹ *Id.*

¹⁰² Sud, *supra* note 11, at 1317.

national security review, the President has the power to compel divestiture.¹⁰³ However, in order to provide certainty to investors, the President may not prohibit a transaction if CFIUS had previously provided written notice to the parties that the transaction was not subject to the Exon-Florio provision, or affirmatively chose to forego review altogether, or the President had chosen to forego intervention for the same transaction.¹⁰⁴

The Exon-Florio provision originally established five factors for the President, as well as individual members of CFIUS, to consider during national security reviews of proposed foreign mergers, acquisitions, or takeovers.¹⁰⁵ In 2007, Congress added seven factors for consideration during the review process.¹⁰⁶ The amended Exon-Florio factors range from the proposed foreign investment's impact on production capacity to meet national defense requirements to its effect on energy security, strategic assets, critical infrastructure, or even U.S. "technological leadership in areas affecting U.S. national security."¹⁰⁷ Consequently, opponents of the

¹⁰³ Travalini, *supra* note 58, at 784.

¹⁰⁴ Sud, *supra* note 11, at 1317.

¹⁰⁵ Defense Production Act of 1950, Pub. L. No. 100-418 § 502, 50 USC App. § 2170 (1988).

¹⁰⁶ JACKSON, *supra* note 63, at 12–13.

¹⁰⁷ *Id.* For a comprehensive list, the amended Exon-Florio factors are:

- (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 transactions identified by the Secretary of Defense as "posing a regional military threat" to the interests of the United States;
- (5) the potential effects of the transaction on U.S. technological leadership in areas affecting U.S. national security;
- (6) whether the transaction has a security-related impact on critical infrastructure in the United States;
- (7) the potential effects on United States critical infrastructure, including major energy assets;
- (8) the potential effects on United States critical technologies;
- (9) whether the transaction is a foreign government-controlled transaction;
- (10) in those cases involving a government-controlled transaction, a review of (A) the adherence of the foreign country to nonproliferation control regimes, (B) the foreign country's record on cooperating in counter-terrorism efforts, (C) the potential for transshipment or diversion of technologies with military applications;
- (11) the long-term projection of the United States requirements for sources of energy and other critical resources and materials; and

national security review process are concerned that these amended factors subject foreign investment transactions to greater hurdles in the approval process.

Admittedly, CFIUS has evolved into a more intensive review body with greater powers to block proposed foreign investments. Most notably, the amendments broaden the scope of CFIUS review by including a host of other economic security considerations in addition to the former, more traditional national defense interests.¹⁰⁸ In particular, the focus on “critical infrastructure,” as defined broadly in the statute, enables the President to consider a proposed transaction’s effect beyond national security, including “national economic security and national public health or safety.”¹⁰⁹ Finally, the lack of a specific, limited definition of “national security” arguably subjects sound economic investments to an arbitrary and capricious review process.¹¹⁰ Part V of this Comment, however, demonstrates that these economic concerns are either overblown or outweighed by other concerns.

IV. THE CHINESE APPROACH: CFIUS’S COUNTERPART

While the United States’ approach to reviewing foreign investments for national security concerns has evolved for nearly four decades, China’s framework is in its nascent stages. Given that China’s new model came into existence in the wake of several failed acquisitions of U.S. companies in the United States, some fear that the model is reactionary in motive. However, China’s national security review process can also be seen as the next logical step in the continued liberalization of its economy. This portion of the Comment analyzes the historical buildup to China’s adoption of a formal national security review process for foreign mergers and acquisitions, as well as key features of the model.

A. Historical Development of the Chinese Model

Unlike the United States, the historical record for Chinese FDI policies is relatively short. In fact, prior to 1983, China prohibited foreign acquisitions of Chinese businesses altogether.¹¹¹ Since then, however, the world has witnessed an “ongoing transition of [China]’s economy from a centrally planned one to a ‘market economy with socialist

(12) such other factors as the President or the Committee determine to be appropriate.

Id.

¹⁰⁸ *Id.*

¹⁰⁹ *Id.* at 13.

¹¹⁰ See *infra* Part V.

¹¹¹ Destiny Duron Deas, Note, *The Costs of Perceived Hypocrisy: The Impact of U.S. Treatment of Foreign Acquisitions of Domestic Enterprises*, 57 DUKE L.J. 1795, 1803 (2008).

characteristics.”¹¹² As its economy has liberalized, China has become more favorable to foreign investment and capital. In the decades spanning 1983 to 2003, however, the Chinese government lacked a standardized framework for evaluating foreign mergers and acquisitions.¹¹³ Following a contentious failed acquisition in 2006 of Xugong Construction Machinery Group—China’s largest construction machinery manufacturer—by the American-based management firm Carlyle Group,¹¹⁴ China’s Ministry of Commerce adopted a revised set of regulations concerning foreign mergers and acquisitions in China.¹¹⁵

Despite these newly adopted rules, China did not formally provide for a national security review process for foreign mergers and acquisitions until 2007, when it adopted a long-awaited, comprehensive antitrust law.¹¹⁶ Within that legislation, Article 31 formally envisions concurrent national security review of foreign investment, along with the primary antitrust review.¹¹⁷ Even then, China still lacked a formalized national security framework, such as CFIUS, until the United States blocked a controversial merger between Huawei and 3Leaf in 2010.¹¹⁸

Finally, on February 3, 2011, China’s State Council General Office issued the Notice Concerning Establishment of the Security Review System on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (Security Review Notice).¹¹⁹ The Security Review Notice establishes the Chinese counterpart to CFIUS—a national security review process for foreign mergers and acquisitions in Chinese markets.¹²⁰ After a six-month trial period, China’s Ministry of Commerce (MOFCOM) issued the Regulation on Implementing of the Security Review System for Mergers

¹¹² H. STEPHEN HARRIS JR. ET AL., *ANTI-MONOPOLY LAW AND PRACTICE IN CHINA* 1 (2011) (citation omitted).

¹¹³ Deas, *supra* note 111, at 1804.

¹¹⁴ *Id.*

¹¹⁵ Kenneth Y. Hui, *National Security Review of Foreign Mergers and Acquisitions of Domestic Companies in China and the United States*, 5 Cornell Law School Inter-University Graduate Student Conference Papers, Paper 34 (2009), available at http://scholarship.law.cornell.edu/lps_clacp/34.

¹¹⁶ Sothmann, *supra* note 57, at 203.

¹¹⁷ *Id.* at 204 (citing Article 31, which states: “Where a foreign investor participates in the concentration of business operators by merging or acquiring a domestic enterprise or by any other means, and national security is involved, besides the examination on the concentration of business operators in accordance with the Law, the examination on national security shall also be conducted according to the relevant provisions of the State”).

¹¹⁸ *See infra* Part V.

¹¹⁹ Ross & Zhou, *supra* note 12.

¹²⁰ Henry L. T. Chen & Frank Schoneveld, *China Formalizes National Security Review System for M&A Transactions by Foreign Investors*, NAT’L L. REV. (Sept. 22, 2011), <http://www.natlawreview.com/article/china-formalises-national-security-review-system-ma-transactions-foreign-investors>.

and Acquisitions of Domestic Enterprises by Foreign Investors.¹²¹

The motive behind China's decision to pursue a formal national security review process remains hotly contested. Arguably, the temporal proximity of the Security Review Notice to the adverse CFIUS review of the Huawei-3Leaf transaction suggests protectionist backlash. On the other hand, China's new review process for incoming foreign investments was inevitable in light of its mention in Article 31 of China's antitrust law. Regardless of the reason, the international business community has witnessed the rise of dueling national security review frameworks in the United States and China—the world's top two recipients of FDI.¹²²

B. Key Features of the Chinese Model

Similar to CFIUS's broad membership across governmental departments, China's national security review process involves an inter-ministerial approach.¹²³ China's review body is referred to as the Joint Inter-Ministerial Security Review Committee.¹²⁴ At the helm, the National Development and Reform Commission (NRDC) and MOFCOM serve as the leadership for the national security review process under the Chinese model.¹²⁵ Similar to FINSA's effect on CFIUS, the new national security review legislation grounds the NRDC's role with statutory authority, unlike previously, where it served as an informal consultant to the review of mergers and acquisitions for antitrust violations.¹²⁶

Unlike the CFIUS framework, however, China's new national security review process mandates investors to file applications with MOFCOM in order to initiate review of proposed transactions.¹²⁷ The Chinese model's equivalent of a covered transaction is defined as a foreign merger or acquisition involving any one of the following:

- [1] A foreign investor purchases the equity interests of a Chinese enterprise or subscribes to the increased capital of a Chinese enterprise[;]
- [2] A foreign investor purchases the equity interests of a Chinese shareholder of a foreign-invested enterprise (FIE) in China or subscribes to the increased capital of an FIE[;]
- [3] A foreign investor sets up an FIE and uses it to purchase and

¹²¹ *Id.*

¹²² *FDI by Country*, GREYHILL ADVISORS, <http://greyhill.com/fdi-by-country/> (last visited Dec. 28, 2012). In 2011, the United States received the most foreign investment, totaling \$236.2 billion, while China received the second most with \$185.1 billion. *Id.*

¹²³ *Id.* at 3.

¹²⁴ Ross & Zhou, *supra* note 12.

¹²⁵ *Id.*

¹²⁶ *Id.*

¹²⁷ Chen & Schoneveld, *supra* note 120, at 2.

operate the assets of a Chinese enterprise, or uses the FIE to purchase the equity interests of a Chinese enterprise[;]

[4] A foreign investor directly purchases the assets of a Chinese enterprise, and sets up an FIE in use of the assets, which then operates on the assets[.]¹²⁸

In addition to the Chinese review process's coverage of direct mergers and acquisitions, the framework also exercises jurisdiction over transactions that would lead to de facto control of Chinese entities through foreign investment. This includes:

(1) direct or indirect acquisition by a foreign investor of 50% or more of the shares in a domestic enterprise; (2) acquisition by a group of foreign investors of 50% or more of the shares in a domestic enterprise; (3) acquisition of material influence over decisions of the shareholders meeting or board of directors even with less than 50% of the shares; or (4) acquisition of actual control over a domestic enterprise's policies, finances, personnel or technology. The application to acquisition of actual control signifies that the Security Regulations, like the AML, can reach offshore transactions.¹²⁹

Foreign investors that fall within the ambit of these investment categories are required to file an application with MOFCOM to determine whether further review is required.¹³⁰ Similar to the CFIUS model, China's Security Review Committee is also empowered to independently open national security investigations into proposed foreign investment transactions.¹³¹ Unlike the U.S. framework, however, "other government ministries, national trade associations, other companies in the industry and domestic enterprises can also ask MOFCOM to initiate an investigation."¹³² Thus, the Chinese model offers far greater avenues and opportunities to scrutinize foreign mergers and acquisitions through the national security review process.

Unlike the initial month-long investigation under CFIUS, once MOFCOM initiates the review process, it will conduct a general review lasting no longer than twenty days, during which the Security Review Committee will "solicit written opinions from the relevant authorities."¹³³ Similar to the initial stage under CFIUS, this review enables MOFCOM to clear a transaction where there is no evidence of an adverse national

¹²⁸ *Id.* at 1–2 (bracketed numbers, semi-colons, and period added).

¹²⁹ Ross & Zhou, *supra* note 12.

¹³⁰ Chen & Schoneveld, *supra* note 120, at 3.

¹³¹ Ross & Zhou, *supra* note 12.

¹³² *Id.*

¹³³ Chen & Schoneveld, *supra* note 120, at 3.

security impact stemming from the proposed transaction. However, if the proposed transaction does raise national security concerns, the Security Review Committee will conduct a heightened, secondary review process that lasts no longer than sixty days.¹³⁴ Similar to the American approach under CFIUS, parties to a proposed transaction are free to withdraw their application for review at any time during the heightened security review.¹³⁵

At the conclusion of the secondary review stage, the Security Review Committee can render three potential recommendations to MOFCOM: (1) approve the transaction, (2) block the transaction, or (3) like the American approach under FINSA, allow the transaction to proceed subject to remedial preconditions.¹³⁶ These recommendations, however, are non-binding, and unlike the U.S. model where the President makes the final determination, MOFCOM has the authority to take its own action, including the option to divest the transaction.¹³⁷

Similar to the CFIUS framework and its implementing regulations, the rules set forth in China's 2011 legislation establishes various factors for consideration during its national security review process. These factors include:

- [1] Influence of the M&A transaction over national [defense] (including capacity of manufacturing domestic products, providing domestic services or providing the facilities and equipments in question for national [defense]);]
- [2] Influence of the M&A transaction over the stable running of China's economy[;]
- [3] Influence of the M&A transaction over basic social life and order[;]
- [4] Influence of the M&A transaction over research and development of key technology regarding national security[.]¹³⁸

Interestingly, the scope of review under the Chinese model is much broader than the U.S. model. While the factors for consideration under CFIUS also extend beyond national defense interests, the Chinese model purportedly covers "transactions involving important agricultural products, energy and resources, infrastructure facilities, and transportation services[,] core technologies[,] and important equipment manufacturing enterprises."¹³⁹ While both models raise hurdles for proposed transactions, the Chinese national security review framework seemingly could cover

¹³⁴ *Id.*

¹³⁵ Ross & Zhou, *supra* note 12.

¹³⁶ *Id.*

¹³⁷ Chen & Schoneveld, *supra* note 120, at 2.

¹³⁸ *Id.* (bracketed numbers, semi-colons, and period added).

¹³⁹ Ross & Zhou, *supra* note 12.

transactions that have almost no nexus with national security.¹⁴⁰ Thus, China's national security review model enjoys a broader scope of review than its U.S. counterpart.¹⁴¹

V. CFIUS IN ACTION: A RESPONSE TO CRITICISM

While the immediate impact of China's new model for reviewing foreign mergers and acquisitions remains to be seen, its creation has reinvigorated critics of national security reviews. Their concerns revolve around issues of general transparency,¹⁴² ambiguous scope,¹⁴³ potential backlash from perceived protectionism,¹⁴⁴ and the politicization of economics.¹⁴⁵ The common thread linking the diverse critiques of national security reviews of foreign investment is a general uneasiness over Congress's perceived interference in free trade and economics. However, it is common knowledge that the U.S. Constitution secures the role of Congress in regulating interstate commerce.¹⁴⁶ The more relevant question is whether Congress's regulation of foreign mergers and acquisitions vis-à-vis CFIUS is sufficiently transparent to minimize the chilling effect on economic relations. By this measure, CFIUS has admittedly rendered mixed results in the past, thereby validating—at least in part—the above-mentioned criticisms.

This portion of the Comment addresses past arbitrary congressional action involving CFIUS reviews of proposed Chinese acquisitions of U.S. companies. This Part argues that legislative amendments to CFIUS have since addressed concerns of transparency, ambiguity, and politicization of trade. Various case studies demonstrate that a changing national security landscape, as well as an evolving national security review process, negates or outweighs the proposed costs of CFIUS and its Chinese counterpart.

A. Ensuring Transparency

Perhaps the most controversial transaction that fell victim to national security concerns in the United States involves China National Offshore Oil Corporation (CNOOC) and its attempted takeover of California-based

¹⁴⁰ *Id.*

¹⁴¹ *Id.* (“The Security Review Committee has substantive authority under the Security Regulations, including analysis of the impact of foreign M&A on national defense, study and coordination of key issues identified during the security review, examination of foreign M&A and in some instances ultimate decision-making power.”).

¹⁴² See generally Mamounas, *supra* note 4.

¹⁴³ JACKSON, *supra* note 55, at 18.

¹⁴⁴ See generally Deas, *supra* note 111.

¹⁴⁵ Stagg, *supra* note 54, at 329.

¹⁴⁶ U.S. CONST. art. I, § 8, cl. 3 (“Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.”).

energy firm Unocal in 2005.¹⁴⁷ Amidst negotiations by Chevron—an American multinational energy corporation—to purchase Unocal, CNOOC interjected with an unsolicited \$18.5 billion takeover bid that topped Chevron’s offer by nearly \$2 billion.¹⁴⁸ The very next day, forty-one members of Congress requested immediate CFIUS review of the proposed Chinese takeover as a matter of U.S. national security.¹⁴⁹ Within a week, Congress overwhelmingly passed House Resolution 344, formally voicing its concerns over the proposed acquisition.¹⁵⁰ As a sign of good faith, CNOOC voluntarily requested that CFIUS analyze the transaction for potential national security complications.¹⁵¹ Yet, the intense scrutiny rendered the proposed Chinese takeover dead on arrival—CNOOC ultimately withdrew its bid to acquire Unocal in the face of insurmountable congressional pushback.¹⁵²

The CNOOC-Unocal fiasco has justifiably served as the poster child for the purported lack of transparency in the U.S. national security review process. In many ways, CNOOC’s failed attempt to acquire UNOCAL demonstrates Congress’s perception of CFIUS as a weak review body prior to the passage of FINSA in 2007. Indeed, CNOOC ultimately withdrew its bid in the face of strong legislative opposition to the proposed merger, rather than formal negative treatment by CFIUS. In its press release following the withdrawal, CNOOC blamed “unprecedented political opposition” from Congress that ultimately created a “level of uncertainty that present[ed] an unacceptable risk” to completing the merger.¹⁵³ Still, it is unlikely that CNOOC would have secured approval from the President even if CFIUS had the opportunity to review the transaction for potential national security concerns.¹⁵⁴

It is important to note that Congress’s staunch opposition to the CNOOC-Unocal transaction—though controversial—was justified. Indeed, Congress expressed a variety of national security concerns surrounding a

¹⁴⁷ Ben White, *Chinese Drop Bid to Buy U.S. Oil Firm*, WASH. POST, Aug. 3, 2005, available at <http://www.washingtonpost.com/wp-dyn/content/article/2005/08/02/AR2005080200404.html>.

¹⁴⁸ Michael Petrusic, *Oil and the National Security: CNOOC’s Failed Bid to Purchase Unocal*, 84 N.C. L. REV. 1373, 1374 (2006).

¹⁴⁹ Travalini, *supra* note 58, at 788.

¹⁵⁰ For bill status and summary, see H.R. Doc. No. H5592 (2005) (indicating passage of the resolution without amendment by a vote of 398 to 15 and 20 abstaining). See also Mamounas, *supra* note 4, at 404.

¹⁵¹ Sud, *supra* note 11, at 1305.

¹⁵² *Id.* at 1306.

¹⁵³ Press Release, CNOOC Ltd., CNOOC Limited to Withdraw UNOCAL Bid (Aug. 2, 2005), available at <http://www.cnooltd.com/encnooltd/newszx/news/2005/961.shtml>.

¹⁵⁴ Petrusic, *supra* note 148, at 1375.

potential CNOOC-Unocal merger in House Resolution 344.¹⁵⁵ While the proposed merger fell apart prior to formal CFIUS review, the objections offered in the Resolution provide insight into the likely outcome had the proposed deal reached the formal national security review process.

Arguably, Congress's fundamental concern with the merger—as House Resolution 344 indicates—stemmed from CNOOC's corporate structure and identity: “China owns approximately 70 percent of CNOOC.”¹⁵⁶ In addition to CNOOC's significant ties to the Chinese government, the proposed merger would have been “financed and heavily subsidized” by state-owned banking institutions.¹⁵⁷ In a parallel investigation of the proposed transaction, the House Armed Services Committee expounded on this concern: “Chinese enterprises do not behave as normal commercial companies on the international market.”¹⁵⁸ Unlike purely private foreign investment, the CNOOC-Unocal transaction would have effectively injected a foreign power into the U.S. economy.

Second, the Resolution voices national security concerns arising from CNOOC's potential control over oil and natural gas resources, which are paramount strategic assets.¹⁵⁹ Citing China's increasingly voracious appetite for oil, the Resolution emphasized the strategic importance of maintaining U.S. control over its own energy resources.¹⁶⁰ The proposed merger, on the other hand, “would result in [Unocal's] strategic assets . . . being preferentially allocated to China by the Chinese government.”¹⁶¹ As a result, the Resolution found that CNOOC would directly control nearly one-third of excess oil supply in the world.¹⁶² Moreover, the House Armed Services Committee found that Unocal's oil reserves spanned the globe “from the Gulf of Mexico to the Caspian region to Southeast Asia, as well as in Africa, Europe, and South America.”¹⁶³ Thus, China's acquisition of Unocal's strategic assets vis-à-vis CNOOC would present a zero-sum

¹⁵⁵ H.R. Res. 344, 109th Cong., 151 CONG. REC. H5570 (2005).

¹⁵⁶ *Id.*

¹⁵⁷ *Id.*

¹⁵⁸ *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. 2 (2005) [hereinafter *Merger Hearings*] (statement of Duncan Hunter, Chairman, House Armed Services Committee) (“[I]t's not a normal commercial exchange when one of the parties to a deal is owned and operated by a totalitarian communist government that does not answer to the rules of the market . . .”).

¹⁵⁹ Mamounas, *supra* note 4, at 404.

¹⁶⁰ H.R. Res. 344.

¹⁶¹ *Id.*

¹⁶² Mamounas, *supra* note 4, at 405.

¹⁶³ *Merger Hearings*, *supra* note 158 (statement of Hon. C. Richard D'Amato, Chairman, U.S.-China Economic and Security Review Commission on House Armed Services).

reduction of U.S. influence in those regional oil markets.¹⁶⁴

Finally, the Resolution forewarned of the potential proliferation of sensitive dual-use technologies¹⁶⁵ employed in the oil industry for exploration, production, and refining.¹⁶⁶ “The dangerous possibility of these dual commercial/military use technologies falling into Chinese hands is alarming given the tenuous nature of Sino-American relations.”¹⁶⁷ Coupled with China’s unconcealed desire to acquire advanced technology through FDIs,¹⁶⁸ its oil companies, like CNOOC, operate in countries currently facing U.S. economic and military sanctions.¹⁶⁹ The risk of secondary proliferation of these sensitive, dual-use technologies to adverse countries, such as Iran, would also threaten U.S. national security.¹⁷⁰

Nevertheless, the failure of the formal national security process to take effect in the proposed CNOOC-Unocal acquisition feeds the perception that Congress may obstruct viable transactions in an arbitrary and capricious manner. Admittedly, “without thorough statutory review, the case-by-case approach in each transaction provides little regularity and poor transparency.”¹⁷¹ Despite CNOOC’s late attempt to voluntarily submit information about the proposed transaction to CFIUS, “congressional leaders haphazardly held press conferences, gave interviews, and introduced legislation, the product of which was a political snowball against which CNOOC . . . had no hope.”¹⁷² The lack of clear, identifiable criteria within the national security review process will stoke future criticism of CFIUS as a non-transparent, unbridled oversight body.¹⁷³

Fortunately, CFIUS has undergone various transformative changes since the CNOOC-Unocal debacle.¹⁷⁴ In 2007, Congress approved FINSA, which made several critical changes to the preexisting iteration of CFIUS, primarily to ensure a more transparent national security review process.¹⁷⁵ For example, FINSA now mandates initial review of all covered transaction, which “ensur[es] that every transaction involving foreign

¹⁶⁴ Mamounas, *supra* note 4, at 408.

¹⁶⁵ H.R. Res. 344 (referencing examples of sensitive technologies, including “seismic analysis and processing downhole logging sensors, and modeling software”).

¹⁶⁶ Petrusic, *supra* note 148, at 1379.

¹⁶⁷ Mamounas, *supra* note 4, at 405.

¹⁶⁸ U.S.-CHINA ECON. & SEC. REVIEW COMM’N, *supra* note 24, at 20.

¹⁶⁹ Mamounas, *supra* note 4, at 405.

¹⁷⁰ *Id.*

¹⁷¹ *Id.* at 412.

¹⁷² *Id.*

¹⁷³ *Id.* at 413.

¹⁷⁴ For a detailed discussion on the legislative evolution of the U.S. national security review process for foreign mergers and acquisitions, see *infra* Part III.A.

¹⁷⁵ Jensen, *supra* note 25, at 173.

investment receives attention from the CFIUS.”¹⁷⁶ Thus, parties to a proposed foreign merger, acquisition, or takeover can expect to provide preliminary information about the deal regardless of whether CFIUS initiates the review or the parties themselves voluntarily seek government approval.

Additionally, FINSA serves to provide parties to a covered transaction with common risk factors that have implicated U.S. national security in the past.¹⁷⁷ For instance, CFIUS is now required to “issue guidance on the types of transactions previously reviewed that presented national security and critical infrastructure concerns.”¹⁷⁸ Also, “Implementing regulations finalized in 2008 provide many illustrative examples to show what level of corporate control is sufficient to trigger CFIUS review.”¹⁷⁹ Prior to the passage of FINSA, foreign corporations like CNOOC lacked notice of thresholds for transactional risk that could trigger CFIUS review.

Furthermore, FINSA introduces specific reporting requirements for CFIUS in an effort to limit broader congressional intervention in the national security review process. Prior to FINSA, “The Exon-Florio amendment required quadrennial reports to Congress, yet after an initial report in 1993 no such reports were submitted for the next dozen years.”¹⁸⁰ Following passage of FINSA, CFIUS must now submit an annual report to Congress that “summarize[s] trends and the previous year’s activity.”¹⁸¹ For pending transactions under review, FINSA also mandates that CFIUS provide notice and certification of its findings during the forty-five-day, secondary review phase for a specified transaction.¹⁸² These amended requirements increase the transparency of the CFIUS review process, define Congress’s role in national security reviews of foreign investment, and deter premature, capricious governmental intervention.¹⁸³

In retrospect, critics of CFIUS are admittedly correct to point out the review body’s checkered history of operational transparency. The botched CNOOC-Unocal merger certainly fanned the fears of an arbitrary national

¹⁷⁶ Travalini, *supra* note 58, at 794.

¹⁷⁷ *Id.*

¹⁷⁸ Michael J. O’Neil, *Did You Expect Less Scrutiny? After Dubai Ports World, Congress Broadens Review of Foreign Investment*, LEGAL TIMES, Sept. 17, 2007, at 41.

¹⁷⁹ Matthew C. Sullivan, *CFIUS and Congress Reconsidered: Fire Alarms, Police Patrols and a New Oversight Regime*, 17 WILLAMETTE J. INT’L L. & DISP. RESOL. 199, 237 (2009).

¹⁸⁰ *Id.* at 234.

¹⁸¹ *Id.* These reports must detail “all CFIUS reviews and investigations, including information on the types of transactions approved, statistics on the number of withdrawals, and information on the effects of monitoring arrangements designed to mitigate national security concerns.” Travalini, *supra* note 58, at 794.

¹⁸² Sullivan, *supra* note 179, at 235.

¹⁸³ *Id.* at 234–37.

security review process that left foreign investors uncertain about future transactions. Congress has since legislated improvements to CFIUS in an effort to increase transparency and to clarify congressional involvement in these national security reviews. Indeed, the CNOOC-Unocal controversy is a reminder of the importance of such measures, which serve to render a more predictable review process where the transaction does in fact implicate U.S. national security interests.

B. Defining National Security

Since CNOOC withdrew its bid to acquire Unocal, two other failed foreign acquisitions involving Chinese corporations have fueled criticism of CFIUS's scope. In particular, Congress has failed to establish a "functional definition of the national economic security implications of foreign direct investment."¹⁸⁴ This lack of a clear statutory definition of the term "national security" raises fears of far-reaching reviews.¹⁸⁵ As a result, critics contend that heightened congressional involvement will lead to the politicization of foreign investment.¹⁸⁶

However, this fear of congressional over-involvement overlooks the historical foundation of U.S. economics, as well as the current realities of global threats.¹⁸⁷ In response to the heightened security environment following the September 11, 2001 terrorist attacks,¹⁸⁸ Congress broadened the scope of national security considerations through the passage the USA PATRIOT Act of 2001, which added "critical infrastructure" as part of the nation's security apparatus.¹⁸⁹ In light of this shift in congressional attitude, "policymakers have concluded that economic activities are a separately identifiable component of national security."¹⁹⁰ Thus, a broader approach to CFIUS review of foreign investment is *necessary* to address modern

¹⁸⁴ JACKSON, *supra* note 55, at 19 (discussing the lack of precise definitions for various terms in the Summary).

¹⁸⁵ Georgiev, *supra* note 74, at 133.

¹⁸⁶ Stagg, *supra* note 54, at 355.

¹⁸⁷ See FRANK BOURGIN, *THE GREAT CHALLENGE: THE MYTH OF LAISSEZ-FAIRE IN THE EARLY REPUBLIC* (1989) (arguing that the Founders intended for direct governmental participation in the U.S. economy).

¹⁸⁸ JACKSON, *supra* note 55, at 14.

¹⁸⁹ See USA PATRIOT ACT of 2001, Pub. L. No. 107-56, § 1016, 115 Stat. 272, 400-02 (2001) (codified at 42 U.S.C. § 5195c (2012)). Within the USA PATRIOT Act, "critical infrastructure" is defined as "systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems and assets would have a debilitating impact on security, national economic security, national public health or safety, or any combination of those matters." USA PATRIOT ACT § 1016(e) (codified at 42 U.S.C. § 5195c(e)).

¹⁹⁰ JACKSON, *supra* note 55, at 14.

threats of economic espionage.¹⁹¹

In fact, Congress intentionally declined to provide a more limited definition of “national security” within the Exon-Florio statute.¹⁹² Instead, Congress envisioned a flexible interpretation of the term in order to cut across various critical industries.¹⁹³ While this approach does invite some unpredictability, the Department of Treasury states that “each member of CFIUS is expected to apply that definition of national security that is consistent with the representative agency’s specific legislative mandate.”¹⁹⁴ Congress also added several factors to consider in evaluating national security implications of FDI, in particular, the proposed transaction’s impact on “critical infrastructure” in the United States.¹⁹⁵

Critics ultimately fear that such a broad definition of national security enables Congress to politicize foreign investment by disfavoring countries, such as China, that might represent a threat to U.S. economic hegemony.¹⁹⁶ Admittedly, this concern arises each time a political body like Congress regulates any field. By constitutional design, however, FDI falls within the Legislature’s purview to regulate interstate and foreign commerce. As such, “many policymakers apparently perceive greater risks to the economy arising from foreign investments in which the foreign investor is owned or controlled by foreign governments.”¹⁹⁷ More importantly, critics that reject Congress’s broad role in regulating FDI fail to appreciate a new reality—national economy and national security are inherently intertwined.

1. Firstgold & Northwest Non-Ferrous International Investment Company

Following the passage of FINSA and Congress’s attempt to clarify the national security review process, CFIUS again found itself embroiled in controversy during a Chinese investment company’s friendly takeover bid of Firstgold—a relatively small mining company based in Nevada. In July 2009, Firstgold announced that China’s Northwest Non-Ferrous International Investment Company (Northwest) had agreed to purchase

¹⁹¹ See *infra* Part II.

¹⁹² Mamounas, *supra* note 4, at 391. Similarly, the Department of Treasury, which heads CFIUS, also rejected legislative proposals to define ‘national security’ more specifically. *Id.*

¹⁹³ *Id.*

¹⁹⁴ JACKSON, *supra* note 55, at 14. For instance, the Department of Defense has established its own industrial security standards based on the term “Foreign Ownership, Control or Influence (FOCI). *Id.*

¹⁹⁵ See JACKSON, *supra* note 63, at 12–13. Under FINSA, the “regional military threat” consideration in factor 4, and factors 6–12 were added to the Exon-Florio provision. *Id.*

¹⁹⁶ Christopher R. Fenton, Note, *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, 211 (2002) (arguing that Exon-Florio “could be utilized as a shield to protect domestic industry in the context of broad and aggressive industrial policy”).

¹⁹⁷ JACKSON, *supra* note 55, at 15.

\$26.5 million in secured debt in return for a “51 percent of outstanding common shares to become Firstgold’s majority shareholder.”¹⁹⁸ Unlike the CNOOC-Unocal fiasco, however, Congress “made no public statements regarding the Firstgold deal, instead allowing CFIUS alone to resolve its security concerns.”¹⁹⁹ Nonetheless, Northwest’s bid to acquire Firstgold ultimately shared the same fate as CNOOC, as the deal fell apart in the face of impending negative treatment by CFIUS.²⁰⁰

As the two parties to the agreement voluntarily withdrew from CFIUS review, Firstgold CEO Terry Lynch publicly expressed that he failed to understand the nexus between his company’s assets, which primarily consisted of an open-pit facility at Relief Canyon Mine,²⁰¹ and U.S. national security.²⁰² In fact, neither party seemingly believed that the transaction would implicate national security, given the relatively small size of the investment and the nature of Firstgold’s business as compared to other transactions that triggered CFIUS review in the past.²⁰³ However, once Firstgold and Northwest volunteered for national security review, CFIUS found that the deal was clearly a “covered transaction,” given that the proposed acquisition would result in foreign control over Firstgold.

Upon closer examination, a unique set of circumstances surrounding the transaction led CFIUS to render an adverse recommendation to President Obama to block the acquisition. First, the identity and corporate structure of Northwest—an investment firm owned and operated by the Chinese provincial government of Shaanxi—raised the same red flag as in the CNOOC ordeal. “Procedurally, Section 721 [of the Defense Production Act of 1950] virtually mandates that CFIUS proceed to the full investigation stage where the foreign investing party is state-owned or controlled.”²⁰⁴ Though this factor is not conclusive to CFIUS’s ultimate findings, Firstgold’s shock that CFIUS chose to conduct the secondary forty-five-day review appears unfounded.²⁰⁵

¹⁹⁸ Matthew C. Sullivan, *Mining for Meaning: Assessing CFIUS’s Rejection of the Firstgold Acquisition*, 4 PUBLICIST 12, 15 (2010).

¹⁹⁹ Sullivan, *supra* note 179, at 238.

²⁰⁰ Theodore Kassinger, *Location, Location, Location: Observations On CFIUS Opposition To Investment By Chinese Mining Company In Firstgold Corporation*, O’MELVENY & MYERS (Jan. 8, 2010), available at <http://www.mondaq.com/unitedstates/article.asp?articleid=91996>.

²⁰¹ Sullivan, *supra* note 198, at 16.

²⁰² *Id.*

²⁰³ Kassinger, *supra* note 200.

²⁰⁴ *Id.*

²⁰⁵ Sullivan, *supra* note 198 (“CFIUS officials informed the parties it would be undertaking a full, 45-day investigation pursuant to Section 721(b)(2)—a mandatory step for government-controlled acquisitions, but one that, for reasons that are not clear, appeared to take the parties by surprise.”).

The second and perhaps the most determinative factor that compelled CFIUS to render an adverse recommendation was the target company's location. While the proposed transaction arguably did not involve a strategic asset—such as oil in the earlier CNOOC-Unocal merger—the physical site of Firstgold's assets posed a unique threat to U.S. national security interests.²⁰⁶ “The primary source of concern among CFIUS officials was the proximity of four mines to the Fallon Naval Air Station.”²⁰⁷ Moreover, in a publicly leaked memorandum of the Committee's communication with Firstgold, CFIUS officials suggested a possible national security threat to “other sensitive and classified security and military assets that cannot be identified.”²⁰⁸ Arguably, these unique circumstances surrounding the Firstgold-Northwest transaction made an adverse CFIUS review unavoidable.²⁰⁹ The bottom line is that “location matters when military facilities occupy the neighborhood.”²¹⁰

2. Huawei & 3Leaf Systems

More recently, CFIUS again flexed its newfound authority in requesting the divestment of a completed acquisition involving Huawei Technologies Company and California-based 3Leaf Systems.²¹¹ In May 2010, Huawei spent \$2 million for intellectual property rights from 3Leaf, a company that “specializes in building servers to run together as more powerful mainframe computers.”²¹² Huawei—China's largest telecommunications equipment manufacturer—and 3Leaf consummated the deal without voluntary notice to CFIUS.²¹³ Acting on its independent

²⁰⁶ Eric Lipton, *Questions on Security Mar Foreign Investments*, N.Y. TIMES, Dec. 18, 2009, at B1, available at <http://www.nytimes.com/2009/12/18/business/18invest.html>.

²⁰⁷ Sullivan, *supra* note 198.

²⁰⁸ Memorandum from Davis Graham & Stubbs LLP and Reed Smith LLP to Firstgold and Northwest (Dec. 14, 2009) at 3 [hereinafter Memorandum], available at <http://graphics8.nytimes.com/packages/images/nytint/docs/memo-regarding-the-sale-of-firstgold-corp/original.pdf>.

²⁰⁹ Kassinger, *supra* note 200 (arguing that close scrutiny was predictable given “the current environment of exceptional concern about electronic warfare and intelligence gathering by potential adversaries, the combination of Northwest's identity as a Chinese state-owned enterprise and the proximity of Firstgold's mining properties to known, secretive military installations”).

²¹⁰ *Id.*

²¹¹ Chris V. Nicholson, *The Big Chill: Huawei Imbroglio Puts Countries at Odds*, N.Y. TIMES, (Feb. 18, 2011, 4:49 AM), <http://dealbook.nytimes.com/2011/02/18/the-big-chill-huawei-imbroglio-puts-countries-at-odds/>.

²¹² Michael Kan, *China's Huawei to Reverse Controversial Deal for 3Leaf*, PCWORLD, (Feb. 19, 2011, 2:02 PM), http://www.pcworld.com/businesscenter/article/220183/chinas_huawei_to_reverse_controversial_deal_for_3leaf.html#tk.mod_stln.

²¹³ Sinead Carew & Jessica Wohl, *Huawei Backs Away from 3Leaf Acquisition*, REUTERS,

review authority, CFIUS requested that Huawei initiate the review process to determine if national security issues were present in the completed transaction.²¹⁴ Nearly nine months after Huawei acquired various technology patents from 3Leaf, CFIUS ultimately recommended “voluntary” divestment or risk an adverse recommendation to President Obama to undo the deal.²¹⁵

Similar to the fates of CNOOC and Northwest in their acquisition attempts, Huawei came under close scrutiny given its corporate identity. However, its failed attempt to acquire 3Leaf assets is not the first time Huawei has been subjected to the national security review process for foreign mergers and acquisitions.²¹⁶ In the past five years, Huawei repeatedly found itself on CFIUS’s radar due to security concerns with failed transactions involving 3Com and Sprint.²¹⁷ Indeed, American lawmakers have shown a deep-seated distrust of Huawei due to its purported ties with the Chinese military.²¹⁸ According to a 2005 RAND report, Huawei—touted as a “national champion” in China—purportedly “maintains deep ties with the Chinese military, which serves a multi-faceted role as an important customer, as well as Huawei’s political patron and research and development partner.”²¹⁹

Given these findings, it is no surprise that CFIUS has repeatedly scrutinized Huawei’s attempts to enter into the U.S. telecommunications market, a critical infrastructure directly implicating the Exon-Florio factors for consideration in the national security review process.²²⁰ Indeed, Huawei’s purported link to the Chinese military raises the specter of economic or cyber espionage by allowing Huawei to potentially corrupt

Feb. 19, 2011, <http://www.reuters.com/article/2011/02/19/us-huawei-3leaf-idUSTRE71I38920110219>.

²¹⁴ Michael Kan, *Report: U.S. Panel to Recommend Reversing Huawei Deal*, PCWORLD, (Feb. 11, 2011, 5:20 AM), http://www.pcworld.com/businesscenter/article/219414/report_us_panel_to_recommend_reversing_huawei_deal.html#tk.mod_rel.

²¹⁵ Nicholson, *supra* note 211.

²¹⁶ Edmond Lococo, *Huawei Calls for ‘Accountability’ as U.S. Blocks Network Bid*, BLOOMBERG NEWS, (Oct. 12, 2011), *available at* <http://www.businessweek.com/news/2011-10-12/huawei-calls-for-accountability-as-u-s-blocks-network-bid.html>.

²¹⁷ Carew & Wohl, *supra* note 213.

²¹⁸ Kathrin Hille et al., *China and the US: Access Denied*, FIN. TIMES (Apr. 7, 2011, 10:01 PM), <http://www.ft.com/intl/cms/s/0/9080ccaa-614d-11e0-ab25-00144feab49a.html#axzz1lcpMcarP>.

²¹⁹ See EVAN S. MEDEIROS ET AL., RAND CORP., A NEW DIRECTION FOR CHINA’S DEFENSE INDUSTRY 218 (2005), *available at* www.rand.org/pubs/monographs/2005/RAND_MG334.pdf. The company was also founded by Ren Zhengfei, a former Chinese soldier and director of the People’s Liberation Army’s Information Engineering Academy. *Id.*

²²⁰ JACKSON, *supra* note 63, at 12–13.

telecommunications equipment that the Department of Defense or other vestiges of the national security apparatus relies upon.²²¹ Coupled with the uptick in Chinese cyber-attacks on U.S. critical infrastructures, Huawei's potential ties to China's military poses a considerable roadblock to its aspirations in penetrating markets that potentially implicate U.S. national security interests.²²²

Ultimately, the failed foreign investment transactions between Northwest and Firstgold, as well as Huawei and 3Leaf, demonstrate the need for a broad approach to defining national security within the CFIUS review process. While both transactions suggest hostility toward Chinese multinational corporations, CFIUS's response in each appropriately considered real national security implications in the proposed transactions. The target company's physical proximity to military installations or the acquiring company's ties to a foreign military raises red flags for any sovereign, because these attributes increase the potential for economic or military espionage. More importantly, a narrow interpretation of "national security" in the review process for foreign investments would likely overlook such possibilities for information leakage or technology transfer. Thus, the broader conceptualization of "national security" by CFIUS is necessary to deal with nuanced threats in the era of globalization.

C. Managing Economic Repercussions

As a response to the realities of the post-9/11 security environment, an increased role for CFIUS in regulating foreign investment is well-intended. However, the unintended or perceived consequences of a particular policy can ultimately be as important to its success. Prior to the passage of FINSA, critics forewarned that "[s]ubstantial changes in the analytical framework governing [CFIUS's] evaluation of national security considerations related to proposed mergers, acquisitions and takeovers could have sweeping implications for investor confidence."²²³ This criticism is grounded in the overblown charges of non-transparency and ambiguity addressed above.²²⁴ If true, investor uncertainty theoretically "could lead foreign firms to abandon plans to merge, or acquire American companies entirely."²²⁵ Moreover, the added scrutiny admittedly increases delays in foreign acquisitions, which could negatively impact FDI in the United States.²²⁶

Even worse, some fear that foreign investors—and their respective

²²¹ Gliberman & Shapiro, *supra* note 39, at 174.

²²² See *infra* Part II.

²²³ Fenton, *supra* note 196, at 247.

²²⁴ See *infra* Part V.A–B.

²²⁵ Fenton, *supra* note 196, at 247.

²²⁶ Travalini, *supra* note 58, at 795-796.

governments—will perceive heightened CFIUS review as economic protectionism.²²⁷ At least one critic goes so far as to argue that “identifying the factors that lead to blockage of the deal might be the equivalent of declaring hostilities against the acquiring company’s government.”²²⁸ Given the United States’ traditional policy of open investment, critics contend that perceived hostility to foreign mergers or acquisitions involving U.S. companies will trigger protectionist backlash.²²⁹ It is argued that such “[o]verreaching U.S. regulation of foreign investment will trigger retaliation by other governments and undoubtedly hurt U.S. investors abroad.”²³⁰ China’s recent CFIUS-like model regulating foreign investment provides timely fodder for such criticisms.²³¹

Much like the complaints regarding CFIUS’s overbroad scope and lack of transparency, these economic concerns are ultimately outweighed. Above all, the United States is one of many major economies that permits governmental regulation of foreign mergers, acquisitions, or takeovers.²³² Arguably, “there are more, and better developed, statutory restrictions on foreign investment in place in foreign jurisdictions than in the United States.”²³³ While China’s newly-created national security review framework follows on the heels of the failed Huawei-3Leaf transaction, its policy to review foreign investment for potential national security threats was already well-established by its antitrust regulations released in 2007.²³⁴

Rather, China’s heightened national security review process—much like CFIUS in the United States—comports with global standards. For example, many of the world’s prominent international trade regimes, like the WTO, “allow signatory nations the right to deny foreign investment in areas of the economy deemed integral to the national security interests of that nation.”²³⁵ The notion that CFIUS undercuts the global liberal

²²⁷ Georgiev, *supra* note 74, at 125-126.

²²⁸ Stagg, *supra* note 54, at 354.

²²⁹ Fenton, *supra* note 196, at 248 (“Sending mixed signals could sacrifice Washington’s diplomatic leverage position in future negotiations over international economic agreements, as restrictive American policies would justify foreign resistance to market liberalization along similar grounds.”).

²³⁰ Stagg, *supra* note 54, at 333.

²³¹ See generally Deas, *supra* note 111.

²³² Sud, *supra* note 11, at 1312-14 (discussing restrictions on foreign investment in countries, such as the United Kingdom, Germany, Austria, China, Japan and India); see also Sothmann, *supra* note 57, at 205 (“The critical consideration is that several nations, including many western nations, have some form of restrictions on international mergers and acquisitions in industries that are considered integral to ‘national security.’”).

²³³ Sud, *supra* note 11, at 1314.

²³⁴ Sothmann, *supra* note 57, at 203, 205. For further discussion of China’s regulations on foreign investment, see *infra* Part IV.

²³⁵ *Id.* at 205 (identifying prominent global trade regimes with national security exceptions, including the WTO, the European Union, the North American Free Trade

economy is inconsistent with the widely-held belief that a nation has the right to protect its national security from adverse foreign investment. “This exception to free trade has been a part of the global economy since the earliest free trade agreements.”²³⁶ CFIUS is no exception to that international standard.

This defense of CFIUS’s role in the global economy does not purport to argue that national security reviews have no impact on a nation’s economic calculus. On the contrary, as one policy expert explains:

Within the economy, economic theory maintains that demand and supply forces determine the market prices for labor and for capital as the various sectors compete for these scarce resources. These market prices, then, work to allocate resources within the economy among the vast array of economic activities that use the resources in the most efficient manner. Interference in this process, regardless of the reason, can cause a misallocation of resources in the economy and a loss of efficiency, which imposes a cost on the economy as a whole.²³⁷

Admittedly, the national security review process for foreign investment potentially interferes with otherwise economically viable mergers or acquisitions. For example, in the failed CNOOC-Unocal acquisition, Unocal was arguably deprived of capitalizing on CNOOC’s offer, which exceeded Chevron’s eventual winning bid by approximately \$2 billion.²³⁸ Thus, regulatory frameworks like CFIUS “may also alter the allocation of capital within the economy and, thereby, incur short-term and long-term costs to the economy.”²³⁹

Nonetheless, critics’ claims regarding the adverse economic impacts of CFIUS fail to capture the complexity of calculating economic costs. Simply calculating the lost value of a CFIUS-blocked foreign investment as a tell-tale economic cost ignores the national security benefits captured. Critics are correct in pointing out that such national security benefits are not easily quantifiable and are context-dependent.²⁴⁰ That contention, however, is a double-edged sword. Simply put, there is no “precise way . . . to estimate the exact dollar amount for the economic costs and benefits of national policies that attempt to direct or restrict foreign direct investment for national security concerns.”²⁴¹ However there is one certainty: the costs

Agreement, and the Association of Southeast Asian Nations).

²³⁶ *Id.*

²³⁷ JACKSON, *supra* note 55, at 20.

²³⁸ Petrusic, *supra* note 148, at 1374.

²³⁹ JACKSON, *supra* note 55, at 20.

²⁴⁰ *Id.* at 20–21.

²⁴¹ *Id.* at 1.

associated with adverse foreign investment, including economic espionage or the transfer of lucrative intellectual property to the acquiring country are staggering.²⁴² Accordingly, in order to justify CFIUS's intervention in any particular proposed foreign investment, policymakers will have to weigh the economic and non-economic costs and benefits. This balancing approach is more of an art than a science, which critics tend to overlook.

Instead, critics of CFIUS review—and its foreign counterparts—focus on statistics that seemingly support their fears of regression in the face of increased regulations. For example, it is true that the amount of FDI declined by nearly twenty-five percent from 2008 to 2009.²⁴³ That statistic, however, is hardly conclusive of the purported decline in FDI as a result of a heightened national security review process following passage of FINSA in 2007. For instance, the amount of FDI into the United States in 2008 “set a record in nominal terms for the most amount of foreign direct investment in the economy in a year.”²⁴⁴ While fiscal year 2009 failed to match that impressive mark from the year before in absolute terms, cumulative FDI still increased by seven percent.²⁴⁵

More importantly, critics relying on general year-to-year changes in FDI ignore the importance of economic conditions in encouraging foreign investment in the first place. “The decrease in foreign direct investment flows mirrors a slowdown in global flows.”²⁴⁶ It is no secret that the U.S. economy is not immune to the global economic crisis, which has adversely impacted foreign mergers and acquisitions.²⁴⁷ Conversely, “As the rate of growth of the U.S. economy rises, interests rates stay low, and the rate of price inflation stays in check, foreign direct investment . . . likely will continue to rise.”²⁴⁸ Given these current global economic conditions, it would be disingenuous to argue that CFIUS is the driver of a contraction in foreign investment. Rather, foreign investment is as much a function of a complex globalized economy as it is of a heightened domestic regulatory regime.

Nonetheless, “[t]he real test for the amended regulatory framework” will rest in part upon “the ability of the executive branch to inspire and

²⁴² See *supra* Part II.

²⁴³ JAMES K. JACKSON, CONG. RESEARCH SERV., RS21857, FOREIGN DIRECT INVESTMENT IN THE UNITED STATES: AN ECONOMIC ANALYSIS I (2011).

²⁴⁴ *Id.* at 8.

²⁴⁵ *Id.* at 1 (“The cumulative amount, or stock, of foreign direct investment in the United States on a historical cost basis rose from \$2.2 trillion in 2008 to about \$2.3 trillion in 2009.”).

²⁴⁶ *Id.* Specifically, “[a]ccording to the United Nations’ *World Investment Report*, global foreign direct investment inflows decreased by 16% in 2008 and 37% in 2009.” *Id.*

²⁴⁷ *Id.* at 2.

²⁴⁸ *Id.* at 6.

maintain public confidence in the new CFIUS process.”²⁴⁹ Fortunately, legislative amendments to CFIUS since its inception provide significant measures to ensure investor confidence in foreign mergers and acquisitions in the United States. FINSA in particular strengthened the CFIUS framework to reify an open investment policy while assuaging Congress that national security concerns are also addressed.

Above all, FINSA significantly normalized the CFIUS review process by increasing congressional oversight vis-à-vis reporting requirements.²⁵⁰ Moreover, the latest iteration of CFIUS regulations require the Department of Treasury to conduct extensive analysis of FDI in the United States that may implicate national security interests.²⁵¹ These requirements “allow for greater transparency while maintaining the evaluation and decision-making process entirely within the [E]xecutive branch.”²⁵² This added congressional oversight increases overall accountability, which ensures foreign investors that CFIUS will “be armed with a strong case in support of its decision and would be able to respond more persuasively to close congressional scrutiny.”²⁵³ Ultimately, this assurance is crucial to preserving confidence in the national security review framework for foreign investments.

VI. CONCLUSION

While the United States has always been a staunch supporter of open investment policies globally, national security concerns have long been recognized as a valid limitation on foreign mergers. These national security

²⁴⁹ Georgiev, *supra* note 74, at 134.

²⁵⁰ *See supra* Part V.A.

²⁵¹ JACKSON, *supra* note 63, at 15. Specifically:

The Secretary of the Treasury, in consultation with the Secretary of State and the Secretary of Commerce, is required to conduct a study on investment in the United States, particularly in critical infrastructure and industries affecting national security by: (1) foreign governments, entities controlled by or acting on behalf of a foreign government, or persons of foreign countries which comply with any boycott of Israel; or (2) foreign governments, entities controlled by or acting on behalf of a foreign government, or persons of foreign countries which do not ban organizations designated by the Secretary of State as foreign terrorist organizations. In addition, CFIUS is required to provide an annual evaluation of any credible evidence of a coordinated strategy by one or more countries or companies to acquire U.S. companies involved in research, development, or production of critical technologies in which the United States is a leading producer. The report must include an evaluation of possible industrial espionage activities directed or directly assisted by foreign governments against private U.S. companies aimed at obtaining commercial secrets related to critical technologies.

Id. at 15–16.

²⁵² Georgiev, *supra* note 74, at 132.

²⁵³ *Id.*

considerations are understandably heightened in the era of globalization, where transnational forces easily penetrate national borders. Since the 1970s, the U.S. national security review process for foreign mergers, acquisitions, and takeovers of U.S. corporations has undergone several transformations. At each stage of its development, proponents of economic liberalism have challenged the review process as being antithetical to open investment policies. Since the passage of the Foreign Investment and National Security Act of 2007, however, the U.S. national security review process has featured an intricate balance in protecting U.S. national security while promoting national economic interests.

However, one fear of the U.S. approach has seemingly come to fruition. Perhaps in retaliation to well-documented failed foreign acquisition attempts in the United States due to national security concerns, China has established its own national security review process. This Comment argues, CFIUS's new counterpart in mainland China is not surprising given the projected influx of foreign investment into China and its booming economy. Rather, China's model, despite its over-breadness, is a natural reaction to protect its national security. Indeed, the United States established its security review process for foreign mergers in the 1970s. Despite concerns from economists, both countries enjoy a healthy dose of FDI. For China, however, it remains to be seen whether its review process successfully balances its national security and economic interests as well as its U.S. counterpart in CFIUS.