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NAVIGATING THROUGH U.S.-CHINA POLICY:

An Investigation of China National Off-Shore Oil Corporation's Proposed Acquisition of  
Unocal Corporation and How Domestic Politics Plays a Role in Balancing U.S. Trade  
Policy with National Security Policy

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A Dissertation

Presented to

The Faculty of the Korbel School of International Studies

University of Denver

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In Partial Fulfillment

of the Requirements for

the Degree Doctor of Philosophy

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by

Vicki L. Spencer

June 2010

Advisor: Professor Suisheng (Sam) Zhao

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Title: Navigating Through U.S.-China Policy: An Investigation of China National Off-Shore Oil Corporation's Proposed Acquisition of Unocal Corporation and How Domestic Politics Plays a Role in Balancing U.S. Trade Policy with National Security Policy

Advisor: Sui-sheng ("Sam") Zhao

Degree Date: June 2010

## **ABSTRACT**

When Chinese National Offshore Oil Corporation, Ltd. ( CNOOC) attempted to buy American-owned Unocal Corporation, it unleashed a "perfect storm" in Washington. Members of Congress immediately called upon President Bush to invoke his Exon-Florio authority to prevent the transaction. After the president claimed action would be premature, Congress quickly coalesced to block the deal. The Chinese expressed surprise at the political backlash and ultimately CNOOC was forced to withdraw its bid.

The purpose of this study is to explain the fervor that arose over CNOOC's proposed acquisition of Unocal. The study builds upon the theoretical approach of new institutionalism which emerged in response to the shortcomings of theories that diminished the importance of political values and collective choice in foreign policy making. Since institutionalism emphasizes the significance of history and assumes the infusion of societal values over time, the study applies historical research methodology to the case study. Sources of data include the U.S. Constitution, statutes, judicial opinions, congressional hearings and reports, White House papers, administrative rules, and published biographies. Secondary sources include the media, journals, and think-tank publications.

The study examines how the president and Congress rely upon formal rules for making policy, and how these rules reinforce the status quo and create obstacles for change. Over the years, the president has acquired greater foreign policy making authority which has upset the balance of power between the two decision-making bodies. Since policy making is incremental, members of Congress have needed to be resourceful in devising informal mechanisms for change. One such mechanism is politicization of an event to raise public awareness, elevate an issue to the top of the policy agenda, and build coalitions essential to passing legislation.

The research finds that competition between the president and Congress over foreign and national security policy authority is played out in Washington and is reflected in policy outcomes. In the Unocal acquisition case, politicization allowed members of Congress to advance their agenda to tighten up the president's process for reviewing foreign acquisitions and to give Congress greater oversight authority.

This study is important and timely because China has become a major player in the global economy and is driving the global search for new and reliable sources of energy. As China extends its reach, competition with the U.S. and other major energy importers will increase. Although competition is considered essential for a healthy capitalist economy, other factors influence whether competition will have a positive or negative impact on competitors. One of these factors is the perception of how China's emergence in the global economy will affect U.S. national security. The future of U.S.-China relations will depend upon the ability of our political institutions to achieve balance and compromise in energy, foreign trade, and national security policies.

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## CHAPTER ONE: INTRODUCTION

Early in 2005 the Chinese National Offshore Oil Corporation, Ltd. (CNOOC) expressed interest in purchasing American-owned Unocal Corporation. The Chinese company's proposal unleashed a "perfect storm" in the world of Washington politics.<sup>1</sup> Claiming that the foreign acquisition of an American oil corporation would threaten national security, a group of U.S. legislators called on President Bush to invoke his Exon-Florio authority and prevent the transaction.<sup>2</sup> But when the Bush Administration stated this action would be premature, Congress quickly coalesced to block the deal. The speed with which Congress reached consensus to intervene in the proposed transaction was exceptional. At the same time, media coverage elevated the event in the public's eye and further politicized the issue of foreign acquisitions of American businesses.

The Chinese expressed surprise about the reaction in Congress, emphasizing that CNOOC had proposed a routine business transaction and the company's management had made every effort to be transparent and comply with American law. Heated debates

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<sup>1</sup> In 1997, Sebastian Junger adopted the phrase "perfect storm" as the title of his book about the 1991 Nor'easter storm. Here, we use it to describe a perfect situation where a rare combination of circumstances occurs to generate a political outcry that results in policy change.

<sup>2</sup> The Exon-Florio Amendment to Section 721 of the *Defense Production Act of 1950* was initially introduced in Congress to order the executive branch to examine trade with countries that had a large trade surplus. The law has evolved over time and will be discussed in detail in chapter 4.



ensued, lasting throughout the summer until the eleventh hour when CNOOC directors finally withdrew the bid just before it was to go to the Unocal stockholders for a vote on August 10, 2005. In spite of severe criticism against China, Beijing did not escalate the issue beyond strongly admonishing Congress for its tactics. The CNOOC bid slowly faded from the American press but continued to be a point of discussion in Congress as key legislators sought greater oversight of foreign mergers and acquisitions under statutory authority of the Exon-Florio Amendment and how it was being implemented.

Meanwhile, the Chinese were particularly perplexed by the national security concerns voiced by American legislators. Ever since the 1980s, the Chinese leadership had pursued a foreign policy based on the principles of “independence and peace.” The primary goal had been to accelerate economic growth so as to attain a higher standard of living for Chinese citizens and the consensus in China was that economic growth can best be realized in a peaceful global environment. For more than two decades, the U.S. government had supported China’s cooperative approach and encouraged China to become more engaged in the global economy. Given the mutually beneficial economic relationships that had developed between the two nations, why would the U.S. Congress oppose CNOOC’s bid to purchase a failing U.S. corporation when mergers and acquisitions are a basic feature of competition in the capitalist market?

The purpose of this study is to explain the fervor that arose in Congress over the CNOOC bid. We examine American political institutions from a socio-historical perspective which views these institutions as being embedded with values that are reflected in the formal rules for policy making that develop over time. Although formal

rules reinforce institutional stability, they often create obstacles and constraints that inhibit efficient policy making and restrict institutional actors from accomplishing their own policy goals. As a result, institutional actors often turn to informal mechanisms for creating change.

Sometimes these informal mechanisms are straight forward and transparent, and eventually become formalized. But sometimes these mechanisms are obtuse and difficult to comprehend. For this reason, scholars have relegated informal policy making to the “black box” where the process may be obvious or intuitive to institutional actors, but appears mysterious to outside observers. This mystery is especially ominous when the outside observers are from a foreign nation and have not been immersed in the American culture and values which have shaped the formal rules and have influenced the political dynamics that take place within the “black box.”

The study is an attempt to delve into the obscurity of the “black box” where actors filter information and devise alternative mechanisms for circumventing or overcoming the formal rules that are inherently resistant to change. The analysis examines the dynamics of formal constraints and informal mechanisms of change, how these dynamics may elevate a particular issue to the top of the foreign policy agenda and, by doing so, may influence political outcomes which have broader implications for future policy making.

This dissertation considers these institutional characteristics within the context of a changing world – a twenty-first century global economy adjusting to China’s global expansion and America’s heightened sense of vulnerability and increased emphasis on

national security. This specific case study investigating the political reaction which surfaced when Chinese-owned CNOOC attempted to acquire a floundering American-owned corporation is both important and timely. China has become a major player in the global economy and China's economic growth is driving its global search for new sources of energy. As China extends its reach, competition with the United States and other major energy importers will increase.

Although competition is considered essential for a healthy capitalist economy, other factors influence whether competition will have a positive or negative impact on the competitors.<sup>3</sup> Perhaps most significant, is that China's emergence in the global economy has occurred at a time when there has been increased discussion about "peak oil," increased concern that global supplies of recoverable fossil fuel are decreasing, and increased concern about the impact of greenhouse gases generated by the burning of fossil fuels. If China's demand for energy continues to increase at its current rate, global fuel shortages will be accompanied by increased costs worldwide. As a result, American citizens may no longer be able to enjoy the low-priced energy and steady economic growth that they have come to take for granted.<sup>4</sup>

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<sup>3</sup> Flynt Leverett and Jeffrey Bader, "Managing China-U.S. Energy Competition in the Middle East," *The Washington Quarterly* (Winter 2005-06): 187-201. Leverett and Bader cite Henry Kissinger's concern that competition over energy is likely to cause international conflict. The authors argue that "prudent" management of the competition for Middle Eastern oil will be necessary to avoid friction between China and the U.S. See also Caroline Daniel, "Kissinger Warns of Energy Conflict," *Financial Times*, June 2, 2005; and Robert A. Manning, *The Asian Energy Factor: Myths and Dilemmas of Energy, Security and the Pacific Future* (New York: Palgrave, 2000).

<sup>4</sup> For an introduction to this debate see, for example, Gal Luft and Anne Korin, "The Sino-Saudi Connection," *Commentary* 117, no. 3 (March 2004): 26-29; and Dan

China's aggressive development policies may also impact the global balance of power which, in turn, will influence how nations perceive their need for national security. Although the capitalist economy is based on free trade and the United States values free trade, the U.S. government also uses trade policies to influence foreign governments and promote American ideals. If China pursues global expansion and negotiates trade agreements which do not impose similar policies or do not aspire to achieve similar ideals, it may undermine the preeminence of the United States in the global economy. This may lead to a change in the balance of power among nation states and threaten U.S. national security.

Past studies have shown that corporations seeking to extend their operations beyond national boundaries face a number of issues they do not face when operating within the borders of a single nation-state. There are risks and conflicts that arise in trying to do business in nation-states with different cultures, values, and political systems. Historically, there has been a perception that the interests of global corporations are identical with the interests of the governments in the home countries of those corporations. This perception has been reinforced by the international relations literature dominated by the realism and balance of power theories.

However, theories that explained foreign policy during the Cold War have less explanatory power today. After the fall of the Soviet Union, the United States claimed status as the most preeminent world power; but during the last decade China has emerged

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Blumenthal, "China and the Middle East: Providing Arms," *Middle East Quarterly* 12, no. 2 (Spring 2005): 11-19.

as a major player in the global economy. In addition, the United States has lost negotiating power as terrorist groups have expanded their activities. Terrorism in the twenty-first century extends beyond the boundaries of the nation-state and threatens national security at the same time that it challenges the tenants of traditional international relations theories.

New theories are needed to understand the complexity of U.S.-China relations in which the two nations espouse contradictory ideologies, yet pursue foreign policies which have created mutual dependence on one another for economic growth. The lines of demarcation are becoming blurred as the Chinese Communist Party is abrogating some of its economic powers to private corporations, while the U.S. Congress is reining in capitalist corporations with increased regulatory constraints.

This study builds upon the theoretical approach of new institutionalism. The theory first emerged in response to the shortcomings of realism and other strains of thought which diminished the importance of political values and collective choice. While institutionalism has substantial explanatory powers, recent theory-building efforts have focused on distinguishing separate strains within the institutional school of thought. This study challenges bifurcation of the theory by identifying a common theoretical core.

This approach to institutionalism assumes the significance of an institution's history and the infusion of societal values over time. These factors affect the institution's structure and role within the polity. In the United States, policy makers operate under the rule of law, which the founders intended to be transparent, and these rules constitute institutional constraints which reinforce stability. The tendency towards institutional

stasis benefits society by creating a sense of security which is important in a democratic society where individualism prevails and where individuals are expected to take responsibility for planning their futures. These institutional rules and values encourage innovation and entrepreneurship, but the system of checks and balances (and the constraints it imposes on political actors) affects legislative efficiency and makes it difficult for Congress to react quickly and enact laws in a timely manner.

This approach looks at the endogenous institutional factors that impact decision making, but also acknowledges that external factors – such as the role that the U.S. and China play in the global economy, increased competition for steady and reliable supplies of energy, and predictions concerning peak oil – play a role in decision making. When CNOOC began its quest to purchase Unocal, the company thought it was playing according to the rules of the American capitalist economy. Even CNOOC's foreign advisors, who assisted with crafting the proposal, seem to have been caught off guard when they did not foresee the reaction in Congress. The significance of the ongoing political tug-of-war between the U.S. president and Congress concerning foreign commercial transactions seems to have escaped others as well, including U.S.-China analysts and international economists, who also expressed surprise over the politicization of CNOOC's business proposal.

This study aims to build an awareness of how the built-in tension between the executive and legislative branches causes U.S. legislators to resort to informal mechanisms to accomplish their personal agendas. It delves into the question of whether the proposed CNOOC purchase really constituted a national security threat, or whether

there were other motives behind politicization of this particular business transaction. The research indicates that the underlying reason for bringing the proposed acquisition to the public's attention was to build support for modifying the Exon-Florio Amendment. Even though Congress had passed the Exon-Florio Amendment decades earlier, presidents have intervened in very few business interactions and have prohibited only a handful of deals from being consummated. For years, legislators had been calling for increased oversight over the president's implementation of the statute. But they faced institutional constraints which weakened their ability to reform the Exon-Florio provisions. This case study shows how individual members of Congress acted strategically to politicize CNOOC's proposed acquisition of Unocal as a means of overcoming these institutional constraints.

The complexity of this single event and the depth of misunderstanding by the Chinese and other foreign observers call for examination of three separate, yet integrated, matters affecting U.S.-China policy. The first concerns China's unique approach towards economic development and integration into the world economy. The second concerns the fragmented approach towards policy making in the United States and its impact on U.S.-China policy decisions. The third concerns the impact of September 11, 2001 on the lives of American citizens and elevation of national security on the U.S. policy making agenda.

Chapter 2 sets the stage for analyzing the politicization of CNOOC's bid for Unocal by discussing China's development strategy and the need for continually increasing energy supplies to support economic growth. Chapter 3 lays the foundation

for understanding the incessant competition between the U.S. president and Congress by examining the historical process of institutionalization in which formal rules were developed and values were embedded in the political system. Chapter 3 also examines how the September 11, 2001 terrorist attacks empowered the presidency and ultimately led the 109th Congress to reach a consensus that congressional oversight over the president's Exon-Florio authority needed to be strengthened. These two chapters set the stage for the case study analysis in Chapter 4.

Chapter 4 distinguishes laws that govern domestic mergers and acquisitions from those that govern foreign mergers and acquisitions. It discusses the legislative history of the Exon-Florio Amendment which was enacted to delegate authority to the president to prevent foreign mergers and acquisitions when national security was at stake. Once implemented, members of Congress realized the shortcomings of the Exon-Florio Amendment, but found it difficult to correct those shortcomings within the formal constraints imposed by the institutional structures, rules, and standards. Analysis of the Unocal case shows how members of Congress resorted to informal mechanisms, including politicization of this specific event, to accomplish their policy goals.

Chapter 5 continues the story of the Unocal by examining the outcomes of the perfect storm that the CNOOC bid unleashed in 2005. Politicization of the event unified Congress in moving forward to modify the Exon-Florio Amendment, but the coup de grâce came several months later when Congress learned that the United Arab Emirates-owned Dubai Ports World was purchasing London-based Peninsular and Oriental Steam Navigation Company which operated ports in the United States. The chapter argues that



the back-to-back foreign acquisitions proposed by CNOOC and Dubai Ports World, within the context of the need for heightened national security after 9/11 and a growing phobia of China's dominance in the global market provided the impetus for members of Congress to use informal mechanisms to reassert their legislative prerogatives and take back power from the presidency. In short, the analysis shows that the CNOOC deal fell victim to a domestic power struggle in the United States.

The rest of this introductory chapter focuses on the development of the theoretical approach for this case study. First we review the realist approach to the study of international relations and how it assumes a national consensus regarding foreign policy decisions. Then we explain how new institutionalism emerged in response to the realist approach as a means of "bringing the state back in" to the discussion of international relations and how institutional theory allows for consideration of the role that domestic conflict plays in determining foreign policy outcomes. Finally, we describe our theoretical approach and methodology in more detail.

## **I. LITERATURE REVIEW**

### **A. Realism**

In our quest to answer the Unocal puzzle, we first turn to international relations theory as it developed after World War II when nations divided into two major camps – those which adhered to a capitalist world-view and those which adhered to a communist world-view. The chasm created by this bi-polar world, dominated by the United States and the Soviet Union, led international relations scholars to focus foreign policy concerns

on the distribution of power, the causes of war, and the conditions necessary for peaceful coexistence.<sup>5</sup> At the same time, there was a movement towards bringing more credibility to the field of study by emphasizing the importance of developing a scientific approach.<sup>6</sup> Since then, international relations scholars have held to the tenet that intellectual progress depends on rigorous theory and systematic empirical testing; that is, better theory and better methods of theory testing are necessary for the field to be relevant to policy makers and those concerned with foreign policy issues. The presumption is that policy makers would make better decisions if they could identify the causal forces that drive international relations and foreign policy.<sup>7</sup>

It is within this context that realism emerged as the favored approach to the study of international relations.<sup>8</sup> Realists assume the structure of the international system is defined by the formal arrangement and position of states within that system. The primary

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<sup>5</sup> Morton Kaplan, *System and Process in International Politics* (New York: Wiley, 1957); Hans Morgenthau, *Politics among Nations: The Struggle for Power and Peace* (New York: Free Press, 1967); Kenneth N. Waltz, *Man, the State, and War* (New York: Columbia University, 1979); and Chris Brown and Kirsten Ainley, *Understanding International Relations*, 3<sup>rd</sup> ed. (New York: Palgrave MacMillan, 2005).

<sup>6</sup> See for example, David J. Singer, "The Incomplete Theorist: Insight without Evidence," in *Contending Approaches to International Politics*, ed. James N. Rosenau and Klaus Knorr (Princeton, NJ: Princeton University, 1969).

<sup>7</sup> Jeffrey A. Friedan and David A. Lake, "International Relations as a Social Science: Rigor and Relevance," *ANNALS of the American Association of Political and Social Science* 600 (July 2005):137.

<sup>8</sup> Joseph S. Nye Jr. and Sean M. Lynn-Jones, "International Security Studies: A Report of a Conference on the State of the Field," *International Security* 12 (Spring1988): 8. Two primary schools of realist thought were elaborated by Hans Morgenthau (political) and Kenneth Waltz (structural), but we will not distinguish between these schools here.

attribute of the system is that it lacks central authority. Anarchy “provides both the motivating rationale for state behavior as well as the ontological essence that drives international policies – the search for security in a hostile, violence prone, self-help international system.”<sup>9</sup> In this environment, self-preservation is of primary importance.<sup>10</sup> Because self-preservation is subject to each state’s position within the system, and is dependent upon the distribution of power, states must constantly compete for power.<sup>11</sup>

During the Cold War, realism provided a means for understanding the on-going power struggle between the United States and the Soviet Union (and other communist states) and proposed that balance of power is a necessary condition for peace. Upon the collapse of the Soviet Union, the United States emerged as the dominant power and some scholars began to suggest that realism had lost its explanatory power.<sup>12</sup> But Waltz defended the realist approach by emphasizing that unipolarity is the “least durable of

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<sup>9</sup> Darryl S.L. Jarvis, “Multinational Enterprises, International Relations and International Business: Reconstituting Intellectual Boundaries for the New Millennium,” *Australian Journal of International Affairs* 59 (June 2005): 205.

<sup>10</sup> Paul R. Viotti and Mark Kauppi, eds., *International Relations Theory: Realism, Pluralism, Globalism and Beyond* (Boston: Allyn and Bacon, 1999), 55-57.

<sup>11</sup> Kenneth N. Waltz, “Realist Thought and Neorealist Theory,” *Journal of International Affairs* 44, no. 1 (Spring/Summer 1990): 21-38; and Hans Morgenthau, *Politics among Nations: The Struggle for Power and Peace* (New York: Free Press, 1967).

<sup>12</sup> Stefano Guzzini, “The Enduring Dilemmas of Realism in International Relations,” *European Journal of International Relations* 10, no. 4 (December 2004): 533-568; Margarita H. Petrova, “The End of the Cold War: A Battle or Bridging Ground between Rationalist and Ideational Approaches in International Relations?” *European Journal of International Relations* 9, no. 110 (March 2003): 115-163; and Charles W. Kegley, Jr., “The Neoidealist Moment in International Studies? Realist Myths and the New International Realities,” *International Studies Quarterly* 37 (June 1993): 131-146.

international configurations” – just as “nature abhors a vacuum, so international politics abhors unbalanced power” – and so the power struggle will continue.<sup>13</sup> Therefore, when China initiated its “open door” policy and began the journey towards rapid economic development, realists began to view this policy as a strategy for global expansion and an effort to tip the balance of power in China’s favor.

Although realism is compelling for its parsimony and its ability to explain the dynamics of states vying for power within an international system, its adherents have recognized that the international system is simply one factor “shaping and shoving” foreign policy.<sup>14</sup> There is also a need to open the “black box” of domestic politics and look at the various domestic systems and institutions that contribute to the formation of states’ foreign policies.<sup>15</sup> This is especially the case in trying to understand why the U.S. Congress reacted so vehemently to CNOOC’s proposed acquisition of Unocal, and to

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<sup>13</sup> Kenneth N. Waltz, “Structural Realism after the Cold War,” *International Security* 25 (Summer 2000): 28; and Michael Mastanduno, “Preserving the Unipolar Moment: Realist Theories and U.S. Grand Strategy after the Cold War,” *International Security* 21 no. 4 (Spring 1997): 88.

<sup>14</sup> Kenneth N. Waltz, *Man, the State, and War* (New York: Columbia University, 1979), 70-72; and Kenneth N. Waltz, “Reflections on *Theory of International Politics*: A Reply to My Critics,” in *Neorealism and its Critics*, ed. Robert O. Keohane (New York: Columbia University, 1986), 322-46.

<sup>15</sup> G. John Ikenberry, David A. Lake, and Michael Mastanduno, “Introduction: Approaches to Explaining American Foreign Economic Policy,” *International Organization* 42 (Winter 1988): 5; Stacie E. Goddard and Daniel N. Nexon, “Paradigm Lost? Reassessing Theory of International Politics,” *European Journal of International Relations* 11 (March 2005): 24; Sheldon W. Simon, “Is there a U.S. Strategy for East Asia?” *Contemporary Southeast Asia: A Journal of International & Strategic Affairs* 21 (December 1999): 325-343; and Peter A. Gourevitch, “The Second Image Reversed: The International Sources of Domestic Politics,” *International Organization* 32 (Autumn 1978): 882, 901.

understand how Congress was able to achieve a consensus to block the acquisition with speed which is uncharacteristic of the fragmented system of American policy making.

## **B. New Institutionalism**

To understand the role that domestic political institutions play in facilitating or inhibiting financial transactions in a global economy we turn to the analytical approach of new institutionalism. New institutionalism delves into the “black box” of domestic politics by looking at institutions as mechanisms for channeling and constraining individual behavior and shaping policy outcomes. Because new institutionalism places the “black box” within the context of the larger world, this approach allows us to integrate our analysis of U.S. domestic politics with the twenty-first century global environment characterized by China’s expanded approach to economic development and America’s new emphasis on homeland security.

The theoretical approach of “new institutionalism” first emerged in response to the shortcomings of realism and other strains of thought which diminished the importance of political values and collective choice. March and Olsen observed that the ideas behind this new approach

deemphasize the dependence of the polity on society in favor of an interdependence between relatively autonomous social and political institutions; they deemphasize the simple primacy of micro processes and efficient histories in favor of relatively complex processes and historical inefficiency; they deemphasize metaphors of choice and allocative outcomes in favor of other logics of action and the centrality of meaning and symbolic action.<sup>16</sup>

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<sup>16</sup> James G. March and Johan P. Olsen, “The New Institutionalism: Organizational Factors in Political Life,” *The American Political Science Review* 78 (September 1984): 738.

Although “far from coherent or consistent,” new institutionalism claims a “more autonomous role for political institutions” without denying the importance of social context of politics, the economy, or the motives of individual actors.<sup>17</sup>

As interest in this approach increased, attempts at theory building were so extensive and so diverse that it became unclear as to what exactly new institutionalism was, how it could be distinguished from other approaches, and how it could be measured.<sup>18</sup> Hall and Taylor proposed that some of the ambiguities could be dismissed by recognizing that institutionalism is not one unified body of thought. Instead, they suggested the three schools of thought emerged to “elucidate the role that institutions play in the determination of social and political outcomes.”<sup>19</sup> While it would be beyond the scope of this dissertation to fully elucidate these approaches, a brief summary of the three bodies of thought is relevant to the development of our theoretical framework.

The first approach, historical institutionalism, seeks to improve upon political theories which focus on micro-analysis by “bringing the state back” into the discussion.<sup>20</sup> Although influenced by the structural-functionalist view that the polity is a system of interacting parts historical institutionalism does not accept the idea that individuals are

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<sup>17</sup> March and Olsen, 738.

<sup>18</sup> B. Guy Peters, *Institutional Theory in Political Science: The ‘New Institutionalism’* (New York: Continuum Press, 2005), 44.

<sup>19</sup> Peter A. Hall and Rosemary C.R. Taylor, “Political Science and the Three New Institutionalisms,” *Political Studies* 44, no. 5 (December 1996): 936.

<sup>20</sup> Theda Skocpol, “Bringing the State Back In: Strategies of Analysis in Current Research,” in *Bringing the State Back In*, ed. Peter B. Evans, Dietrich Rueschemeyer, and Theda Skocpol (Cambridge: Cambridge University, 1985), 9.

the driving force.<sup>21</sup> Instead, historical institutionalism builds upon theories that assign importance to formal political institutions by examining them during their formative periods.<sup>22</sup> The premise is that history is important because institutions create a system of collective values as they are being formed and these values are embedded in the structures of the institutions and thereby affect the policy-making process.<sup>23</sup> One needs an understanding of institutional legacies in order to fully understand subsequent policy outcomes.<sup>24</sup>

Over time, historical institutionalism evolved into a complex framework centered on the impact of formal administrative and political institutions on policymaking. According to Skocpol, this approach “views the polity as the primary locus of action, yet understands political activities, whether carried out by politicians or by social groups, as conditioned by the institutional configurations of governments and political party

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<sup>21</sup> See Gabriel Almond and G. Bingham Powell, *Comparative Politics: A Developmental Approach* (Boston: Little, Brown, 1966) for a comprehensive discussion of the structural-functional view.

<sup>22</sup> Harry Epstein and David Apter, eds., *Comparative Politics* (Glencoe, IL: Free Press, 1963).

<sup>23</sup> Aaron Wildavsky, “Choosing Preferences by Constructing Institutions: A Cultural Theory of Preference Formation,” *American Political Science Review* 81 (March 1987):12; and Peter A. Hall and Rosemary C.R. Taylor, “Political Science and the Three New Institutionalisms,” *Political Studies* 44, no. 5 (December 1996): 938.

<sup>24</sup> Daniel Béland, “Ideas, Interest, and Institutions: Historical Institutionalism Revisited,” in *New Institutionalism*, ed. André Lecours (Toronto: University of Toronto Press, 2005), 29; B. Guy Peters and Jon Pierre, “Institutions and Time: Problems of Conceptualization and Explanation,” *Journal of Public Administration Research and Theory* 8, no. 4 (1998): 570-71; and Peter A. Hall and Rosemary C.R. Taylor, “Political Science and the Three New Institutionalisms,” *Political Studies* 44, no. 5 (December 1996): 940-41.

systems.”<sup>25</sup> Rather than focusing exclusively on state autonomy, Skocpol suggests that institutionalism should focus on four factors:

(1) the establishment and transformation of state and party organization...; (2) the effects of political institutions and procedures on the identities, goals, and capacities of social groups...; (3) the “fit” – or lack thereof – between goals and capacities of various politically active groups, and the historically changing points of access and leverage allowed by a nation’s political institutions; and (4) the way in which previously established social policies affect subsequent politics.<sup>26</sup>

By contrast, the second approach of rational choice institutionalism was largely inspired by the application of conventional rational choice assumptions to the study of congressional behavior. Assuming that individuals tend to make decisions based on maximizing utility, legislators have multiple preferences, and political issues are multidimensional, rational choice theorists have tended to conclude that it would be quite difficult to achieve the majority votes needed to pass legislation in Congress.<sup>27</sup> But, as Hall and Taylor point out, empirical research shows the opposite; there is a strong tendency towards stability in congressional decision making.<sup>28</sup>

To resolve this paradox, rational choice institutionalism focuses on “the importance of institutions as mechanisms for channeling and constraining individual

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<sup>25</sup> Theda Skocpol, *Protecting Soldiers and Mothers: The Political Origins of Social Policy in the United States* (Cambridge, Mass.: Harvard University Press, 1992), 41.

<sup>26</sup> Theda Skocpol, *Protecting Soldiers and Mothers, The Political Origins of Social Policy in the United States*, 41; Daniel Béland, “Ideas, Interest, and Institutions: Historical Institutionalism Revisited,” 32.

<sup>27</sup> Peter A. Hall and Rosemary C.R. Taylor, “Political Science and the Three New Institutionalisms,” *Political Studies* 44, no. 5 (December, 1996): 942-43.

<sup>28</sup> *Ibid.*, 943.



behavior.”<sup>29</sup> Individual actors are still expected to maximize their personal utilities, but they are constrained by institutional structure, rules and procedures.<sup>30</sup> Or, as Ostrom suggests, rational actors are “fallible learners” who will engage in a “continuous trial-and-error process until a rule system is evolved that participants consider yields substantial net benefits.”<sup>31</sup> Either way, institutions tend to be characterized by the majority of actors, rather than any one individual.

Rational choice theorists suggest individuals define their goals and preferences independent of, but subject to the constraints of, institutions. Proponents of this approach emphasize that it allows political actors to have multiple goals.<sup>32</sup> For example, individual legislators may be motivated by a desire to be re-elected, the need to secure campaign contributions, aspirations for power or position within the legislature, and ideological commitment to specific policy outcomes at the same time that they are subject to constraints imposed by legislative coalitions and committee membership and their political party.<sup>33</sup> Rational choice institutionalism is attractive because it helps us

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<sup>29</sup> B. Guy Peters, *Institutional Theory in Political Science: The ‘New Institutionalism’* (New York: Continuum Press, 2005), 49.

<sup>30</sup> Kenneth A. Shepsle, “Studying Institutions: Some Lessons from the Rational Choice Approach,” *Journal of Theoretical Politics* 1, no. 2 (1989): 131-47.

<sup>31</sup> Elinor Ostrom, “A Behavioral Approach to the Rational Choice Theory of Collective Action,” *American Political Science Review* 92 (March, 1998): 8.

<sup>32</sup> Elisabeth R. Gerber, “Legislatures, Initiatives, and Representation: The Effects of State Legislative Institutions on Policy,” *Political Research Quarterly* 49 (June 1996): 266.

<sup>33</sup> Robert Dahl, *Democracy and Its Critics* (New Haven, CT: Yale University Press, 1989); David Mayhew, *Congress: The Electoral Connection* (New Haven, CT: Yale University Press, 1974); Anthony Downs, *An Economic Theory of Democracy* (New

understand how political actors respond to the incentives and constraints introduced by their institutions at the same time that it permits us to see how individuals have an interest in shaping institutions to meet their personal goals.

Scott asserts that the third approach of sociological institutionalism disagrees with the rational choice perspective and suggests that the institutional forms and procedures of modern organizations are the result of cultural values and practices.<sup>34</sup> Sociological institutionalism defines institutions broadly to include “symbol systems, cognitive scripts, and moral templates” that guide human actions.<sup>35</sup> This approach also focuses on the interactive relationship between institutions and individual actions. Although actors may be purposive or rational, institutions influence their behavior by providing scripts to follow, and actors influence institutions by asserting their preferences.<sup>36</sup>

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York: Harper and Row, 1957); Thomas Romer and James M. Snyder Jr., “An Empirical Investigation of the Dynamics of PAC Contributions,” *American Journal of Political Science* 38 (1974): 745-69; Kevin B. Grier and Michael C. Munger, “Committee Assignments, Constituent Preferences, and Campaign Contributions,” *Economic Inquiry* 29 (1992): 24-43; Richard R. Fenno, Jr., *Congressmen in Committees* (Boston: Little, Brown and Company, 1973); and Gary W. Cox and Matthew D. McCubbins, *Legislative Leviathan: Party Government in the House* (Berkeley: University of California Press, 1993).

<sup>34</sup> W.R. Scott, *Institutions and Organizations* (Thousand Oaks, CA: Sage, 1995).

<sup>35</sup> Peter A. Hall and Rosemary C.R. Taylor, “Political Science and the Three New Institutionalisms,” *Political Studies* 44, no. 5 (December, 1996): 947.

<sup>36</sup> B. Guy Peters and Jon Pierre, “Institutions and Time: Problems of Conceptualization and Explanation,” *Journal of Public Administration Research and Theory* 8 no. 4 (1998): 566; Peter A. Hall and Rosemary C.R. Taylor, “Political Science and the Three New Institutionalisms,” *Political Studies* 44, no. 5 (December 1996): 948-50; and Donald D. Searing, “Roles, Rules, and Rationality in the New Institutionalism,” *The American Political Science Review* 85 (December 1991): 1241.

In comparing these approaches, scholars have emphasized both similarities and differences. For example, Thelen focuses on distinguishing rational choice institutionalism from historical institutionalism. She suggests that rational choice theorists, working at the mid-range of theory building, often attempt to develop grand theories with more general theoretical claims; whereas, theorists who adopt historical institutionalism often focus on a limited range of cases that are unified in space and/or time.<sup>37</sup> Thelen identifies another difference in the approaches to hypothesis building. While rational choice theorists derive their research questions from situations in which observed behavior seems to deviate from theoretical expectations, historical institutionalism theorists often begin with questions that emerge from observed events.<sup>38</sup>

Although both approaches are interested in identifying and understanding regularities in politics over time, Thelen concludes the main distinction is that the rational choice approach emphasizes coordinating functions and equilibrium order while the historical approach emphasizes historical process. Rational choice theorists see institutions as holding together a particular pattern of politics while historical institutionalism theorists tend to reverse causality to suggest that institutions “emerge from and are sustained by features of the broader political and social context.”<sup>39</sup>

The exercise of distinguishing among different approaches to new institutionalism has value in trying to isolate the theory’s essential elements, but the risks associated with

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<sup>37</sup> Kathleen Thelen, “Historical Institutionalism in Comparative Politics,” *Annual Review of Political Science* 2 (1999): 373.

<sup>38</sup> *Ibid.*, 373-74.

<sup>39</sup> *Ibid.*, 384.

this exercise are dilution of the theoretical richness and loss of its explanatory powers. For example, although the rational choice approach may lend insight into individual decision making within the institutional context, the impact of individual decision making on political outcomes may not be understood without understanding the institutional structure and functions. Similarly, the study of an institution's historical evolution may provide insight into institutional constraints, but it may not be able to explain why individual actors within an institution prefer certain choices over others or why some actors may have greater ability to influence colleague's choices than others.

Rather than distinguishing among the three approaches to new institutionalism, this study is based on the assumption that there are common elements in the institutional research to suggest a unified theory. It suggests that the theoretical core includes the significance of an institution's history and infusion of societal values that affect the institution's role within the polity. Within this context, the focus is on the "black box" where formal rules govern yet informal mechanisms shape and filter political interests in order to produce policy outcomes.<sup>40</sup> The general framework for looking into the "black box" of domestic politics is described below.

## **II. THEORETICAL FRAMEWORK**

### **A. An Integrated Theoretical Approach to U.S. – China Foreign Policy**

Institutionalism refers to an approach to the study of political institutions which includes a set of ideas and hypotheses concerning the relations between institutional

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<sup>40</sup> Ellen M. Immergut, "The Theoretical Core of the New Institutionalism," *Politics and Society* 26 (March 1998): 25.

characteristics and political actors. It assumes that institutions are shaped by history and infused with shared values that influence their structures, rules, and standards. These endogenous characteristics create stability and predictability needed for long term planning. At the same time that these formal structures, rules, and standards facilitate the actions of political actors, they also create constraints. As a result, political actors will tend to adapt, but one way that they adapt is to rely upon informal mechanism for creating policy change.

This dissertation develops an integrated theory by adopting core elements of the historical, rational choice, and sociological approaches to new institutionalism that were discussed in the literature review above. The following premises constitute the core elements of the theoretical framework:

1. The premise that history is important because institutions create a system of collective values during their formative stage, and these values are embedded in institutional structures that affect the policy making process.

2. The premise that institutional actors tend to base decisions on maximizing utility, but political issues are complex and multidimensional, and institutional actors must constantly weigh multiple preferences.

3. The premise that democratic institutions are characterized by formal constraints that provide institutional stability, but allow for informal mechanisms that permit individual actors to assert their own preferences in the decision making process.

4. The premise that the success of an individual legislator in Congress overcoming institutional constraints that impact foreign policy making depends upon

manipulation of a variety of factors, including: (a) public awareness, (b) constituent and party support, (c) coalition building, (d) presidential support, and (e) timing.

This approach to institutionalism suggests that policy change is incremental and gives weight to the significance of previously enacted laws. In explaining how policy change takes place, the dissertation considers the content of existing law and legislative proposals as well as the reasons why individual actors conceived of or chose to support various policy alternatives. By grasping the motivation behind the actors' policy choices, it will be possible to gain a better understanding of the strategies that the actors develop to persuade others to support their policy alternatives. One of the best ways to get at the heart of policy initiatives is to analyze the actors' discourse.<sup>41</sup>

The dissertation's theoretical approach assumes that when corporations enter into the global capitalist market, they organize their economic activities so as to maximize profits. This assumption holds true regardless of whether the corporation is private enterprise or a jointly-owned public/private entity. A corollary of this assumption is that corporations are motivated to manage risk in the global capitalist market and that they have a variety of strategies at their disposal. Some of the risks are political and social instability, bureaucratic complications, local interference with national laws, high fees and administrative charges, undeveloped infrastructure, and supply problems. Risk management strategies include encouraging the country of origin to establish stable diplomatic relations with the host country, encouraging the host country to improve the

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<sup>41</sup> Daniel Béland, "Ideas, Institutions, and Policy Change," *Journal of European Public Policy* 15, no. 5 (August 2008): 701-04.

legal environment for foreign investment in local enterprises, relying upon the protections provided by international law, crafting creative financial arrangements for doing business within the host country, and integrating foreign capital, labor, and other resources into the enterprises operations within the host country.<sup>42</sup>

The approach also assumes that foreign policy decisions do not take place within a vacuum; they are influenced by the international environment as well as the domestic environment. One of the most outstanding characteristics of the international environment in 2005 was China's emergence as a major economic power. After a decade of explosive growth, there was no indication that China's economy would break pace with its impressive track record. In fact, China's foray into the capitalist world economy had become so successful in stimulating the domestic economy that it became part of a comprehensive strategy for developing geopolitical alliances that was virtually inconceivable when communist China and capitalist America first entered into diplomatic talks under the Nixon Administration.

Another feature dominating the global environment in 2005 was the U.S. war on terror which followed the September 11, 2001 terrorist attack on the World Trade Center. For the first time in recent memory American citizens had been subjected to a sense of vulnerability and fears of subsequent attacks on their homeland. As a result, national security took on a new meaning in the American psyche and came to play a new and more prominent role in both domestic and foreign policy making.

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<sup>42</sup> Zhu Ang, "China's Investment Environment, Laws, and Regulations," in *China's Energy and Mineral Industries: Current Perspectives*, ed. James P. Dorian and David G. Freidley (Boulder, CO: Westview Press, 1988), 128-130 discusses the advantages and disadvantages of the investment environment in China.

This global environment has set the stage for our inquiry into why Congress politicized CNOOC's business proposal to acquire the underperforming Unocal Corporation. The research questions that we address in the study are as follows:

1. What are the roles and responsibilities of the executive and legislative branches in overseeing foreign mergers, acquisition, or takeovers?
2. What laws may the president or Congress invoke in order to block a particular foreign merger, acquisition, or takeover?
3. Are there different laws and procedures for blocking a foreign merger, acquisition or takeover for economic reasons as opposed to national security concerns?
4. If one branch of government perceives either an economic or a national security threat and the other branch does not, must the branch perceiving the threat obtain consent or support from the other branch in order to prevent the merger, acquisition or takeover?
5. Are there certain situations in which one branch or the other may act independently?
6. What mechanisms did Congress employ to block CNOOC's proposed acquisition of Unocal?
7. What role did individual legislators play in the attempt to block the deal and what were their individual beliefs as to why the deal needed to be blocked?
8. Since Congress is comprised of independent actors, and the policy making process is fragmented, how can Congress influence executive action when current laws do not require action and a threat is deemed imminent?



## **B. Methodology**

This study uses historical research methodology which focuses on analysis of original documents. Since the study is concerned with identifying the constraints that political institutions create and the opportunities for implementing policy change the researcher sought sources of data that would provide specific content of the policy proposals that the actors promoted. This data was found in the following types of documents: (1) legal sources such as the Constitution, statutes, and judicial opinions; (2) official government documents such as congressional reports, white house papers, and administrative rules; and (3) presidential and legislative testimonials found in published biographies. The study supplements these original sources with secondary sources including media sources such as newspapers, magazines, radio/television transcripts, and public opinion polls; peer-reviewed journals; and think tank publications.

Initially, the research design included a survey instrument that was sent to all members of the 109<sup>th</sup> Congress. The survey included both multiple choice and open-ended questions designed to be broad in nature to provide interviewees latitude in prioritizing and bringing out issues of greatest importance to them. Although some legislators responded, there was an overwhelming reluctance to participate in a written survey, or to respond to follow-up telephone calls or email inquiries from anyone other than members of their own congressional districts.

The survey was attempted during an election year and the responses support the author's hypothesis that legislators' individual actions are driven primarily by the desire for re-election. This motive leads legislators to focus their individual policy agendas on

issues perceived to be of priority to their constituents. Since the survey response was not statistically significant, the study relies upon the sources of data described above. Any comments received from legislators will be treated as anecdotal and will be reinforced by documentary evidence.

While direct access to the president and executive staff would have been ideal, it was not possible given the president's leadership style and the confidential treatment of foreign business transactions within the White House. Foreign policy and international relations scholars have long encountered similar difficulties in acquiring detailed information about the decision making process. The information is hard to find and often incomplete. In recent years, there has been an information explosion with increased access to information over the World Wide Web, but care must be taken to ensure authenticity of the information. At the same time, the media has become much more involved in interviewing individuals involved in the decision-making process and in analyzing their decisions. There has also been an increase in autobiographies in which decision makers feel a need to document their own actions and perceptions of the process.<sup>43</sup> These secondary sources added to interpretation of the political environment, but our analysis primarily relies on official White House documents, press releases, and statements to the media.

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<sup>43</sup> Ryan K. Beasley, Juliet Kaarbo, Charles F. Hermann, and Margaret G. Hermann. "People and Processes in Foreign Policymaking: Insights from Comparative Case Studies," *International Studies Review* 3 (Summer 2001): 217-250; reprinted in *Leaders, Groups, and Coalitions*, ed. Joe D. Hagan and Margaret G. Hermann (Blackwell Publishers, 2002).

### III. CONCLUSION

This chapter suggests that CNOOC unleashed a “perfect storm” in 2005 when it proposed to purchase American-owned Unocal Corporation. Although CNOOC claimed the bid was simply a business transaction, members of Congress claimed it was a threat to national security and immediately called upon President Bush to invoke his Exon-Florio authority to prevent the transaction. On the surface, it appeared to the Chinese that Congress politicized the CNOOC bid to prevent China from developing its economy. This study questions why Congress felt compelled to intervene in this particular business proposition.

Traditional international relations theories which assume foreign policy is based upon a struggle for power cannot explain how domestic politics influence a nation’s foreign policy decisions. For this, the study turns to the approach of new institutionalism which focuses on an examination of what happens within the “black box” of domestic policy making. The study suggests that an understanding of institutional constraints and the mechanisms that institutional actors employ to overcome these constraints may lend insight into foreign policy making and help explain why some foreign policy issues are politicized while others are not.

The study adopts a socio-historical approach to new institutionalism which requires the laying of a foundation for the analysis by placing the event of CNOOC’s bid for Unocal within the context of that particular point in history. Chapter 2 describes China’s rapid and continuous economic growth, the energy resources needed to maintain this growth, and the disparity between demand and domestic supplies. The facts indicate

that China has no alternative but to look outside its borders for access to energy supplies that will continue fueling economic development.

The socio-historical approach also assumes institutions are infused with values and that these values influence the institution's structures, rules, and standards, and ultimately the leaders' decision making processes. Chapter 3 examines the historical processes which have shaped American political institutions. It discusses how these institutions have been infused with values that transcend the values of any one individual within the institutions, and how these values are essential to the survival and expansion of the capitalist economy.

In crafting the American Constitution, the Founding Fathers established an institutional structure which provided political stability. The Constitution also defined separate powers for the executive and legislative branches, but incorporated a system of "checks and balances" which prevents either one of the institutions from becoming too powerful. As a result, policy making in the United States is fragmented and inefficient and often times difficult to predict. When CNOOC contemplated its bid for Unocal, the corporation focused on the business opportunity but failed to foresee that the bid would become entangled in an institutional struggle between Congress and the president over foreign policy powers.

Chapter 4 discusses the details of the Unocal case. It begins with the laws that govern mergers and acquisitions in the United States and focuses specifically on the Exon-Florio Amendment. An examination of the 2005 congressional hearings indicates that the Exon-Florio Amendment, and Congress's concern about how it had been

interpreted and implemented by the presidency, was at the heart of the Unocal acquisition controversy. The analysis in this chapter shows how informal mechanisms and strategies serve as a means of overcoming the institutional inefficiencies of the American political system.

Sometimes these mechanisms operate within the “black box” of policy making in Congress and, in spite of laws requiring transparency, may be hidden from public scrutiny. Even though we may never be able to discover all the details of deals that are negotiated in private, we may acquire more insight into the policy outcomes through case studies that analyze the informal methods that key decision makers use to accomplish their policy goals.

Chapter 5 draws conclusions as to why and how some members of Congress used informal mechanisms available to them to politicize the CNOOC bid for Unocal. Extending the analysis beyond the House of Representative’s enactment of Resolution 344 (which focused on preventing CNOOC from acquiring Unocal and received so much press) provides for greater understanding as to why politicization of CNOOC’s proposal was instrumental to achieving long-sought statutory changes in the Exon-Florio provisions. In 2006, as Congress was debating an amendment to Exon-Florio to provide greater oversight of presidential authority over foreign acquisitions, United Arab Emirates-owned Dubai Ports World attempted to control Peninsular and Orient Steam Navigation, a British company that operated terminals at several American ports. This case study shows how politicization of CNOOC’s bid for Unocal helped Congress defeat

the Dubai Ports World acquisition and set the stage for future legislative oversight of foreign acquisitions of American corporations.

## CHAPTER TWO: THE UNOCAL PUZZLE

### I. CHINA'S DEVELOPMENT STRATEGY

#### A. Entering the Global Economy

Self-reliance had been a major strategic priority for nearly three decades under Mao's leadership. Then in the late 1970s after Deng Xiaoping came to power, China's leadership began to look outward for economic growth.<sup>44</sup> Exhausted by the disruptions and uncertainties of perpetual political campaigns, the Chinese people embraced the idea of stabilizing their economy and raising their standard of living to levels enjoyed by the world's more developed countries. At the Third Plenum of the Eleventh Congress in December 1978, the Chinese Communist Party initiated a "fundamental change in its domestic as well as its foreign policy priorities."<sup>45</sup> These changes required an openness that had not been seen for decades as exemplified by the State Statistical Bureau's 1979

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<sup>44</sup> Philip Andrews-Speed, Xuanli Liao, and Roland Dannreuther, *Strategic Implications of China's Energy Needs* (New York: Oxford University Press, 2000), 53; Stanley Lubman, "Through a Glass, Dimly," *Problems of Post-Communism* 47, no. 2 (March/April 2000): 34; and Philip Andrews-Speed and Sergei Vinogradov, "China's Involvement in Central Asian Petroleum: Convergent or Divergent Interests?" *Asian Survey* 40, no. 2 (March/April 2000): 379.

<sup>45</sup> Chen Zhimin, "Nationalism, Internationalism and Chinese Foreign Policy," *Journal of Contemporary China* 1, no. 42 (February 2005): 460.

publication and widespread distribution of national economic data which was a first step towards greater transparency in the Chinese economy.<sup>46</sup>

The Party confirmed its backing of economic liberalization at the 1980 National People's Congress by appointing Zhao Zhiyang as prime minister and Hu Yaobang as secretary-general of the Party. Zhao Zhiyang called for abandoning "once and for all" the idea of self-reliance and urged the nation to enter the world markets.<sup>47</sup> Secretary-general Hu Yaobang proclaimed China's foreign policy should be based on the principles of "independence and peace," that is, independence to pursue relationships that would promote China's economic goals and a peaceful environment that would not threaten China's national security.<sup>48</sup>

The leadership endorsed gradual transformation from a centrally planned economy toward a more market-based economy as they pursued policies that would accelerate economic growth and lead to higher standards of living.<sup>49</sup> Although state-owned industries continued to dominate key sectors, the government began to privatize small and medium sized state-owned enterprises and allow the emergence of a non-state sector led by private entrepreneurs. The private sector continued to grow, and by 2001, the International Monetary Fund (IMF) estimated that the non-state sector accounted for

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<sup>46</sup> The author discussed the significance of this publication with the faculty at Nankai University in 1980 and with Xu Ming, professor at the Graduate School of Chinese Academy of Social Sciences and visiting scholar at the University of Denver.

<sup>47</sup> *China Business Review* 8, no. 6 (November/December 1981): 51.

<sup>48</sup> Chen Zhimin, "Nationalism, Internationalism and Chinese Foreign Policy," 460.

<sup>49</sup> Constitution of the People's Republic of China, *Beijing Review* (1982): 25.



three-fourths of industrial output, approximately half of gross domestic product, and 60 percent of nonagricultural employment.<sup>50</sup>

Since recovering a seat in the United Nations,<sup>51</sup> China has established economic, political, and cultural relations with capitalist nations world-wide and has become increasingly integrated into the global economy. But membership in nongovernmental organizations (NGOs), such as the IMF, the World Bank (WB), and its affiliate, the International Development Association (IDA), the World Trade Organization (WTO), and the ASEAN Regional Forum, has been accompanied by very strict conditions.<sup>52</sup> These conditions, in turn, have led to liberalization of trade and investment which accompanies capitalist management practices, borrowing technological innovations, and engaging in joint ventures with foreign business partners.<sup>53</sup> In spite of occasional menacing rhetoric, China's leadership has focused on diplomacy rather than costly military activities to accomplish economic development goals.<sup>54</sup>

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<sup>50</sup> U.S. Department of State (2002), 2.

<sup>51</sup> See United Nations, General Assembly Official Records of the 26<sup>th</sup> Session, 1971.

<sup>52</sup> W. Klatt, "Chinese Statistics Updated," *China Quarterly* 84 (December 1980):737-738.

<sup>53</sup> U.S. Department of Energy, Energy Information Administration, *Country Analysis Briefs: China*, (Updated August 2006), available at <http://www.eia.doe.gov/cabs/china/pdf.pdf> (accessed March 28, 2009).

<sup>54</sup> Fareed Zakaria, "Is Robert Gates a Genius?" *Newsweek* (April 20, 2009): 29. Even with what is characterized as a military push, four years after the Unocal event, China's defense budget was \$70 billion compared to the U.S. defense budget of \$655 billion.

China's economy began to take off almost immediately after adopting the "open-door" policy which sought foreign investment as a means of stimulating the economy.<sup>55</sup> From 1980 to 2005, China reports that its GDP grew at an average rate of 9.6 percent (adjusted) per year, reaching 1,823 trillion yuan (2.23 trillion U.S. dollars).<sup>56</sup> The IMF estimates that GDP based on purchasing-power-parity per capita GDP grew from \$419 in 1980 to \$6,193 in 2005.<sup>57</sup> The United Nations (UN) estimates that per capita income has grown from less than \$400 in the 1980s, to an estimated \$1,500 - \$3,000 in 1993.<sup>58</sup> Rural per capita income alone has grown by a factor of more than four in the last thirty years, reaching \$1,700 in 2007.<sup>59</sup>

Foreign trade and investment increased significantly after the Chinese government established Special Economic Zones (SEZs). In 1950, the total value of China's imports and exports was about \$1.1 billion, less than one percent of total world

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<sup>55</sup> International Energy Agency, *China's Worldwide Quest for Energy Security* (Paris: International Energy Agency, 2006), 13–43 provides an overview of modern China's foreign investment policy.

<sup>56</sup> *People's Daily*, January 10 and January 26, 2006. Hereafter, references to dollars (\$), throughout this dissertation will be to U.S. dollars, unless otherwise specified

<sup>57</sup> International Monetary Fund, *World Economic Outlook* (Washington, D.C.: IMF, 2005), available at <http://www.imf.org/external/pubs/ft/weo/2005/02data/docssubm.com> (accessed March 29, 2009).

<sup>58</sup> United Nations Development Programme, *Human Development Report* (New York: UN, 1993); and International Monetary Fund, *World Economic Outlook* (Washington D.C.: IMF, May 1993).

<sup>59</sup> Khalid Malik, Opening Address at the Launch of *China Human Development Report*, (November 16, 2008) Beijing, available at <http://www.undp.org.cn/modules> (accessed on March 28, 2009).

trade. Although world trade experienced a six-fold increase from 1950 to 1978, China's total share of that world trade stagnated due to disruptions caused by Mao zedong's political campaigns.

In the eight years after China introduced the open door policy, the state approved 8,332 foreign-funded enterprises and committed \$19.14 billion to foreign investment.<sup>60</sup> From 1978 to 2003 the country's trade increased at an average annual rate of fifteen percent, and its share of total world trade increased from less than one percent to more than five percent, while its national ranking in world trade (merchandise) jumped from thirty-second place in 1978 to third place in 2004.<sup>61</sup>

By 2004, the government had begun encouraging foreign investment by allowing foreigners to establish investment corporations in China. The only qualifications were "fine credit and economic strength" (which consisted of meeting stipulated financial requirements, such as the total sum of \$400 million property the year before applying to invest in China), more than ten foreign invested enterprises, and invested sum of registered capital actually paid of more than \$10 million in China.<sup>62</sup> During 2004, trade and investment deals were made with Thailand, Malaysia and eight other Southeast Asian

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<sup>60</sup> Zhu Ang, "China's Investment Environment, Laws, and Regulations," in *China's Energy and Mineral Industries: Current Perspectives*, ed. James P. Dorian and David G. Fridley (Boulder, Westview Press, 1988), 127.

<sup>61</sup> See *Collection of Statistics of Foreign Economic Relations and Trade of China*, 2001; *China Statistical Abstract*, 2002; and WTO, *International Trade Statistics*, 2005 for detailed data concerning China's growth over this period of time.

<sup>62</sup> "Foreign Investors Can Establish Investment Company," *China Chemical Reporter* 15, no. 34 (December 6, 2004): 4.

countries and by 2005 China had opened free-trade talks with South Korea, Pakistan, Australia and Iceland.

In 2004, China surpassed the United States as Japan's largest trading partner. But historical animosities over Japan's occupation of China during World War II kept the relationship from blossoming. In addition, the two Asian countries were competing over access to Siberian oil and China lost the larger prize. Then tensions began to escalate when China began oil exploration in the South China Sea where Japan had claims of sovereignty.<sup>63</sup> This heightened the concern in Beijing regarding military protection for China's access to oil.

In addition to Asia, the Chinese government has also established a foothold in the developing countries in Africa and Latin America. In 2000, the China-Africa Cooperation Forum was formed to promote trade and investment in forty-four African countries.<sup>64</sup> Since then, several high level delegations have visited the continent and Beijing has negotiated partnerships with governments in the Angola, Nigeria, Chad,

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<sup>63</sup> U.S. Congressional Research Service, *China-U.S. Relations in the 109<sup>th</sup> Congress*, (RL32804; December 31, 2006), by Kerry Dumbaugh, (Washington, D.C., 2006), 15, LexisNexis® Congressional Research Digital Collection (accessed January 15, 2008).

<sup>64</sup> *Xinhua News Agency*, Beijing, (English edition) 0706 (Oct 12, 2000). The "Beijing Declaration" stated the Chinese perspective that "All countries should have the right to participate in international affairs on an equal footing. No country or group of countries has the right to impose its will on others, to interfere, under whatever pretext, in other countries' internal affairs, or to impose unilateral coercive economic measures on others. The North and the South should strengthen their dialogue and co-operation on the basis of equality." See also, Craig Smith, "China Forgives Some African Debt" *New York Times*, October 12, 2000.

Congo, Libya, Niger, Sudan, and the Central African Republic. Chinese trade with Africa more than tripled from 2000 to nearly \$30 billion in 2004.<sup>65</sup>

In 2004, while visiting Brazil with a number of business leaders, President Hu announced \$20 billion in new investments for oil and gas exploration and related projects. This global outreach became a source of concern in Washington as some White House advisors and legislators in Congress feared a weakening of U.S. influence in these regions.<sup>66</sup> Aside from the competition for trade, observers began to worry that Beijing was striking deals with governments that do not adhere to international laws, support human rights agendas, or promote democratic ideas. Although Chinese Deputy Foreign Minister Zhou Wenzhong has stated that Beijing tries to “separate politics from business,”<sup>67</sup> the boundaries are not clear, especially when foreign regimes have different interests and adhere to different values.

## **B. Producing Energy for Economic Growth**

### **1. Economic Growth Spurs Energy Demands**

Throughout its history, China had been primarily an energy exporter. But the structural changes initiated by Deng Xiaoping and carried forward by today’s leaders have led to unprecedented industrial growth and technological progress accompanied by

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<sup>65</sup> Howard W. French, “In a Class for Diplomats, China Cultivates African Ties,” *International Herald Tribune* (Paris), November 21, 2005.

<sup>66</sup> David Zweig and Jianhai Bi, “China’s Global Hunt for Energy,” *Foreign Affairs* 84, no. 5 (September/October 2005): 25.

<sup>67</sup> David Zweig and Jianhai Bi quote Zhou Wenzhong in “China’s Global Hunt for Energy,” *Foreign Affairs* 84, no. 5 (September/October 2005), available at Academic Search Complete Database (accessed March 13, 2010).

explosive economic development. These changes, along with the demands of a surging population, have led to significant increases in energy consumption and rapid shifts in oil trade patterns. In 1990, China exported nearly five times as much crude oil as it imported. But China became an energy importer for the first time in its history in 1993 as crude oil imports grew to twice the size of exports.

The surge in economic growth and demand for energy is shown in Tables 1 to 3 below.

**Table 1 – GDP Based on Purchasing-Power-Parity Per Capita from 1980 to 2005**

YEAR	GDP	YEAR	GDP	YEAR	GDP
1980	\$ 419	1990	\$ 1,329	2000	\$ 3,852
1981	\$ 476	1991	\$ 1,483	2001	\$ 4,211
1982	\$ 543	1992	\$ 1,713	2002	\$ 4,606
1983	\$ 617	1993	\$ 1,967	2003	\$ 5,087
1984	\$ 728	1994	\$ 2,236	2004	\$ 5,641
1985	\$ 840	1995	\$ 2,495	2005	\$ 6,196
1986	\$ 920	1996	\$ 2,758	2006	
1987	\$ 1,037	1997	\$ 3,020	2007	
1988	\$ 1,175	1998	\$ 3,517	2008	
1989	\$1,251	1999	\$	2009	

*Source: International Monetary Fund, World Economic Outlook, 2005*

**Table 2 – Chinese Data on Energy Production and Consumption**

<b>Energy Production (10<sup>4</sup> tce)</b>	103,216 (=100)
Coal	74,533 (72.2)
Crude Oil	22,916 (22.2)
Natural Gas	3,351 ( 3.2)
Hydropower	2,416 ( 2.3)
<b>Energy Consumption (10<sup>4</sup> tce)</b>	124,033 (=100)
Coal	88,481 (71.3)
Crude Oil	30,188 (24.3)
Natural Gas	2,863 ( 2.3)
Hydropower	2,501 ( 2.0)

*Source: China Energy Statistical Annual (1996-1999)*

**Table 3 – Total Primary Energy Production and Consumption (Quadrillion Btu)**

<b>Year</b>	<b>1980</b>	<b>1985</b>	<b>1990</b>	<b>1995</b>	<b>2000</b>	<b>2005</b>
Production	18.1	24.3	29.4	35.1	35.3	63.2
Consumption	17.5	22.0	27.0	34.9	35.5	67.1

*Source: EIA, International Energy Annual, Short Term Energy Outlook, Table 3a, Table 3b (Forecast values)*

Table 3 shows that China's total primary energy consumption rose by twenty-six percent from 17.5 to 67.1 quadrillion Btu in the twenty-five years from 1980 to 2005. Although China uses less energy per capita than more developed countries, its energy use is very inefficient. In 2006, the International Energy Administration (IEA) estimated that China's energy consumption per GDP was five times that of the U.S. and twelve times that of Japan.<sup>68</sup> Industrial processes are outdated and require large amounts of fuel compared to modern processes that have been adopted in more industrialized nations. Even though a study by China's Energy Research Institute suggests that China has potential to cut energy use by thirty to fifty percent by adopting international industrial standards, the size of China's population and the sustained high pace of economic growth, will continue to push energy demand even higher.<sup>69</sup>

As the gap between domestic supply and demand in energy sectors continues to widen, it will have an increasingly significant impact on the nation's economic security.

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<sup>68</sup> International Energy Agency, *China's Worldwide Quest for Energy Security* (Paris, 2006), 17. The world's oil-consuming nations pool information about their petroleum stocks and coordinate actions pertaining to their strategic petroleum reserves through the IEA.

<sup>69</sup> IEA, *China's Worldwide Quest for Energy Security* (Paris, 2006), 17.

The forecasts are staggering. In 2000, the IEA predicted China would “surpass Japan as the second largest world oil consumer within the next decade and reach a consumption level of 10.5 million barrels per day by 2020.”<sup>70</sup> In 2004, the IEA predicted that eighty percent of China’s oil demand in 2030 would have to be met by imports.<sup>71</sup>

## **2. Regional Variances**

One of the problems associated with China’s rapid growth policy has been widening of the gap in the level of economic development between urban and rural areas and across geographic regions. Not only has the leadership been faced with finding ways to equalize regional variances in standards of living, it has also needed to find ways to balance energy resource supplies and demands between western and eastern China. While western China is rich in all kinds of energy resources, seventy percent of the country’s hydropower resources lie in the south-west. Fossil-fuel resources (coal, crude oil and natural gas) and long-term reserves, located mostly in the northwest, account for approximately two-thirds of the country’s whole supply.<sup>72</sup> The twelve western provinces contain eighty percent of the country’s total renewable resources, but the eleven eastern coastal provinces are the largest energy consumers. Consistent with the location of population centers and the distribution of energy resources, the main energy flows are

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<sup>70</sup> IEA, *International Energy Outlook: Energy Profile for China* (Paris, 2000), 10, available at [http://www.bu.edu/cees/binna/304/energy\\_profiles/China.htm](http://www.bu.edu/cees/binna/304/energy_profiles/China.htm) (accessed 24 January 2005).

<sup>71</sup> IEA, *World Energy Outlook* (Paris, 2004).

<sup>72</sup> J. Fan, W. Sun, and D.M. Ren, “Renewables Portfolio Standard and Regional Energy Structure Optimization in China,” *Energy Policy* 33 (2005): 281, available at <http://www.elsevier.com/locate/enpol> (accessed June 30, 2005).



from west to east and from north to south. The main methods for distribution have been transportation of coal by rail and ship and transmission of electric power through energy grids.

China's use of its energy supplies from 1949 to the early twenty-first century is summarized as follows:

(a) Coal - Historically, China has depended heavily on coal as its primary source of energy and China has been the world's largest coal producer.<sup>73</sup> The U.S. Department of Energy, Energy Information Agency (DOE/EIA) reported that China accounted for twenty-eight percent of world coal production in 2004.<sup>74</sup> It is estimated that China holds 126.2 billion short tons of recoverable coal, the third largest in the world behind the U.S. and Russia.<sup>75</sup>

In spite of these reserves, in 1993, China's coal consumption exceeded domestic coal production and annual coal production peaked at 1.4 billion tons a few years later.<sup>76</sup> By 2004, China was consuming 2.1 billion short tons of coal, representing one-third of

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<sup>73</sup> Chinese State Economic and Trade Commission (SETC) (1997), 198-201. In March 2003, the responsibilities of SETC were taken over by the National Development and Reform Commission (NDRC), and SETC no longer exists as a Commission.

<sup>74</sup> U.S. Department of Energy, Energy Information Administration (DOE/EIA), *China Country Analysis Brief* (August 2005), <http://www.eia.doe.gov/emeu/cabs/china.html> (accessed March 3, 2009).

<sup>75</sup> DOE/EIA, *China Country Analysis Brief* (November 8, 2007).

<sup>76</sup> SETC (1997), 198-201.

the world total, and a 46 percent increase over 2002.<sup>77</sup> Clearly, China could no longer depend upon coal to sustain high levels of economic growth.

(b) Oil - Compared to coal, China's oil reserves are comparatively limited, with 85 percent of oil production on shore. At the beginning of 2006, DOE/EIA estimated proven oil reserves at 18.3 billion barrels.<sup>78</sup> China's largest producing field has been Daqing which accounted for more than 900,000 billion barrels per day, or one-quarter of China's total crude production in 2005.<sup>79</sup> However, Daqing is a mature field and, by the new millennium, production levels had to be reduced to extend the life of the field.<sup>80</sup> The second largest producing field is Shengli which produced over 500,000 billion barrels per day in 2006. Another 190,000 billion barrels per day is produced from CNOOC's offshore fields in Bohai Bay and South China Sea.<sup>81</sup>

Since the Bohai Bay region is estimated to hold more than 1.5 million barrels of recoverable oil reserves, it has attracted the attention of major oil corporations. To encourage exploration and development in the region, CNOOC initiated production sharing contracts with international companies, such as ConocoPhillips, Kerr-McGee, Apache, Chevron, and Royal Dutch Shell. "ConocoPhillips holds the largest acreage with total discovered reserves estimated at 732 million barrels. ConocoPhillips has a

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<sup>77</sup> DOE/EIA, *China Country Analysis Brief* (November 8, 2007).

<sup>78</sup> DOE/EIA, *Country Analysis Briefs: China* (August 2006), 2.

<sup>79</sup> *Ibid.*, quoting the *Oil and Gas Journal*.

<sup>80</sup> DOE/EIA, *China Country Analysis Brief* (November 8, 2007).

<sup>81</sup> *Ibid.*

forty-nine percent stake in the Bozhong 11/05 block and has produced 30,000 billion barrels per day of crude oil from its Peng Lai 19-3 field since 2002.”<sup>82</sup> In 2006, the DOE/EIA reported that it was expected to produce 140,000 billion barrels per day.<sup>83</sup>

According to the IEA, China consumed 6.6 million barrels per day of oil and imported 3.0 million barrels per day in 2005.<sup>84</sup> Assuming the current rate of growth, the EIA estimated that consumption in China would increase in 2006 by close to half million barrels per day, or 7.4 million barrels per day of oil, which the EIA projected to represent thirty-eight percent of the world total increase in demand.<sup>85</sup> Other projections by Chinese and international energy experts estimated that China’s oil demand in 2020 would range from 10 to 13.6 million barrels per day, but China’s oil production would only range from 2.7 to 4 million barrels per day.<sup>86</sup> Based upon these predictions, imports of 6 to 11 million barrels per day would be needed to satisfy domestic demand. In weighing the growth in demand against domestic supplies of oil, the Chinese leadership could not ignore the potential for natural gas to supplement oil.

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<sup>82</sup> DOE/EIA, *Country Analysis Briefs: China* (August 2006), 3.

<sup>83</sup> *Ibid.*

<sup>84</sup> Erica S. Downs, citing the IEA in a statement before the U.S.-China Economic and Security Review Commission, “China’s Role in the World: Is China a Responsible Stakeholder?” (August 4, 2006), 1.

<sup>85</sup> DOE/EIA, *Country Analysis Briefs: China* (August 2006), 2.

<sup>86</sup> Erica S. Downs, citing the IEA in a statement before the U.S.-China Economic and Security Review Commission, “China’s Role in the World: Is China a Responsible Stakeholder?” (August 4, 2006), 2.

(c) Natural Gas - Traditionally, natural gas has been a minor fuel in China. It has been secondary to coal, oil and hydro power with the largest known reserves in the western and north-central regions. The first year the Communists were in power, natural gas output in China was only 7 million cubic meters the first year, but it had risen to more than four times the 1949 level by 2000 with approximately 28 billion cubic meters of output.<sup>87</sup>

In the 1990s, proven reserves were estimated at 1.5 Tcm.<sup>88</sup> Although more recent estimates by the *Oil and Gas Journal* place proven reserves at 53.3 Tcm, which is considerably greater than earlier estimates, natural gas still accounted for only 3 percent of energy consumption by 2004.<sup>89</sup>

Since most of the earlier discoveries had been found near oil fields, natural gas was used mostly for oil production which resulted in a highly fragmented transmission and distribution network. Without a national natural gas pipeline grid, the domestic market had been limited to local producing regions. As the economy continued to grow throughout the 1990s, lack of an adequate infrastructure to transport natural gas to high energy consuming markets in the east and south east became a major obstacle. However, with foreign financial and technical assistance, gas pipelines increased to 9,112 kilometers in length with transporting capacity of approximately 10.5 billion cubic meters

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<sup>87</sup> See National Bureau of Statistics, *China Statistical Yearbook 2000* (Beijing: Statistical Publishing House, 2000).

<sup>88</sup> Keun-Wook Paik, "China Moves on Gas for Supplies and Environment," *Petroleum Economist* 66 (February 1999): 23.

<sup>89</sup> DOE/EIA, *China Country Analysis Brief* (November 8, 2007).

in 1996.<sup>90</sup> By the beginning of 2006, plans were in place “to establish a more integrated and complete oil pipeline network to better satisfy growing demand.”<sup>91</sup>

Along with aggressive development of indigenous natural gas, greater expansion of the infrastructure for delivery to consumers, and increased importation of liquefied natural gas in the last decade, the government began looking into alternative energy as a means of meeting its energy demands.

(d) Alternative Energy Sources - In spite of the developments that had taken place by 2004, the leadership recognized additional diversification would be needed to keep pace with projected increases in energy demand. The DOE/EIA projects that consumption of every primary energy source will increase over the twenty-one year forecast horizon, with the exception of nuclear.<sup>92</sup> However, developing alternative energy sources, such as hydropower, nuclear power, and renewable energy, requires significant investment and technological development which does not take place over night.

Chinese leaders have encouraged enterprises to seek foreign supplies in an effort to support continued economic growth in the short-term and to secure supplies for the long-term. Although there has not been a significant focus on energy conservation as a means of coping with domestic shortages, Premier Wen Jiabao did suggest in 2005 that

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<sup>90</sup> Xu Xiaojie, “Long-range Strategies for China’s Energy Security,” *Pipeline & Gas Journal* 226, no. 8 (1999), <http://0=galenet.galegroup.com.bianca.penlib.du.edu/servlet/BCRC?vrsn=149&locID=ude> (accessed December 8, 2005).

<sup>91</sup> DOE/EIA, *Country Analysis Briefs: China* (August 2006), 5.

<sup>92</sup> DOE/EIA, *International Energy Outlook 2008*, Report # DOE/EIA-0484 (June 2008).

energy conservation would be needed “to reconcile rapid economic growth with limited energy resources.”<sup>93</sup>

### **C. Restructuring the Energy Industry to Support Economic Growth**

China’s transformation from nearly complete reliance on coal to other sources of energy began with economic reforms in the early 1980s. The leadership recognized a need to “rejuvenate” the oil and gas industry which had been lagging under the Ministry of Petroleum Industry.<sup>94</sup> The reforms took place in two stages. The first stage involved transition from inefficient management under the command economy system. The transition was initiated by contracting with the Ministry of Petroleum Industry for annual production targets and allowing producers to sell excess oil in domestic markets. This provided incentive for further exploration and development and investment funds for technological improvements.

The second stage involved separating regulatory and commercial functions (which had been centralized in the Ministry of Petroleum Industry) by abolishing the Ministry and creating three national corporations to focus on exploration, production, and marketing. Sinopec was created for refining and petrochemical production, primarily in the south and east and China National Petroleum Corporation (CNPC) was created to operate principally in the north and west. A third corporation, China National Offshore

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<sup>93</sup> Wen Jiabao, Report to the National People Congress, March 5, 2005, cited in Warwick J. McKibbin, “Environmental Consequences of Rising Energy Use In China,” paper prepared for the Asian Economic Policy Review conference held in Tokyo on October 22, 2005.

<sup>94</sup> Teresa Finn, “China’s National Oil Companies,” *The China Business Review* (September/October 2005):12.

Oil Corporation was created to control exploration, development, and production of oil and gas in China's territorial waters.<sup>95</sup> Further restructuring within these corporations took place throughout the 1990s with the goal of creating vertically integrated oil and gas companies that would be globally competitive.

After 1993, when China first began to rely on imported oil, the fear that shortages could threaten growth of the domestic economy and political stability elevated the need for a comprehensive energy policy. In May 1997, former Premier Li Peng wrote a policy paper encouraging greater involvement in the exploration and development of international oil and gas resources, and endorsing diversification of import sources and transportation routes.<sup>96</sup> In support of this policy position, the leadership encouraged China National Offshore Oil Corporation, Sinopec, and CNPC to establish relationships in other countries, to engage in production sharing contracts, and to negotiate joint ventures that would enhance China's energy supplies. The government expanded diplomatic relations with other countries which allowed the corporations to initiate deals in Angola, Burma, Ecuador, Egypt, Indonesia, Iran, Iraq, Kazakhstan, Kuwait, Libya, Nigeria, Oman, Peru, Russia, Saudi Arabia, Sudan, Thailand, Venezuela, and Yemen, among others.<sup>97</sup>

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<sup>95</sup> Teresa Finn, "China's National Oil Companies," *The China Business Review* (September/October 2005):12.

<sup>96</sup> *People's Daily*, May 30, 1997, overseas edition. See also, IEA, *China's Worldwide Quest for Energy Security* (Paris, 2006), 10, 61-62.

<sup>97</sup> Erica S. Downs, *China's Quest for Energy Security* (Santa Monica, CA: Rand, 2000), 1-23; and Gal Luft and Anne Korin, "The Sino-Saudi Connection," *Commentary* 117, no. 3 (March 2004): 26-29.

To facilitate foreign investment, the national corporations began to spin off or eliminate unprofitable ancillary activities; they placed their most profitable, high quality assets into subsidiaries; and they carried initial public offerings on the Hong Kong and New York exchanges.<sup>98</sup> China National Offshore Oil Corporation created and transferred all its valuable commercial assets to its subsidiary, CNOOC Ltd. (CNOOC), which listed on global markets in February 2001. The initial public offering was only for 27.5 percent and only offered minority shares. Nearly seventy percent of CNOOC's share capital remained with its parent company.<sup>99</sup>

Although China's entry into the global market was incremental, CNOOC successfully generated interest from foreign operators anxious to get a foothold in China. To this end, Kerr McGee, ChevronTexaco, Apache, EDC, Devon, Burlington, Phillips, Husky, ConocoPhillips, and Devon Energy became involved in offshore areas.<sup>100</sup> CNOOC's foreign partners in Bohai Bay, its largest production area, include ChevronTexaco, ConocoPhillips, and Devon Energy. Foreign investors have assisted CNOOC with developing liquefied natural gas operations and China's liquid natural gas (LNG) infrastructure in Guangdong, Fujian, Shanghai, and Zhejiang. Other foreign operators are involved with CNOOC in the South China Sea, Beibu Gulf and East China Sea.

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<sup>98</sup> DOE/EIA, *Country Analysis Briefs: China* (August 2006), 2.

<sup>99</sup> DOE/EIA, *Country Analysis Briefs: China* (August 2006), 2; and Teresa Finn, "China's National Oil Companies," 12.

<sup>100</sup> Tony Sitathan, "Exploration and Development Encouraged," *World Oil* 223, no. 8 (2002): 67; DOE/EIA, *Country Analysis Briefs: China* (August 2006), 3.



In spite of successes, implementation of joint agreements with foreign corporations has not been a smooth process. For instance, CNOOC and Sinopec entered into a series of agreements with two multinational corporations, Royal Dutch/Shell Group and Unocal, to set up what promised to become China's largest offshore natural gas project. The project was applauded as a significant step towards satisfying China's energy needs by producing gas from the Xihu trough, 250 miles southeast of Shanghai, and transporting it by pipeline to the eastern coast. Not only would the pipeline provide low-pollution natural gas to Shanghai, it would help meet the energy needs of other industrial centers along the way.<sup>101</sup> But just one year later, Royal Dutch/Shell and Unocal announced they would be pulling out of the multibillion-dollar project for commercial reasons,<sup>102</sup> leaving China's second and third largest domestic oil companies the only players.<sup>103</sup> This was the second large project that Shell abandoned in 2004, having also pulled out of the west-east natural gas transportation project.<sup>104</sup>

Despite setbacks, China's national energy corporations did not relinquish efforts to engage foreign corporations in exploration and development pursuits. In 2005, CNPC, the country's largest player in terms of production and reserves, produced 1.3 trillion cubic meters of natural gas in 2005 and Sinopec produced a total of 222 billion cubic

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<sup>101</sup> *New York Times*, August 20, 2003.

<sup>102</sup> *New York Times* September 30, 2004.

<sup>103</sup> *China Chemical Reporter*, October 16, 2004.

<sup>104</sup> *Ibid.*

feet.<sup>105</sup> Meanwhile, CNOOC, which was in the forefront of natural gas development, introduced plans to construct LNG import facilities in Guangdong, Fujian and Zhejiang provinces.<sup>106</sup>

By 2005, CNPC had acquired interests in overseas exploration and production which included investments in Sudan, Kazakhstan, Ecuador and Syria. CNPC also announced its intent to invest \$18 billion in foreign oil and gas assets by 2020. In 2005, Sinopec was also pursuing overseas opportunities. Sinopec had already signed a memorandum of understanding with the Iranian government to acquire a fifty-one percent stake in the Yadavaran oil field; it was considering a \$70 billion deal in which China would import liquefied natural gas from Iran; and it had acquired a forty percent stake in Synenco Energy's oil sands project in Canada.<sup>107</sup> Meanwhile, in addition to bidding to acquire Unocal, CNOOC purchased Repsol-YPF's oil interests in Indonesia, making CNOOC the largest operator in the Indonesian offshore oil sector.<sup>108</sup> In spite of this breath of commercial activity, by mid-year, the contribution of China's three national energy corporations to oil imports was less than 300,000 billion barrels per day or 8.5 percent of total oil imports at that time.<sup>109</sup>

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<sup>105</sup> DOE/EIA, *Country Analysis Briefs: China* (August 2006), citing CNPC and Sinopec data.

<sup>106</sup> Martin Clark, "LNG: China – Fools Rush In," *Petroleum Economics* 71, no. 7 (2004): 24-25.

<sup>107</sup> DOE/IEA, *Country Analysis Briefs: China* (August 2006).

<sup>108</sup> *Ibid.*

<sup>109</sup> DOE/IEA, *Country Analysis Briefs: China* (August 2006).

#### **D. Acquiring Foreign Energy Supplies to Support Economic Growth**

Ever since 1993, China's leaders have become more and more concerned that energy shortages could threaten growth of the domestic economy and political instability. This concern has been the impetus behind a strategy emphasizing diversification of oil and gas imports and transport routes, and pursuit of oil deals with Russia and Central Asian countries. The need for secure transportation routes has served to strengthen China's position towards reunification with Taiwan. Since the United States has pledged its support of Taiwan in the event of a Chinese attack, the fear that U.S. control over shipping in East China might inhibit Chinese trade is ever present in the leaders' minds.

In pursuing foreign oil and gas supplies, the Chinese sought lessons from other nations' experiences. Learning from Japan's mistakes, the Chinese modeled their entry into the global energy system upon the American example. When Japan's economy took off in the 1960s and 1970s, the government focused on exploration and financed dozens of small players. The Japanese companies were unable to compete with larger, wealthier, and more experienced corporations. They pursued small projects instead, but these pursuits led to an inordinate number of dry wells. It is estimated that the Japanese spent \$50 billion for oil-exploration, yet nearly three decades later only 5.7 percent of Japan's oil imports come from Japanese-owned fields.<sup>110</sup> By contrast, the Chinese government is financing large corporations which can be competitive in the world energy market. These

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<sup>110</sup> Yuka Hayashi, "China Studies Japan's Mistakes as the Pursuit for Oil Companies," *Wall Street Journal*, August 3, 2005, eastern edition.

corporations are following the strategies of major international corporations by targeting proven reserves and working wells.

At first, the Chinese national corporations sought import relationships with smaller Middle Eastern states, such as Oman and Yemen, because they produced a light, “sweet” crude oil that was compatible with China’s existing refineries.<sup>111</sup> The Chinese national corporations also established trade relationships with other small nations such as Kuwait, the United Arab Emirates, Algeria, Egypt, Libya, and Sudan.

By the second part of the 1990s, the Chinese corporations turned their focus to the primary producing areas in the Persian Gulf – Iraq, Iran, and Saudi Arabia. In 1997, after the UN lifted sanctions on Iraq, Chinese national energy companies joined with China North Industries Corporation to enter into a 22-year production-sharing agreement with Saddam Hussein to develop Iraq’s second largest oil field. But the Chinese had not predicted the U.S. war with Iraq and the uncertainty that would follow.<sup>112</sup> As such, according to energy expert Tong Lixia, the Iraq war was the “turning point” in China’s energy strategy. It was the point at which Chinese “companies and the government realized that China could not rely on one or two oil production areas.”<sup>113</sup>

The lesson in geopolitics that came out of the Iraq War did not go unheeded. According to Shen Dingli, Fudan University international relations expert, China’s

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<sup>111</sup> Jin Liangxiang, “China and the Middle East: Energy First,” *Middle East Quarterly* 12, no. 2 (Spring 2005): 3-10.

<sup>112</sup> Flynt Leverett and Jeffrey Bader, “Managing China-U.S. Energy Competition in the Middle East,” *Washington Quarterly* 29, no. 1 (Winter 2005-06): 190.

<sup>113</sup> Peter S. Goodman, “Big Shift in China’s Oil Policy,” *Washington Post*, July 13, 2005.

leadership has become more concerned about a future in which there might not be enough oil to meet worldwide demand and this concern has led to the perception that the United States is a major competitor.<sup>114</sup> To remain competitive, China has initiated investments and trade arrangements with foreign energy firms in primary producing areas beyond the Middle East, particularly in North Africa and the Caspian Sea Basin. This “going out” (zou chu qu) policy encouraged the three national oil companies to seek supplies by purchasing equity shares in foreign markets, exploring and drilling in other countries, building refineries, and building pipelines to connect China with Siberia and Central Asia.<sup>115</sup>

Some analysts suggest the Chinese and their energy corporations are undertaking the same strategies as the United States and the major energy corporations. For example, a National Petroleum Council study, conducted at the request of Secretary of Energy Spencer Abraham, recommended a strategy for improving supply diversity, encouraging conservation and efficiency, improving demand flexibility and efficiency, sustaining and enhancing natural gas infrastructure, and promoting the efficiency of natural gas markets.<sup>116</sup> Along these lines, the Chinese attempted to minimize their vulnerability to foreign supply interruptions and trade embargos by diversifying import suppliers, cultivating diplomatic relations with resource rich countries, establishing a physical presence in producing regions, negotiating investment and trade deals, acquiring equity

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<sup>114</sup> Ibid.

<sup>116</sup> Bobby S. Shackouls, “How to Achieve a Balanced Natural Gas Policy,” *World Energy* 7, no. 4 (2004):32-34; President Bush’s “National Energy Policy” announced on May 17, 2001; and Michael T. Klare, “Fueling the Dragon: China’s Strategic Energy Dilemma,” *Current History* (April, 2006): 182.

stakes in foreign exploration and production assets, developing alternate transportation routes, and developing its own large-scale oil tanker fleet.<sup>117</sup>

Another mechanism the Chinese have adopted for minimizing vulnerability is constructing an American-style strategic oil reserve along the Zhejiang province coast. Beginning in 2005, the first phase included fifty-two tanks with capacity for 25 million gallons of gasoline. The stated goal was to create a reserve large enough to support the economy and allow the military to function for three months without imported oil.<sup>118</sup> In short, the basic energy security strategies the Chinese are pursuing include “maximum development of domestic resources, creation of strategic reserves, seeking foreign technology and investment, establishing reliable and secure oil trading channels, and making strategic investments in upstream production facilities abroad.”<sup>119</sup>

## II. CONCLUSION

Although China and the United States have followed separate and distinct development models, the two countries have emerged as the world’s largest and strongest economies in the twenty-first century. While some may see this as an anomaly, it is

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<sup>117</sup>Michael T. Klare, *Blood and Oil* (New York: Metropolitan Books, 2004), 169; IEA, *China’s Worldwide Quest for Energy Security*, (2000): 53, 64-69; Chang Ning, “China’s Importation of Mineral Resources and Oceanic Shipping,” *Chinascoped* (June 2005): 28-29; Erica S. Downs, Statement before the US-China Economic and Security Review Commission, “China’s Role in the World: Is China a Responsible Stakeholder?” August 4, 2006, 2-3.

<sup>118</sup> Joseph Kahn, “Behind China’s Bid for Unocal: A Costly Quest for Energy Control,” *New York Times*, (June 27, 2005): 1.

<sup>119</sup> IEA, *China’s Worldwide Quest for Energy Security* (Paris, 2000), 9, 74.

clearly the result of an increasingly global economy and China's conscious efforts to become integrated into that economy.

China's steady economic growth over the past thirty years has been dependent upon a steady supply of energy. But unlike the United States, which has always relied upon private entrepreneurs to meet its energy requirements, China has relied upon three state-owned companies, China National Offshore Oil Corporation (CNOOC), China National Petrochemical Corporation (Sinopec), and China National Petroleum Corporation (CNPC), rather than independent corporations, to engage in energy transactions. While subject to government controls, these corporations are part of the two-stage reorganization program discussed in this chapter and may be viewed as instruments for transitioning from a command economy to a more market-based economy.

When China's energy demand required its energy corporations to extend their global reach and develop business deals in other countries, the corporations also began to diversify the energy imports into China.<sup>120</sup> The Chinese government provides these corporations low-cost loans to assist their outreach efforts, and Chinese diplomats often facilitate negotiation of exploration and drilling rights in foreign countries.<sup>121</sup> Similarly, while the U.S. government may not be directly involved in negotiating business deals, it

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<sup>120</sup> IEA, *China's Worldwide Quest for Energy Security* (Paris, 2006), 31. By 2004, the International Energy Agency was projecting dramatic increases in China's energy imports. See IEA 2004 Report.

<sup>121</sup> Michael T. Klare, "Fueling the Dragon: China's Strategic Energy Dilemma," *Current History* (April 2006): 182.

certainly plays a role in the success of those deals by establishing diplomatic relations and trade agreements with energy surplus countries.

China began establishing relationships with energy surplus countries nearly a decade before it came to depend on foreign supplies. For example, in the mid-1980s, China and Saudi Arabia initiated their relationship through military commerce; established full diplomatic ties in 1990; and in 1999, President Jiang Zemin announced a strategic oil partnership in which Saudi Arabia quickly became China's number one foreign supplier of crude oil.<sup>122</sup> Similarly, China established a trade relationship with Iran by supplying ballistic-missile components, air-, land-, and sea-based cruise missiles, and by 2004 Iran had become China's second largest supplier of oil.<sup>123</sup>

These trading relationships point to a second distinction between the rationale that leaders in the U.S. and China give for engaging in the global energy system. Historically, the U.S. government has restricted American firms by imposing trade policies which reflect political or ideological goals, such as human rights agendas, the pursuit of democracy, nuclear disarmament, or the war against terrorism. But the Chinese government refrains from imposing similar policy limitations on their national energy corporations. Instead, the Chinese national corporations capitalize on relationships with oil-rich states by distancing themselves from domestic human rights issues, by providing foreign aid, by focusing on economic outputs rather than political inputs, and by

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<sup>122</sup> Gal Luft and Anne Korin, *The Sino-Saudi Connection*, *Commentary* 117, no.3 (March 2004): 26-29.

<sup>123</sup> *Ibid.*, 26-29.



engaging in trade in armaments and dual-use technologies. As a result, China has been able to cultivate trade relationships with countries such as Iran, Syria, Libya, and Sudan which have been characterized by the U.S. government as “an increasing threat to U.S. security interests.”<sup>124</sup>

Chinese national corporations do not operate according to the same rules as the major international oil companies. For example, Bader and Downs have observed, that the national corporations “are not constrained by the Foreign Corrupt Practices Act, by OECD guidelines on export credit competition and tied loans, or by segregation from other businesses that can be added to a package to make it more attractive, such as non-energy construction and engineering projects.”<sup>125</sup> This suggests that the U.S. and its allies might have more leverage in preventing China from entering into business deals which undermine efforts by the international community to influence how countries spend their oil revenues if they would invite China more often to the decision making table.<sup>126</sup> More recently, as Erica Downs, China Energy Fellow at the Brookings Institution, has indicated, the Chinese government has used its seat on the United

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<sup>124</sup> Gal Luft and Anne Korin, The Sino-Saudi Connection, *Commentary* 117, no.3 (March 2004): 29.

<sup>125</sup> Jeffrey A. Bader, “The Energy Future: China and the U.S. – What the United States Ought to Do,” (paper presented at Conference on China Energy, William Davidson Institute, Ross School of Business, University of Michigan, February 2006).

<sup>126</sup> Jeffrey A. Bader and Erica S. Downs, “Oil Hungry China Belongs at Big Table,” *Calgary Herald*, September 8, 2006.

National Security Council “to deflect international diplomatic pressure on a country in which a Chinese oil company has substantial investments.”<sup>127</sup>

A more recent feature of the Chinese model is the push to acquire oil and gas fields. Even before the Iraq War and the CNOOC bid for Unocal, there were signs of China’s increasing interest in acquiring foreign assets. By 2005, the volume of transactions involving a Chinese buyer and an international target rose to nearly \$23 billion.<sup>128</sup> Erica Downs suggests that this strategy is based on the assumption by some “that oil obtained through foreign investment is more secure and less expensive than that purchased on the international market.”<sup>129</sup> If China’s national oil companies acquire equity oil then the companies could send their foreign equity production to China in the event that China has sufficient funds, but is unable to purchase enough oil on the world market. But American energy experts contend there is no real advantage to owning oil fields. While the Chinese may broker a deal to purchase supplies from energy rich

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<sup>127</sup> Erica S. Downs, statement before the US-China Economic and Security Review Commission, “China’s Role in the World: Is China a Responsible Stakeholder?” (August 4, 2006), 4.

<sup>128</sup> Baosteel, China’s largest steelmaker invested in Brazil; TCL, a leading television producer, bought most of France’s Thomson TV-manufacturing business and Alcatel’s mobile handset-making business; SAIC, China’s leading car manufacturer, was looking into expansion in South Korea. See *Economist* 376, no. 8433 (July 2, 2005): 54-56.

<sup>129</sup> Erica S. Downs, statement before the US-China Economic and Security Review Commission, “China’s Role in the World: Is China a Responsible Stakeholder?” (August 4, 2006), 3.

countries, the deals may be of little consequence if they are not able to obtain secure lines of supply.<sup>130</sup>

Chinese leaders share many of the same concerns as their American counterparts when it comes to energy dependency. But the Chinese have an additional concern about relying on supplies from politically volatile areas. They worry about relying on energy supplies from regions where the United States is the preeminent power, and how they would sustain economic growth and political stability if the United States were to cut access to those supplies.<sup>131</sup> As the Chinese economy has become increasingly dependent upon maritime trade passing through the waters adjacent to the South China Sea, and patrolled by the U.S. Navy, the Chinese feel much more vulnerable.<sup>132</sup> Nearly eighty percent of China's oil imports are shipped through the Strait of Malacca. Gordon Feller reported in the *Pipeline and Gas Journal* that approximately 2.45 million barrels per day of oil moved through the Strait to China in 2004.<sup>133</sup>

Greater dependency and vulnerability, combined with the desire for peaceful expansion, provides a strong incentive for diplomacy as a means of maintaining positive

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<sup>130</sup> According to William H. Overholt, director of the Rand Center for Asia-Pacific Policy in Santa Monica, California, the key is in having secure lines of supply. See Goodman 2005, 4.

<sup>131</sup> Michael T. Klare, *Blood and Oil* (New York: Metropolitan Books, 2004), 168; and Erica S. Downs, *China's Quest for Energy Security* (Santa Monica, CA: Rand, 2000), 25.

<sup>132</sup> David A. Adams, "Managing China's Transition," *U.S. Naval Institute Proceedings* 129, no.7 (July 2003):50.

<sup>133</sup> Gordon Feller, "China's Rising Demand for Oil and Pipeline Has Worldwide Implications," *Oil & Gas Journal* (May 2005): 232; 5.

foreign policy relations with the United States. At the same time, the need for energy security provides an incentive to look for reserves in areas closer to home, areas within China's range of military influence where its leaders might have greater bargaining power and control over outside influences. The Chinese leadership has made a concerted effort to build regional relationships which have been based on "a sophisticated blend of trade, confidence building measures, and even development assistance."<sup>134</sup> But Beijing has also encouraged global expansion into Africa, South America, and Central Asia as a means of providing alternative sources of energy to its energy mix.

While some members of the U.S. Congress are encouraged by China's increasingly prominent role in the global economy, others are more leery of an increased global influence that might replace that of the United States. Concerns about China have been expressed in congressional hearings and debates ever since the Nixon Administration when the U.S and China renewed diplomatic relations. Although U.S.-China relations are complex, members of Congress tend to gravitate toward one extreme or another based upon their personal values and ideologies. However, when CNOOC indicated its interest in acquiring an American-owned oil corporation, members of Congress coalesced to oppose the transaction in an unusually unified manner. This phenomenon can be explained by the institutional approach to foreign policy analysis.

This chapter described China's need to import energy and provided the rationale behind CNOOC's bid to purchase Unocal. The study now turns to a discussion of the American political system, the political structures which have been institutionalized, the

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<sup>134</sup> Elizabeth Economy, "China's Rise in Southeast Asia: Implications for the United States," *Journal of Contemporary China* 14, no. 44 (August 2005): 413.

rules and norms which have led to incessant competition between the executive and legislative branches. According to the integrated approach to institutionalism, institutional structures, rules, and values impose constraints on actors within policy making institutions that make policy change difficult at best. The process is fragmented and slow. As a consequence, institutional actors will often turn to informal mechanisms to accomplish policy goals.

Chapter 3 sheds light on how the American Constitution operates to reinforce democratic principles and ensure that no one branch of government becomes too powerful, but also provides for a modicum of creativity in which individuals may serve as instruments of change. Analysis of evolution of the institutions of the presidency and the legislature lends insight into the state of the conflict between the two branches in 2005 when George W. Bush and the 109<sup>th</sup> Congress were responding to the issues of peak energy, growing competition from China in the global economy, and vulnerability to terrorist attacks. It is the understanding of this inter-institutional conflict that provides an explanation as to why Congress politicized the CNOOC bid for Unocal.

## **CHAPTER THREE: INSTITUTIONALIZATION OF THE PRESIDENCY AND CONGRESS**

### **I. INTRODUCTION**

This chapter examines the formation of institutional structures, the historical processes which have shaped the American presidency and Congress, and the infusion of values into these institutions. It also considers how certain values have come to transcend those of any single individual, and how these values support the basic tenants of American democracy and the market economy. Once these characteristically American institutions and values were in place, they began to shape future political discourse and policy formation.

The foundation of the American political system and its institutions is the Constitution. In crafting the Constitution, the Founding Fathers debated what kind of system would provide stability while reinforcing democratic principles. The final solution was a division of powers among executive, legislative, and judicial branches and a system of “checks and balances” which defined separate powers for each branch including the power to question how each of the other branches exercises its authority.

In practice, this American system of governance is dynamic and policy making is in a constant state of flux characterized by a continuous struggle for power between Congress and the executive branch. Although powers are defined, there is always room for interpretation of these powers and the president and Congress are often tempted to

push their limits. As one branch asserts its influence over a policy issue, the other reacts to restrain that influence.<sup>135</sup> While this system allows for policy change, change is incremental and may lead to temporary imbalances in power. The system of “checks and balances” provides a mechanism for the system to resolve political imbalances and move back towards a state of equilibrium.

We begin this chapter with an overview of the American Constitution and a discussion of how it defined the authorities of each branch of government. Congress was designed as a pluralistic institution intended to “represent the people and enact policies in response to the popular will through a complex deliberative process.”<sup>136</sup> The executive branch was designed to function under the guidance of a single individual elected to protect the nation’s stability and security by implementing laws and responding quickly to crises. The federal court system was designed to interpret laws and protect constitutional rights and liberties. The founders hoped this structure would provide for a long-lasting and effective system of governance.

After discussing the foundation upon which the system is based, we move to a discussion of the processes by which the executive and legislative branches became institutionalized; how institutionalization of these two branches ensured that fundamental values underlying the American democratic system would transcend any changes in

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<sup>135</sup> The courts were not engaged in this political struggle but play an essential role in rectifying imbalances when Congress or the president exceeds constitutional boundaries.

<sup>136</sup> David A. Crockett, “The Contemporary Presidency: ‘An Excess of Refinement’: Lame Duck Presidents in Constitutional and Historical Context,” *Presidential Studies Quarterly* 38, no. 4 (Dec. 2008): 707.

executive or legislative leadership; and how institutionalization created constraints on individual actors but left the door open for them to devise informal mechanisms of change.

This overview is significant in that this study's analytic approach is based on a socio-historical perspective which assumes institutions are shaped by history and infused with values. While values are important in the formation of institutional structures, rules and standards and tend to persist over time, the conditions that existed during the formative years may change. The integrated approach to new institutionalism suggests that institutions which are capable of adapting to change are more likely to survive in an evolutionary environment. However, the more the structures and rules are institutionalized, the more difficult it is to change course. Therefore, institutional actors responsible for policy making often adopt informal mechanisms for change. These mechanisms may become institutionalized or they may merely be tolerated as acceptable. Familiarity with the historical background in which the American political institutions were created, and the values underlying these institutional structures, will lead to better understanding of why certain issues and events (such as CNOOC's proposed acquisition of Unocal) are politicized in an effort to accomplish long-term policy goals. Since there is no express provision in the Constitution concerning regulation of foreign investment in the United States, we must look to other federal powers mentioned in the Constitution to understand politicization of foreign investment policies and regulations.

The genius of the American Constitution is that it gave shape to the government and defined the boundaries and limits of the government at the same time that it provided



for fundamental rights which would be protected from temporary changes and political influence.<sup>137</sup> It fulfilled the need for a “kind of social compact – a basic agreement among citizens, and between citizens and state, setting out mutual rights and duties, in permanent form.”<sup>138</sup>

The Constitution created a republican form of government in which the people are the ultimate power, but they transfer that power to representatives elected to govern on their behalf. While the Founding Fathers conceived of a dominant national government which would limit the powers of the individual states, concerns over creating a system in which power might be too centralized led them to include discretionary language in the Constitution which divided powers among executive, legislative, and judicial branches.<sup>139</sup> Each of these branches was granted separate powers, but they were also required to share powers.

The Constitution vests executive powers in the president and provides for executive checks on the legislature which include emergency calling into session of one or both houses of Congress; forced adjournment when both houses cannot agree on adjournment; presidential veto of legislation; and serving as commander in chief of the military. Although the president has the power to oversee matters concerning foreign

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<sup>137</sup> Lawrence M. Friedman, *A History of American Law* (New York: Simon and Schuster, Inc., 1985), 118.

<sup>138</sup> *Ibid.*, 115.

<sup>139</sup> Jack Rakove, “American Federalism: Was there an Original Understanding,” in *The Tenth Amendment and State Sovereignty*, ed. Mark R. Killenbeck, (Lanham, MA: Rowman and Littlefield Publishers, 2002), 107-129.

nations, the Founding Fathers gave Congress policy making and budgetary powers to ensure that the president would not be able to assert absolute control over the government.<sup>140</sup> Legislative checks on the executive include the power to provide for the common defense and general welfare of the United States; the power to declare war; House impeachment power; Senate trial of impeachments; Senate approval of departmental and U.S. Supreme Court appointments; Senate approval of treaties and ambassadors; and legislative override of presidential vetoes.<sup>141</sup> Two of the constitutional bases for legislation concerning foreign investment are the power to regulate interstate and foreign commerce<sup>142</sup> and the power to provide for national defense.<sup>143</sup>

By institutionalizing the system of “checks and balances,” the founders created a tension between the executive and legislative branches that is reflected in the policy making process. While attempting to resolve important and controversial issues the

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<sup>140</sup> This dissertation argues that the balance of power is in a constant state of flux, but at any given point in time one branch may overpower the other. Others argue that there is an absolute difference in the strength of the presidency and Congress in relation to one another. For example, Barbara Sinclair, “Context, Strategy, and Chance,” in *The George W. Bush Presidency: Appraisals and Prospects*, ed. Colin Campbell and Bert A. Rockman, Washington, D.C.: CQ Press, 2004, 105-106, argues that the Constitution “puts the president in the weaker position” because the president is dependent upon Congress for approval of top-level staff and funding to carry out programs.

<sup>141</sup> U.S. Constitution, articles 1 and 2. The founders voiced varying opinions regarding the executive branch, but the driving force behind the role of the presidency today was James Wilson who proposed a single executive. See Library of Congress, *1774-1789 Debates* (June 1, 1787).

<sup>142</sup> U.S. Constitution, art. 1, sec. 8, cl. 3.

<sup>143</sup> U.S. Constitution, art. 1, sec. 8, cl. 12.

president and Congress compete for autonomy and decision making authority.<sup>144</sup> Although this struggle is constant, it is tempered by the institutionalization of values that are biased towards reaching a state of equilibrium. The tendency towards equilibrium in domestic governance often prevails over efficient, or optimal, policy formulation.<sup>145</sup> Nonetheless, greater understanding of the institutional dynamics and how they have evolved over time will lend insight into how or why the president or Congress may choose to politicize particular issues while formulating policies.<sup>146</sup>

The struggle for control over foreign policy had clearly emerged by the beginning of the twentieth century, but the first major congressional challenge to the president's foreign policy prerogative did not occur until the years between World War I and World War II.<sup>147</sup> But after WWII, Congress rarely seemed to oppose the president's foreign

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<sup>144</sup> Jack Rakove, *Original Meanings: Politics and Ideas in the Making of the Constitution* (New York: Alfred A. Knopf, 1996), 160; Martin A. Flaherty, "The Future and Past of U.S. Foreign Relations Law," *Law and Contemporary Problems* 67 (Autumn 2004): 192.

<sup>145</sup> Toshihiro Nakayama, *Politics of U.S. Policy toward China: Analysis of Domestic Factors* (Washington, D.C.: Brookings Institution, 2006), 4; Robert B. Zoellick, "Congress and the Making of US Foreign Policy," *Survival* (Winter, 1999-2000), 20; Richard Bush, "The Roles of Congress in Shaping Washington's China Policy," in *The Heritage Lectures, No. 338, An Asian Studies Center Forum, America's China Policy and the Role of the Congress, the Press, and the Private Sector*, ed. Andrew B. Brick (Washington, DC: Heritage Foundation, 1991), 8.

<sup>146</sup> See Ryan Lee Teten, "The Evolution of the Rhetorical Presidency and Getting Past the Traditional/Modern Divide," *Political Studies Quarterly* 38, no. 2 (June 2008). Teten suggests that scholars "reach into the presidential past of all officeholders" for insight into issues rather than creating an "artificial dichotomy" that separates presidential history into sections which lose their explanatory power.

<sup>147</sup> Aaron Wildavsky, "The Two Presidencies," in *The Presidency*, ed. Aaron Wildavsky, (Boston: Little, Brown, 1969) describes the balance of power between Congress and the president.

policy decisions.<sup>148</sup> Scholars have suggested that congressional deference was due in part to executive leadership in winning the war and in part to recognition that the president had advantages such as greater access to intelligence, the ability to function outside public scrutiny, and the ability to take decisive action, especially in times of crisis.<sup>149</sup>

The semblance of acquiescence began to change after the 91<sup>st</sup> Congress when Senator Fulbright, Chairman of the Senate Foreign Relations Committee and a loyal ally

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<sup>148</sup> John F. Manley, “The Rise of Congress in Foreign Policy-Making,” *Annals of the American Academy of Political and Social Science* 397 (September 1971): 60-70.

<sup>149</sup> The debate over which branch would be in the best position to negotiate foreign policy can be traced back to the Federalist Papers. John Jay argued as follows:

The power of making treaties is an important one, especially as it relates to war, peace, and commerce; and it should not be delegated but in such a mode, and with such precautions, as will afford the highest security that it will be exercised by men the best qualified for the purpose, and in the manner most conducive to the public good.

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Those matters which in negotiations usually require the most secrecy and the most despatch (*sic*), are those preparatory and auxiliary measures which are not otherwise important in a national view, than as they tend to facilitate the attainment of the objects of the negotiation. For these, the President will find no difficulty to provide; and should any circumstance occur which requires the advice and consent of the Senate, he may at any time convene them. Thus we see that the Constitution provides that our negotiations for treaties shall have every advantage which can be derived from talents, information, integrity, and deliberate investigations, on the one hand, and from secrecy and despatch (*sic*) on the other.

*The Federalist No. 64* (John Jay) (The Avalon Project at Yale Law School, 1996). See also James L. Sundquist, *The Decline and Resurgence of Congress* (Washington, DC: Brookings Institution, 1981) chap. 6, for a discussion of the growth of executive power during WWI and WWII.

of President Johnson, began to challenge the president's foreign policy initiatives.<sup>150</sup> In particular, Fulbright objected to the president's handling of military intervention in Santo Domingo which he claimed was a violation of a "treaty which had been solemnly ratified with the consent of the Senate."<sup>151</sup>

Although Senator Fulbright recognized presidential authority for making decisions and taking actions in emergency situations, he concluded that a series of crises over the past twenty-five years had led to an "unhinging of traditional constitutional relationships" in which the Senate's constitutional powers of advice and consent had "atrophied into . . . a duty to give prompt consent with a minimum of advice."<sup>152</sup> In Fulbright's view, the Senate's responsibility was

to review the conduct of foreign policy by the President and his advisers, to render advice whether it is solicited or not, and to grant or withhold its consent to major acts of foreign policy. In addition the Congress has a traditional responsibility, in keeping with the spirit if not the precise words of the Constitution, to serve as a forum of diverse opinions and as a channel of communication between the American people and their government. The discharge of these functions is not merely a prerogative of the Congress; it is a constitutional obligation, for the neglect of which the Congress can and should be called to public account.<sup>153</sup>

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<sup>150</sup> Alfred M. Lilienthal, "In Memoriam: J. William *Fulbright*: A Giant Passes," *The Washington Report on Middle East Affairs* XIII, no. 7 (Washington: May 1995), 50; Gary Stone, *Elites for Peace: The Senate and the Vietnam War, 1964-1968* (Knoxville: University of Tennessee Press, 2007).

<sup>151</sup> J. William Fulbright, *The Arrogance of Power* (New York: Random House, 1966), 49-50.

<sup>152</sup> *Ibid.*, 45.

<sup>153</sup> J. William Fulbright, *The Arrogance of Power* (New York: Random House, 1966), 44-45.

At first, Senator Fulbright's concerns did not seem to be felt to the same extent in the House. For example, while the House Foreign Affairs Committee favorably reported a resolution proposed by the president in support of his foreign policy efforts, the Senate Foreign Relations Committee adopted an alternative resolution requiring "affirmative action by Congress" to commit armed forces abroad.<sup>154</sup> After Johnson announced he would not run for re-election, the Senate withheld the resolution from the floor, but Fulbright responded to the power that President Johnson had amassed by forming an ad hoc Subcommittee on U.S. Security Agreements and Commitments Abroad chaired by Senator Stuart Symington. The subcommittee's stated purpose was to review international military commitments and the relationship of those commitments to U.S. foreign policy.<sup>155</sup> Its underlying purpose was to facilitate Fulbright in asserting his own foreign policy initiatives.

The cleavage between the Senate Foreign Relations Committee and President Johnson set the foreign policy tone for the next decade and beyond. After the Vietnam War and the Watergate scandal led to a loss of confidence in executive leadership there were additional challenges to executive powers.<sup>156</sup> Beginning in 1973 with the War

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<sup>154</sup> U.S. Congressional Research Service, Report No. FAX-0002 (Washington, D.C.: Library of Congress, 1970).

<sup>155</sup> David Taiwei Lee, *The Making of the Taiwan Relations Act: Twenty Years in Retrospect* (Oxford: Oxford University Press, 2000), 32.

<sup>156</sup> Ramon H. Myers and David Shambaugh, "Introduction: The Legacy of U.S. China Policy, 1989-2000," in *Making China Policy*, ed. Ramon H. Myers, Michel C. Oksenberg, and David Shambaugh (Lanham, MD: Rowman and Littlefield Publishers, 2001), 3; Paul E. Peterson, "The President's Dominance in Foreign Policy Making," *Political Science Quarterly* 109, no. 2 (1994), 220; and James A. Robinson, *Congress*

Powers Act,<sup>157</sup> the legislature became more assertive in restricting the executive power to make foreign policy by mandating *prior* consultation with Congress.<sup>158</sup> The following year, Congress went a step further and imposed human rights issues into U.S.-Soviet policy with the Jackson-Vanik Amendment (“Jackson-Vanik”) to the Trade Act.<sup>159</sup>

Although Jackson-Vanik denied the president wholesale authority to grant Most Favored Nation (“MFN”) status to any “non-market economy” (such as the Soviet Union and China) that prevented free emigration, it did permit the president to allow MFN treatment on an annual basis subject to legislative veto by a majority of Congress. After a 1983 Supreme Court decision made the legislative veto unconstitutional, Congress amended Jackson-Vanik to allow legislative rejection of the president’s annual extension of MFN through a joint resolution of disapproval.<sup>160</sup> Unlike the previous amendment, the joint resolution was subject to presidential veto and required two-thirds vote of both the

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*and Foreign Policy-Making: A Study in Legislative Influence and Initiative* (Homewood, IL: Dorsey), 1962.

<sup>157</sup> *War Powers Act of 1973*, Public Law 93-148, *U.S. Statutes at Large* 87 (1973): 555, codified at *U.S. Code* 50, ch. 33 (2009), §1541-1548.

<sup>158</sup> Robert B. Zoellick, “Congress and the Making of US Foreign Policy,” *Survival* (Winter, 1999-2000): 20.

<sup>159</sup> *Trade Act of 1974*, Public Law 93-618, *U.S. Statutes at Large* 88 (1975):402, codified at *U.S. Code* 19, ch. 12 (2009), § 2432. See Congressman John B. Anderson, “Congress and the Plight of Soviet Jews,” extension of remarks, 119 *Cong. Rec.* 687, (January 9, 1973): 702-03 for the history behind the Jackson-Vanik Amendment and the differing perspectives between Congress and President Nixon regarding diplomacy. Senator Anderson declared, “It is important that the Russians understand that they are dealing not only with the Administration but also with Congress.” It seems that history repeated itself in 2005 when Congress sought to teach the Chinese a similar lesson by intervening in CNOOC’s proposed purchase of Unocal.

<sup>160</sup> *INS v. Chada, et al.*, 462 U.S. 919 (1983).

House and the Senate to overrule a presidential decision to extend MFN status. As a consequence, each year as presidents would consider extension of MFN to China, Congress would engage in debates as to whether that status should be extended or not. These debates were replete with innuendos concerning communism and China's foreign and domestic policies.

Throughout the 1980s Congress struggled with determining where to draw the line between its foreign policy making authority and the president's. Japanese technology was gaining a stronger foothold in the American market and some legislators were concerned about the possibility that Japanese corporations might acquire industries deemed essential to U.S. commerce and national security. Senator Exon (D-NE) and Representative Florio (D-NJ) sponsored an amendment to the Defense Production Act of 1950 to authorize executive review of all foreign investments that might undermine national security. The Exon-Florio Amendment passed in 1988 with the expectation that the president would intervene and block foreign acquisitions of American corporations that threatened national security.

Ever since its enactment, Congress has reviewed the impact that the Exon-Florio Amendment has had on foreign acquisitions. Ironically, by drafting legislation with the intent of protecting national security without compromising free trade and proprietary rights of private businesses, Congress had created a situation in which they had excluded themselves from legislative oversight. The secrecy necessitated by executive review of confidential business transactions led some legislators to suspect that presidents were being too lenient in interpreting and implementing their authority under Exon-Florio.



Concerns about implementation of Exon-Florio continued to exist even after President George W. Bush reorganized his administration to protect the homeland from national security threats. This study analyzes the tension between Congress and the White House over foreign policy and the difficulty that both branches face in balancing free trade values with the national security imperatives. The analysis leads to the conclusion that congressional challenges to presidential authority, as demonstrated by the politicization of CNOOC's proposed acquisition of Unocal, may become more pervasive with regards to U.S.-China policy.<sup>161</sup>

## II. INSTITUTIONALIZATION AND POLICY MAKING

Institutionalization is defined as a process by which an organization “acquires value and stability” by attaining high levels of autonomy, adaptability, complexity and coherence.<sup>162</sup> In discussing the evolution of the American political system, this dissertation shows how institutional characteristics have created opportunities as well as constraints for the president to assert foreign policy making powers. Similarly, it shows how institutionalization has created opportunities and constraints for Congress to assert its legislative muscle in the foreign policy arena. Even though there is a constant tension between the two institutions, accompanied by varying levels of support for the president

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<sup>161</sup> Richard Bush, “The Roles of Congress in Shaping Washington’s China Policy,” 8.

<sup>162</sup> Samuel Huntington, *Political Order in Changing Societies* (New Haven: Yale University Press, 1968), 12. In this study, we adopt the four characteristics of institutionalization proposed by Huntington and further defined by Lyn Ragsdale and John Theis, “The Institutionalization of the American Presidency, 1924-1992,” *American Journal of Political Science* 41, no. 4 (1997).

among individual legislators, Congress has successfully enacted major legislation to guide the president in balancing economic goals with national security goals.<sup>163</sup> Analysis of the tension between the two institutions will help explain Congress' efforts to politicize CNOOC's proposed acquisition of Unocal in 2005.

## **A. Institutionalization of Presidential Powers**

### **1. Characteristics of the Institutionalized Presidency**

(a) Autonomy - During much of its history, the office of the president consisted only of the president and some low-level staff, administrative functions were limited to national defense, and the presidency demonstrated few institutional qualities.<sup>164</sup> Some scholars have traced the institutionalization of the presidency to 1921 when Congress enacted the Budget and Accounting Act.<sup>165</sup> Previously, Congress had been wholly responsible for the structure and program responsibilities of the executive branch, including preparing the national budget. But the Budget and Accounting Act transferred this congressional power to the presidency by requiring that the president draft the budget

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<sup>163</sup> Major bills include the *Trading with the Enemy Act* (1917), the *Defense Production Act* (1950), the *Omnibus Trade and Competitiveness Act* (1988), and the *Exon-Florio Amendment* (1989), to name a few.

<sup>164</sup> By the early 1800s, the Federal government's civilian workforce was less than 5,000, most of which were postal workers. It was not until the twentieth century that this workforce began to expand significantly. For further discussion of the growth of the public sector see Glen O. Robinson, Ernest Gellhorn, and Harold H. Bruff, *The Administrative Process*, (St. Paul, MN: West Publishing Co., 1986), 4. See also, Lyn Ragsdale and John Theis, "The Institutionalization of the American Presidency, 1924-1992," *American Journal of Political Science* 41, no. 4 (1997): 1285.

<sup>165</sup> *Budget and Accounting Act of 1921*, Public Law 1367, 67th Cong. 1st sess. (effective June 10, 1921).

with the assistance of the newly established Bureau of the Budget (BOB), which was housed in the Treasury.<sup>166</sup>

The Economy Act of 1933 gave the president limited authority to reorganize the executive branch. Then, in 1939, Congress further strengthened the president's managerial responsibilities by statutorily authorizing the president to issue executive orders proposing reorganization within the executive branch that would reduce expenditures and increase efficiency. A president's reorganization order was to become effective after sixty days unless either the House or Senate adopted a resolution of disapproval. President Roosevelt used this statutory authority to propose a Reorganization Plan to Congress, and some scholars trace the institutionalization of the presidency to the reorganization that followed.<sup>167</sup> After obtaining congressional consent, Roosevelt issued Executive Order 8248 to create the Executive Office of the President (EOP) and the White House Office (WHO) within the EOP. Executive Order 8248 also

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<sup>166</sup> Lauren Cohen Bell, "Following the Leaders or Leading the Followers? The US President's Relations with Congress," *Journal of Legislative Studies* 10, nos. 2-3 (Summer/Autumn 2004): 195; and Lyn Ragsdale and John Theis, "The Institutionalization of the American Presidency, 1924-1992," 1285.

<sup>167</sup> S.J. Res. 138, 76th Cong., 1<sup>st</sup> sess., ch. 193: 813, effective July 1, 1939. For a more in-depth discussion of how this executive order contributed to the institutionalization of the presidency see Stephen Hess with James P. Pfiffner, *Organizing the Presidency* (Washington D.C.: Brookings Institution, 2002); John Burke, *The Institutional Presidency* (Baltimore: Johns Hopkins University, 1992); and Clinton Rossiter, *The American Presidency* (New York: Time Incorporated, 1960).

transferred the Bureau of the Budget, later to become the Office of Management and Budget (OMB), from the Treasury Department to the EOP.<sup>168</sup>

In establishing the Executive Office, Roosevelt made some significant changes in presidential staffing. He added six presidential assistants to his staff and differentiated between secretaries who had substantive responsibilities and administrative assistants who fulfilled other responsibilities and gathered information at the president's request. By moving the Bureau of the Budget into the Executive Office, Roosevelt helped strengthen presidential control over fiscal planning. Over time, the Executive Office of the President has expanded to include a number of advisory and policy-making agencies and task forces. Modern presidents exercise additional powers with their ability to determine which powers shall be granted to the vice president, which individuals shall be given cabinet-level status, and which of those individuals shall carry more influence over the president's decision making process. The status the president grants to each of his advisors in the EOP is an indicator of the president's policy preferences.

Although budget allocations have varied from one Congress to the next, over the years, the executive budget has grown incrementally along with the staffing. For example, before the reorganization in 1939, there were thirty-five employees serving in the BOB, but in less than ten years the staff had increased to more than 600, and over the

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<sup>168</sup> *Reorganization Act of 1939*, Public Law 76-19, 76<sup>th</sup> Cong., 1<sup>st</sup> sess., April 3, 1939. Franklin D. Roosevelt's Reorganization Plan I is documented in "Message to Congress on the Reorganization Act," April 25, 1939, ed. John T. Woolley and Gerhard Peters, *The American Presidency Project* (online), Santa Barbara, CA: University of California, available at <http://www.presidency.uscb.edu/ws/?pid=15748> (accessed June 3, 2009). Roosevelt issued Executive Order 8248 on September 8, 1939.

same time period the bureau's budget had increased from less than \$200,000 to nearly \$3 million.<sup>169</sup> Today, the exact size of the president's staff is not exactly clear. According to Burke, this is because presidents borrow staff from other agencies and departments, and because presidents have "incentives to limit the officially reported size of the staff" to avoid "an outcry by Congress and the public."<sup>170</sup>

Over time, the expansion of the EOP required more than additional staff, it required greater managerial expertise.<sup>171</sup> Presidents tended to emphasize managerial expertise until the Nixon Administration when "the impetus for staff institutionalization shifted significantly toward reducing political uncertainty."<sup>172</sup> As Nixon encouraged tight control over administrative agencies, the White House staff grew more influential. Today, the White House Office is even larger, staff functions have become increasingly specialized with more levels of hierarchy, and presidents have much more autonomy than in the past.<sup>173</sup>

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<sup>169</sup> Allen Schick, "The Problem of Presidential Budgeting," in *The Illusion of Presidential Government*, ed. Hugh Helco and Lester Salamon (Boulder, Colorado: Westview, 1981), 89.

<sup>170</sup> John Burke, *The Institutional Presidency* (Baltimore: Johns Hopkins University, 1992), 12.

<sup>171</sup> Lauren Cohen Bell, "Following the Leaders or Leading the Followers? The U.S. President's Relations with Congress," 197.

<sup>172</sup> Matthew J. Dickinson, "Neustadt, New Institutionalism, and Presidential Decision Making: A Theory and A Test," *Presidential Studies Quarterly* 35, no. 2 (June 2005), 260.

<sup>173</sup> Lyn Ragsdale and John Theis, "The Institutionalization of the American Presidency, 1924-1992," 1286-1288.

Another measure of executive autonomy is the extent to which the presidency provides leadership and offers policy directives independent of other branches of the government. It has been noted that the president's dual roles of leader and administrative clerk are often in conflict.<sup>174</sup> But the leadership role is instrumental to managing foreign policy and diplomatic crises.

Although the Founding Fathers had envisioned Congress as the lawmaking body, executive influence over law-making has expanded over time. President Franklin D. Roosevelt established precedence for the president's new policy-making role when he declared to the nation, "It is the duty of the President to propose and it is the privilege of Congress to dispose."<sup>175</sup> Since Roosevelt's presidency, this concept has been institutionalized to the extent that the public now expects the president to formulate a legislative package, and the president expects his party to support his legislative package within Congress. But, even with this expanded power, presidents continue to have difficulty getting their proposals through Congress, especially when the presidency and Congress are controlled by different political parties.

Presidents attempt to increase their influence over Congress by relying upon a patronage system consisting of personal favors such as inviting individual legislatures to meetings in the White House or making campaign visits to their home districts. Presidents also attempt to influence policy through executive orders. Authority to issue

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<sup>174</sup> Richard E. Neustadt, *Presidential Power and the Modern Presidents: The Politics of Leadership from Roosevelt to Reagan* (New York: Free Press, 1990).

<sup>175</sup> Franklin D. Roosevelt, Excerpts from the Press Conference, July 23, 1937 archived by John Woolley and Gerhard Peters, The American Presidency Project, [http://www.presidency.ucsb.edu/news\\_conferences](http://www.presidency.ucsb.edu/news_conferences) (accessed June 3, 2009).

executive orders is derived from the “take care” clause in the Constitution whereby the president has the power to “take Care that the Laws be faithfully executed.”<sup>176</sup> The Supreme Court has interpreted the “take care” clause to authorize the president to take such actions as necessary to carry out laws passed by Congress or to enforce existing laws and the Constitution.<sup>177</sup>

After Roosevelt carried out the first Reorganization Plan, Congress reviewed the president’s statutory authority to issue executive orders under the Reorganization Act. Congressional review was based on a provision in the act that allowed Congress to disapprove a plan. Then, in 1983, the Supreme Court invalidated congressional reliance upon a concurrent resolution to disapprove a proposed plan in *INS v. Chadha*.<sup>178</sup> In response to the Supreme Court decision, Congress enacted the Reorganization Act Amendments of 1984. The amendments allowed the president to make changes to his plan any time during the sixty calendar days of continuous session of Congress in which it was submitted. But the act also provided that both houses must adopt a joint resolution for approval within ninety days of continuous session. This amendment only continued until the end of 1984 when it automatically expired.<sup>179</sup> No president since Reagan has sought this reorganization authority.

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<sup>176</sup> U.S. Constitution, art. 2, sec. 3.

<sup>177</sup> The landmark case interpreting the “take care” clause is *Youngstown Sheet and Tube Co. v. Sawyer*, 343 U.S. 579 (1952).

<sup>178</sup> 462 U.S. 919 (1983).

<sup>179</sup> *U.S. Code* 5 (1988), §§ 90-912.

In the absence of reorganization plan authority, the president may propose executive branch reorganization through the normal legislative process. But this process is often slow, lacks a time frame, and does not mandate a vote. The president can attempt minor reorganization, such as creating temporary entities, through directives such as executive orders, but this approach is inadequate for major organizational changes.

Although executive orders are often administrative in nature, they have become increasingly “policy-specific” over time.<sup>180</sup> But there are several constraints upon presidents who wish to accomplish policy goals through executive orders. First, the executive order lacks permanency. It has become increasingly common for presidents to revoke executive orders signed by previous administrations by issuing new executive orders that accomplish their own policy agendas. A second constraint is the power of Congress to pass laws which modify or overturn executive orders. This constraint has not been a significant deterrent to presidents as they know that a slow and tedious lawmaking process may prevent legislative action. A third constraint is the judicial power to declare an executive order unconstitutional. However, such rulings are rare since the courts are reluctant to interfere with the executive’s authority over his staff. In short, the Constitution provides these types of checks and balances to limit executive powers; but the fact that they are rarely used in practice has contributed to increased use of executive orders and the expansion of presidential autonomy.

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<sup>180</sup> Lyn Ragsdale and John Theis, “The Institutionalization of the American Presidency, 1924-1992,” 1288-1290.



Another mechanism contributing to the institutionalization of the presidency stems directly from the Constitution. Article 1, section 7 stipulates how bills are presented to the president and how the president may veto or modify bills presented to him. If the president approves the bill, “he shall sign it, but if not he shall return it, with his Objections to the House in which it shall have originated, who shall enter the Objections at large on their Journal, and proceed to reconsider it.” If two-thirds of each house supports the president’s recommendations, the bill will become law.

This signing statement consists of commentary that the president writes to accompany a bill when he signs it into law. Over the years it has evolved into a “multipurpose device” with a number of different uses. It can be used to influence political actors or to challenge the constitutionality of certain provisions of the bill pursuant to the president’s Article 2 “take care” and “oath of office” powers. Or it can be used simply as a rhetorical tool to alert the public as to the president’s position concerning certain aspects of the bill.<sup>181</sup>

Signing statements have long been used by presidents to assert their authority after Congress passes major legislation that threatens presidential power and autonomy in the policy making process. Kelley and Marshall trace the first use of the signing statement to President James Monroe, but their research suggests that the signing statement first attained “strategic importance” with the Reagan presidency and two significant Supreme Court decisions in which the Court relied in part on President

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<sup>181</sup> Christopher S. Kelley and Bryan W. Marshall, “The Last Word: Presidential Power and the Role of Signing Statements,” *Presidential Studies Quarterly* 38, no. 2 (June 2008): 250.

Reagan's signing statements to reach their decisions.<sup>182</sup> The signing statement is a "formidable" tool because it provides the president with a "last-move advantage" after a long sequence of political bargaining.<sup>183</sup>

(b) Adaptability – Adaptability is based on an awareness of internal and external environments and refers to the ability to take action to achieve a balance between the two. The adaptive function is a means by which an institution may modify its internal structures to meet the requirements of a constantly changing external environment.<sup>184</sup> This second feature of the institutionalized presidency refers to "the flexibility presidents have to create, modify, and eliminate units and the resilience of key units no matter who is president."<sup>185</sup> Like autonomy, adaptability increases the potential for the presidency to act independently of other branches of government. For example, when presidents take office, their first task is to set up a system for managing the White House activities and staff. It is not unusual for presidents to add some units that support high presidential priorities and abolish others that do not, but for the most part, presidents have tended to follow a fairly consistent model. This model includes a chief of staff who assumes

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<sup>182</sup> Christopher S. Kelley and Bryan W. Marshall, "The Last Word: Presidential Power and the Role of Signing Statements," 251, 254. See *INS v. Chadha*, 462 U.S. 919 (1983) and *Bowsher v. Synar*, 478 U.S. 714 (1986).

<sup>183</sup> Christopher S. Kelley and Bryan W. Marshall, "The Last Word: Presidential Power and the Role of Signing Statements," 255.

<sup>184</sup> D. Katz and R.L. Kahn, *The Social Psychology of Organizations* (New York: John Wiley, 1966).

<sup>185</sup> Lyn Ragsdale and John Theis, "The Institutionalization of the American Presidency, 1924-1992," 1290.

responsibility for organizing the White House and a cabinet consisting of the vice president and heads of administrative agencies. Because of the complexity of the institutional structure and the wide variety of policy issues which the president must address, the role of the chief of staff has become increasingly important to modern presidents.<sup>186</sup> During the George W. Bush presidency, the vice president's involvement in executive decision making was elevated to a new level as will be discussed later.

(c) Complexity – Ragsdale and Theis suggest that the last two features of institutionalism – complexity and coherence – are indicative of the president's ability to make internal changes in response to external forces. Complexity reflects “increased division of labor and specialization” which enhances institutional stability by making it more difficult to dissolve administrative units.<sup>187</sup> Measures of complexity include the total administrative units within the organization and the amount of staffing. As institutional complexity increases there will be “more discussion points, vetoes, jurisdictional conflicts, and decisions” which may contribute to an individual president's knowledge-base, but may also diminish the efficiency of his decision making powers.<sup>188</sup>

There is no question regarding the degree of complexity in the executive branch. In 2005, there were over 2.7 million federal employees in the executive branch and the

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<sup>186</sup> Karen M. Hult, “The Bush White House in Comparative Perspective,” in *The George W. Bush Presidency: An Early Assessment*, ed. Fred I. Greenstein (Baltimore: Johns Hopkins University Press, 2003), 55.

<sup>187</sup> Ragsdale and Theis, “The Institutionalization of the American Presidency, 1924-1992,” 1291.

<sup>188</sup> Ragsdale and John Theis, “The Institutionalization of the American Presidency, 1924-1992,” 1296.

president was responsible for appointing a small minority of these employees. As a consequence, presidents have valued the role that political appointees play in advancing policy agendas. While expanding policy making authority, the presidency has also sought to expand its control over White House and administrative agency staff. Political appointees grew from 1,229 in the Clinton Administration to 2,000 in the Bush Administration – over thirty-three percent.<sup>189</sup> The highest level appointees, such as cabinet secretaries, are subject to Senate confirmation, and these appointees are responsible for appointing their assistants.

“Virtually all administrations over the past half century have embraced some version of a three-tiered layer cake for interagency policy making.”<sup>190</sup> The top tier consists of the cabinet secretaries who are subject to Senate confirmation. These appointees are responsible for appointing their assistants, the intermediate tier deputies who are second or third in charge of the departments and agencies. The bottom tier consists of assistant secretaries and below. These lower tier employees often retain employment from one president to the next and tend to identify more closely with the mission of their agencies than the president’s policy agenda. The diversity of the administrative work force may create pressure points for individual presidents who seek to impose policy agendas on the administrative agencies, but it helps build the fourth essential characteristic of institutionalization – coherence.

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<sup>189</sup> Office of Personnel Management, *2005 Fact Book* (Washington, D.C.: U.S. Government Printing Office, 2005).

<sup>190</sup> Richard N. Haass, *War of Necessity, War of Choice* (New York: Simon & Schuster, 2009), 45.

(d) Coherence – Coherence reflects the ability of an organization to manage its workload and includes “universalistic rather than particularistic criteria, and automatic rather than discretionary methods for conducting internal business.”<sup>191</sup> Over time, job criteria are developed and the workload begins to follow predictable patterns; daily tasks become more automatic and stability increases.<sup>192</sup> As coherence in personnel increases it tends to transcend changes in presidents and changes in party leadership which ultimately strengthen the office of the presidency.<sup>193</sup> At the same time, increased coherence may make it more difficult for the president to impose his individual preferences in the policy making process.

One of the most obvious measures of coherence may be found in the civil service system in which administrative staff is protected from being dismissed once a new president or a president from a different political party takes office. The magnitude and extent of the administrative bureaucracy’s influence acts not only to ensure stability, but also reinforces the tendency towards institutional stasis.

In short, an individual president’s influence over the policy agenda is subject to the institutional constraints that have been formalized by the Constitution, statutes, and case law. The constraints that the president faces vary from one administration to another. In the domestic arena, the president is challenged by the constraints imposed by

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<sup>191</sup> Nelson Polsby, “The Institutionalization of the U.S. House of Representatives,” *American Political Science Review* 62 (1968): 145.

<sup>192</sup> Ragsdale and John Theis, “The Institutionalization of the American Presidency, 1924-1992,” 1297-1298.

<sup>193</sup> Ragsdale and John Theis, 1301.

Congress and the judiciary. But, in the foreign policy arena, the president is also challenged by external constraints imposed by other nation-states and demanded by the need to protect national security. How well the president is able to manage or overcome these institutional constraints depends upon informal mechanisms, such as his leadership skills, the organizational structure that he establishes within the White House and Executive Office, and how that structure facilitates the president's understanding of the political dynamics and allows him to utilize his special decision making skills.

## **2. The President's Formal and Informal Powers**

Institutional theory suggests that American presidents are bestowed with both formal and informal powers upon taking office. We have stated previously how the president's formal powers arise from constitutional authority, statutes, and case law. Although the Constitution grants the president specific powers, it provides little guidance on how the president should structure an administration to implement these powers.<sup>194</sup> For example, article 2, section 1(2), empowers the president to nominate and appoint, "by and with the Advice and Consent of the Senate," ambassadors, other public ministers and consuls, judges of the Supreme Court, "and all other Officers of the United States" whose appointments are not otherwise provided by the Constitution or established by law. The Constitution also provides that "Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone." How the president executes his powers of appointment has been shaped by historical precedent, legislative

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<sup>194</sup> Glen O. Robinson, Ernest Gellhorn, and Harold H. Bruff, *The Administrative Process*, (St. Paul, MN: West Publishing Co., 1986), 4.

acts, and decisions of the Supreme Court.<sup>195</sup> In the absence of specific legislation, the president has considerable autonomy and flexibility in the authority he delegates to his political appointees and how he interacts with them.

Since informal powers are not specifically delineated by law, they arise from the historical setting and the political climate existing at the time the president is elected. Informal powers continue to evolve throughout the president's term of office. Each president's informal powers are shaped by his personality, world view, and leadership style; the "political capital" that he accumulates prior to taking office; and the set of skills he possesses for managing the endless number of institutional conflicts and constraints that he faces during his administration.

There are many definitions of "world view." This study draws its definition from cognitive philosophy which provides that a person's world view originates from his unique experiences in society, emanates from his socio-economic position, and reflects his religious background, education, ethics, and basic beliefs. This world view becomes part of the president's personality and is manifested in his leadership style.

"Political capital" is often bestowed upon the president by virtue of winning the election. This power is a function of the president's electoral margin, party support in Congress, public approval, and patronage appointments.<sup>196</sup> When a president wins by a landslide, or even a comfortable majority vote, he tends to assume he has been granted a

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<sup>195</sup> Glen O. Robinson, Ernest Gelhorn, and Harold H. Bruff, *The Administrative Process*, 105.

<sup>196</sup> Paul C. Light, *The President's Agenda: Domestic Policy Choice from Kennedy to Carter* (Baltimore, Maryland: John Hopkins University Press, 1983), 15.

popular mandate to implement his political agenda.<sup>197</sup> When the president wins in a close election his political capital is diminished.

The president's informal powers arise out of the organizational structures and decision making processes he adopts and the political appointments he makes. The structural components are subject to the president's management skills and influence his ability to collect, analyze, and evaluate the options available for accomplishing political goals.<sup>198</sup> But the compartmentalization of formal organization structures creates barriers to the decision making process. Informal structures are not found on organization charts, but create links across the formal lines of authority and communications and are a way of breaking down structural barriers.<sup>199</sup>

## **B. George W. Bush's Presidency**

### **1. Historical Setting and Political Climate**

Historically it is during political campaigns that presidential candidates begin to disclose their world views, define their political agendas, accumulate political capital, and set the tone of their leadership styles. The focus in the 2000 presidential campaign was on values and domestic policy, not foreign policy. George W. Bush used vigorous language in his campaign speeches, yet carefully avoided engaging in any lengthy

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<sup>197</sup> David A. Crockett, "The Contemporary Presidency: "An Excess of Refinement": Lame Duck Presidents in Constitutional and Historical Context," *Presidential Studies Quarterly* 38, no. 4 (December 2008): 716.

<sup>198</sup> George C. Edwards III and Desmond S. King, "Introduction," in *The Polarized Presidency of George W. Bush*, ed. George C. Edwards III and Desmond S. King (Oxford: Oxford University Press, 2007), 13.

<sup>199</sup> Charles E. Walcott and Karen M. Hult, *Governing the White House*, (Lawrence, KS: University of Kansas Press, 2007), 313.



discourse regarding specific foreign policy issues. No longer faced with Cold War conflicts fabricated by two contending superpowers, Bush suggested that future threats would come from “rogue nations and terrorists.” He cited a need to prepare for future challenges by creating military forces which would be “more agile, harder to find, easier to move, readily deployable, and lethal in action.”<sup>200</sup>

In regards to foreign trade, Bush extolled the same benefits that Clinton did – an open global economy in which American enterprise and values would prevail.<sup>201</sup> But Bush attempted to distinguish himself from Clinton in his occasional remarks concerning China. Bush described China as a “strategic competitor” as opposed to Clinton’s characterization of China as a “strategic partner.”<sup>202</sup> Beyond these generalizations, substantive foreign policy discussions were virtually absent from the campaign.<sup>203</sup>

With foreign policy in the background, George W. Bush was able to focus on domestic policy and the GOP’s goal of restoring the party to power. The Republican establishment recognized Bush as a winner – a candidate who was loyal to conservative

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<sup>200</sup> See for example, George W. Bush’s campaign speeches to the Veterans of Foreign Wars.

<sup>201</sup> Andrew J. Bacevich, “Different Drummers, Same Drum,” *The National Interest* (Summer 2001): 72.

<sup>202</sup> Toshihiro Nakayama, *Politics of U.S. Policy toward China: Analysis of Domestic Factors* (Washington, D.C.: Brookings Institution, 2006), 2; and Robert G. Sutter, “Grading Bush’s China Policy: A-,” *PacNet* 10 (March 8, 2002), Honolulu: CSIS Pacific Forum, available at [http://www.csis.org/media/csis/pubs/pac0210\[1\].pdf](http://www.csis.org/media/csis/pubs/pac0210[1].pdf) (accessed February 24, 2007).

<sup>203</sup> Norman Birnbaum, “After the Debacle,” *Political Quarterly* 72, no. 2 (April-June 2001): 146-158.

values, but was not divisive. While the Bush name was well respected, George W. Bush himself had the advantage of not being burdened by Washington politics.<sup>204</sup> This was a welcome relief to the party as well as to the American public which had been outraged by Clinton's actions which signaled disrespect for the office.

Although the 2000 election brought victory to the Republican Party, it was tarnished by controversy over the Florida ballots. After losing the popular vote in a disputed election and waiting thirty-six days for the Supreme Court to make its narrow 5-4 decision regarding the Electoral College vote, President Bush was left with very little political capital to build upon. President Bush faced another disadvantage because his Republican Party only held a majority in Congress by a slight margin. The Senate was evenly divided with Vice President Cheney breaking the tie and the House was split 221-212.

The lack of political capital and experience in Washington had potential for inhibiting President Bush's ability to govern. After the Supreme Court's decision, Bush had less than fifty days to hire his staff. To make matters worse, the number of positions requiring Senate confirmation had increased in recent years which meant it could have taken much longer to fill key appointments. Yet, Bush was up to the challenge and did not assume office with the restraint that one might have expected from his narrow and disputed victory.

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<sup>204</sup> William Schneider, "Zealots and Cranks, Be Gone," *National Journal* 31, no. 19 (1999), available at <http://0-find.galegroup.com.bianca.Penlib.du.edu>, Gale doc. # A54775127 (accessed November 15, 2009).

George W. Bush's leadership style and commitment to strengthen the ranks of the Republican Party allowed him to solidify his base of support and overcome these disadvantages. He made structural changes within the EOP that reflected his own goals and approach to governing, he elevated the status of the Vice President, and he moved quickly to fill Senate confirmed positions.<sup>205</sup> In spite of these obstacles he filled political appointments on an average of 8.3 months from nomination to confirmation, which was not much longer than the average of his immediate predecessors, Bill Clinton and George H.W. Bush.<sup>206</sup>

In short, President George W. Bush inherited institutional constraints typical to other presidencies, including prior budget commitments and foreign treaty obligations, as

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<sup>205</sup> Eleven major units composed the EOP under President George W. Bush in 2001: (1) White House Office, (2) National Security Council, (3) Office of Policy Development, (4) Office of Management and Budget, (5) Council of Economic Advisors, (6) Office of Science and Technology Policy, (7) Council on Environmental Quality, (8) Office of the U.S. Trade Representative, (9) Office of Administration, (10) Office of National Drug Control Policy, (11) Office of Homeland Security, and (11) Office of the Vice President.

In 2005, the year that CNOOC proposed to acquire Unocal, the executive departments included Agriculture, Commerce, Defense, Education, Energy, Health and Human Services, Homeland Security, Housing and Urban Development, Interior, Labor, State, Transportation, Treasury, and Veterans Affairs, and the Attorney General. President Bush had also extended cabinet-level rank to the administrator of the Environmental Protection Agency, the director of the Office of Management and Budget, the director of the National Drug Control Policy, and the U.S. Trade Representative, for a total of nineteen cabinet level advisors. Source: White House web site, <http://www.whitehouse.gov/government/cabinet.html> (accessed November 20, 2007).

<sup>206</sup> G. Calvin Mackenzie, "The Real Invisible Hand: Presidential Appointees in the Administration of George W. Bush," *PS: Political Science and Politics* 35, no. 1 (March 2002). The average for George W. Bush's appointments is just slightly more than 8.1 months for George H.W. Bush, and 8.0 months for Clinton, but much higher than Kennedy's 2.4 months and Nixon's 3.4 months. See Brookings Institution, "Presidential Appointee Initiative Urges Senate to End Confirmation Drought," [www.appointee.brookings.org/news/July2402-newsrelease.htm](http://www.appointee.brookings.org/news/July2402-newsrelease.htm) (accessed June 5, 2008).

well as constraints unique to his own presidency. All of these constraints limited his time and ability to collect and analyze information, and also restricted the options for implementing his presidential agenda. Nonetheless, President Bush followed the precedent established by previous presidents when he focused on the power of informal mechanisms to overcome institutional constraints. This study argues that it is the formal constraints created by the American Constitution, statutes, and case law that has contributed to the need for actors within the executive and legislative branches to rely upon informal mechanisms to accomplish policy goals.

## **2. Developing a Leadership Style**

Since our laws grant the president broad discretion in how he organizes the White House, he is able to set up structures that reinforce his own world view and values, and these are manifested in his leadership style. George W. Bush's world view was shaped by his Harvard Business School experiences, his tenure as a corporate executive, and observations of his father's successes and failures as President of the United States. Bush's world view, in turn, helped shape the focus of his campaign for the presidency and his presidential leadership style. According to Daalder and Lindsay, Bush identified three essential challenges for the president: (1) the challenge of leadership which is to "outline a clear vision and agenda," (2) the challenge of building a strong team of effective people to implement the president's agenda, and (3) the challenge of sticking to an opinion even when the polls show the public moving in the opposite direction.<sup>207</sup>

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<sup>207</sup> Ivo H. Daalder and James M. Lindsay, "Bush's Foreign Policy Revolution," in *The George W. Bush Presidency*, ed. Fred I. Greenstein (Maryland: Johns Hopkins University Press, 2003), 103-04.

Daalder and Lindsay suggest that what made Bush unique among presidents was his “logic about how America should act in the world.”<sup>208</sup> Bush believed that the key to securing America’s interests in the world was primacy in a hegemonic world order. This view was based on five propositions that are consistent with realist theory: (1) the world is a dangerous place, (2) the key players in world affairs are self-interested nation states, (3) the key to survival is power, (4) multilateral institutions and agreements are not necessarily conducive to achieving American interests, and (5) the United States is a unique power with a focus on personal freedoms and open markets.<sup>209</sup>

Bush’s strategy for working with Congress was similar to that which he pursued as governor in Texas where he developed proposals that appealed to both Democrats and Independents. Upon taking federal office, he deviated little from the agenda that he had described on the campaign trail. His agenda was a narrow one intended to limit competition among issues for public attention and congressional support. His tax cuts appealed to the Republican base that elected him and his education reforms were a way to reach across party lines to win over moderates. But one of the more difficult issues on the presidential agenda was that of energy security, which meant creating energy independence and economic security.<sup>210</sup>

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<sup>208</sup> Daalder and Lindsay, *Bush’s Foreign Policy Revolution*, 106.

<sup>209</sup> The first four propositions are consistent with the realist view; the fifth proposition is unique to President Bush.

<sup>210</sup> Julian Darley, *High Noon for Natural Gas: The New Energy Crisis*, (White River Junction, Vermont: Chelsea Green Publishing Co., 2004), 142, quoting “President Focuses on Energy Security in Radio Address,” White House, February 23, 2002,

There was increased pressure on both Congress and the presidency to elevate energy policy on their political agendas after California's energy crisis had brought about blackouts. Upon taking office, President Bush acknowledged the energy crisis as the most important task of his presidency. Shortly afterwards he created a task force of senior government representatives, called the National Energy Policy Development Group (NEPDG), with Vice President Cheney as chair to develop a long-range plan to meet American's energy requirements.

The NEPDG released a report on May 17, 2001 which called for drilling in the Arctic National Wildlife Refuge (ANWR) at the same time that it blocked an increase in fuel efficiency standards. The report created strong opposition within the environmental community and Democratic representatives in Congress. Although it was controversial, the proposed drilling in ANWR allowed the Bush Administration to claim commitment to a policy of independence from the Middle East. Actually, as Michael Klare points out, the report did not offer a real plan for decreasing dependence on imported oil.<sup>211</sup> Instead, it supported the priority of increasing and protecting the flow of petroleum from foreign sources to U.S. markets.<sup>212</sup>

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<http://www.whitehouse.gov/news/releases/2002/02/20020223.html> (accessed February 13, 2004).

<sup>211</sup> Michael Klare, "Bush-Cheney Energy Policy: Procuring the Rest of the World's Oil," *Foreign Policy in Focus* (January 2004), [www.commondreams.org/cgi-bin/print/cgi?file=/views04/0113-01.htm](http://www.commondreams.org/cgi-bin/print/cgi?file=/views04/0113-01.htm) (accessed June 12, 2009).

<sup>212</sup> *National Energy Policy Act* (2001). Chapter 8 focuses on strengthening American energy security and prosperity by working with other countries to increase global production. The plan mandates that energy security must become a priority for foreign

Support from Tom DeLay and other House leaders, was instrumental to forming a coalition with Democrats from oil and gas states and other interest groups, such as the Teamsters, to move the energy policy through Congress. The president won a 240-189 victory in the House, but the Senate was more challenging, especially after the unexpected defection of life-long Republican Senator Jeffords to the Democratic Party. Losing the majority in the Senate meant losing the advantages that come with majority status, including control over the timing and substance of the legislative agenda. As a consequence, Bush's team of advisors assumed a key role in moving his energy agenda forward – especially after 9/11 when the focus turned to national security.

Finally, Bush persevered with his commitment to stick to an opinion once it had been formed. Reflecting on his accomplishments, George W. Bush stated that he would “like to be remembered as a person who first and foremost, did not sell his soul in order to accommodate the political process.” He proudly proclaimed, “I came to Washington with a set of values, and I’m leaving with the same set of values, and I darn sure wasn’t going to sacrifice those values; that I was a president that had to make tough choices and was willing to make them.”<sup>213</sup> Bush believed that leaders should not succumb to public opinion, but should adhere to what they believe is the best course of action. He

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trade and policy. Available at <http://www.netl.doe.energy/publications/press/2001/nep/nep.html> (accessed August, 21, 2009).

<sup>213</sup> George W. Bush, Interview with Doro Bush Koch for StoryCorps National Oral History Project, quoted in Kenneth T. Walsh, “Looking Back on a Troubled Presidency; Bush is Hoping to Cast His Legacy in a Positive Light,” *U.S. News & World Report* 145, no. 13 (December 15, 2008).

demonstrated this belief in his commitment to the war on terror and military action in Iraq. It was also an attitude reflected in diplomacy and U.S. China foreign policy.

### **3. Creating a Organizational Structure and Decision Making Scheme**

(a) Political Appointments – Political appointments are at the heart of the executive organizational structure and the president’s decision making scheme. The tradition of the president’s cabinet may be traced back to the beginning of the presidency itself. Based on article 2, section 2 of the U.S. Constitution, one of the principal purposes of the cabinet is to advise the president on any subject he may require relating to the duties of their respective offices.<sup>214</sup> Traditionally, the president’s cabinet has consisted of the vice president and secretaries of the executive departments.

President Bush took great strides to appoint key individuals within his cabinet (as well as the White House and administrative bureaucracy) who shared his world view and ideology. He also focused on honoring political obligations and achieving diversity. Consistent with his business management background, Bush appointed a cabinet that symbolized corporate America.<sup>215</sup> The key appointees and their influence over Bush’s foreign policy decisions are discussed below.

First, and foremost, was Vice President Cheney who began a career in public service when he joined the Nixon Administration in 1969 and then later served on

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<sup>214</sup>White House. <http://www.whitehouse.gov/government/cabinet.html> (accessed Nov. 20, 2007).

<sup>215</sup> The primary source of information on Bush’s cabinet was the White House Web Site, <http://www.whitehouse.gov/government/cabinet.html> (accessed from January 1, 2005 through December 31, 2008).



Congress representing the State of Wyoming. But Cheney also had a distinguished career in business and he was CEO of Halliburton Corporation when he joined Bush's campaign ticket. Although business experience was prevalent in Bush's political appointments, Kenneth Walsh notes that when Bush asked the head of his vice presidential search team, Dick Cheney, "to actually become his running mate, it was clear that he valued Cheney's Washington experience above all."<sup>216</sup> He told Cheney that he would need his advice in good times and bad, but Cheney's advice was actually most valued during times of crisis. President Bush came to rely on his vice president more than any other advisor and confidant. He immediately gave Cheney responsibility for developing the national energy policy and welcomed him to attend any executive meeting of his choice.<sup>217</sup>

Unlike previous administrations, Bush made Cheney chair of the president's Budget Review Board which rules on appeals of OMB decisions regarding proposed funding for executive branch departments. Bush also named two of Cheney's top aides – Lewis Libby and Mary Matalin – assistants to the president.<sup>218</sup> This was quite unusual, but served to bring the White House and vice presidential staff closer together.

Bush also gave Cheney an office in the White House in addition to the one traditionally reserved for the vice president in the Senate. In Cheney's words, his close

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<sup>216</sup> Kenneth T. Walsh, "Looking Back on a Troubled Presidency; Bush is Hoping to Case his Legacy in a Positive Light," *U.S. News & World Report*, 145, no. 13 (December 15, 2008): 22.

<sup>217</sup> Cheney and the Bush Administration focused on developing a national energy policy that would provide energy security (defined as energy independence and economic security). See Julian Darley, *High Noon for Natural Gas: The New Energy Crisis*.

<sup>218</sup> Carl M. Cannon, "The Point Man," *National Journal* 34, no. 41 (October 11, 2002): 2956-64.

relationship with the president created a “seamless operation” in which he and everyone else was there “to serve the president.”<sup>219</sup> In an interview with Cokey Roberts, Vice President Cheney gave insight into the administration’s perspective concerning the historical struggle for power between the presidency and Congress. Cheney explained that the president’s powers had been so compromised by Watergate that it diminished the “ability of the president of the United States to do his job.”<sup>220</sup>

Cheney’s commitment to taking back presidential powers was demonstrated on a number of occasions. One particularly notable case concerned Vice President Cheney’s role as chairman of the NEPDG, which was charged with developing a national energy policy. In April 2001, Representative John Dingell (D-MI), ranking member of the House Committee on Energy and Commerce, and Henry Waxman (D-CA), ranking member of the House Committee on Government Reform, wrote to the GAO Comptroller General Walker to request investigation of the conduct and composition of the NEPDG.

Initially the GAO requested information concerning the composition of the task force, the persons with whom Cheney, in his capacity as chair of NEGDC, and the task force met, the meeting notes and minutes, and the costs incurred in developing policy recommendations. The congressional members claimed they wanted this information to aid with considering proposed legislation, assessing the need and merit of legislative changes and conducting oversight of executive branch administration of existing law.

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<sup>219</sup> Cannon, “The Point Man,” 2956-64.

<sup>220</sup> Charlie Savage, *Takeover: The Return of the Imperial Presidency and the Subversion of American Democracy* (New York: Little Brown, 2007), 75.

Even though Title 31, section 712 broadly authorizes the GAO to investigate all matters relating to the use of public funds, Cheney refused.<sup>221</sup> Even after the GAO voluntarily narrowed its request by eliminating the minutes and notes and information presented to the task force, Cheney still refused to comply. The vice president was resolute in his belief that the presidency had been weakened by “unwise compromises” that were made over the previous thirty to thirty-five years and he refused to release any substantive information.<sup>222</sup> It was his position that the GAO lawsuit was an intrusion into “the inner sanctum of executive-branch deliberations” which threatened to undermine the constitutional powers of the executive branch.<sup>223</sup>

Although the issue was not resolved, the GAO postponed its pursuit of the requested information out of deference to the administration’s need to respond to the events of September 11<sup>th</sup>. Then, early in 2002, after several senators joined the previous request by the House of Representatives, the comptroller general wrote a letter to the chairmen and ranking members of the Senate and House Committees stating that the GAO had exhausted all statutorily required processes for resolving access requests out of court. Cheney’s refusal was an affront to the GAO which is a nonpartisan group that is

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<sup>221</sup> The GAO authorities are set forth in *U.S. Code* 31, §§ 701 et seq.

<sup>222</sup> Dana Milbank, “Cheney Refuses Records’ Release,” *Washington Post*, January 28, 2002; and Joel D. Aberbach, “The State of the Contemporary Presidency” in *The George W. Bush Presidency: Appraisals and Prospects*, ed. Colin Campbell and Bert A. Rockman (Washington, D.C., CQ Press, 2004), 58.

<sup>223</sup> John C. Eastman, “Why Dick Cheney is Fighting the GAO,” Ashbrook Center for Public Affairs, July 2002, [hppt://www.ashbrook.org/tools/printerpage.asp](http://www.ashbrook.org/tools/printerpage.asp) (accessed December 5, 2008).

widely respected in Washington. Although the GAO was sensitive to the vice president’s “need to protect executive deliberations,” it was concerned that Cheney had denied access to information that the GAO had “a statutory right to obtain.”<sup>224</sup> The GAO proceeded to file suit against Vice President Cheney in *Walker v. Cheney* reasoning that “if the Vice President’s arguments were to prevail, any administration seeking to insulate its activities from oversight and public scrutiny could do so by assigning those activities to the Vice President or a body under the White House’s direct control.”<sup>225</sup>

*Walker v. Cheney* was a landmark case because the GAO had never before filed suit against the executive branch for failing to cooperate with an inquiry.<sup>226</sup> It was also distinguished by the fact that the suit was brought by a member of the Republican Party to raise important constitutional questions involving the actions of a Republican vice president exercising executive privilege independent of the president. But the case did not prevent Cheney from continuing with his efforts to bolster executive privilege and elevate his vice presidential authorities to new heights. The more Cheney pushed, the more he gained influence over the president’s leadership style – which became increasingly inflexible, insular, and aggressive. As we will see later, the more the president relied on Cheney, the less the president relied on his other advisors for input into the decision making process.

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<sup>224</sup> *Walker v. Cheney*, 02CV00340, February 22, 2002.

<sup>225</sup> *Walker v. Cheney*, 02CV00340, February 2, 2002, 22.

<sup>226</sup> The GAO lawsuit was dismissed on December 9, 2002 by U.S. District Court Judge John Bates.

Besides Cheney, other appointees brought valuable corporate experience to the Bush Cabinet, including Samuel W. Bodman and Donald Rumsfeld. Bodman joined the Bush Administration in the Department of Commerce after a career in venture capital, serving as chairman, CEO, and director of a number of publicly owned corporations. Then he served a year as deputy secretary of Treasury before being sworn in as the eleventh secretary of Energy on February 1, 2005. Rumsfeld had a distinguished career in the military and politics, as well as the corporate world. He served seven years in Congress, followed by nearly a decade of political appointments, before serving as chief executive officer, president and chairman of G.D. Searle & Company, chairman of General Instrument Corporation, and chairman of the board for Gilead Sciences, Inc. As secretary of Defense, Rumsfeld was characterized as a conservative hawk; he was an advocate for a strong defense policy with a particular emphasis on missile defense systems.<sup>227</sup>

Consistent with campaign promises and the need to strengthen political capital, Bush strategically diversified his cabinet. He appointed two African-Americans (General Colin Powell at the State Department and Roderick Page at the Department of Education), two East Asians, one Hispanic, and three women to highly visible positions.<sup>228</sup> But even these appointments were a reflection of corporate America. For

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<sup>227</sup> During the Clinton Administration, Rumsfeld led a commission to assess the ballistic missile threat to the United States and warned Congress about “potentially hostile nations” such as China. See U.S. Congress, *Report of the Commission to Assess Ballistic Missile Threat*, 104<sup>th</sup> Cong., 2<sup>nd</sup> sess., July 15, 1998.

<sup>228</sup> Daniel Bell, “Election 2000 and Future Prospects,” *Society* (May/June, 2001): 82.

example, Carlos Gutierrez joined Kellogg as a sales representative, but rose to executive office, and was named to chairman of the board before he was nominated as secretary of Commerce in February 2005.

Secretary of State Colin Powell had a distinguished military career, having served as a captain in Viet Nam before his promotion to full general under former President George H.W. Bush's administration and service as chairman of Joint Chiefs of Staff during the Gulf War. Powell was perceived as a moderate with regards to military matters. For instance, in his confirmation hearing before the Senate Foreign Relations Committee, Powell stated that the key to dealing with the Chinese was to expose them "to the powerful forces of a free enterprise system in democracy, so they can see that this is the proper direction in which to move."<sup>229</sup> This moderate approach and the respect that Powell had earned from both Democrats and Republicans led to the Senate's unanimous approval of his appointment.

As a moderate, Powell also preferred a policy of containment regarding Iraq, but this made him the "odd man" among Bush's other hawkish advisors. Even though Powell succumbed to Bush's strategy for overthrowing Saddam Hussein after 9/11, political infighting among the Department of State, the Department of Defense, and the Vice President's Office led to his resignation on November 15, 2004.<sup>230</sup>

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<sup>229</sup> Andrew J. Bacevich, "Different Drummers, Same Drum," *The National Interest* (Summer 2001); 71.

<sup>230</sup> It has been rumored that Powell was asked by resign by Andrew Card. See Karen De Young, "Falling on His Sword: Colin Powell's Most Significant Moment Turned Out to be His Lowest," *Washington Post*, October 1, 2006.

President Bush relied on a number of other appointments to high ranking positions to compensate for his lack of experience in Washington. The *National Journal* reports that forty-three percent of Bush appointees had worked in his father's administration, eighty-six percent had worked for the government previously, and twenty percent had worked for Washington lobbying firms.<sup>231</sup> One of these experienced and trusted appointments was National Security Advisor Condoleezza Rice who later replaced Colin Powell as secretary of state in 2005.

Interestingly, there is no provision in law establishing an assistant to the president for national security affairs, but the position of national security advisor has roots in the National Security Council (NSC) established by President Harry Truman in 1947 with four statutory members – the president, vice-president, secretary of state, and secretary of defense. At first, the assistants that managed the NSC simply reported to the president. Then President Dwight Eisenhower created the position of special assistant for national security to assist with long term planning. President Kennedy, who wanted to be more directly involved with foreign policy, modified the position into one that managed the president's policy affairs and worked to integrate the national security bureaucracy with the president's foreign policy agenda. Daalder notes that the “position gained prominence after President John F. Kennedy's election . . . and has become central to presidential conduct of foreign policy.”<sup>232</sup> National security advisors must balance their

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<sup>231</sup> James A. Barnes, “Bush's Insiders,” *National Journal*, June 23, 2001, <http://nationaljournal.com>, 2

<sup>232</sup> Ivo H. Daalder, “In the Shadow of the Oval Office: The Next National Security Advisor,” *Foreign Affairs* 88, no. 1 (January/February 2009): 114.

allegiance to the president with their commitment to manage a policy process that engages various senior officials and their agencies.

Historically, the national security advisor has influenced the president's foreign policy initiatives and decisions concerning overseas business transactions. Analysts have explained this phenomenon by noting the national security advisor's proximity to the Oval Office and the frequency with which he or she interacts with the president.<sup>233</sup> As foreign policy became more complex, presidents came to rely on their national security advisors to work with various departments to integrate diverse policy dimensions, including defense and diplomacy, finance and trade, the environment and homeland security, and science and technology. By the time George W. Bush took office there was a "general consensus" as to the appropriate role of the national security advisor.<sup>234</sup>

The position requires someone who can balance the need to make decisions with sensitivity to the roles of the other secretaries and advisors. A key ingredient to the national security advisor's success is maintaining the trust of the president and the other senior advisors, all of which must have confidence that he or she will convey their views and advice to the president.

Condoleeza Rice joined George W. Bush's Administration as assistant to the president for national security after a career in academia, and several stints of service in the previous Bush Administration, including service on the National Security Council.

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<sup>233</sup> Ivo H. Daalder, "In the Shadow of the Oval Office: The Next National Security Advisor," 123.

<sup>234</sup> Karl Inderfurth and Loch K. Johnson, *Fateful Decisions: Inside the National Security Council* (New York: Oxford University Press, 2004).



Prior to joining the current administration, she gained experience as a member of several boards and commissions, including the board of directors for the Chevron Corporation. She was an expert on Eastern Europe and the former Soviet Union, and as a “realist,” believed that the U.S. must maintain a position of military strength in its relations with communist countries.<sup>235</sup> She also believed that the administration should focus on strengthening relations with Japan and other East Asian allies while downplaying relations with China.<sup>236</sup>

Ultimately, the national security advisor is responsible for helping the president make the best decisions as expeditiously as possible. Some analysts argue that Rice followed the president’s orders without examining alternative actions or examining the consequences.<sup>237</sup> But given Bush’s managerial style, it is unlikely that he would have been receptive to any attempts to engage him in analysis. He viewed himself as “the Decider” whose primary responsibility was making tough decisions in difficult times.

A distinguishing characteristic of Bush’s presidency was that he did not appoint China experts to his cabinet or to key foreign policy advisory positions. Believing the Clinton Administration had over emphasized China’s importance, Bush did not rush into developing his own China policy. It was only after a U.S. Navy EP-3 surveillance aircraft and a Chinese jet fighter collided in the South China Sea in April 2001 that Bush

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<sup>235</sup> Condoleezza Rice, “Promoting the National Interest,” *Foreign Affairs* 79, no.1 (January/February 2000): 52.

<sup>236</sup> *Ibid.*, 55-56.

<sup>237</sup> Ivo H. Daalder, “In the Shadow of the Oval Office: The Next National Security Advisor,” 121.

was forced to turn his attention to China. Even though U.S.-China relations were tense, Bush pledged to do “whatever it takes” to protect Taiwan,<sup>238</sup> which included military measures as well as downgrading China’s stature in foreign policy by working through State Department and Defense Department channels.<sup>239</sup>

Although China experts did not define Bush’s cabinet, two senior policymakers had significant experience in Asia – Deputy Secretary of State Richard L. Armitage and Deputy Secretary of Defense Paul D. Wolfowitz. Armitage served three tours of duty in Vietnam and was in Saigon with it fell to the North Vietnamese. During the Reagan Administration, he served as deputy assistant secretary of defense for East Asia and Pacific Affairs and also assistant secretary of defense for international security affairs. Like Rumsfeld, Armitage saw the relationship with Japan as fundamental to U.S. national security supported a missile defense policy. Wolfowitz had served as ambassador to Indonesia and assistant secretary of state for East Asia and Pacific Affairs. He, too, advocated for stronger ties with Japan, at the expense of ties with China, and a policy of increased missile defense.

Another political appointment relevant to the development of foreign policy under the Bush Administration was U.S. Trade Representative Robert B. Zoellick. Zoellick gave a preview of the Bush Administration’s trade agenda when he testified before the

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<sup>238</sup> Steve Mufson, “President Pledges Defense of Taiwan,” *Washington Post*, April 26, 2001; and David E. Sanger, “Bush Tells Beijing the U.S. is Ready to Defend Taiwan,” *New York Times*, April 26, 2001.

<sup>239</sup> Robert Sutter, “Bush Administration Policy toward Beijing and Taipei,” *Journal of Contemporary China* 12, no. 36 (August, 2003): 480, 485.

House Ways and Means Committee. Emphasizing that “[t]rade policy is the bridge between the President’s international and domestic agendas,” Zoellick pushed for trade liberalization and the free exchange of goods and services to boost domestic economic growth. Assuring the Committee he would consult with them often, he asked Congress to give him “the strong hand of presidential trade promotion authority.”<sup>240</sup>

(b) Bush’s Hierarchical Approach to Decision Making

The president’s decision making scheme consists of how recommendations are made to the president – whether he is presented with one perspective of each policy issue or whether he was alerted to disagreements across policy issues; whether he looks at just one dimension or multiple dimensions of the information presented; whether he receives single or multiple recommendations for action; and how he communicates policy issues and decisions to the public.<sup>241</sup> Ultimately, the president’s decision making scheme has an impact on whether he is able to build coalitions, coalesce congressional support, and win public endorsement. But just as the separation of powers has created issues of control and responsibility among the various branches of government, it has also created conflicts within each branch as the cabinet members, advisors, and executive staff, often have overlapping responsibilities.

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<sup>240</sup> Robert B. Zoellick, speaking before the U.S. House of Representatives Committee on Ways and Means, on March 7, 2001, cited in Bruce Stokes, “Free Trade-Offs,” *Foreign Policy* (May/June, 2001): 62-63.

<sup>241</sup> See Matthew J. Dickinson, “Neustadt, New Institutionalism, and Presidential Decision Making: A Theory and A Test,” *Presidential Studies Quarterly* 35, no. 2 (June 2005): 259-288 for a discussion of the elements of the president’s decision making scheme.

Initially, President Bush took a restrained approach to his executive responsibilities which seemed to reflect his limited background in public policy. Although the organizational structure that existed when he took office mirrored the structure of presidents before him, he drew upon his business school education and the successes he had as Governor of the State of Texas, to form a structure and managerial style that relied upon a hierarchical approach to decision making.<sup>242</sup> For example, in organizing the White House staff, President Bush appointed Andrew Card as his chief of staff, but did not make Card the only senior advisor who reported directly to him. He also appointed Karl Rove as his political strategist and Karen Hughes as his public relations advisor. Karl Rove was put in charge of the newly created Office of Strategic Initiative (OSI) which was designed to “think ahead and devise long term political strategies.”<sup>243</sup>

According to Hult, forming the triad of Andrew Card, Karl Rove, and Karen Hughes was “consistent with reports of [the president’s] desire for multiple sources of information” and was also a mechanism for maintaining control and keeping any one of his advisors from becoming too powerful.<sup>244</sup> But after Karen Hughes left the president’s

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<sup>242</sup> Initially Bush retained the National Economic Council (NEC) created under executive order by President Clinton to coordinate policy making for domestic and international issues and to monitor implementation of the president’s economic policy agenda. See Kenneth I. Juster and Simon Lazarus, *Making Economic Policy: An Assessment of the National Economic Council* (Washington D.C.: Brookings Institution, 1997) for details on the National Economic Council.

<sup>243</sup> Kathryn Dunn Tempas and Stephen Hess, “The Contemporary Presidency: The Bush White House: First Appraisals, *Presidential Studies Quarterly* 32 (September 2002): 579.

<sup>244</sup> Karen M. Hult “The Bush White House in Comparative Perspective,” 55-56.

staff early in 2002 Karl Rove's influence over the president increased substantially.<sup>245</sup> Evidence of Rove's influence is abundant, but one example is the impact he had regarding the president's political appointments which extended from the executive branch to the federal judiciary. The evaluation criterion for political appointments included partisan as well as ideological standards. This criterion came to play when the White House Personnel Office sought advice concerning nominees. The Personnel Office would not just consult the staff in the Office of Political Affairs, as had been done in previous administrations, but would go to Senior Advisor Karl Rove as well.<sup>246</sup>

President Bush often chose to achieve policy goals through his cabinet (to which he had delegated some "untraditional" functions),<sup>247</sup> political appointees, and bureaucratic channels rather than through Congress or the party apparatus.<sup>248</sup> For example, when Bush came to office, he admitted that he was weak in foreign relations experience and assembled a team of experts to counterbalance that weakness. This group of eight Republican experts, nicknamed the "Vulcans," was led by National Security Advisor Condoleezza Rice and Paul Wolfowitz, dean of Johns Hopkins School of Advanced International Studies. Both Rice and Wolfowitz had served under the elder

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<sup>245</sup> See Richard L. Berke and David E. Sanger, "Some in Administration Grumble as Aide's Role Seems to Expand," *New York Times*, May 13, 2002.

<sup>246</sup> James A. Barnes, "Bush Insiders," *National Journal*, June 23, 2001, 1870.

<sup>247</sup> Ellen Nakashima and Dana Milbank, "Bush Cabinet Takes Back Seat in Driving Policy," *Washington Post*, September 5, 2001.

<sup>248</sup> Christopher S. Kelley, "Rethinking Presidential Power – the Unitary Executive and the George W. Bush Presidency" (paper presented at the 63<sup>rd</sup> Annual Meeting of the Midwest Political Science Association, Chicago IL, April 7-10, 2005).

Bush – Rice as the president’s advisor on Soviet affairs and Wolfowitz as undersecretary for defense policy. Other Vulcans who served in the previous Bush Administration, and their previous titles, included: Robert Blackwill, White House advisor on European and Soviet affairs; Stephen J. Hadley, assistant secretary of defense for international security policy; Robert Zoellick, undersecretary of state for economic affairs and White House deputy chief of staff. Vulcans who served under President Reagan, and their titles, included Richard Armitage, assistant secretary of defense for international security affairs; Richard Perle, assistant secretary of defense for international security policy; Dov Zakheim, deputy undersecretary of defense for planning and resources.

These appointments were significant because they indicated Bush’s “own foreign policy predispositions.”<sup>249</sup> In contrast to Republican “sovereignists” who served in Congress in the mid-1990s and favored isolationism, the Vulcans supported engagement and free trade. It was this preference for letting the free market reign that caused some legislators in Congress to question whether the Bush Administration was taking the Exon-Florio Amendment seriously, or whether the presidency was more inclined to let corporate profits prevail over all other national interests.

In laying the foundation for understanding Bush’s decision making scheme, we have examined his leadership style, his key political appointments, and how he interacted with his advisors and cabinet members. Now we turn to the strategies he used to build coalitions, congressional support, and public endorsement.

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<sup>249</sup> Ivo H. Daalder and James M. Lindsay, “*Bush’s Foreign Policy Revolution*,” 102-03.

#### **4. Building Coalitions and Congressional Support**

Under institutional theory one might expect a strong tendency towards cooperation when the president and the majority in Congress represent the same party. This is because members of the same party are more likely to adhere to similar ideologies and political views. There is also strength that can be garnered from party cohesiveness when it comes to a candidate's ability to finance political campaigns and secure electoral votes. Once a candidate is elected, the public tends to judge the elected official based upon his or her ability to fulfill campaign promises. Given the division of power in the American system, individual politicians are more likely to be successful if they can build a coalition of support, and the party is fundamental to building coalitions.

By contrast, when members of Congress and the president are from opposing parties they tend to adhere to different ideologies and view one another as a threat to attaining personal and political goals. In spite of the expectation of cooperation along party lines, there are occasions in which the president and legislators from the same party may disagree. This may be because legislators want to be re-elected and are motivated by a desire to serve their constituents, but not all of their constituents support all of the president's policies. Or, as in the Unocal Case, it may be because individual legislators become concerned about the president diminishing the importance of respecting congressional oversight.

While it is in the president's best interest to cooperate with members of his party in Congress, the diversity of interests represented in Congress means that it is not always

possible. The president must constantly lobby legislators and form coalitions of support. But the coalitions of support will vary depending upon the issue, the particular circumstances surrounding that issue, and the cohesiveness of the party as a whole. Sometimes the president will need to reach across the aisle and cultivate support from the opposite party, but this type of coalition building becomes much more difficult when one or both chambers of Congress are controlled by the opposition party.

In his campaign, Bush had run as a “compassionate conservative,” suggesting that he would work to overcome the strong partisanship that had characterized the 1990s, as well as the Texas statehouse when he was governor. But President Bush quickly learned that the political game in Washington was much more challenging than Texas politics. Even though Bush had begun to reach out to individual Democrats before he was declared the winner in the Florida election, he still failed to convince Democrats and Republicans to work together to push legislation through Congress.

Given the circumstances, President Bush enjoyed exceptional legislative success in the early years of his administration. Some attribute this phenomenon to Bush’s ideological and partisan compatibility with Republicans in Congress and the majorities that his party held in the House for the first six years and the Senate for the first four years.<sup>250</sup> Some attribute it to the strategy of focusing on just a few issues and playing to interests held by both Democrats and Republicans, such as education reforms and lower taxes. And some attribute it to 9/11 and the unique situation in which Americans rallied

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<sup>250</sup> Lawrence R. Jacobs, “The Promotional Presidency and the New Institutional Toryism: Public Mobilization, Legislative Dominance, and Squandered Opportunities,” in *The Polarized Presidency of George W. Bush*, ed. George C. Edwards III and Desmond S. King (Oxford: Oxford University Press, 2008), 298.



around the president and the firm stance he took in preventing America from being the target of future terrorist acts.

Certainly, President Bush had the advantage of a Republican-controlled Congress when he took office, but the lack of political capital made him dependent upon his the cabinet, the White House staff, and administrative agencies for promoting his political agenda. Fortunately, he had the advantage of the Republican majority in the House of Representatives, and even though it was by a narrow margin, the House is biased towards the majority and a cohesive majority has substantial power. This meant Bush was well-positioned to take advantage of the procedural and organization tools in the hands of the Speaker of the House.

By contrast, the Senate operates by more permissive rules and the 50-50 split between the parties in the Senate presented a challenge to the president. The divided Senate “forced Republicans to enter into a power sharing agreement with Democrats specifying equal numbers of members on every committee” even though Republicans would chair committees.<sup>251</sup> Tension between President Bush and his party in Congress began to emerge shortly after Senator Jeffords’ defection from the Republican Party on May 24, 2001.<sup>252</sup> Noting that many Republicans in Congress had never served with a

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<sup>251</sup> Barbara Sinclair, “Context, Strategy, and Chance,” in *The George W. Bush Presidency: Appraisals and Prospects*, ed. Colin Campbell and Bert A. Rockman (Washington, D.C.: CQ Press, 2004), 113.

<sup>252</sup> Senator Jeffords changed the Senate composition from an even split along party lines, with Vice President Dick Cheney breaking tie votes. Jeffords made a deal with the Democrats to vote with them on procedural matters in exchange for the committee seats which would have been available to him if he had been a Democrat during his entire Senate tenure.

president of their own party and none had served in the majority with a Republican president, Sinclair suggests that “congressional Republicans were accustomed to setting their own course.” They may have had unrealistic expectations from the president, but they were disappointed when President Bush asked them to “make tough votes that conflicted with their ideology.” After losing the majority, Republican senators became much more outspoken when they did not agree with the president, that is, until September 11, 2001.<sup>253</sup>

Throughout his administration, whenever President Bush found that he could not win Congress over, he turned to his veto power to object to specific provisions of a bill without vetoing the entire bill. Although the Constitution grants this power to the president, it does not provide any formal rules mandating how the president may or may not use the signing statement to accomplish his own goals. According to a study by David Birdsell, the Reagan, George H.W. Bush, and Clinton administrations used signing statements to argue “on behalf of a president’s right not to enforce ‘constitutionally unsound’ provisions and all three presidents made much more frequent use of signing statements than their predecessors.”<sup>254</sup> But Birdsell suggests that President George W. Bush went far beyond previous presidents in expanding his executive prerogative beyond congressional will.

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<sup>253</sup> Barbara Sinclair, “Context, Strategy, and Chance,” in *The George W. Bush Presidency: Appraisals and Prospects*, 121.

<sup>254</sup> David S. Birdsell, “George W. Bush’s Signing Statements: The Assault on Deliberation,” *Rhetoric & Public Affairs* 10, no.2 (2007): 339.

What made President Bush's approach unique was not just the number of signing statements accompanying the bills he signed, but the character of the statements. Rather than following the precedent of framing statements in the first person, Birdsell points out that President Bush framed his statements in the third person. He asserted the constitutional authority "of the President" rather than his own authority as it related to the particular bill. His signing statements also lacked specificity regarding his objections, which made it virtually impossible for Congress to respond. Finally, the language he used was "formulaic and broad, asserting power without a detailed rationale for the power."<sup>255</sup>

A successful president does not just limit himself to winning over Congress he also works to win over the public. Public opinion is instrumental in bolstering the president's position vis à vis Congress because legislators votes are influenced by vocal interest groups and supportive constituents. This means that presidents must be astute in managing their communications with the public. How President Bush handled communications is discussed below.

### **5. President Bush's Communications Network and Public Endorsement**

The White House communications network is complex and multifaceted, and focused on briefings, press releases, and advance copies of speeches as tools for managing the media. The modern communications network may be attributed to President Wilson who expanded relations with the press, centralized control in the White

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<sup>255</sup> David S. Birdsell, "George W. Bush's Signing Statements: The Assault on Deliberation," 342.

House, reinstated the tradition of orally delivering the State of the Union address to Congress, and initiated national campaigns. White House ties to the media expanded under President Franklin D. Roosevelt after he gave the press secretary greater authority to coordinate the media and its contacts with the administration and to discipline executive departmental staff to project a public message designed by the president.<sup>256</sup> The role of the media has continued to grow ever since.

In today's world, the communications operations are needed to promote the president's brand of leadership and advocate for the policies, laws, and programs that he wants to accomplish. Communications are a serious matter and are handled by the Offices of Communications, Media Affairs, Speechwriting, and Global Communications. By Bush's second term, communications staff exceeded 300, ranging from senior officials down to personnel who record presidential speeches, press conferences, and briefings, and transcribe the sessions.<sup>257</sup> One reason behind the growth of the communications staff is that modern technology has increased the channels of

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<sup>256</sup> Lawrence R. Jacobs, "The Promotional Presidency and the New Institutional Toryism: Public Mobilization, Legislative Dominance, and Squandered Opportunities," in *The Polarized Presidency of George W. Bush*, ed. George C. Edwards III and Desmond S. King (Oxford: Oxford University Press, 2008), 288.

<sup>257</sup> Martha Joynt Kumar, "Managing the News," in *The Polarized Presidency of George W. Bush*, ed. George C. Edwards III and Desmond S. King (Oxford: Oxford University Press, 2008), 353-54.

communication and the president can no longer make “off the record” remarks to a unique audience.<sup>258</sup> Everything is open to public scrutiny.

President Bush’s communications and advocacy were shaped by a White House structure organized around the management principles that he followed in private business and as governor of Texas. Martha Kumar suggests that his management style was based on Peter Drucker’s principles which call for setting goals, developing plans for getting to the desired goal, assigning operational responsibilities, and allowing staff to implement the plans.<sup>259</sup> By appointing loyalists to the White House staff and top administrative positions, he was able to accomplish the mandate that the administration “talk about what we want to talk about, not what the press want to talk about”<sup>260</sup> The communications system was also influenced by Chief of Staff Andrew Card’s “compartmentalized” operating system based on a “need to know”, and Karl Rove’s attempts to integrate policy, politics and publicity.<sup>261</sup>

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<sup>258</sup> Martha Joynt Kumar, “Source Material: The White House and the Press: News Organizations as a Presidential Resource and as a Source of Pressure,” *Presidential Studies Quarterly* 33.3 (2003): 669+, *Academic OneFile*, <http://0-find.galegroup.com.bianca.penlib.du.edu/gtx/start.do?prodId=AONE&userGroupName=Udenver> (accessed November 15, 2009).

<sup>259</sup> Martha Joynt Kumar, “The Contemporary Presidency: Communications Operations in the White House of President George W. Bush: Making News on His Terms,” *Presidential Studies Quarterly* 33, no. 2 (June 2003): 366-93.

<sup>260</sup> Lawrence R. Jacobs, “The Promotional Presidency and the New Institutional Toryism: Public Mobilization, Legislative Dominance, and Squandered Opportunities,” in *The Polarized Presidency of George W. Bush*, ed. George C. Edwards III and Desmond S. King (Oxford: Oxford University Press, 2007), 289.

<sup>261</sup> Martha Joynt Kumar, “Managing the News,” 353-54.

James Wilkinson has described President Bush's goal as a communicator as wanting "to make news on his own terms."<sup>262</sup> Because Bush wanted to avoid communications mistakes that might make him more vulnerable, he rarely allowed staff, who might not be sophisticated in dealing with the press, to appear in the news or the briefing room to provide background policy information. While this was a change from previous administrations in which policy specialists and cabinet secretaries often explained policy initiatives, the approach was relaxed a bit by Bush's second term when his ratings began to fall. As Martha Joynt Kumar has observed, Card's system was efficient in avoiding overlap of duties, but often resulted in situations where the staff was "caught by surprise on some major issues."<sup>263</sup> This may have been the case when the CNOOC bid for Unocal became an explosive issue in the American press. When confronted by the media, the administration's spokespersons gave vague responses, dodging any official response, other than a statement that executive review of the proposed acquisition was premature.

Like other modern presidents, President Bush tracked public opinion, although his administration sought to convey the impression that it was not as "obsessed" as the previous Clinton Administration.<sup>264</sup> Edwards suggests that public relations are fundamental to the modern presidency and there are three premises about the relationship between public opinion and presidential leadership: (1) public support is a "crucial

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<sup>262</sup> Martha Joynt Kumar, "Managing the News," 357.

<sup>263</sup> *Ibid.*, 354.

<sup>264</sup> Karen M. Hult, "The Bush White House in Comparative Perspective," 72.

political resource” for the president because it makes it difficult for Congress to deny the demands of a president with popular support, (2) the president earns public support through his performance and by actively taking his case to the people, (3) the president can persuade and mobilize the public through a “permanent campaign.”<sup>265</sup> Typically, there is a honeymoon period in which presidents have a high degree of public support. Americans tend to want the president to succeed, and even if they did not support the president during the campaign, they are likely to give him some time to get acclimated.

From the very beginning of his term, President George W. Bush took his case to the people with a public relations campaign that surpassed that of any new president. But this was not a surprising tactic given that he took office after losing the popular vote by less than one percent. The election had become even more controversial as it hinged on the outcome of controversies which emerged concerning the voting mechanics in the State of Florida where his brother was governor. After thirty-six days, the Supreme Court declared Bush the winner and he took office with an air of confidence that belied his thin victory.

Although Bush went to the public to promote his proposals, he did so in a controlled environment. With little national speaking experience, he relied heavily on prepared scripts. But even the most eloquently written speeches – such as the 2001 inaugural address – lost some of their dramatic impact from poor delivery. The press began to question his absence from the public view just three months into his

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<sup>265</sup> George C. Edwards III, “Riding High in the Polls: George W. Bush and Public Opinion,” in *The George W. Bush Presidency: Appraisals and Prospects*, Colin Campbell and Bert A. Rockman (Washington, D.C.: CQ Press, 2004), 16-17.

presidency<sup>266</sup> and, later on, others noted that prior to the night of the September 11, 2001 tragedy he had not addressed the nation once from the Oval Office.<sup>267</sup>

Bush worked diligently to achieve the promises he had made to the Republicans who had played a key role in bringing him to office. While it is common for presidents to campaign for the party's congressional candidates in the mid-term elections, Fortier and Ornstein describe President Bush's effort as "unprecedented."

He made a record ninety campaign appearances, including campaign stops for twenty-three congressional candidates, sixteen Senate hopefuls, and candidates in a number of hotly contested gubernatorial races. Along the way he attended nearly seventy-five fund-raisers and raised a record of more than \$144 million. His campaign trips had him on the road nearly nonstop in the weeks leading up to the November 5 election, including a whirlwind tour of fifteen states in the last five days before the election."<sup>268</sup>

In spite of an ambitious travel schedule, he also sent proposals to Congress to support his campaign issues of income tax cuts, education reform, and overhauling the military. Then, even when Congress changed key elements of his proposed policies, he emphasized his success in getting the legislation through Congress rather than bringing attention to how Congress had modified his proposals.<sup>269</sup>

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<sup>266</sup> David S. Broder, "The Reticent President," *Washington Post*, April 22, 2001.

<sup>267</sup> Fred I. Greenstein, "The Leadership Style of George W. Bush," in *The George W. Bush Presidency*, ed. Fred I. Greenstein (Maryland: Johns Hopkins University Press, 2003), 6-8.

<sup>268</sup> Fortier, John C. Fortier and Norman J. Ornstein, "President Bush: Legislative Strategist," in *The George W. Bush Presidency*, ed. Fred I. Greenstein (Baltimore: Johns Hopkins University Press, 2003), 166.

<sup>269</sup> George C. Edwards III, "Riding High in the Polls: George W. Bush and Public Opinion," 27.



This discussion of George W. Bush's presidency illustrates how a president may take advantage of informal mechanisms to upset the institutional balance of power so as to dominate foreign policy decision making. Although taking office as a Washington outsider with little experience and even less political capital, President Bush built upon on his political connections to assemble an impressive team of advisors with expansive corporate experience. The president and his advisors were inclined to support free trade policies with minimal oversight and regulation.

After 9/11, Bush took a strong and decisive position against global terrorism which gave him the political capital needed to push his policy agendas through Congress. At the same time, members of Congress were also concerned about protecting national security. When CNOOC made its offer to buy Unocal in 2005, it created a perfect storm in Washington and Congress demanded that the president take immediate action. This next section will discuss the institutionalization of legislative powers and the tensions between Congress and the presidency that encourages individual members to resort to informal mechanisms to achieve their policy goals.

### **C. Institutionalization of Legislative Powers**

#### **1. Characteristics of the Institutionalized Legislature**

(a) Autonomy – By the end of World War II, Congress's policy making role had diminished to such an extent that some congressmen were beginning to question the institution's survival.<sup>270</sup> With the burgeoning growth of the federal economy and increasing budget deficits, Congress delegated more and more legislative authority to

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<sup>270</sup> Estes Kefauver and Jack Levin, *A Twentieth Century Congress* (New York: Essential Books, 1947), 4-5.

administrative agencies, but often failed to provide meaningful oversight. In 1946, Congress responded to its loss of power by initiating several reforms, including the Administrative Procedure Act (APA), the Legislative Reorganization Act (LRA), and the Employment Act.<sup>271</sup> Each of these acts demonstrated Congress's ability to adapt to a more complex society. The Administrative Procedure Act was designed as a means of relying on administrative agencies to perform legislative functions.<sup>272</sup> At the same time that Congress alleviated its work load when it delegated rule-making procedures to the agencies, it improved transparency by requiring that agencies hold public hearings and obtain citizen input in the rule-making process.

The LRA was particularly significant because it radically restructured the organization of Congress. It provided rules of the Senate and the House of Representatives and recognized the constitutional right of either chamber to change its own rules. It reduced the number of standing committees, gave parallel jurisdiction to the House and Senate committees, and designed the overall committee structure to coincide with the structure of the federal administration.<sup>273</sup> For the first time, the LRA defined

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<sup>271</sup> *Administrative Procedure Act*, Public Law 79-404, *U.S. Statutes at Large* 60 (1946): 637, codified at *U.S. Code* 5 (1946), §§ 500 et. seq.; *Legislative Reorganization Act*, Public Law 79-601, *U.S. Statutes at Large* 60 (1946): 812, codified at *U.S. Code* 15 (1946), §§ 1021 et seq.; and *Employment Act*, Public Law 79-304, *U.S. Statutes at Large* 60 (1946): 23, codified at *U.S. Code* 15 (1946), § 1021.

<sup>272</sup> David H. Rosenbloom, "Whose Bureaucracy Is This, Anyway?' Congress' 1946 Answer," *PS: Political Science and Politics* 34, no. 4 (December 2001): 774.

<sup>273</sup> *Stamler v. Willis*, 293 U.S. 217 (per curiam) (1968) discusses the history of the *Legislative Reorganization Act of 1946* and how it changed the Rules in both the House and the Senate.

and assigned to standing committees an implicit responsibility for “legislative oversight.”<sup>274</sup> This improved supervision of administrative agencies contributed to the institutionalization of Congress.

(b) Adaptability – In our discussion of the presidency, we defined adaptability as awareness of internal and external environments the ability to take action to achieve a balance between the two. While both the president and Congress are constrained by the Constitution and statutory law, Congress faces additional challenges. It is a democratic body whose interests and positions are defined by the states and the constituents they represent. As such, this study assumes that the legislature is more restricted in its ability to adapt to changes in the external environment. It is much more difficult to achieve a consensus when members of Congress are accountable to their states rather than one ultimate authority. History has taught legislators that they must form coalitions and support groups to accomplish their policy goals. For this reason, they have taken advantage of their powers under the Constitution to develop their own committees, with rules and operating procedures to guide the committee’s work.

Throughout the evolution of standing committee structure, two principles have remained constant: (1) the principle that the majority controls the committees, and (2) the principle that the minority is entitled to an equitable voice in proportion to its

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<sup>274</sup> Walter Kravitz, “The Legislative Reorganization Act of 1970,” *Legislative Studies Quarterly* 15, no. 3 (August, 1990): 383; Walter Kravitz, “Evolution of the Senate’s Committee System,” *The ANNALS of the American Academy of Political and Social Science* 411 (1974): 36-37, <http://ann.sagepub.com/cgi/content/abstract/411/1/27> (accessed October 20, 2009); and David H. Rosenbloom, “‘Whose Bureaucracy Is This, Anyway?’ Congress’ 1946 Answer,” *PS: Political Science and Politics* 34, no. 4 (December 2001): 774.

representation in the house of Congress as a whole.<sup>275</sup> The ability of Congress to adapt to internal and external conditions is demonstrated by the changes in the seniority system which accompanied changes in the standing committees. Initially, committee chairmanship was awarded to those delegates with the greatest length of service in Congress. However, as the number of issues increased and as the issues become more complex, Congress recognized the need for more equitable committee assignments and the dispersal of power beyond just a few legislators. Seniority still plays a role, but it is now seniority on the committee, rather than in Congress as a whole, that positions a member for leadership.

A committee's power is also preserved by the convention in which members of the standing committee are assigned as conferees when a bill is considered by both chambers. This practice was institutionalized in the House during the 109<sup>th</sup> Congress by Rule I, clause 11 which specifies the members of the House appointed to conference committees "shall to the fullest extent feasible, include the principal proponents of the major provisions of the bill or resolution passed or adopted by the House."<sup>276</sup> But the House can adapt to the particular circumstances in which a bill is passed. If a bill is modified on the floor, the Speaker can appoint conferees who supported the floor position rather than the committee position. Although this study focuses on the House, the Senate showed a similar ability to adapt with the changes in its own rules.

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<sup>275</sup> Walter Kravitz, "The Legislative Reorganization Act of 1970," 383; and Walter Kravitz, "Evolution of Senate's Subcommittee System," 30.

<sup>276</sup> Rule 1, clause 11, available at [www.rules.house.gov/rulepred/109\\_house\\_rules\\_text\\_.htm](http://www.rules.house.gov/rulepred/109_house_rules_text_.htm) (accessed July 6, 2009).

(c) Complexity – Complexity involves an increased division of labor and specialization. In the earlier section on the presidency we discussed the Legislative Reorganization Act. The LRA provided greater coherence to both the presidency and Congress by delineating organizational structures and responsibilities; it also contributed to institutional independence and flexibility. But the LRA had some unexpected outcomes for Congress. First, by authorizing the standing committees to hire professional staff, the LRA led to explosive growth in the number of congressional staff and enlarged support services for research and policy analysis. Not only did the number of individual legislative aides increase<sup>277</sup> but, in 1970, the Congressional Research Service replaced the outdated Legislative Reference Service as Congress’s primary source for research and policy analysis.<sup>278</sup> Since then, a variety of improvements to the General Accounting Office has increased its capacity to evaluate administrative performance; and the Chief Financial Officers Act of 1990 has also contributed to legislative oversight.<sup>279</sup> Today, the General Accounting Office, the Congressional Research Service, the Congressional Budget Office, and the Office of Technology

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<sup>277</sup> According to the *Congressional Quarterly Weekly Report* (November, 24 1979): 2631-2652, the number of aides to individual legislators increased from an average of 1.3 per House member in 1973 to 2.2 in 1978 and from an average of 3.9 per Senator in 1973 to 5.5 in 1979.

<sup>278</sup> Walter Kravitz, “The Legislative Reorganization Act of 1970,” 395. From FY 1970 to FY 1980, CRS budgeted positions increased from 323 to 868. Similarly, from FY 1972 to FY 1988, requests for CRS assistance grew by 260%, with committee requests increasing by approximately 460%.

<sup>279</sup> See Thomas M. Franck and Edward Weisband, *Foreign Policy by Congress* (New York: Oxford University Press, 1979), 84.

Assessment all include foreign specialists. With its own staff, Congress was no longer dependent upon the executive branch for information resources.

A second unexpected outcome of the 1946 LRA was the uncontrolled growth of subcommittees. The consolidation of committees resulted in larger jurisdictions, which led to the need for more and more subcommittees to divide the work load. The proliferation of subcommittees led to the creation of more chair positions, which resulted in the distribution of influence among more members of Congress. Concern over increasing subcommittee autonomy led to revision of the Legislative Reorganization Act in 1970. Specifically, section 110 reinforces the principle that Senate committees control the funds of their subcommittees<sup>280</sup> and section 129(a) reinforces the rule that subcommittees are part of House committees and subject to its authority and direction.<sup>281</sup>

Congress has a number of mechanisms for influencing administrative agencies without having to amend authorizing statutes. In addition to the regularity of decision making promoted by the APA, the Senate has the constitutional power of “advice and consent” to the President’s nominations of agency heads. Although some believe this power has devolved into nothing more than a formality, others believe it is still a powerful tool in shaping public opinion.<sup>282</sup> Congress also has the power of

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<sup>280</sup> See U.S. Congress. Joint Committee on the Organization of the Congress, *Final Report*. 89<sup>th</sup> Cong., 2d sess., S. Rep. 1414 (1966): 13-14.

<sup>281</sup> Walter Kravitz, “The Legislative Reorganization Act of 1970,” 377. See House of Representatives Committee on Rules, *Legislative Reorganization Act of 1970*, 91<sup>st</sup> Cong., 2<sup>nd</sup> sess., H. Rep. 91-1215 (1979): 8.

<sup>282</sup> J.M. Graham, and V.H. Kramer, *Appointments to the Regulatory Agencies: The Federal Commerce Committee and the Federal Trade Commission (1949-1971)*, report

appropriations, which may be even more influential today. Annual budget hearings in both houses provide an opportunity for Congress to review agencies' performance, to hear and express opinions, and to further influence agency actions by approving or denying specific expenditures.<sup>283</sup> With the evolution of statutory laws Congress contributed to the institutionalization of a "legislative-centered" federal administration where agencies assist with legislative functions, where Congress plays a role in overseeing agency work, and where Congress may intervene in agency decision making "through casework and other forms of constituency service."<sup>284</sup>

(d) Coherence – As stated previously, coherence reflects the ability of an institution to manage its workload based upon universal criteria. Each individual legislator has benefited from increased staff support, but Congress as a whole manages its workload through its organizational structure and rules.

While the presidency has benefited from the coherence provided by the civil service system, Congress has benefited from the coherence provided by the system of incumbency and social networks. Few incumbents are defeated and, as a result, some members of the House of Representatives have served for more than thirty years. Members with greater length of service are more likely to have cultivated relationships and built supportive networks among other legislators, within the federal agencies, and

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prepared for the Senate Commerce Committee, 94<sup>th</sup> Cong., 2<sup>nd</sup> sess. (Washington D.C.: U.S. Government Printing Office, 1976).

<sup>283</sup> Glen O. Robinson, Ernest Gellhorn, Harold H. Bruff, *The Administrative Process* (St. Paul, MN: West Publishing Co., 1986), 81.

<sup>284</sup> David H. Rosenbloom, "'Whose Bureaucracy Is This, Anyway?' Congress' 1946 answer," *PS: Political Science and Politics* 34, no. 4 (December 2001): 773.

with experts who populate think tanks and advisory boards and commissions that influence policy making in Washington. Senior legislators are also more knowledgeable of the rules and procedures and how to manipulate them to accomplish policy goals. For example, since Congress operates on the basis of standing committees, those with the most seniority in the majority party chair the most important committees.<sup>285</sup> This committee structure creates a formidable challenge to presidents and will be discussed in the next section.

## **2. The Legislature's Formal and Informal Powers**

Institutional theory suggests that Congress is bestowed with formal and informal powers. Just as the Constitution grants the president specific powers, article 1, section 1 provides that all legislative powers shall be vested in Congress. As the fundamental source of lawmaking, Congress plays a primary role in controlling and overseeing administrative agencies. Article I, section 8 (18) of the Constitution provides that Congress has the power to

. . . make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof.

These laws include statutes that create agencies and define their substantive and procedural limits, as well as statutes that define foreign policy criteria and restrictions.

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<sup>285</sup> In the House of Representatives, Ways and Means, Appropriations, Budget, and Armed Services dominate; in the Senate, Foreign Relations, Armed Services, Budget, and Appropriations committees dominate.



(a) Constitution and Congressional Rules

The Constitution provides that each house may determine the rules of its proceedings and must keep and publish a journal of its proceedings.<sup>286</sup> Legislators are required to follow these rules when introducing legislation. But the rules have become extensive and are often cumbersome. Because the rules have slowed down the policy making process or created inefficiencies, over time Congress has devised a system of informal mechanisms that legislators may utilize to accomplish their goals.

These informal mechanisms for policy making take place throughout the formal process. Although there are specific formal procedures for introducing bills and violation of the procedures can kill a bill, the formal procedures do not necessarily give insight into why legislators introduce certain bills. Nor do the formal procedures help us understand the political strategy that an individual legislator chooses to adopt. However, institutionalism suggests that the informal mechanisms underlying Congressional actions may provide insight into legislative outcomes.

Why legislators introduce bills depends upon a variety of factors. They may introduce legislation in response to pressure by interest groups; they may want to publicize issues that they are personally concerned about; they may want to convey a message to the president or an executive agency; or they may simply want to go on the record as doing something about an issue for the benefit of their constituents and to gain constituent support. This study suggests that examination of public records and statements to the media regarding the particular legislation will give insight into why

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<sup>286</sup> U.S. Constitution, article 1, sec. 5, cls. 2-3.

individual legislators introduced the legislation. The theoretical approach also suggests that insight may be gained from examining precedent established in the legislative history. Some of the questions raised by the institutional approach are as follows: Does the legislator have a history regarding the particular issue? What positions has he taken in the past? Has he been able to generate support for the issue in the past, or has he faced opposition?

Legislators adopt informal tools at each stage of the legislative process. During the first stage of introducing legislation, the experienced legislator may consider the following factors: (1) how to title the bill so that it has the broadest appeal to the public or attracts the media's attention; (2) whether to include co-sponsors and how to determine who has the greatest potential to influence others over the issue; (3) whether to introduce the bill early in the legislative session so as to compensate for Senate filibuster, or late in the session to take advantage of public pressure for Congress to act quickly before recess; (4) whether to introduce companion bills concurrently in the other chamber; and (5) how to draft the language of the bill so that it falls within the jurisdiction of a committee that might be more sympathetic to the issue and more capable of pushing the bill through the legislative process.<sup>287</sup>

Although both chambers are guided by rules of procedure, the rules in the House are much more formal because of its size. In addition, the House has developed different procedures for handling minor legislation and uncontroversial issues compared to major

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<sup>287</sup> Walter J. Oleszek, *Congressional Procedures and the Policy Process*, Washington D.C.: CQ Press, 2007):78.

bills or more controversial issues. There are four legislative calendars for scheduling legislative actions in the House. These are as follows:

(1) Calendar of the Committee of the Whole House on the State of the Union which handles actions concerned with raising, authorizing, or spending funds;

(2) Private Calendar which handles actions concerned with matters of concern to individual persons or entities;

(3) Discharge Calendar which handles bills that have been removed from committees through special procedures; and

(4) Corrections Calendar which is concerned with unnecessary or cumbersome rules and regulations. This last calendar was removed from the House rulebook at the beginning of the 109<sup>th</sup> Congress.<sup>288</sup>

One tool that the Speaker uses to control the agenda is the suspension of the rules. Prior to the 109<sup>th</sup> Congress, the suspension procedure was in effect on Mondays, Tuesdays, and the last six days of the session. At the beginning of the 109<sup>th</sup> Congress, Rules Chairman David Dreier (R-CA) added Wednesdays to the suspension calendar.<sup>289</sup> There are three rules that govern suspension procedures: (1) debate is limited to forty minutes and is divided between proponents and opponents, (2) amendments to a bill may be included if the amendments are included in the motion to suspend the rules, and (3) the only vote on the measure is a vote to suspend the rules and pass the bill. A quorum

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<sup>288</sup> Walter J. Oleszek, *Congressional Procedures and the Policy Process*, 116-117.

<sup>289</sup> Representative David Drier of California speaking for H. Res. 5, § 2 changes to Rule XV, cl. 1(a), on January 4, 2005, to the House of Representatives, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151:H13..

must be present for the vote and it must pass by a two-thirds vote. Typically, the Speaker will not schedule bills under the suspension rule unless he or she is confident of the two-thirds vote. But, if the bill fails to pass under the suspension rule, it may be considered again under the regular House procedures.<sup>290</sup>

The suspension procedure helps expedite legislation that appeals to a majority of the House. Committee chairs tend to support the suspension rules because they protect a bill from amendments on the floor and points of order. Majority party leaders like to use the suspension procedure to move their legislative agenda forward, but minority party leaders may oppose the suspension rule procedure on bills which they believe require more lengthy debate or wish to amend.<sup>291</sup> In recent years, suspension procedures have been used more often. Oleszek suggests that this is because it “gives lawmakers who are frustrated by their inability to modify major bills a chance to offer additional suspension measures that serve their constituents, make policy, and enhance their influence in the chamber.”<sup>292</sup>

House rules allow five standing committees direct access to the floor for certain bills. They initiate legislation measures as follows: Appropriations Committee may report general appropriations bills; Budget Committee may report budget resolutions; House Administration Committee may report matters relating to enrolled bills, House expenditures and committee funding; Rules Committee determines rules and the order of

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<sup>290</sup> Walter J. Oleszek, *Congressional Procedures and the Policy Process*, 118.

<sup>291</sup> *Ibid.*

<sup>292</sup> *Ibid.*, 119.

business; and Standards of Official Conduct Committee may recommend action regarding conduct of a member or employee of the House.

Other standing committees do not have the same privilege and act only on legislation referred to them. Most legislation does not go directly from the committee to a calendar and to the House floor. A bill must have privilege, that is, precedence over the regular order of business.<sup>293</sup> Major bills get to the floor through the Rules Committee.

The First Congress appointed an eleven-member body in April 1789 to draft its procedures. For nearly a century afterwards, each Congress would appoint a panel to prepare its rules. The Rules Committee became a permanent committee in 1880 and soon developed the practices followed today, such as reporting rules agreed to by the majority that control the time allowed for debate and the extent to which bills could be amended from the floor. Traditionally, the Rules Committee is an agent of the leadership and functions to implement the majority party's agenda. The Speaker has the power of appointment and the disproportionate partisan ratio guarantees majority control.

The power of the Rules Committee is in its scheduling responsibilities. As bills are reported out of committee, they are entered in chronological order on the Union or House Calendar. Major legislation is granted precedence for consideration on the floor through a special order obtained from the Rules Committee. The chair of the committee reporting the bill submits a written request for the special order to the chair of the Rules Committee. The Rules Committee holds a hearing in which witnesses are limited to

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<sup>293</sup> William Holmes Brown and Charles W. Johnson, *House Practice: A Guide to the Rules, Precedents, and Procedures of the House* (Washington, D.C.: Government Printing Office, 2003), 657.

lawmakers who debate the proposal. This has been described as a “dress rehearsal” in which the committee serves as the first audience for the legislation outside of the committee or subcommittee reporting it.<sup>294</sup> After the hearing, the Rules members write their rule and vote on it. Then the rule is considered on the House floor as privileged matter which means no more than one hour of debate and no amendments before a vote.

Rules serve several purposes: (1) the order of precedence on the Calendars, (2) the length of general debate, (3) dispensing with the first reading of the bill and amendments that are preprinted in the Congressional Record, (4) limiting the number of amendments, and (5) moving the bill to an immediate vote. The Rules Committee has the power to block or delay legislation from reaching the floor. The committee serves as an informal mediator of disputes among House members and over legislation with overlapping jurisdiction.

The Rules Committee grants three basic kinds of rules: open, closed, and modified. The distinction pertains to the amendment process. Under an open rule, amendments may be offered from the floor as long as they comply with House rules and precedents, such as the writing requirement. During the Bush Administration there was a decline in the number of open rules. Rules Committee member James P. McGovern (D-

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<sup>294</sup> *A History of the Committee on Rules, 97<sup>th</sup> Cong., 2nd sess.* (Washington, D.C.: Government Printing Office, 1983).

MA) observed that only one non-appropriations bill out of 190 was considered under an open rule in the 109<sup>th</sup> Congress.<sup>295</sup>

Closed rules prohibit floor amendments except those offered by the reporting committees. In recent years there has been an increase in the number of closed rules that require a bill be considered in the House and not the Committee as a Whole under procedures that limit debate to one hour and restrict or prohibit amendments.<sup>296</sup> Some critics, like Representative McGovern (D-MA), believe closed rules hamper legislative process and violate democratic values; while supporters such as Representative Capito (R-WV) say they are needed for complex measures subject to intense lobbying.<sup>297</sup>

Modified rules may be open or closed. A modified open rule may indicate all parts of a bill are open to amendment except a few sections. A modified closed rule may state that an entire bill is closed to amendment except for certain sections. During the 109<sup>th</sup> Congress Republicans began to characterize modified closed rules as “structured” rules, thereby suggesting that they were not restrictive, but fair and systematic.<sup>298</sup>

In addition to these three forms, the House rules allow for waivers, or temporarily setting aside certain procedures or points of order. The primary purpose is to waive points of order against consideration of legislation that is privileged but has violated

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<sup>295</sup> Representative Jim McGovern of Massachusetts speaking against the House resolution Adopting House Rules for the 109<sup>th</sup> Congress, on December 7, 2006, H. Res. 5, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.* 152, no. 134: H8896.

<sup>297</sup> Representative Shelley Moore Capito of West Virginia speaking for the House resolution Adopting House Rules for the 109<sup>th</sup> Congress, on December 7, 2006, H. Res. 5, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.* 152, no. 134: H8896.

<sup>298</sup> Walter J. Oleszek, *Congressional Procedures and the Policy Process*, 133.

House rules. It is typically used at the end of the session when legislators want to wrap up business quickly.

(b) Legislative Seniority System

Although modern legislators are much more individualistic than in the past, they are conscious of their position in the legislative hierarchy. This is reflected in a variety of situations, ranging from their committee assignments to voting patterns and electoral vulnerability.<sup>299</sup>

Committees can be divided into different types – policy committees are those that attract members who want to make good public policy; power committees are those that expand the member’s legislative jurisdiction. For example, the House Energy and Commerce Committee is a powerful committee because it combines strong legislative jurisdiction with effective oversight responsibilities.

To overcome opposition to policy initiatives presidents have developed strategies to push legislation through Congress. One such strategy involves appointment of liaison staff to establish and maintain relations with Congress. These staff members target key legislators in both houses, keep the president informed of “power clusters,” keep congressional members informed of presidential initiatives, and recommend tactics to the president for developing support of his initiatives.”<sup>300</sup>

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<sup>299</sup> Lawrence S. Rothenberg and Mitchell S. Sanders, “Modeling Legislator Decision Making: A Historical Perspective,” *American Politics Research* 30, no. 3 (May 2002): 235-264.

<sup>300</sup> Sam C. Sarkesian, John Allen Williams and Stephen J. Cimbala, *U.S. National Security: Policymakers, Processes, and Politics*, 4<sup>th</sup> ed. (Boulder, CO: Lynne Rienner Publishers, 2008), 180.



Although the committee structure is essential to how Congress functions, the internal power system is not totally dependent upon the committees. The power of Congressional leadership positions, such as the Speaker of the House and majority and minority leaders in both houses, often trump the powers of the committee chairs. As a consequence, power in Congress is fragmented and derived from a variety of sources, such as leadership status, personal relationships, and the “power of the purse,” all of which may be utilized to act as a check on the president’s authority over foreign and national security policies.

(c) Delegation of Powers and Legislative Oversight

In the early years, as Congress began enacting legislation to delegate powers to administrative agencies, it also began conferring some decision making discretion on the administrators of those agencies.<sup>301</sup> Perhaps unexpectedly, while creating broad administrative powers, Congress also provided the presidency with increased autonomy and budgetary control. This transfer of powers was gradual at first.<sup>302</sup> Following the

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<sup>301</sup> Initially, the Supreme Court denied the permissibility of delegation, *Field v. Clark*, 143 U.S. 649 (1892), but as pressure grew for doctrinal change, delegation was permitted where the legislature sets standards to limit the scope of agency discretion, *Buttfield v. Stranahan*, 192 U.S. 470 (1904).

<sup>302</sup> See Herbert Hoover, Presidential Publication No. 112 - Special Message to the Congress Proposing a Study of the Reorganization of Prohibition Enforcement Responsibilities, June 6, 1929, documented at [www.presidency.ucsb.edu/ws/index.php?pid=21819&st=hoover&st1=reorganization](http://www.presidency.ucsb.edu/ws/index.php?pid=21819&st=hoover&st1=reorganization). See President Herbert Hoover, Pub. Paper 50, Special Message to the Congress on the Reorganization of the Executive Branch, February 17, 1932 and June 30, 1932, documented at [www.presidency.ucsb.edu/ws/index.php?pid=23449&st=hoover&st1=reorganization](http://www.presidency.ucsb.edu/ws/index.php?pid=23449&st=hoover&st1=reorganization); and President Herbert Hoover, Pub. Paper 423, Special Message to the Congress on the Reorganization of the Executive

Great Depression, President Hoover sought authority to reorganize the executive and administrative agencies, but was cautious about overstepping his constitutional powers.<sup>303</sup> Assured by such prudence, Congress granted the president authority to consolidate the agencies and “to segregate regulatory agencies and functions from those of an administrative and executive character.”<sup>304</sup> To increase efficiency, Congress also authorized the president to make changes by Executive Order but restricted this executive authority by stipulating that Executive Orders could not abolish the statutory functions of agencies. To ensure executive compliance with this restriction Congress required that the president transmit Executive Orders to Congress while in session and provided that the orders would not become effective for 60 days unless Congress approved them earlier.<sup>305</sup>

President Franklin D. Roosevelt continued the quest to update the administrative machinery so as to give the chief executive greater managerial control. He appointed a Committee on Administrative Management to examine inefficiencies and to make recommendations for change. President Roosevelt passed the committee’s “five-point”

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Branch, June 30, 1932, [www.presidency.ucsb.edu/ws/index.php?pid=23381&st=hoover&st1=reorganization](http://www.presidency.ucsb.edu/ws/index.php?pid=23381&st=hoover&st1=reorganization) (accessed August 21, 2009).

<sup>303</sup> For example, when President Hoover sought to strengthen protection of the nation’s borders against illegal aliens, he recommended that Congress appoint a “joint select committee” to study the border issue and offered to appoint a committee from the departments to cooperate with the congressional committee.

<sup>304</sup> *Reorganization Act of 1932, U.S. Code*, part 2, § 401(d).

<sup>305</sup> President Herbert H. Hoover, “Special Message to Congress on Reorganization of the Executive Branch,” Dec. 9, 1932, Pub. Paper 423 in John T. Woolley and Gerhard Peters, *The American Presidency Project* (online), Santa Barbara, CA: University of California (hosted), available at [www.presidency.ucsb.edu/ws/index.php?pid=15343](http://www.presidency.ucsb.edu/ws/index.php?pid=15343) (accessed August 21, 2009).

program on to Congress for legislative action. The recommendations included expanding the White House staff to help the president keep in touch with administrative affairs and to obtain the knowledge required for decision making.<sup>306</sup>

After adopting the Reorganization Act of 1939, Congress applied the legislative veto to resolve delegation problems related to national security and foreign affairs issues. Congress continued to include the legislative veto in statutes delegating legislative power, and presidents continued to accept the legislative veto as the price to pay for obtaining exceptional authority, but the constitutionality of the veto was uncertain.<sup>307</sup>

#### **D. 109<sup>th</sup> Congress**

##### **1. Historical Setting and Political Climate**

Historically, Congress has focused primarily on domestic matters. But as influence within the executive branch has continued to move away from the State Department toward the White House and functional departments with international responsibilities, congressional access to foreign policy decision making has been increasing. This change is the result of increased complexity of foreign policy issues and greater crossing of domestic and international considerations on many non-security issues. By 2005, congressional members were more likely to take the initiative to join

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<sup>306</sup> President Franklin D. Roosevelt, “Message to Congress Recommending Reorganization of the Executive Branch, January 12, 1937, Pub. Paper No. 9 in John T. Woolley and Gerhard Peters, *The American Presidency Project* (online), Santa Barbara, CA: University of California (hosted), available at [www.presidency.ucsb.edu/ws/index.php?pid=15748](http://www.presidency.ucsb.edu/ws/index.php?pid=15748) (accessed August 21, 2009).

<sup>307</sup> The Supreme Court finally considered the constitutionality of the legislative veto in the landmark case, *INS v. Chada*, 464 U.S. 919 (1983).

with like-minded colleagues in asserting independent positions on foreign policy matters, whereas earlier in our nation's history they might have simply accepted guidance from the White House or other executive departments.<sup>308</sup>

Although Congress asserts its policy making muscle from time to time, the president still has an advantage in the national security arena because intelligence, operational instruments, and the power bases are still located in his office. Even though Congress has increased its staff and has greater research capabilities, the departments of Defense, State, and Homeland Security, and the National Security Council, the Central Intelligence Agency, and the Chiefs of Staff continue to dominate national security policy.<sup>309</sup>

## **2. Legislative Decision-Making**

There is a significant body of research with a diversity of opinion as to who influences U.S. foreign policy and the policy preferences of public officials. The most prevalent external influences may be categorized into three groups: organized interest groups, knowledge-based experts, and voters or public opinion.<sup>310</sup> Business corporations and associations are particularly influential because of their effects on the economy, their

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<sup>308</sup> Barbara B. Crane and Jason L. Finkle, "The United States, China, and the United Nations Population Fund: Dynamics of U.S. Policymaking," *Population and Development Review* 15 (March 1989).

<sup>309</sup> Sam C. Sarkesian, John Allen Williams and Stephen J. Cimbala, *U.S. National Security: Policymakers, Processes, and Politics*, 4<sup>th</sup> ed. (Boulder, CO: Lynne Rienner Publishers, 2008), 181.

<sup>310</sup> Lawrence R. Jacobs and Benjamin I. Page, "Who Influences U.S. Foreign Policy?" *American Political Science Review* 99, no. 1 (February 2005).

powerful lobbying efforts, and the link between lobbying and campaign contributions.<sup>311</sup> Knowledge-based experts have become more and more important to legislators as our society has become more complicated. The range and variety of issues in which legislators must be conversant has expanded exponentially, while the number of legislators representing the population has grown incrementally. Even with the growth of support staff, it is impossible for any one legislator to be fully informed on every issue considered in Congress. Although it is commonly accepted that legislators must be responsive to public opinion, it is more likely that members of the House of Representatives will be more sensitive to public opinion because of the frequency of their elections in small, decentralized districts, whereas Senators are more insulated from public opinion because of their longer terms.<sup>312</sup> But these differences may have diminished in an information society dominated by C-Span and the internet. Legislators will tend to weigh the merits of a proposed policy against their assessment of its acceptability.<sup>313</sup> But it is generally agreed that there is a hierarchy of values when legislators consider foreign policy, with domestic political factors taking precedent over foreign policy decisions.<sup>314</sup>

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<sup>311</sup> Helen Milner, *Interests, Institutions, and Information: Domestic Politics and International Relations* (Princeton, NJ: Princeton University Press, 1997).

<sup>312</sup> Lawrence R. Jacobs and Benjamin I. Page, "Who Influences U.S. Foreign Policy?" 109.

<sup>313</sup> Barbara Farnham, "Impact of the Political Context on Foreign Policy Decision-Making," *Political Psychology* 25, no. 3 (2004): 443-445.

<sup>314</sup> Barbara Farnham, "Impact of the Political Context on Foreign Policy Decision-Making," 443-445; see also George, A. "Domestic Constraints on Regime Change in

The preceding discussion of legislative institutionalization identifies informal mechanisms that the 109<sup>th</sup> Congress had at its disposal to shift the balance of foreign policy making power back in its direction. For instance, increases in legislative staff and support services have bolstered Congress' research and policy analysis capabilities and its capacity to evaluate administrative performance. Changes in subcommittee structures have redistributed control over legislative priorities and disbursed the ability to amass votes among more members. The power of appropriations has resulted in greater administrative accountability to Congress. And, while the procedural rules may create constraints, more experienced members of Congress have learned how to manipulate rules to move bills through the process. The following chapters will discuss in more detail how the 109<sup>th</sup> Congress took advantage of these types of informal tools to politicize the CNOOC bid for Unocal.

Before moving to the analysis of official records showing that politicization of CNOOC's business proposal was a mechanism for asserting congressional power, the next section will discuss the post 9/11 sense of vulnerability that created a sense of urgency for reexamining executive review of foreign mergers and acquisitions for national security implications.

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U.S. Foreign Policy," in *Change in the International System*, ed. O.R. Holsti, R. Siverson, and A.L. George (Boulder, CO: Westview, 1980).

### **III. INSTITUTIONAL CHANGES TRIGGERED BY SEPTEMBER 11, 2001**

#### **A. Changes in the Relationship Between the President and Congress**

Early in his presidency, Bush had followed a minimalist approach to foreign policy which was intended to contrast with Clinton's interventionist approach. Upon entering the White House, Bush knew he would have to balance the foreign policy interests of both the conservatives and neoconservatives that had supported his election.<sup>315</sup> One way of achieving this balance was with his political appointments. For example, one appointee, Deputy Secretary of Defense Paul Wolfowitz, believed in the use of force to promote American ideals in foreign nations, while another appointee, Secretary of State Colin Powell, believed in a cautious approach which stressed the importance of cultivating allies.

In the aftermath of the Cold War, President Bush acknowledged that neither China nor Russia presented a global threat and this allowed him to turn his attention to other areas of the world. By way of example, he received President Vicente Fox as the first visiting foreign head of state. Not only did this stress the role that Bush saw Mexico

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<sup>315</sup> During the Cold War conservatives and neoconservatives put a premium on national security and saw the Soviet threat, not China, as calling for a global strategy. After the Cold War ended differences between the two factions emerged. Conservatives concentrated on interests in areas that had material significance to the U.S. and sought to withdraw from peripheral commitments. For example, during the Reagan Administration conservatives feared potential threats to stable Western access to oil and emphasized the importance of diplomatic relations with Arab oil-exporting states. (Since China was just beginning to open up to the West and was not yet an energy exporter, it was not considered a threat.) Meanwhile, neoconservatives were fearful of rogue elements in the Third World, especially the Muslim world, and believed that people in the Middle East respected U.S. military superiority. Therefore, neoconservatives supported a stronger military presence there.

playing in the American economy, but it could also be seen as an attempt to shift public debate away from the Middle East.

Before President Bush had an opportunity to define any specific or controversial foreign policy initiatives, the events of September 11, 2001 marked a turning point in the presidency and for the nation as a whole. American citizens were unified in their demand for an immediate response to this act of aggression. National security was elevated to the top of the policy agenda and elected officials in both the executive and legislative branches of government were forced to refocus their priorities. Partisanship took a backseat while the president and Congress joined forces to manage the crisis. Both houses of Congress acted quickly to approve a resolution authorizing the president to use all necessary and appropriate force” against nations, organizations, and persons who had aided in the terrorist attacks.<sup>316</sup> This meant that President Bush could no longer tolerate different foreign policy perspectives in his administration.

It was critical that the president regain control over the nation’s security. One of the first steps he took was to assemble a “domestic consequences group” with Deputy Chief of Staff Joshua Bolten serving as chair.<sup>317</sup> The Office for Strategic Initiatives (OSI) shifted its focus from long-term planning to research how previous presidents had responded to crises. Karl Rove began to work with the domestic consequences task force

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<sup>316</sup> U.S. Congress, *Congressional Quarterly Weekly* (September 15, 2001), 2158.

<sup>317</sup> *The 9/11 Commission Report*, (New York: W.W. Norton and Co., Inc., July 2004), 326. The report was prepared by the National Commission on Terrorist Attacks on the United States which Congress and the President created under Public Law 107-306, November 27, 2002.



and helped manage congressional relations. The National Security Council began to meet daily with the president's war cabinet which included Vice President Cheney, Chief of Staff Card, National Security Advisor Rice, Secretary of State Powell, and CIA Chief George Tenet.<sup>318</sup>

Based on the organization of other administrations one might expect that National Security Advisor Condoleezza Rice would have been instrumental in setting the president's foreign policy priorities and reassigning those priorities to reorder the president's post 9/11 policy agenda. But Rice's role in national security was overshadowed by Vice President Dick Cheney, Secretary of Defense Donald Rumsfeld, and to a lesser degree, Secretary of State Colin Powell. Cheney was known to circumvent Rice and attempt to take over her major responsibilities while Rumsfeld often refused to share information with her. Even though many of Bush's top advisors had worked together in previous administrations, and had appeared to be unified in their support of the President, internal disagreements among them began to emerge after the terrorist attacks and the pressures of an impending war.

Some analysts argue that Rice followed the president's orders without examining alternative actions or examining the consequences.<sup>319</sup> But given Bush's managerial style, it is unlikely that he would have been receptive to any attempts to engage him in analysis. He viewed himself as "the Decider" whose primary responsibility was making tough

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<sup>318</sup> Karen M. Hult, "The Bush White House in Comparative Perspective," 51-77. See also Dana Milbank and Bradley Graham, "With Crisis, More Fluid Style at White House," *Washington Post*, October 10, 2001.

<sup>319</sup> Ivo H. Daalder, "In the Shadow of the Oval Office: The Next National Security Advisor."

decisions in difficult times and he often cut Rice and other advisors off before they could provide their complete assessment of the situation.

A second step that Bush took after 9/11 was to evaluate his ability to make immediate and unilateral decisions to secure the homeland against repeated terrorist attacks within the existing organizational structure. Many of the administrative functions related to national security were dispersed among a variety of administrative agencies and coordination of these agencies would be an unwieldy task. The September 11 attack on the United States made it clear to the president that he would have to undertake the most massive reorganization of the Executive Office since Congress approved Roosevelt's Administrative Plan in 1932.<sup>320</sup>

In October 2001 President Bush used his executive authority to create the Office of Homeland Security (OHS) and the Homeland Security Advisory Council (HSAC) to coordinate the executive branch's efforts to "detect, prepare for, prevent, respond to, and recover from, terrorist acts within the United States."<sup>321</sup> Initially, the OHS and the HSAC were to function much like cabinet councils established by previous presidents.<sup>322</sup> Bush

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<sup>320</sup> During Roosevelt's administration, Congress had authorized the president to issue executive orders to propose reorganization within the Executive Branch for the purpose of reducing expenditures and increasing efficiency in government. Reorganization authority remained available to presidents until the Supreme Court invalidated congressional reliance on the concurrent resolution to disapprove a president's proposed plan in 1983. The *Reorganization Act Amendments of 1984*, signed by President Reagan resolved this issue, but the act expired at the end of 1984. This meant that President Bush could make minor changes in administrative agencies, but larger adjustments had the potential of incurring congressional disfavor or, even worse, could be declared illegal.

<sup>321</sup> Executive Order no. 13,228, *Federal Register* 66 (October 10, 2001): 51882.

<sup>322</sup> Even though OHS and HSAC were to perform much like president's councils had in the past, clearly, in the aftermath of 9/11, there were differences. See *The 9/11*

proposed that the HSAC have a membership consisting of “not more than 21 members appointed by the President” who would be “selected from the private sector, academia, professional service associations, federally funded research and development centers, nongovernmental organizations, State and local governments, and other appropriate professions and communities.”<sup>323</sup> The council included secretaries of Treasury, Defense, Health and Human Services, and Transportation; the attorney general; the directors of the OMB, CIA, FBI, and Federal Emergency Management Administration; and chiefs of staff to Bush and Cheney.<sup>324</sup> The HSAC was to meet periodically upon the request of the Assistant to the President for Homeland Security to advise the president on strategy to secure the U.S. against terrorist attacks.

The president distinguished the Homeland Security Advisory Council from the existing National Security Council under Rice’s leadership. The HSAC was delegated responsibility for protecting the homeland from terrorist attacks while the NSC was still responsible for advising the President regarding foreign policy. In spite of efforts by

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*Commission Report*, (New York: W.W. Norton and Co., Inc., July 2004), 326. The report was prepared by the National Commission on Terrorist Attacks on the United States which Congress and the President created under Public Law 107-306, November 27, 2002.

<sup>323</sup> The Homeland Security Council was established by executive order on March 19, 2002, and was later codified in the *Homeland Security Act of 2002*. For additional discussion, see Karen M. Hult, “The Bush White House in Comparative Perspective,” 60-61.

<sup>324</sup> For additional discussion, see William W. Newmann, “Reorganizing for National Security and Homeland Security,” *Public Administration Review* 62, no. 1 (September 2002): 126-137.

Cheney to undermine Rice's credibility, she still maintained her status with the president who relied upon her to get things done.

President Bush appointed Thomas Ridge the first assistant to the president for homeland security, but shortly after being sworn in, the administration ran into a conflict. Even though widespread support for the president was undeniable, it did not mean that every member in Congress was willing to grant the president *carte blanche*. Even in a crisis situation, legislators were vigilant in protecting their oversight authority. For example, Senators Robert Byrd (D-WV) and Ted Stevens (R-AK) wrote a letter to Ridge requesting that he testify before the Senate Appropriations Committee. The administration refused stating that advisors to the president did not have to testify before Congress.<sup>325</sup> This response was reminiscent of Cheney's refusal to disclose information to the GAO earlier in the year and illustrated once again that Congress and the administration did not see eye to eye regarding executive privilege and legislative oversight. In spite of this conflict, the administration benefited from the nation's solidarity in the immediacy of the crisis as both Democrats and Republicans alike rallied to support the president.

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<sup>325</sup> Later, when Bush sent his plan to Congress to establish a cabinet-level Department of Homeland Security, Congress again wanted Ridge to testify. Ridge explicitly stated that he would not testify about any opinions that he may have shared with the president as an advisor, but that he would testify "about the reorganization of the executive branch." See Keith Koffler, "Ridge to Testify, Within Limits, on Cabinet Creation Plan," *GovExec.com*, June 7, 2002, [www.govexec.com](http://www.govexec.com); and Joel D. Aberbach, "The State of The Contemporary American Presidency: Or, Is Bush II Actually Ronald Regan's Heir?" in *The George W. Bush Presidency: Appraisals and Prospects*, ed. Campbell, Colin and Bert A. Rockman (Washington, D.C.: CQ Press, 2004), 62.

It is not uncommon for executive power to expand during times of war when presidents are granted a full array of administrative tools (including national security directives, executive orders and proclamations) to design and implement policy objectives. Clearly, Bush took advantage of the situation to assert unilateral powers during his second term. This power play was backed by the White House counsel's claim that "[T]he framers of the Constitution, I think, intended there to be a strong presidency in order to carry out certain functions, and [President Bush] feels an obligation to leave the office in better shape than when he came in."<sup>326</sup>

The president's forceful response to 9/11 bolstered his approval ratings and his surge in popularity gave him leverage over the 107<sup>th</sup> Congress which passed the Patriot Act in spite of concerns about constitutional issues.<sup>327</sup> The 107<sup>th</sup> Congress also showed overwhelming support for a bill creating a new Transportation Security Administration within the Department of Transportation.<sup>328</sup> From this point on, Bush wholeheartedly pursued the War on Terror and exuded new confidence in declaring to the world that our allies were either with us or against us.

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<sup>326</sup> Alison Mitchell, "Cheney Rejects Broader Access to Terror Brief," *New York Times*, May 20, 2002.

<sup>327</sup> *U.S. Patriot Act of 2001*, Public Law 107-56, 107<sup>th</sup> Cong. 1<sup>st</sup> sess. (October 25, 2001). Many provisions were set to sunset in December 2005. In July, the Senate passed a reauthorization bill with substantial changes, but the House kept most of the original language. The bills were reconciled in conference and passed on March 26, 2006 and were signed into law by President Bush on March 9 and March 10, 2006.

<sup>328</sup> *Aviation and Transportation Security Act*, Public Law 107-71, 107<sup>th</sup> Cong., 1<sup>st</sup> sess. (November 19, 2001). *U.S. Statutes at Large* 115 (2001): 597.

At the beginning of 2002, President Bush laid out the American response to 9/11 and won over American citizens, in spite of concerns that his “axis of evil” characterization might alienate some U.S. allies. While Vice President Cheney focused on making the administration’s case for invading Iraq, President Bush focused on defusing underlying congressional discontent by initiating one of the most ambitious midterm campaigns of any president. At the expense of domestic issues that have typically favored Democrats, President Bush shifted the public’s attention to national security issues that favored Republicans and helped the GOP gain more congressional seats.

Another example of the president’s popularity, and perhaps his most enduring success in expanding executive powers, was when the 108<sup>th</sup> Congress gave in to the White House version of the Department of Homeland Security Act. In October 2002, Congress passed legislation to merge the Office of Homeland Security with the Homeland Security Advisory Council to form the Department of Homeland Security, but retained the assistant to the president for homeland security in the Executive Office.<sup>329</sup> This organizational change resulted in four centers of power with influence over the formation of national security policy: (1) the policy triad comprised of the secretary of state, secretary of defense, and the national security advisor; (2) the director of national

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<sup>329</sup> *Homeland Security Act of 2002*, Public Law 107-296 (October 2002); Homeland Security Presidential Directive/HSPD-5, sections (4) and (11) February 28, 2003 [http://dhs.gov/xabout/laws/gc\\_1214592333605.shtm#1](http://dhs.gov/xabout/laws/gc_1214592333605.shtm#1) (accessed June 12, 2009).

intelligence and the chairman of the joint chiefs of staff; (3) the president's closest White House advisers; and (4) the secretary of Homeland Security.<sup>330</sup>

The Homeland Security Act allowed Bush to turn his back on the anti-interventionist foreign policy rhetoric of his 2000 campaign which pledged to work with U.S. allies for peacekeeping and nation-building. President Bush and Vice President Cheney advocated for a tough policy against terrorists, and Americans supported military intervention to make their homeland safe again.

Although 9/11 unified Congress, the consensus over the need to protect and defend national security began to crumble when the Iraq invasion failed to disclose weapons of mass destruction. At first, Bush held fast to his original strategy for the War on Terror, but after Stephen Hadley succeeded Rice as national security advisor, Bush became more open to considering alternative recommendations. This is not to say that Rice had been ineffective, but that Hadley had benefited from a different environment, one in which the president had come to realize that his policies were not working as expected.<sup>331</sup> The National Security Council went through several changes early in 2005, including: (1) simplification of internal organization with communications and legislative affairs functions returning to the White House; (2) a thirty percent reduction in staffing,

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<sup>330</sup> Sam C. Sarkesian et al., "Introduction," in *National Security: Policymakers, Processes, and Politics*, ed. Sam C. Sarkesian, John Allen Williams, Stephen J. Cimbala, (Boulder, CO: Lynne Rienner Publishers, 2008), 19.

<sup>331</sup> Ivo H. Daalder, "In the Shadow of the Oval Office: The Next National Security Advisor," 114.

and (3) adding a second deputy to coordinate economic strategy, national security, and foreign policy.<sup>332</sup>

Even though few legislators had challenged President Bush publically, conflicting political views continued to churn beneath the façade of a unified position towards the administration’s approach to protecting national security.<sup>333</sup> Democrats and Republicans had concerns about constitutional separation of powers, about maintaining the prerogatives of the legislative branch, and about threats to civil liberties.<sup>334</sup> But they had not felt empowered to voice their concerns until the failure to find weapons of mass destruction, combined with administrative bungling of Hurricane Katrina caused Bush’s ratings to plunge. Even though Bush attempted to modify his foreign policy tone at the beginning of his second term, it was too late to stave the backlash that was brewing in Congress.

## **B. Changes in U.S.-China Foreign Policy**

### **1. Pre-9/11 Institutional Tensions Over U.S.-China Policy**

To set the stage for understanding how institutional tensions have affected post-9/11 China policy we briefly review the executive-legislative relationship that has evolved since the Nixon Administration first pursued normalization of relations. Even though the joint communiqué signed by Nixon and Chou Enlai in February 1972 was a

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<sup>332</sup> Karen M. Hult, “The Bush White House in Comparative Perspective,” 63.

<sup>333</sup> For example, see John C. Fortier and Norman J. Ornstein, “President Bush: Legislative Strategist,” in *The George W. Bush Presidency*, ed. Fred I. Greenstein, Baltimore: Johns Hopkins University Press, 2003, 159-160 for a discussion of the conflict underlying the passage of the Patriot Act.

<sup>334</sup> *Congressional Quarterly Weekly*, September 15, 2009, 2119.



major breakthrough in U.S.-China diplomatic relations, Sino-American talks stalled under the Ford Administration.

When President Carter took office, one of his stated foreign policy goals was normalization of relations with China.<sup>335</sup> The Policy Review Committee headed by Secretary of State Vance cautioned that diplomatic relations with China might harm arms control negotiations, but still recommended that the president pursue negotiations and accept the Chinese demand to end diplomatic relations with Taiwan.<sup>336</sup> Meanwhile, knowing this demand would create opposition from the hawks in Congress, National Security Advisor Zbigniew Brzezinski convinced the president to enter into secret negotiations to avoid publicity.<sup>337</sup> While the president argued publicly that China intended to resolve the Taiwan issue peacefully and the Chinese cooperated by not challenging his pledge to protect Taiwan.

Carter argued for normalization, claiming it would “contribute to the welfare of the American people, to the stability of Asia where the United States has major security and economic interest, and to the peace of the entire world.”<sup>338</sup> But his failure to consult

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<sup>335</sup> Zbigniew K. Brzezinski, *Power and Principle: Memoirs of the National Security Advisor* (New York: Farrar, Straus, Giroux, 1983), 54.

<sup>336</sup> Policy Review Memorandum 24 was prepared for the president by the State Department, the National Security Council, and the Defense Department. For further discussion, see Michael Oksenberg, “A Decade of Sino-American Relations,” *Foreign Affairs* 61 (Fall 1982): 175-195.

<sup>337</sup> Jean A. Garrison, “Explaining Change in the Carter Administration’s China Policy: Foreign Policy Advisor Manipulation of the Policy Agenda,” *Asian Affairs: An American Review* 29, no.2 (Summer 2002): 85.

<sup>338</sup> *Ibid.*, 86.

prominent congressional leaders in the decision process led to an immediate political reaction. Nonetheless, the response was mixed. For instance, Senate Majority Leader Robert Byrd said it was “an important step that would help secure world peace;” Senator Gerald Ford voiced “terse” approval; and Senator Goldwater called it a “cowardly act.” It was the criticism from angry conservatives that suggested President Carter would face a fight in Congress.<sup>339</sup> The political struggle continued until Congress deleted language about a specific U.S. commitment to Taiwan in the Taiwan Relations Act. Afterwards, the act passed 90-6 in the Senate, 345-55 in the House, and the president approved it April 10, 1979.<sup>340</sup>

By midsummer 1979, President Carter indicated a willingness to consider Most Favored Nation (MFN) status for China.<sup>341</sup> Unlike the previous debates over

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<sup>339</sup> Jean A. Garrison, “Explaining Change in the Carter Administration’s China Policy: Foreign Policy Advisor Manipulation of the Policy Agenda,” 86.

<sup>340</sup> James Mann, *About Face: A History of America’s Curious Relationship with China, from Nixon to Clinton* (New York: Knopf, 1999). See chapter 3 for a discussion of how Sino-American cooperation evolved in the 1970s.

<sup>341</sup> The U.S has applied MFN tariff treatment as a matter of statutory policy to its trading partners since 1934. In 1951, the policy was modified by Section 5 of the *Trade Agreements Extension Act*, Public Law 82-50, which required the president to suspend MFN tariff treatment of the Sino-Soviet bloc countries, and President Truman suspended China’s most-favored-nation tariff status. In 1974, Congress set out the conditions and procedures for temporary restoration of MFN status to “nonmarket economy” countries in Title IV of the 1974 *Trade Act*. The key elements of the procedure for temporary restoration of the MFN status to a nonmarket country like China are (1) conclusion of a bilateral agreement containing a reciprocal grant of the MFN status and additional provisions required by law, and approved by the enactment of a joint resolution; and (2) compliance with the freedom-of-emigration requirements under the Jackson-Vanik Amendment, Public Law 93-618, *U.S. Code 19*(January 3, 1975): § 402: 2432. These requirements can be fulfilled either by a presidential determination that the country in

normalization of trade relations, congressional opposition to an expanded relationship did not materialize. In fact, MFN status drew support from Senator Henry M. Jackson (D-WA) who was the author of the earlier Jackson-Vanik trade restrictions that affected both China and Russia.

According to Richard Bush, three explanations for cooperation between the president and Congress in 1979 regarding China's MFN status have dominated the literature.<sup>342</sup>

1. China's policies toward Asia and bilateral issues either paralleled or reinforced U.S. objectives,
2. China was seen as an adversary of the Soviet Union and could cooperate with the U.S. on that front,
3. The reforms in China appeared to be improving the political and economic well-being of the people.<sup>343</sup>

For most of the 1980s, consensus prevailed in U.S.-China policy and Congress generally supported the president's initiatives.<sup>344</sup>

After the collapse of the Soviet Union, the bi-polar nature of international politics changed and communist aggression was no longer a primary concern. As traditional

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question places no obstacles to free emigration of its citizens, or, under specified conditions, by a residential waiver of such full compliance.

<sup>342</sup> Richard Bush, "Clinton and China: Scenarios for the Future," *China Business Review*, January/February 1993, 16-17.

<sup>343</sup> Nakayama recaps Richard Bush's summary of the three explanations in Toshihiro Nakayama, *Politics of U.S. Policy toward China: Analysis of Domestic Factors* (Washington, D.C.: Brookings Institution, 2006), 6.

<sup>344</sup> It was during this period that MFN status went into effect (February 1, 1980), and the communiqué on arms sales to Taiwan was signed.

security issues diminished in significance, the door opened for non-traditional issues with a moral undertone. Congress, and the public, turned their attention to concerns about the global economy, human rights, and the environment. A wide spectrum of private businesses, special interest groups, and non-government organizations sought to influence these foreign policy debates.

After the 1989 Tiananmen Square incident, religious and human rights groups, labor unions, and students lobbied to elevate moral issues on the foreign policy agenda. Many legislators, believing President George H.W. Bush was too lenient towards China, relied on Tiananmen to interpret Jackson-Vanik as authorizing Congress to withhold China's MFN status as an economic sanction against human rights violations.<sup>345</sup> Policy differences expressed in the ensuing MFN debates ushered in the end of a China consensus.<sup>346</sup>

In 1990 the House of Representatives passed the "conditionality bill" that proposed to place restrictions on China's future eligibility for MFN status. But the bill died when the Senate failed to act. The next year, differences between the president and Congress intensified and the House of Representatives passed legislation to suspend China's MFN status with a nearly unanimous vote. With the president threatening a veto,

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<sup>345</sup> Toshihiro Nakayama, *Politics of U.S. Policy toward China: Analysis of Domestic Factors* (Washington, D.C.: Brookings Institution, 2006), 9-10.

<sup>346</sup> Kerry Dumbaugh, "Interest Groups: Growing Influence," in *Making China Policy*, ed. Ramon H. Myers, Michel C. Oksenberg, and David Shambaugh (Lanham, MD: Rowman and Littlefield Publishers, 2002), 114-1. Review Memorandum 24 was prepared for the president by the State Department, the National Security Council, and the Defense Department 15.

the Senate deferred once again and China was granted MFN status for another year.<sup>347</sup> This set the stage for MFN to become an annual vehicle for debating U.S. policy towards China, and U.S.-China policy became hostage to domestic politics.<sup>348</sup>

During the final weeks of the second session of the 102<sup>nd</sup> Congress, Senators Byrd (D-WV) and Bingaman (D-NM) sponsored legislation concerning the Exon-Florio Amendment.<sup>349</sup> This bill, called the Byrd Amendment, was designed to strengthen Exon-Florio by limiting presidential discretion to avoid investigation of proposed takeovers and increase scrutiny of foreign governments and foreign government-owned companies.<sup>350</sup> More importantly, the Byrd Amendment increased opportunities for legislators to apply political pressure to the president to conduct a review of proposed acquisitions.

Meanwhile, during the 1992 election year, Bill Clinton's campaign criticized President Bush for "coddling tyrants" in Beijing and pledged to be more assertive

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<sup>347</sup> Robert S. Ross, "The Bush Administration: The Origins of Engagement," in *Making China Policy*, ed. Ramon H. Myers, Michel C. Oksenberg, and David Shambaugh (Lanham, MD: Rowman and Littlefield Publishers, 2002), 30-32.

<sup>348</sup> Toshihiro Nakayama, *Politics of U.S. Policy toward China: Analysis of Domestic Factors* (Washington, D.C.: The Brookings Institution, 2006), 10.

<sup>349</sup> The 102<sup>nd</sup> Congress ran from January 3, 1991 through January 3, 1993, but the second session ended on October 9, 1992.

<sup>350</sup> *Byrd Amendment, U.S. Code 50*, app. § 2170a(c)(1)(Supp. IV 1992).

towards human rights violations.<sup>351</sup> Newly elected in 1993, President Clinton announced he would link MFN status to human rights in the future.<sup>352</sup>

Prior to 1993, the business community had relied on the presidential veto to protect its business interests, but seeing this would no longer a guarantee under the Clinton Administration, and facing the possibility that China's MFN status could be terminated, "the business community organized one of the most aggressive and effective lobbying efforts ever made in the foreign policy sphere" to push for renewal of China's MFN status.<sup>353</sup> Clinton then proposed a compromise in which the Chinese would have to attain bench marks to ensure continued MFN status and he imposed these benchmarks by executive order.<sup>354</sup> Clinton effectively removed China policy from the grasp of politically motivated legislators but economic agencies within the executive branch asserted that the executive order had not given adequate emphasis to economic

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<sup>351</sup> Robert Suettinger, *Beyond Tiananmen: The Politics of U.S.-China Relations 1989-2000* (Washington, DC: The Brookings Institution Press, 2003), 155.

<sup>352</sup> John W. Deitrich, "Interest Groups and Foreign Policy: Clinton and the MFN Debates," *Presidential Studies Quarterly* 2, no. 29 (June, 1999): 280-96.

<sup>353</sup> Toshihiro Nakayama, *Politics of U.S. Policy toward China: Analysis of Domestic Factors*, (Washington, D.C.: Brookings Institution, September 2006), 12. See also David M. Lampton, "America's China Policy in the Age of the Finance Minister: Clinton Ends Linkage," *China Quarterly* 139 (September, 1994): 600. Lampton notes that Nakayama cites the efforts of the U.S.-China Business Council, the Emergency Committee for American Trade, and the U.S. Chamber of Commerce, in particular, as gaining support from a "centrist coalition" representing Democrats and Republicans. Lampton identifies Senators Dole (D), Boren (D), Baucus (D), Bradley (D), Johnston (D); and Representatives Foley (D), Hamilton (D), Gibbons (D), Matsui (D), McDermott (D), Ackerman (D), and Leach (R) as belonging to the coalition.

<sup>354</sup> Executive Order 12,850, signed by President Clinton on May 28, 1993 extended China's MFN status for 12 months beginning July 3, 1994; see *Federal Register* 58 (June 1, 1993): 31327.

considerations.<sup>355</sup> Ultimately, Clinton was persuaded to move away from the concept of conditionality towards delinking international human rights issues from economic issues.

Following this flurry of activity over China's MFN status, the Clinton Administration became preoccupied mostly with domestic issues and the state of the American economy. While some analysts argue this domestic focus emerged because Clinton did not have a map to guide the foreign policy agenda during this initial post-Cold War period, others argue that it emerged because the Republican-led Congress made such a strong effort to micromanage foreign policy.<sup>356</sup> Yet, in spite of Clinton's domestic focus, he did have some foreign policy successes. Over the course of his presidency, institutions with foreign policy agendas multiplied and more and more of these institutions began to utilize Congress as their point of entry into the policy making process.

By the time President Bush took office, most legislators had an opinion regarding U.S.-China policy, even if foreign policy was not their area of expertise. China has long held a place in the hearts and minds of Americans, and many continue to struggle with the concept of granting privileges, such as MFN, to a country that is governed by the Communist Party, even if those privileges benefit the American economy. This ideological struggle is intensified when one considers that benefits may accrue to one sector of the economy, but may be detrimental to other sectors. This tension is played out every day in Congress.

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<sup>355</sup> Toshihiro Nakayama, *Politics of U.S. Policy toward China: Analysis of Domestic Factors*, 13.

<sup>356</sup> David M. Lampton, "America's China Policy in the Age of the Finance Minister: Clinton Ends Linkage," *China Quarterly* 139 (September 1984): 600.

## 2. Post-9/11 Tensions Regarding U.S.-China Policy

After September 11, 2001, the Bush Administration advocated for a global antiterrorist campaign with cooperation from similarly-minded nations and American defense policy changed from deterrence to preemption. In East Asia, this effort began with a conference between senior officials from Washington and ten member-states of the Association of South East Asian Nations (ASEAN). During the conference, American officials discussed the strategic importance of Southeast Asia and convinced the ten ASEAN member-states to sign a counterterrorism pact.<sup>357</sup>

President Bush also announced he would travel to Shanghai in October 2001 to attend the Asia Pacific Economic Cooperation (APEC) council heads-of-state meeting, to be followed by an official visit to China.<sup>358</sup> The administration pursued several diplomatic exchanges with China with President Bush making two trips to China and China's Vice President Hu Jintao and President Jiang Zemin visiting the United States. Although Bush did not relent in his support of Taiwan during these exchanges, a "new cordiality" began to emerge.<sup>359</sup>

The Bush Administration's shift in priorities from Clinton-era economics to military and security priorities was evident in the Pentagon's 2001 *Quadrennial Defense*

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<sup>357</sup> Renato Cruz de Castro, "U.S. War on Terror in East Asia: The Perils of Preemptive Defense in Waging a War of the Third Kind," *Asian Affairs, An American Review* 31, no. 4 (Winter 2005): 216-18.

<sup>358</sup> "Bush Vows to Attend APEC Meet," *Taipei Times*, Sept. 14, 2001; *Remarks by President Bush and President Jiang in Press*, October 19, 2001, [http://beijing/usembassy\\_china.org.cn/highlevel.html](http://beijing/usembassy_china.org.cn/highlevel.html) (accessed December 26, 2009).

<sup>359</sup> Gilbert Rozman and Noah Rozman, "The United States and Asia in 2002: Needing Help Against 'Evil,'" *Asian Survey* 43, no. 1 (January-February 2003): 4-8.



*Review Report* which classified Asia as a “critical region.”<sup>360</sup> A year later, in September 2002, the Bush Administration released the *National Security Strategy of the United States of America* which solidified a policy of military predominance in which the United States committed to take whatever actions are necessary to protect its security and the security of its allies. This preemptive approach recognizes governments are responsible for what happens within their territory, but assumes an American right of intervention if another government fails to act against terrorist activity. Fearing legitimization of intervention in domestic affairs, many Asian nations, including China, began to question the increased U.S. military presence in East Asia,<sup>361</sup> but the Bush Administration held fast to its policy of swift military responsiveness to future military challenges in the region.<sup>362</sup>

Some analysts suggest Bush’s interest in high level exchanges had as much to do with U.S. military strategy in Asia as with U.S. policy towards China because once the administration began to consider foreign policy, it stated that it wanted to strengthen ties with traditional allies in the Asia-Pacific region, which excluded China.<sup>363</sup> For example, in his testimony to Congress prior to Bush’s February 2002 visit to China, Assistant

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<sup>360</sup> Donald H. Rumsfeld, *Quadrennial Defense Review Report, September 30, 2001* (Washington, D.C.: Department of Defense, 2001), 32.

<sup>361</sup> J. Mohan Malik, “Dragon on Terrorism: Assessing China’s Tactical Gains and Strategic Losses after 11 September,” *Contemporary Southeast Asia* 24, no. 2 (August 2002): 252-293.

<sup>362</sup> Kirt M. Campbell and Celeste Johnson Ward, “New Battle Stations,” *Foreign Affairs* 82, no. 5 (September/October 2003): 97.

<sup>363</sup> Robert Sutter, “Bush Administration Policy toward Beijing and Taipei,” 485.

Secretary James Kelly praised U.S.-Japan relations and U.S.-South Korea relations, but pointed out the negative as well as the positive when commenting on China.<sup>364</sup> In another example, when Bush and his secretary of defense, Donald Rumsfeld, committed to the buildup of national and theater missile defense systems, they looked to Japan, not China, for potential support.<sup>365</sup> This approach did not escape attention in Beijing and raised concern over a more aggressive United States, perhaps encouraging Chinese leaders to engage in their own military buildup.

In the following years, the Bush Administration continually warned against any power challenging U.S. interests with military force; and even though the Chinese had toned down their anti-American hegemony rhetoric, the administration continued to view China as a potential threat. President Bush issued the strongest statements supporting Taiwan's defense since the normalization of relations with China; he increased the Taiwan arms sale package; and he imposed more sanctions on China over reported proliferation of military weapons than any other president. In addition to his firm position regarding military affairs, President Bush took a strong stand against China's domestic policies, focusing on human rights abuses and repressed religious freedoms.<sup>366</sup>

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<sup>364</sup> Robert Sutter, 487.

<sup>365</sup> David Bachman, "The United States and China: Rhetoric and Reality," *Current History* (September 2001): 259.

<sup>366</sup> Robert Sutter, "Bush Administration Policy toward Beijing and Taipei," 486-87.

The president's hard line stance seemed to be in line with mainstream thought at the time and there was little opposition in Congress or the media.<sup>367</sup>

Some speculate that China supported the U.S. anti-terrorist policies to avoid interrupting the domestic economy and commercial relations that were so important to China's economic growth.<sup>368</sup> While the U.S. focused on fighting terrorism, tensions over U.S.-China trade issues continued to ferment in Congress. Following China's membership in the WTO, an increase in the U.S.-China trade imbalance led to more and more complaints from U.S. manufacturing firms. Several manufacturers charged China with unfair trade practices that threatened their ability to compete and resulted in the loss of American jobs. Even though businesses were concerned about trade issues, they were also concerned about avoiding a disruption in trade with China. The Bush Administration seemed to respect the need to maintain advantageous economic relations with China despite ideological differences, but members of Congress began calling on the administration "to take a more aggressive stance" against Chinese "unfair" trade policies.<sup>369</sup>

On several occasions, President Bush criticized China's currency valuation policies, and he even raised the issue in a meeting with Chinese President Hu Jintao on October 19, 2003. But on October 30, 2003, when the Treasury Department released its

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<sup>367</sup> Robert Sutter, "Bush Administration Policy toward Beijing and Taipei," 481.

<sup>368</sup> See for example, Arthur Waldron, "Guess Hu's Coming to the White House," *Wall Street Journal* (Eastern Edition), (May 1, 2002) (accessed December 26, 2009 from ProQuest Central, Document ID: 117221713).

<sup>369</sup> U.S. Congressional Research Service, *China-U.S. Trade Issues*, Report No. IB91121, by Wayne M. Morrison (Washington, D.C.: Library of Congress, July 1, 2005): 1.

semiannual report on exchange rate policies, it fell short of stating that China manipulated its currency. Therefore, by U.S. law, Treasury was not required to negotiate an end to China's currency practices.<sup>370</sup>

In January, 2005, Secretary of Commerce Donald Evans traveled to Beijing to engage in a dialogue concerning China's commitments to its WTO membership. In meetings with Vice Premier Wu Yi and Minister of Commerce Bo Xilai, Secretary Evans focused on reducing intellectual property counterfeiting and piracy by strengthening the enforcement structure; eliminating non-tariff barriers to open up markets; moving to a flexible exchange rate; and creating a level playing field for all trading partners.<sup>371</sup>

A few months later, when the Unocal issue arose in Congress, it appeared to the administration that Beijing was ready to change its position regarding China's currency valuation. At a G-7 meeting in April, U.S. Treasury Secretary John Snow indicated that China was ready to adopt a more flexible exchange rate. Snow's reading of China's willingness to change may have been based on his belief that the Bush Administration was strengthening its position, as illustrated in the Treasury's International Economic and Exchange Rate Policies report to Congress, and not on any firm commitment by the Chinese.<sup>372</sup> Less than one month later, in Treasury's May 17, 2005 report, Snow changed

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<sup>370</sup> U.S. Congressional Research Service, *China-U.S. Trade Issues*, Report No. IB91121, by Wayne M. Morrison, 8.

<sup>371</sup> U.S. Department of Commerce Press Release, Jan. 13, 2005, available at [http://www.commerce.gov/opa/press/Secretary\\_Evans/2005\\_Releases/January/13\\_China](http://www.commerce.gov/opa/press/Secretary_Evans/2005_Releases/January/13_China) (accessed June 10, 2007).

<sup>372</sup> *The Omnibus Trade and Competitiveness Act of 1988* mandates that the Treasury Department must consult with the International Monetary Fund to prepare the report for

his tune and stated that the valuation issue is a “substantial distortion to world markets,” and he warned that Treasury planned to monitor China’s progress closely.<sup>373</sup>

But at the same time that the Treasury Department was monitoring currency related issues, the U.S. Trade Representative (USTR) was facing intellectual property rights issues. Under the terms of China’s WTO accession, China had agreed to bring its intellectual property rights law in compliance with the WTO agreement on Trade Related Aspects of Intellectual Property Rights. Although the Bush Administration had stated repeatedly that China was making progress by passing new laws, training judges and law enforcement officials, closing illegal production lines, seizing illegal products, and preventing exports of pirated products, the USTR held fast to the conviction that much more needed to be done to improve China’s intellectual property rights protection.<sup>374</sup>

Complaints from the business community continued and the USTR responded by announcing, on April 29th that it had placed China on the Special 301 Priority Watch List due to “serious concerns” over compliance with WTO obligations and failure to implement pledges to reduce IPR infringements.<sup>375</sup> On July 11, 2005, the U.S.-China

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Congress. In 2005, the report was published in May and November. The November report covers the period from January 1 – June 30, 2005 and is available at [http://www.treas.gov/offices/international-affairs/economic-exchange-rates/112005\\_report.pdf](http://www.treas.gov/offices/international-affairs/economic-exchange-rates/112005_report.pdf) (accessed 12/26/2009).

<sup>373</sup> U.S. Congressional Research Service, *China-U.S. Trade Issues*, Report No. IB91121, by Wayne M. Morrison, 8.

<sup>374</sup> U.S. Congressional Research Service, *China-U.S. Trade Issues*, Report No. IB91121, by Wayne M. Morrison, 11-12.

<sup>375</sup> *Ibid.*, 13.

Joint Committee on Commerce and Trade (JCCT) met and discussed intellectual property rights related issues.

In July 2005, Secretary of State Condolezza Rice visited Beijing to discuss North Korea, counter terrorism, human rights and religions rights. When asked about economic and trade issues, she deferred to Secretary of Commerce Gutierrez and the JCCT who were also in China. Although recused from addressing the Unocal bid due to her ten years of service on the Chevron board, Secretary Rice stated that the relationship with China has

improved dramatically over the last several years. Our trade relations, while they are not uncomplicated and while the Chinese economy is transitioning in ways that are sometimes problematic for the American economy, it's still a very healthy, robust and active economic relationship.<sup>376</sup>

When asked about the Bush Administration's characterization of China as a threat, Rice responded that the administration did not perceive China as a threat; it was simply taking note of the size and pace of China's military buildup. In her view, the pressing issues for Washington were keeping up with China's military; safeguarding intellectual property rights; and honoring the long-held One-China policy, the three joint communiqués, and obligations under the Taiwan Relations Act.<sup>377</sup> Later, in an interview with Time Magazine, Rice emphasized that the Chinese relationship is complex.

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<sup>376</sup> Statements of Secretary of State Condolezza Rice quoted in U.S. Department of State press release (Beijing), July 10, 2005, <http://www.state.gov/secretary/rm.2005/49113.htm> (accessed June 20, 2007).

<sup>377</sup> Statements of Secretary of State Condolezza Rice quoted in U.S. Department of State press release (Beijing), July 10, 2005, <http://www.state.gov/secretary/rm.2005/49113.htm> (accessed June 20, 2007).

Although China cannot be characterized as “all positive or negative,” it is the administration’s job is “to make China a positive influence on international politics.”<sup>378</sup>

Clearly, Secretary Rice was downplaying Congress’s negative reaction to the Unocal bid.

Similarly, other State Department officials refrained from commenting on the CNOOC bid and the congressional reaction it precipitated. Deputy Secretary Robert Zoellick flatly refused to offer any thoughts on whether Congress was overreacting.<sup>379</sup>

When asked if the administration had no formal position, National Security Advisor Steve Hadley responded, “The position is going to come out of the CFIUS process.”

Elaborating further, he stated:

There are a series of administrative and legal processes that get triggered . . . a standard process in law and regulation that we would have to pursue . . . if it becomes a formal proposal, then those procedures will have to be invoked, and we’ll have to take a look at it.<sup>380</sup>

Hadley also refused to take a political stand, making no comment on congressional outrage over the issue. The administration’s position, as stated by Hadley was indicative of the classical “time-buying” strategy identified by Farnham. When faced with trade-offs that reduce acceptability (such as making a choice between promoting free trade and protecting national security), political decision makers will “often bide their time, relying

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<sup>378</sup> Secretary of State Condoleezza Rice interview with *Time Magazine* editorial board, September 19, 2005, 4:20 p.m. EDT, <http://www.state.gov/secretary/rm/2005/53630.htm> (accessed June 16, 2007).

<sup>379</sup> U.S. Department of State, *Briefing on Trip to Sudan, Jordan, and Egypt*, July 5, 2005, <http://www.state.gov/s/d/former/zoellick/rem/48994.htm> (accessed June 16, 2007).

<sup>380</sup> U.S. Department of State, “Press Gaggle by Scott McClelland and Steve Hadley,” *National Security Advisor*, July 5, 2005, <http://www.state.gov/p/eur/rls/rm/49003.htm> (accessed June 16, 2007).

on the logic of events. If there is nothing to be done at the moment, they are content to wait for change in a more favorable direction” so as to “alienate fewer people” while evaluating opportunities to increase the public’s receptivity to the policy issue.<sup>381</sup>

#### IV. CONCLUSION

According to the theoretical framework of new institutionalism, policy making in the United States is in a constant state of flux in which the institutions of the presidency and Congress continually act (either formally or informally) to assert powers granted under the Constitution to influence foreign policy decisions. Formal rules set parameters for introducing legislation, and delineate the steps that a bill must go through to become law. But policy making is much more complex than the rules set forth under the Constitution and in statutes and procedural rules. This study hypothesizes that what takes place informally is what really matters when trying to explain why some issues become politicized when they are formally introduced as legislation, and why some bills become law and others do not.

When presidents rely upon informal powers to increase their authority it threatens to destabilize the formal balance of power between the executive and legislative institutions. To overcome this tendency, members of Congress will use formal constitutional powers to propose new laws and policies to bring the system back into

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<sup>381</sup> Barbara Farnham, “Impact of the Political Context on Foreign Policy Decision-Making,” *Political Psychology* 25, no. 3 (2004): 453.



equilibrium.<sup>382</sup> However, because institutional constraints also inhibit Congress from acting quickly and decisively, individual legislators will turn to informal powers as a means of increasing their political influence and ability to get legislation passed.

While a natural ebb and flow is expected in a political system based on “checks and balances,” by the end of the twentieth century, the president’s formal authority had expanded while legislative oversight authority had diminished. Some of the drift towards presidential dominance may be explained by specific measures modern presidents have taken to gain more decision making autonomy; and some of this trend may be explained by the Congress’s failure to foresee the full spectrum of outcomes that could result from executive implementation of legislative mandates. What distinguished President Bush from other presidents was the combination of his hierarchical approach to managing his staff and delegation of responsibilities with an almost absolute insistence upon loyalty and discipline. By Bush’s second term, policy weaknesses created by a limited flow of information and advice became more evident. These weaknesses heightened concerns regarding executive powers and some members of Congress saw the controversy surrounding CNOOC’s proposed acquisition of Unocal as an opportunity to assert congressional oversight authorities.

Institutional tensions between the president and Congress have created a policy making process that is fragmented, inefficient, and often difficult to predict. This phenomenon is illustrated by the Unocal Case discussed in this dissertation. When Chinese-owned CNOOC contemplated its bid to acquire Unocal, CNOOC did not foresee

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<sup>382</sup> When presidents overstep constitutional boundaries, the courts will also come into play to bring the system back into balance.

that it would become entangled in the institutional struggle between Congress and the presidency – a struggle in which each institution was vying for greater authority and autonomy in foreign policy decision making.

Research shows that a variety of factors contributed to a legislative desire to shift the balance of power in foreign policy decision making during President Bush's second term. Immediately after September 11, 2001, Congress deferred to Bush and Cheney in the war on terror and the public supported the president's decisive actions. By 2005, foreign policy decision making had become decidedly weighted towards the presidency. But this shift in the balance of power did not go unnoticed by members of Congress – even legislators in the president's own party who supported his political agenda were becoming concerned about the loss of legislative authority.

Even though Congress had done very little to rein in the President Bush prior to 2005, during that summer, the proposed Unocal takeover provided an opportunity for Congress to take on administrative shortcomings and transgressions. Congress held hearings, issued proclamations, and modified legislation to make the president more accountable for the review of foreign acquisitions under the Exon-Florio Amendment. The Bush Administration seemed to just sit back while the issue played out in the legislature. Was this because the Unocal bid caught President Bush off guard, like it did the Chinese, and he was confident that the Republican majority in Congress would shape policy to his liking? Or was it because the president determined it was not a battle worth fighting? The answer to this question lies in the institutions themselves and the historical context in which the institutions found themselves reacting to the CNOOC proposal.

One of the issues that had been brewing in Congress concerned presidential implementation of the Exon-Florio Amendment. Some legislators had begun questioning whether the Bush Administration's singular focus on the War on Terror had left the nation's security vulnerable in other respects – such as foreign acquisition of corporations with access to essential resources, technology, and know how. Others had become concerned that they had abdicated congressional oversight responsibilities when giving the president such liberty to respond to terrorist attacks. By the time CNOOC contemplated its bid to acquire Unocal a movement was already underway in Congress to strengthen legislative oversight of presidential authority over foreign acquisitions of U.S. corporations under the Exon-Florio provision.

From the president's perspective, other policy issues may have been deemed more important at the time. He may also have felt he could afford to let his Republican colleagues handle the issue. However adept President Bush was at measuring the level of opposition in Congress and adapting his position to obtain his goals, he may have overlooked the more subtle, yet tangible, tools that Congress has available to impact executive powers. A president's unilateral powers are not absolute and Congress and the courts are always standing ready to reverse any executive actions should the president overextend his powers. Such was the case with the Unocal acquisition.

The next chapter reviews the primary statutes governing foreign acquisitions with a focus on the Exon-Florio Amendment enacted to provide the president statutory authority to block foreign acquisitions impacting national security. The chapter begins with a discussion of the history of Exon-Florio – how presidents have used their statutory

authority to promote or discourage foreign business transactions and how Congress has responded to the exercise of this authority. Then, within the context of the CNOOC bid for Unocal, the chapter examines the struggle between the institutions of the presidency and Congress over the implementation of Exon-Florio. Examining the Unocal Case from the analytical perspective of institutionalism provides insight into why Congress politicized the Chinese company's offer to purchase the American-owned oil and gas corporation.

**CHAPTER FOUR:  
EFFECTUATING CHANGE IN STATUTORY LAW THROUGH  
POLITICIZATION OF CNOOC’S BID TO ACQUIRE UNOCAL**

**I. INTRODUCTION**

Foreign capital has played a role in the American economy and has contributed to the country’s development ever since colonial times. Even though it is generally believed that there are mutual benefits to foreign investments, most countries impose restrictions of one sort or another. In the United States, there are no express provisions in the Constitution for the federal government to regulate foreign investment, so we look to other constitutional powers for justification of these powers. Most commonly, regulation of foreign investment is interpreted as falling under Congress’s authority to “regulate Commerce with foreign Nations, and among the several States”<sup>383</sup> and to provide for national defense.<sup>384</sup> In spite of this constitutional basis, not every legislator perceives the impact of foreign investment in the same way. Some may encourage it as a means of offsetting the loss of jobs from U.S. companies investing abroad while others may see it as a threat to American industry. But if foreign investment threatens to impair the nation’s security, legislators are faced with the challenge of weighing national security

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<sup>383</sup> U.S. Constitution, art. 1, § 8, cl. 3.

<sup>384</sup> U.S. Constitution, art. 1, § 8, cl. 12 -15.

needs against open trade principles. Finding the balance between these two important national interests is dependent upon access to relevant and timely information.<sup>385</sup>

After World War I the United States became a creditor nation with exports exceeding foreign imports. By the 1970s foreign investment in American businesses had begun to rise, and Congress began to debate the merits and disadvantages of foreign investments. Realizing the importance of access to data in the policy making process, Congress passed a number of statutes focused on how information is gathered and disclosed. For example, the International Investment and Trade in Services Survey Act of 1976 states that the president shall collect information regarding international investment and U.S. foreign trade in services.<sup>386</sup> In 1990, Congress amended the act to require that the president publish periodic information regarding foreign investment, including ownership by foreign governments,<sup>387</sup> and to allow the president to request reports on the best available information from the Department of Commerce's Bureau of Economic Analysis (BEA) regarding the extent of foreign direct investment in any given industry.<sup>388</sup> Another example is the Foreign Direct Investment and International

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<sup>385</sup> U.S. Congressional Research Service, *Foreign Investment in the United States: Major Federal Statutory Restrictions*, (Report No. RL33103, March 27, 2008), by Michael V. Seitzinger (Washington, D.C.: Library of Congress, 2009), 3-4.

<sup>386</sup> *U.S. Code 22*, §§ 3101 et seq. The president delegated responsibility for direct investment to the Commerce Department and for portfolio investment to the Treasury Department under Executive Order 11961, *Federal Register* 42 (January 19, 1977): 4321.

<sup>387</sup> *U.S. Code 22*, § 3103(a)(5).

<sup>388</sup> *U.S. Code 22*, § 3103(h). Foreign direct investment is defined by statute as the ownership or control, directly or indirectly, by one foreign person (individual, branch, partnership, association, government, etc.) of 10% or more of the voting securities of an

Financial Data Improvements Act of 1990 which allows the BEA to access data from the Census Bureau.<sup>389</sup> The purpose of the statute is to provide the BEA with additional data so that it can improve the accuracy and analysis in the reports that it provides to the Congress and the public regarding foreign direct investment.

In spite of the statutes directed at collecting and disclosing data regarding foreign investment in the United States, members of Congress have grown increasingly concerned about loss of control over resources and industries that are essential to our economy and our national security. This has been less of a concern for the economy when foreign investment is made by persons or governments from nations that provide reciprocal investment opportunities. But concerns have been heightened when investments are made by citizens or governments from nations that do not follow reciprocal trade policies, or when foreign investments are made in industries and resources deemed vital to national defense. Whenever concerns are heightened, Congress considers specific legislation to regulate mergers, acquisitions, and takeovers of American corporations.

Globerman and Shapiro suggest that even though there has “always been political opposition” to foreign direct investment, particularly when it involves acquisitions of large host country corporations, legal barriers to inward foreign direct investment have been “substantially weakened” in both developed and emerging economies in recent decades. This seems to suggest that host economies recognize net benefits to the host

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incorporated U.S. business or an equivalent interest in an unincorporated U.S. business enterprise. *Code of Federal Regulations*, title 15, §806.15(a)(1).

<sup>389</sup> *U.S. Code* 22, § 3141.

country.<sup>390</sup> Given this trend, one would expect the 109<sup>th</sup> Congress to have viewed CNOOC's proposed acquisition more favorably. But the history of this case shows that the pendulum may be swinging in the other direction as members in Congress push for more rigorous delineation of the executive's statutory authority over foreign acquisitions and greater scrutiny of executive decisions.

## II. LAWS GOVERNING MERGERS, ACQUISITIONS, AND TAKEOVERS

Over the years, Congress has enacted specific laws to govern mergers, acquisitions, and takeovers of American corporations.<sup>391</sup> Which laws apply, and how they apply, depend upon the origins of the entities proposing the corporate acquisitions and the particular details of each offer. Acquisitions proposed by domestic entities are governed by the Premerger Notification Act (PNA) and are subject to review by the Federal Trade Commission (FTC) or the Antitrust Division of the Department of Justice (DOJ).<sup>392</sup> Acquisitions proposed by foreign entities are governed primarily by the International Emergency Economic Powers Act (IEEPA)<sup>393</sup> and the Defense Production

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<sup>390</sup> Steven Globerman and Daniel Shapiro, "Economic and Strategic Considerations Surrounding Chinese FDI in the United States," *Asia Pacific Journal of Management* 26 (2009), 164-165.

<sup>391</sup> For simplicity, we will use the terms "mergers," "acquisitions," or "takeovers" interchangeably to discuss the offers that ChevronTexaco and CNOOC proposed for the purchase of Unocal.

<sup>392</sup> *Premerger Notification Act, U.S. Code* 15, §18a.

<sup>393</sup> *International Emergency Economic Powers Act of 1977, Public Law 95-223*, codified at *U.S. Code* 50, §1701 et. seq.



Act of 1950 (DPA) and its subsequent amendments,<sup>394</sup> and may be subject to review by the Committee on Foreign Investment in the United States (CFIUS).<sup>395</sup> Because the two corporations that proposed to takeover Unocal and its wholly owned subsidiary Union Oil of California in 2005 had different origins they were subject to different laws. As a domestic entity, ChevronTexaco's offer was subject to review by the FTC. As a foreign entity, CNOOC's offer was subject to review by the CFIUS.

#### **A. Domestic Mergers, Acquisitions, and Takeovers**

Although the PNA does not indicate which agency is to review which domestic transaction, traditionally, those in the petroleum industry have when been reviewed by the FTC.<sup>396</sup> In 2005, when ChevronTexaco announced its plan to acquire Unocal, the PNA required the reporting of all transactions resulting in the acquiring party's holding assets or voting securities: (1) in excess of \$200 million, or (2) between \$50 million and \$200 million plus the assets or voting securities of the acquired party.<sup>397</sup> A 30-day waiting period begins on the day the reviewing agency receives the materials specified in

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<sup>394</sup> *Defense Production Act of 1950*, Public Law 81-744, codified at *U.S. Code* (1950).

<sup>395</sup> *Omnibus Trade and Competitiveness Act of 1988*, § 5021, Public Law 100-418, *U.S. Statutes at Large* 102 (1988): 1107, 1425-26, amending Title VII of the *Defense Production Act of 1950*, codified at *U.S. Code* 50 (1989), § 2170 *et seq.*

<sup>396</sup> *U.S. Code* 15, § 18a. See also, U.S. Congressional Research Service, "Unocal: Legal Implications of Acquisition Bids by Chevron Corp. and China National Offshore Oil Corporation," (Report No. RS22192, August 5, 2005), by Janice E. Rubin and Michael V. Seitzinger, (Washington D.C.: Library of Congress, 2005).

<sup>397</sup> *U.S. Code* 15, § 18a(a), (b).

section 18a.<sup>398</sup> If the reviewing agency requests “additional material or documentary material relevant to the proposed acquisition” prior to the expiration of the initial 30 days, the waiting period may be extended an additional 20 days.<sup>399</sup> Alternatively, the original waiting period may be terminated prior to the end of 30 days if the reviewing agency provides notice in the *Federal Register* that it intends no further action.<sup>400</sup> But if the merger partner or the acquiring party is a non-U.S. entity, national security may be an issue and other legislation is controlling.

The primary purpose of FTC review is to ensure competition in the American domestic markets. When investigating acquisitions, the FTC is committed to gathering extensive information; obtaining input from a wide variety of sources; and emphasizing scientific methodology in its analyses. For example, in July 2004, William E. Kovacic, General Counsel of the FTC, appeared before a subcommittee of the House Committee on Government Reform to present testimony on factors that contributed to recent gasoline price increases and steps that might decrease gasoline prices in the short and long term.<sup>401</sup> A week later he appeared before a subcommittee of the House Committee on Energy and

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<sup>398</sup> *U.S. Code* 15, § 18a(b)(1)(A), (B).

<sup>399</sup> *U.S. Code* 15, § 18a(e).

<sup>400</sup> *U.S. Code* 15, § 18a(b)(2).

<sup>401</sup> William E. Kovacic presenting prepared statement of the Federal Trade Commission, “Market Forces, Anticompetitive Activity, and Gasoline Prices: FTC Initiatives to Protect Competitive Markets,” on July 7, 2004, to the Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs, Committee on Government Reform, U.S. House of Representatives, 108<sup>th</sup> Cong., 2<sup>nd</sup> sess. Available at [www.ftc.gov/speeches/Kovacic.shtm](http://www.ftc.gov/speeches/Kovacic.shtm) (accessed December 12, 2007).

Commerce to present testimony on initiatives to protect competitive markets in the production, distribution and sale of gasoline.<sup>402</sup> In his testimony, he identified the basic tools the FTC uses to promote competition in the petroleum industry as “challenges to potentially anticompetitive mergers, prosecution of non-merger antitrust violations, monitoring industry behavior to detect anticompetitive conduct, and research to understand petroleum sector developments.”<sup>403</sup> Kovacic emphasized the premium that the FTC places on “careful research, industry monitoring, and investigations” to understand the industry and to identify obstacles to competition.<sup>404</sup>

The FTC plays an important role in protecting competition in the petroleum industry. From 1981 to 2004, the FTC had taken enforcement action against 15 major petroleum mergers, four of which were either abandoned or blocked as a result of FTC or court action; in the remaining 11 cases, the FTC required the merging companies to

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<sup>402</sup> William E. Kovacic presenting prepared statement of the Federal Trade Commission, “Market Forces, Anticompetitive Activity, and Gasoline Prices: FTC Initiatives to Protect Competitive Markets,” on July 15, 2004 to the Subcommittee on Energy and Air Quality, Committee on Energy and Commerce, Hearing on Status of U.S. Refining Industry, U.S. House of Representatives, 108<sup>th</sup> Cong., 2<sup>nd</sup> sess. Available at [www.ftc.gov/speeches/Kovacic.shtm](http://www.ftc.gov/speeches/Kovacic.shtm) (accessed December 12, 2007).

<sup>403</sup> William E. Kovacic presenting prepared statement of the Federal Trade Commission, , “Market Forces, Anticompetitive Activity, and Gasoline Prices: FTC Initiatives to Protect Competitive Markets,” on July 7, 2004, to the Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs, Committee on Government Reform, U.S. House of Representatives 108<sup>th</sup> Cong., 2<sup>nd</sup> sess. Available at [www.ftc.gov/speeches/Kovacic.shtm](http://www.ftc.gov/speeches/Kovacic.shtm). (accessed December 12, 2007).

<sup>404</sup> *Ibid.*

divest substantial assets.<sup>405</sup> The openness of the FTC process is illustrated by the availability and depth of its reports.<sup>406</sup>

## **B. Foreign Mergers, Acquisitions, and Takeovers**

Foreign mergers, acquisitions, and takeovers are distinguished from domestic acquisitions in that they are subject to different laws, both within the United States and the home country. Although U.S. citizens value free markets, both the president and Congress have long been aware of how difficult is it to balance free trade principles with national security concerns, especially during times of war. Early in the twentieth century, Congress found it necessary to pass the Trading with the Enemy Act of 1917 to give the federal government authority to prohibit financial transactions in time of war.<sup>407</sup> Similarly, the Defense Production Act of 1950 (DPA), which broadened the government's power to channel domestic production capacity to meet national defense needs, also served to limit foreign investment in sectors of the economy that were particularly sensitive during wartime.<sup>408</sup>

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<sup>405</sup> William E. Kovacic presenting prepared statement of the Federal Trade Commission, "Market Forces, Anticompetitive Activity, and Gasoline Prices: FTC Initiatives to Protect Competitive Markets," on July 7, 2004, to the Subcommittee on Energy Policy, Natural Resources and Regulatory Affairs, Committee on Government Reform, U.S. House of Representatives, 108<sup>th</sup> Cong., 2<sup>nd</sup> sess. Available at [www.ftc.gov/speeches/Kovacic.shtm](http://www.ftc.gov/speeches/Kovacic.shtm) (accessed December 12, 2007).

<sup>406</sup> See for example, Federal Trade Commission Horizontal Merger Investigation Data, Fiscal Years 1996-2003 (February 2, 2004), available at [http://www.ftc.gov/opa/2004/05/040527\\_petroactionsHHIdeltachart.pdf](http://www.ftc.gov/opa/2004/05/040527_petroactionsHHIdeltachart.pdf) (accessed March 5, 2009).

<sup>407</sup> *Trading with the Enemy Act, U.S. Code* 12 (1917), § 95a.

<sup>408</sup> *Defense Production Act of 1950*, Public Law 81-744.

While a foreign acquisition may not give rise to an actual national emergency, it may have implications regarding future national security concerns. In 1975, President Ford established the interagency Committee on Foreign Investment in the United States to address this issue.<sup>409</sup> President Ford granted the CFIUS broad responsibilities for monitoring and evaluating the impact of foreign investment, but in reality, the committee had little authority. President Ford's successors issued subsequent executive orders to expand these powers, but they too had varying and debatable degrees of success.<sup>410</sup>

In 1977, the 95<sup>th</sup> Congress amended the Trading with the Enemies Act by passing the International Emergency Economic Powers Act.<sup>411</sup> The IEEPA grants the president broad powers to deal with any "unusual and extraordinary threat" to the national security, foreign policy, or economy of the United States.<sup>412</sup> However, to invoke these powers, the

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<sup>409</sup> President Ford formed the CFIUS in response to the Arab Oil Embargo in 1973 and fears that the influx of Arab "petrodollars" would allow the foreign countries to control corporate America. See Executive Order no. 11,858, *Federal Register* 40 (May 7, 1975): 20263.

<sup>410</sup> Executive Order no. 11,858, *Federal Register* 40 (May 7, 1975): 20,263 has been amended by Executive Order no. 12,188, *Federal Register* 45 (January 2, 1980): 969; Executive Order no. 12,661, *Federal Register* 54 (December 27, 1988): 779; Executive Order no. 12,860 *Federal Register* 58 (September 3, 1993): 47,201; and Executive Order no. 13,286, *Federal Register* 68 (February 28, 2003): 10619.

<sup>411</sup> *International Emergency Economic Powers Act (IEEPA)*, Public Law 95-223, Title II, § 201, *U.S. Statutes at Large* 91 (1977): 1625, codified as amended at *U.S. Code* 50 (1977), §§ 1701-1707.

<sup>412</sup> *IEEPA*, Public Law 95-223, Title II, § 201, *U.S. Statutes at Large* 91 (1977): 1625, codified at *U.S. Code* 50 (1977), § 1701.

threat must be imminent enough for the president to declare a national emergency.<sup>413</sup> According to former Commerce Secretary Baldrige, taking such an action would be “the equivalent of a declaration of hostilities against the government of the acquirer company.”<sup>414</sup> Therefore, in many instances, presidents (who are respectful of the innuendos of diplomacy) were powerless to take action against foreign mergers, acquisitions, and takeovers for political reasons and because the business transactions fell short of an “imminent threat.”

By the 1980s, growing concern over Japan’s rise as an economic power and competitor in the technology industry, led Congress to amend section 721 of the Defense Production Act of 1950 with the Omnibus Trade and Competitiveness Act of 1988.<sup>415</sup> Since then, exclusive of a national emergency, foreign acquisitions have been governed

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<sup>413</sup> *IEEPA*, Public Law 95-223, Title II, § 201, *U.S. Statutes at Large* 91 (1977): 1625, codified as amended at *U.S. Code* 50 (1977), § 1702 (a)(1)(B).

<sup>414</sup> Commerce Secretary Baldrige, speaking about “Acquisitions by Foreign Companies,” on at hearing before the Senate Committee on Commerce, Science, and Transportation, 100<sup>th</sup> Cong., 1<sup>st</sup> sess., 1987, 15

<sup>415</sup> *Omnibus Trade and Competitiveness Act of 1988*, § 5021 enacted H.R. 4848, Public Law 100-418, *U.S. Statutes at Large* 102 (1988):1107, amending Title VII of the *Defense Production Act of 1950*, codified at *U.S. Code* 50 (1989), app. § 2170. It was signed into law by President Reagan and lapsed in October 1990. The original authorization was scheduled to expire in 1991, but was made permanent by Section 8 of the *Defense Production Act Extension and Amendments of 1991*, Public Law 102-99, *U.S. Statutes at Large* 105 (1991): 487 (1991). President George Bush signed H.R. 991, which made Exon-Florio a permanent provision of the *Defense Production Act*, Public Law 102-99, 105 *U.S. Statutes at Large* 487 (August 17, 1991). See “Bush Signs Defense Measure Making Exon-Florio Permanent,” *International Trade Representative*; 1248 (August 21, 1991).

by the Omnibus Trade and Competitiveness Act.<sup>416</sup> This act has come to be known as the “Exon-Florio Amendment” after its sponsors Senator J. James Exon (D-NE) and Representative James J. Florio (D-NJ).<sup>417</sup>

### **C. Legislative History of Exon-Florio Amendment**

The congressional hearings regarding the Omnibus Trade and Competitiveness Act are instructive as to foreign trade concerns as well as the institutional tensions between the president and Congress. The act was first introduced in the House as an amendment to H.R. 3 by Rep. Dick Gebhardt (D-MO) to order the executive branch to examine trade with countries that had a large trade surplus with the U.S. In the hearing on April 28, 1987, debate was limited and time was divided and controlled by the chair and ranking minority members of eleven committees.<sup>418</sup>

Banking Committee Chair Mary Rose Oakar (D-OH) objected to section 905 of the bill, which would require the secretary of Commerce to immediately investigate, upon the request of the head of any agency, any foreign takeover of a U.S. corporation to

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<sup>416</sup> *Omnibus Trade and Competitiveness Act of 1988*, Public Law 100-418, 5021, 102 U.S. Statutes at Large 1107, (codified at U.S. Code 50 (1989), app. § 2170 reprinted in H.R. Rep. No. 576, 100<sup>th</sup> Cong., 2<sup>nd</sup> sess., 1-497 (1988) (hereinafter “*Exon-Florio Amendment (1988)*” or “*Exon-Florio (1988)*” or “§ 2170”). The provisions of the 1988 *Exon Florio Amendment* were amended again under the *Foreign Investment and National Security Act of 2007* (FINSAs) on October 24, 2007.

<sup>417</sup> *Exon-Florio Amendment*, § 2170.

<sup>418</sup> Hearing on *Trade and International Economic Policy Reform Act of 1987*, Cong. Rec., 100<sup>th</sup> Cong. 1<sup>st</sup> sess., April 28, 1987, 133, no. 66: H2548. One hour was provided to the following committees: Ways and Means; Foreign Affairs; Energy and Commerce; Agriculture; Banking, Finance and Urban Affairs. One-half hour was provided to Education and Labor; Government Operations; Public Works and Transportation; Judiciary; Merchant Marine and Fisheries; and Small Business.

determine the effect on national security. She reminded the House that the Banking Committee had sole jurisdiction over defense production and the Defense Production Act of 1950. She objected to “usurping” the committee’s jurisdiction under the guise of an omnibus trade bill. However, Mr. LaFalce (D-NY), chairman of the House Banking Subcommittee on Economic Stabilization, reminded the delegates that President Reagan’s trade policies had caused the trade deficits that were the root of the problem. As a consequence, U.S. competitiveness had reached “crisis proportions” and the trade bill was necessary to address a multitude of trade policy problems.

Meanwhile, Democrats in the Senate had been working on their own version of a bill ever since the 1986 elections had made trade an “urgent legislative priority.”<sup>419</sup> The cosponsors of S. 1420 introduced the bill on February 5, 1987. After 19 days of hearings, the bill was favorably reported to the Senate upon a 19-1 vote. When the clerk reported S. 1420 on June 23, 1987, Majority Leader Robert Byrd (D-WV) emphasized the bipartisan nature of the bill and the effort to include the administration in its formation. He noted that the Finance Committee had held 60 days of hearings and heard over 650 witnesses during the 99<sup>th</sup> and 100<sup>th</sup> Congresses.<sup>420</sup>

Senate Finance Committee Chair Lloyd Bentsen (D-TX) stressed the bipartisan consensus that trade should be the “number one legislative priority” of the 100<sup>th</sup> Congress

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<sup>419</sup> Senator Lloyd Bentsen of Texas, speaking for the *Omnibus Trade and Competitiveness Act*, on June 25, 1987, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.* 133: 177450. In 2005, then Minority Leader Byrd had asked Bentsen to head a study group. After issuing a report in April, Bentsen then recommended trade legislation which was the impetus for S. 1420.

<sup>420</sup> Senator Robert Byrd of West Virginia, speaking for the *Omnibus Trade and Competitiveness Act*, on June 25, 1987, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.* 133: 177448-9.



which he said was demonstrated by fact that he was able to introduce S. 1420 with the support of 56 cosponsors, 25 of which were Republicans.<sup>421</sup> Bentsen also stated that the committee had tried to bring the president on board, but hinted at the tension between the administration and Congress when he declared: “No president can be a strong and effective negotiator unless he has the support of the American people. And no President can be certain of that support unless he works with Congress.” In this spirit, Bentsen believed the provisions of the bill would “make Congress a partner, and not a puppet, in our trade policy.”<sup>422</sup>

Senator Byrd addressed the media’s criticism of the Democratic Congress and denied the suggestion that Democrats were inclined towards protectionist legislation.<sup>423</sup> Senator Phil Gramm (R-TX) commented that the Senate bill was “less protectionist” than the House bill, and Ranking Finance Committee Member Bob Packwood (R-OR), warned Congress against being “panicked into protectionism by grim statistics.” Packwood said he was persuaded by Chairman Bentsen’s arguments that “by tolerating unfair practices in some special cases, we encourage them in all cases.” As such, Packwood emphasized that there is a “powerful national interest . . . in making clear that the United States will not tolerate trade agreement violations.”<sup>424</sup>

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<sup>421</sup> Senator Bentsen, speaking for the *Omnibus Trade and Competitiveness Act* to the Senate, on June 25, 1987, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.* 133: 14750.

<sup>422</sup> *Ibid.*, 14751.

<sup>423</sup> Senator Byrd, speaking for the *Omnibus Trade and Competitiveness Act* to the Senate, on June 25, 1987, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.* 133: 147523.

<sup>424</sup> Senator Packwood of Oregon, speaking for the *Omnibus Trade and Competitiveness Act*, on June 25, 1987, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.* 133: 17453.

Clearly, the hearing was focused on U.S. competitiveness in relation to the growth of other economies, particularly Japan and to a lesser degree, Germany. There were only a few passing comments concerning China in the lengthy hearing with the most substantive comment being made by Senator Heinz (R-PA). He warned that there may be an amendment to the trade bill to provide favored treatment for the People's Republic of China – not for economic reasons but for the political purpose of advancing U.S.-China foreign relations.

The Chinese are very skillful; they are very bright, and they have quickly figured out that their price for such improvement should be improved economic relations, which to them means selling more here, regardless of whether it is dumped, subsidized, or fraudulently entered in violation of our bilateral textile agreement. The amendment that we might face would throw trade policy to the winds when the Chinese have their eyes firmly fixed on the proper objective -- the economic bottom line.<sup>425</sup>

Senator Danforth (R-MO) reminded the Senate that Congress, not the executive branch has responsibility for foreign commerce under the Constitution. As a practical matter, Congress delegated the day-to-day operation of trade policy to the president because the legislative branch is not equipped to conduct the administrative details. Danforth summarized the debate as follows:

[T]he overall responsibility for international trade is in the hands of the Congress and, therefore, we do have a strong role to play and if the current system is not operating effectively, if it has broken down, then Congress should step in and make sure that we have a trading system that does work.

Now, I say that the existing system has obvious problems. I would say that it has obvious problems because it is not really a system. We have so

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<sup>425</sup> Senator Heinz of Pennsylvania, speaking for the *Omnibus Trade and Competitiveness Act*, on June 25, 1987, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.* 133: 17485.

delegated responsibility to the President that the President almost on the basis of whim can determine when to act and when not to act in enforcement of the laws that have been enacted.

One of the ongoing debates that has occurred both in committee and in the press and will occur on the floor of the Senate in the next week or so has to do with the issue of Presidential discretion. It is a tough question, Presidential discretion.

On one hand, we recognize that we do not want to tie the President's hands completely. The President has overall responsibility for foreign policy, for the faithful execution of the law. We do not want to be in a situation where the President has absolutely no room to maneuver.

But, on the other hand, we have so delegated authority to the President of the United States, we have so granted him discretion in the past, that the laws that have been enacted by the Congress have often been dead-letter laws. . . .<sup>426</sup>

This legislative history is particularly instructive for analysis of the politicization of CNOOC's bid for Unocal. The Exon-Florio Amendment was formally introduced in 1988 when President Reagan's open investment policy and growing U.S. foreign debt reinforced the perception in Congress that U.S. firms were becoming particularly vulnerable to foreign takeovers. President Reagan had delegated the executive's regulatory and investigative authority under Exon-Florio to the CFIUS, an inter-agency committee which had been created by President Ford to include members from executive branch departments and the Executive Office of the President, and was chaired by secretary of Treasury.<sup>427</sup> [See Table 4] But the potential takeover of two U.S. companies raised Senator Exon's concern about how the White House was handling its authority

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<sup>426</sup> Senator Danforth of Missouri, speaking for the *Omnibus Trade and Competitiveness Act*, on June 25, 1987, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.*133: 17465.

<sup>427</sup> Executive Order no. 12,661, *Federal Register* 54 (December 27, 1988): 779.

under the legislation. Fujitsu, Ltd. of Japan proposed the purchase of Fairchild Semiconductor Corporation and Sir James Goldsmith of Great Britain attempted a hostile takeover of Goodyear Tire and Rubber Company. Goodyear Tire & Rubber had a large facility in Nebraska and had appealed to Senator Exon to help prevent the offer.<sup>428</sup>

Several government agencies agreed with Senator Exon that the two companies were important to national security – Fairchild produced a microchip with military applications and Goodyear had several Pentagon contracts – but the White House said that it could not prevent the takeovers unless there were a national emergency.<sup>429</sup> The Pentagon objected to Fujitsu purchasing Fairchild because it had no confidence that Fujitsu would protect classified technology. The Commerce Department objected because U.S. companies had been denied the right to compete with Fujitsu in Japan when they had proposed to sell supercomputers there.<sup>430</sup> On the other hand, the Office of Management and Budget, the State Department, and the Treasury Department leaned towards supporting foreign investment in the U.S. and they were more inclined to approve the transaction.<sup>431</sup>

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<sup>428</sup> Nathans, “Meet Wall Street’s New Bugaboo: CFIUS,” *Business Week*, June 12, 1989, 90.

<sup>429</sup> Lachia, “Pentagon Split on Implications of Bid by Fujitsu for Fairchild Semiconductor,” *Wall Street Journal*, December 29, 1986; Nathans, “Meet Wall Street’s New Bugaboo: CFIUS,” *Business Week*, June 12, 1989.

<sup>430</sup> Schlender, “Fujitsu, Fairchild Semiconductor Plan Ventures Even Though Merger is Ended,” *Wall Street Journal*, March 18, 1987.

<sup>431</sup> Schlender, “Fairchild Semiconductor Plan Ventures Even Though Merger Is Ended,” *Wall Street Journal*, March 18, 1987.

In the end, neither the Fujitsu nor the Goldsmith transactions were consummated. The Japanese firm responded to the increasing support for protectionist legislation in the U.S. by backing down from their proposal. Goldsmith's bid did not receive the same degree of opposition at the Federal level, but it did lead the Ohio legislature to strengthen the ability of state corporations to resist hostile takeovers from foreign interests.<sup>432</sup> This was accomplished by allowing corporate directors to consider not just the impact of a proposed takeover on the shareholders, but also the impact upon employees, suppliers, creditors, and customers.

The stated purpose of the 1988 Exon-Florio Amendment was to strengthen the process by which proposed foreign transactions are analyzed by "the President or the President's designees" and to give the president authority to prevent or restructure foreign acquisitions that threatened to undermine national security. According to Christopher A. McLean, Senator Exon's legal counsel and staff co-author of the law, the senator "had to fight every step of the way for this Presidential authority."<sup>433</sup> The proposed bill had stated that prohibition or suspension of a transaction was authorized when a transaction threatened to impair "national security and essential commerce." But the Reagan Administration objected to the phrase "essential commerce."<sup>434</sup> Secretary of Commerce

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<sup>432</sup> Rivetti and Gumm, "The Case at Akron," *Buyouts & Acquisitions* (July-August 1987): 4.

<sup>433</sup> Christopher A. McLean, "Exon Florio – The Spirit of Late Senator Jim Exon Still Soars," e-Copernicus, available at [www.e-copernicus.com/Press20%Releases/ExonFlorio.pdf](http://www.e-copernicus.com/Press20%Releases/ExonFlorio.pdf) (accessed on June 26, 2009).

<sup>434</sup> Letter from Paul Volker, chair of the Federal Reserve, to Earnest F. Hollings, chairman of the Senate Committee on Commerce, Science, and Transportation (June 9,

Baldrige contended that the language was too broad and the Exon proposal would “mean a diversion away from the principles” that the administration had been trying to espouse – that is, “national treatment for investment, open investment policy, and everything that goes with it.”<sup>435</sup> Former Treasury Deputy Secretary Richard Darman argued that the language potentially represented a “radical reversal of U.S. policy favoring increasingly open investment regimes” and, as written, would have “a chilling effect on foreign investment in the United States.”<sup>436</sup> In the end, the “essential commerce” phrase was removed.

There was also considerable debate in Congress over the definition of the “national security.” In hearings before the House, Representative Florio argued for expansion of the term “so as to be able to go beyond very militaristic interpretations.”<sup>437</sup>

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1987), published in “Acquisitions by Foreign Companies,” hearing before the Senate Committee on Commerce, Science, and Transportation, on June 10, 1987, 100<sup>th</sup> Congress, 1<sup>st</sup> sess. (Washington, D.C.: U.S. Govt. Printing Office, 1987), 69. See also Jose E. Alvarez, “Political Protectionism and United States International Investments Obligations in Conflict: The Hazards of Exon-Florio,” *Virginia Journal of International Law* 30, 65-77.

<sup>435</sup> Testimony of Secretary of Commerce Malcomb Baldrige published in “Acquisitions by Foreign Companies,” hearing before the Senate Committee on Commerce, Science, and Transportation, on June 10, 1987, 100<sup>th</sup> Congress, 1<sup>st</sup> sess. (Washington, D.C.: U.S. Government Printing Office, 1987), 3.

<sup>436</sup> Testimony of Treasury Deputy Secretary Darmanat published in “Acquisitions by Foreign Companies,” hearing before the Senate Committee on Commerce, Science, and Transportation,” on June 10, 1987, 100<sup>th</sup> Congress, 1<sup>st</sup> sess. (Washington, D.C.: U.S. Government Printing Office, 1987), 47.

<sup>437</sup> Representative Florio of New Jersey, statement made in “Foreign Takeovers and National Security: Hearings on § 905 of H.R. 3,” before Subcommittee on Commerce, Consumer Protection, and Competitiveness of the House Committee on Energy and Commerce, on October 20, 1987, 100<sup>th</sup> Cong., 1<sup>st</sup> sess. (Washington, D.C.: U.S. Government Printing Office; 1987), serial, 100-110: 26.

Later, Representative Fish (R-NY) attempted to define “national security” with a warning that national security “is not limited to those industries which develop and produce rifles, and fighter bombers. It includes the ability to provide a broad range of human services, materials, products and technological innovations.”<sup>438</sup> Ultimately the definition was omitted purposefully from the final bill to give the president broad discretion in invoking the statute.<sup>439</sup> Afterwards, during the administrative rulemaking process, the Department of Treasury received over 500 pages of comments from more than seventy parties. The comments focused primarily on clarifying the meaning of “national security,” but Treasury rejected the comments based on the rationale that it needed to maintain the congressional intent expressed in the Conference Report.<sup>440</sup>

As enacted in 1988, Exon-Florio gave the president broad discretionary authority to take “appropriate” action to suspend or prohibit proposed or pending foreign mergers,

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<sup>438</sup> Representative Hamilton Fish, Jr. of New York, statement made in *Cong. Rec.*, 100<sup>th</sup> Cong. 1<sup>st</sup> sess., April 21, 1988, 134: H2297.

<sup>439</sup> See *Cong. Rec.*, 100<sup>th</sup> Cong., 1<sup>st</sup> sess., April 20, 1988, 134: H2118; see also Jose E. Alvarez, “Political Protectionism and United States International Investments Obligations in Conflict: The Hazards of Exon-Florio,” *Virginia Journal of International Law* 30, 77 (quoting 1988 Trade Act Conference Report, 926-27.)

<sup>440</sup> The Department of the Treasury published the proposed Regulations Pertaining to Mergers, Acquisitions and Takeovers by Foreign Persons in *Federal Register* 54 (July 14, 1989): 29744. The purpose of the proposed regulations was to implement Section 721 (hereinafter referred to as “Section 721”) of Title VII of the *Defense Production Act of 1950*, as added section 5021 of the *Omnibus Trade and Competitiveness Act of 1988*, Public Law 100-418, relating to mergers, acquisitions, and takeovers of U.S. persons by or with foreign persons. Section 721, which was subject to the sunset provision of the DPA, later lapsed on October 20, 1990, but was reinstated and made permanent law by Public Law 102-99 (signed August 17, 1991). The Final Rule was published in the *Federal Register* 56 (November 21, 1991):58,774, codified at *Code of Federal Regulations*, title 31, 800, app. A (1991).

acquisitions, or takeovers of U.S. businesses by persons engaged in interstate commerce which “threaten[s] to impair the national security.” The president “may” make an investigation, but “only if” he determines that other laws are inadequate or inappropriate to protect national security and there is “credible evidence” that the transaction would impair national security.<sup>441</sup> The president’s determination as to whether Exon-Florio kicks in was not subject to judicial review.<sup>442</sup>

Although members of Congress could not agree on certain definitions, and decided to exclude them, they did agree on several factors that the president could consider when deciding whether to block a foreign merger, acquisition or takeover. These were:

- (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.<sup>443</sup>

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<sup>441</sup> Public Law 100-418, title V, Subtitle A, Part II, *U.S. Code* 50, app. § 2170 (1988).

<sup>442</sup> *U.S. Code* 50, app. § 2170(c) (1988).

<sup>443</sup> *U.S. Code* 50, app. § 2170(e) (1988). Other factors such as 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 the potential effects of the transaction on U.S. technological leadership in areas affecting U.S. national security were added later by the *Byrd Amendment*. *U.S. Code* 50, app. § 2170(f) (1992).



The 1988 Exon-Florio Amendment established the following process: (1) investigation of the acquisition must commence within 30 days after receipt of written notification of the proposed or pending acquisition of a U.S. company to determine whether there are any national security concerns, (2) 45 days to complete the investigation to determine whether those concerns require a recommendation to the president for possible action, and (3) a presidential decision to permit, suspend, or prohibit the acquisition.<sup>444</sup> Then the president may seek judicial remedy, including divestiture, in federal courts if necessary to enforce his decision.

As a means of protecting corporate interests, the information provided in the Exon-Florio investigation was made exempt from disclosure under the Freedom of Information Act, except for the purpose of an administrative proceeding or judicial action.<sup>445</sup> In addition, the statute provided that Congress or any of its authorized committees could access information provided during the investigation.<sup>446</sup>

#### **D. Presidential Implementation of Exon-Florio**

Not only is Exon-Florio's legislative history important for understanding the politicization of China's bid for Unocal in 2005, but how presidents have interpreted and implemented their statutory authority under the amendment is also important. In this section, we analyze congressional hearings and debates, and subsequent efforts to amend

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<sup>444</sup> *U.S. Code* 50, app. § 2170( a),(b),(d)(1988).

<sup>445</sup> *U.S. Code* 50, app. § 2170(b) (1988). See also *The Freedom of Information Act*, Public Law 89-554, codified at U.S. Code 5 (1989), § 552 for exemptions.

<sup>446</sup> *U.S. Code* 50, app. § 2170(b) (1988).

the statute, in order to understand the statute's flaws and the difficulties presidents have encountered in implementing the statute as enacted.

On February 2, 1990, during the Senate's recess, former President George H.W. Bush reported that he had invoked his Exon-Florio authority for the first time. The president's report informed the Senate of his decision to order the China National Aero-Technology Import and Export Corporation (CATIC) to divest all its interest in MAMCO Manufacturing, Inc., a company incorporated under the laws of the State of Washington, which manufactured aircraft components that had potential commercial or military use. Former President Bush based his decision on finding "credible evidence" that the "foreign interest exercising control might take action that threatens to impair the national security" and that no other law provides adequate and appropriate authority for him to protect national security.<sup>447</sup>

CATIC was an export-import company of the Chinese Ministry of Aerospace Industry which engaged in research and development, design, and manufacturer of military and commercial aircraft, missiles, and aircraft engines, and had business dealings with various U.S. companies. MAMCO voluntarily notified the CFIUS of CATIC's intention to acquire MAMCO, and the acquisition was consummated in November 1989 while the CFIUS review was in process. On December 4, 1989, the CFIUS made a determination to conduct a formal investigation and informed the parties to the transaction. During the investigation, officials from the Departments of Commerce and Defense visited MAMCO on behalf of CFIUS and gathered data regarding MAMCO's

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<sup>447</sup> *Cong. Rec.*, 101<sup>st</sup> Cong., 1<sup>st</sup> sess., February 5, 1990, 136: S761-05.

production and technological capabilities. President Bush made his decision to order divestment based on the results of this investigation. However, because of the “sensitive nature of the evidence,” the report did not specify details. Instead, the President informed the Senate that CFIUS would “be available, on request, to provide the appropriate committees, meeting in closed sessions, with a classified briefing.”<sup>448</sup>

Although the publically stated reason was that by acquiring MAMCO, the Chinese could have access to U.S. aerospace companies and products which were restricted by export controls, some have suggested that the president’s determination was politically motivated.<sup>449</sup> This hypothesis is supported by the fact that the case was reviewed just one year after the political riots in Tiananmen Square when there was considerable anti-China sentiment and many legislators were seeking human rights sanctions. During the initial 45-day review of the MAMCO acquisition, the Bush Administration did not impose any restrictions to protect against the transfer of sensitive information and technology and there was no immediate action taken to protect national security. Furthermore, even though the statute provided that mediation occur within three months of the president’s order, the president did not ensure that CATIC surrender its interest in MAMCO until one year later. If national security had been an imminent concern, one would have expected more immediate action.

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<sup>448</sup> *Cong. Rec.*, 101<sup>st</sup> Cong., 1<sup>st</sup> sess., February 5, 1990, 136: S761-05.

<sup>449</sup> For a discussion of political motivations see for example W. Robert Shearer, “Comment: The Exon-Florio Amendment: Protectionist Legislation Susceptible to Abuse,” *Houston Law Review* 30 (1993); 1756-57.

President George H.W. Bush's handling of the MAMCO case was questioned by certain members of Congress and a number of foreign investment related bills began to appear in both chambers. For example, on April 25, 1990, Senator James Exon (D-NE) introduced S. 2516, cosponsored by Senators Orrin Hatch (R-UT), Arlen Specter (R-PN), and David Boren (D-OK), to allow the Department of Commerce's Bureau of Economic Analysis (BEA) access to information collected by the Bureau of the Census. It was determined that this access would improve the accuracy and analysis of BEA reports to the public and to Congress on foreign direct investment in the United States, and would enable CFIUS to conduct more thorough and informed analysis regarding the impact of foreign takeovers of American companies.

The Committee on Commerce, Science, and Technology held a hearing in which the Departments of Commerce and Treasury testified in support of the bill. On July 31, 1990, the Committee on Commerce, Science, and Technology ordered S. 2516 favorably reported by voice vote with an amendment offered by Senator Ted Stevens (R-AK) and Senator Exon providing for a BEA foreign investment report to CFIUS. The report would be made, upon request, and would outline the level and extent of foreign direct investment in an industry, including foreign government investment, by country, without disclosing individual investment information.<sup>450</sup> Now, under P.L. 101-533, when a request for a report is made to BEA in connection with a CFIUS investigation under Section 721, the report must be provided within 14 days.

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<sup>450</sup> S. Rep. 101-443, 101<sup>st</sup> Cong., 2<sup>nd</sup> sess. (1990).

Meanwhile, during House proceedings and debates, Representative Helen Bentley (R-MD) expressed disappointment in the 1988 Exon-Florio Amendment. Although the CFIUS was comprised of “heads of eight federal agencies, and chaired by the Secretary of the Treasury,” Representative Bentley lamented,

There is absolutely no requirement for foreign investors to notify anyone in the Government of their intent to purchase anything . . . . Foreign investors can purchase U.S. companies and do purchase them at will. Any attempt Congress has made, as in the Bryant bill of last year, to get some kind of registration of foreign ownership, has been knocked down every time.<sup>451</sup>

Representative Bentley identified other signs of weakness in the 1988 legislation, including: (1) Exon-Florio only offered the option of CFIUS review if someone challenges the foreign acquisition; (2) Even though eight agencies were represented on CFIUS, only three needed to agree to a sale; (3) In two years, CFIUS had made only three recommendations to the president, and of those, only one was to stop a sale; (4) In just three months during 1990, 209 U.S. companies had passed into foreign ownership.<sup>452</sup> From the context of her testimony, it appeared that Representative Bentley was more concerned with the amendment’s ineffectiveness in protecting U.S. assets than protecting national security interests.

In spite of the conflict in the Gulf area, and congressional concern about foreign direct investment in the U.S., the 101<sup>st</sup> Congress failed to enact the DPA authorization bill in 1990, and the DPA expired for the first time since it was first enacted.

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<sup>451</sup> *Cong. Rec.*, 101<sup>st</sup> Cong., 1<sup>st</sup> sess., May 3, 1990, 136: H2036-04.

<sup>452</sup> *Ibid.*

Representative Thomas Carper (D-DE) responded in the House by introducing H.R. 991 to extend the expiration of the DPA until September 30, 1991, and to make it retroactive to October 20, 1990.<sup>453</sup> In testifying as the new chairman of the House Economic Stabilization Subcommittee of the Banking, Finance, and Urban Affairs Committee, which had jurisdiction over the DPA, Carper discussed three “relatively noncontroversial” amendments.<sup>454</sup> The first was to provide antitrust protection to voluntary agreements as part of petroleum-related international agreements. The second was to clarify defense contract priority and allocation provisions, and the third was to make permanent the 1988 Exon-Florio provisions which require executive review of foreign mergers, acquisitions, and takeovers of domestic firms that might affect U.S. security interests adversely.<sup>455</sup>

Representative Tom Ridge (R-PA), the ranking member of the subcommittee, emphasized the importance of the DPA, and danger of forcing the president to operate without the benefit of the DPA during critical stages of the Gulf crisis. He also stressed how the 1988 Exon-Florio provisions give the president necessary authority to review proposed mergers that might adversely affect U.S. national security. Representative Mary Rose Oaker (D-OH), past chairwoman of the Economic Stabilization Committee,

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<sup>453</sup> Representative Carper introduced H.R. 991 on February 20, 1991. *The Defense Production Act Extension and Amendments of 1991* was first introduced in the House on February 20, 1991. It was presented to the President on August 7, 1991 and became public law on September 11, 1991 (Public Law 102-99).

<sup>454</sup> Representative Carper of Delaware speaking for H.R. 991, on March 6, 1991, before the House, 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 137: H1428-01.

<sup>455</sup> *Ibid.*

spoke of extensive efforts to “modernize the act,” consultations with “an advisory group composed of high former military and civilian executives and industrialists,” and strong bipartisan support. Representative Chalmers Wylie (R-OH), ranking member of the Committee on Banking, Finance, and Urban Affairs, echoed the others’ comments and reiterated the need to make the Exon-Florio provisions permanent with an illustration of “a takeover involving the transfer of nuclear technology [that] could have potentially gone through because DPA had expired.”<sup>456</sup>

Representative Cardis Collins (D-IL) noted a diversity of views as to how the administration had handled implementation of Exon-Florio. While some criticized the administration for not being aggressive enough and others felt the administration’s “reluctance to intervene” was appropriate, the overwhelming consensus was that Exon-Florio should be exempt from the sunset terminations of the DPA. Again, citing the example of the proposed Japanese takeover of Moore Special Tool Company, the sole U.S.-owned supplier of ultra-high-precision grinding equipment to the U.S. nuclear program, Representative Collins pointed to the significance of providing CFIUS with the statutory authority to act. In this case, she said, it was only after the Economic Stabilization Subcommittee announced it would consider the takeover at a hearing that the Japanese firm, Fanuc Machine Tool, withdrew its offer.<sup>457</sup>

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<sup>456</sup> Representative Wylie of Ohio speaking for H.R. 991, on March 6, 1991, before the House, 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 137: H1428-01.

<sup>457</sup> Representative Cardis Collins of Illinois, speaking for the *Defense Production Act*, before Congress, on March 6, 1991, 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 137: H1428-01.

Aside from the national security issue, Representative Philip Sharp (D-IN) noted two other benefits from making Exon-Florio permanent. First, it would strengthen Congress's institutional leverage over how the administration implements its Section 721 authority. Second, it would create greater confidence on the part of the international business community, rather than the ambiguity of an unpredictable statute.<sup>458</sup> Within this context, it is not surprising that the House voted 416 in favor of H.R. 991 with no opposition, and 17 not voting, and the bill was sent to the Senate.<sup>459</sup> On August 2, 1991, the Senate agreed to the conference report on H.R. 991 to extend the expiration date of the Defense Production Act of 1950.<sup>460</sup>

Representative Sharp emphasized his concern about Congress's ability to monitor and regulate transnational mergers, joint ventures, and takeovers by introducing the International Mergers and Acquisitions Review Act to the Commerce, Consumer Protection and Competitiveness Subcommittee of the House Energy and Commerce Committee on June 12, 1991.<sup>461</sup> He noted that some transnational mergers may not fall into the commonly accepted definition of national security, but may raise other concerns, such as antitrust or competitiveness issues. The bill was an attempt to provide a linkage between the regulatory domains of the Hart-Scott-Rodino premerger notification

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<sup>458</sup> Representative Phillip Sharp of Indiana, speaking for the *Exon Florio* Amendment, before Congress, on March 8, 1991, 102<sup>nd</sup> Cong. 1<sup>st</sup> sess., *Cong. Rec.*, 137: E856-02.

<sup>459</sup> *Cong. Rec.* 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., March 6, 1991, 137: H1428-01.

<sup>460</sup> *Cong. Rec.* 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., August, 21, 2001, 137: E2965-092 and S12140-02.

<sup>461</sup> *International Mergers and Acquisitions Review Act*, H.R. 2631, *Cong. Rec.*, 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., June 19, 1991, 137: 15575.



regulation of the Clayton Antitrust Act and the national security review under the Exon-Florio Amendment.

At the House Energy and Commerce Subcommittee hearing, Theodore Moran, international business professor at Georgetown University, testified that there are “genuine national security threats associated with foreign investment” and these national security threats arise when foreign companies attempt to acquire U.S. companies in “industries where external suppliers are extremely concentrated.”<sup>462</sup> Furthermore, he noted, global “proliferation of restrictions on flows of technology and capital” also threatens U.S. national security and welfare.<sup>463</sup> Mr. Moran proposed a “concentration test” where the largest four firms (or countries) should control no more than fifty percent of the market, so that they would lack the ability to collude to manipulate the market. He concluded that this approach, based on “principles that have always guided the American preference for free markets” would allow the market, rather than government bureaucrats to pick winners and losers.<sup>464</sup>

In addition to antitrust protection, Representative Sharp expressed a need to oversee businesses engaged in commerce related to the United States’ defense industrial base. Sharp’s bill proposed making the Hart-Scott-Rodino mandatory premerger requirement of the Clayton Antitrust Act the starting point for review of foreign direct

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<sup>462</sup> Testimony of Theodore Moran before the Commerce, Consumer Protection and Competitiveness Subcommittee of the House Energy and Commerce Committee, on June 12, 1991, 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 137: 15576.

<sup>463</sup> *Ibid.*

<sup>464</sup> *Ibid.*, 15576-77.

investment. But, in addition to the normal antitrust thresholds set by Hart-Scott-Rodino, H.R. 2631 would “establish clear and precise national security triggers.”<sup>465</sup> While the bill would give the president additional authority under Exon-Florio to precondition a merger or acquisition so that national security concerns are met, it also addressed Congress’ institutional concern that presidential implementation of Exon-Florio lacked transparency and accountability. So that Congress and the public could better understand how CFIUS operates, the bill required an annual public report on CFIUS investigations.<sup>466</sup> In 1991, after extensive comment, the Treasury Department issued final regulations implementing the Exon-Florio provision.<sup>467</sup> These regulations created a voluntary system of notification by the parties to an acquisition, but allowed for notice by agencies that are members of CFIUS.<sup>468</sup> It was assumed that large firms would have an incentive towards voluntary notification because the regulations stipulate that when companies do not notify CFIUS of foreign acquisitions which are governed by Exon-Florio, the acquisitions remain subject indefinitely to divestment or other appropriate actions by the President.

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<sup>465</sup> Extension of Remarks by Mr. Sharpe in the House of Representatives concerning the International Mergers and Acquisitions Review Act, on June 19, 1991, 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 137: 15575-77.

<sup>466</sup> *International Mergers and Acquisitions Review Act*, H.R. 2631, *Cong. Rec.*, 102<sup>nd</sup> Cong., 1<sup>st</sup> sess., June 19, 1991, 137: 15575.

<sup>467</sup> Regulations Pertaining to Mergers, Acquisitions, and Takeovers by Foreign Persons. *Code of Federal Regulations*, title 31, p. 800 (1991).

<sup>468</sup> *Code of Federal Regulations*, title 31, p. 800.504(b); p. 800.601(d) (1991).

In 1992, Congress again expressed concern about the review process after a French state-owned company, Thomson-CSF, Inc., proposed to acquire LTV Corporation's missile division. Originally, Senator Byrd drafted a bill that would have prohibited the sale of LTV Corporation to any non-U.S. company,<sup>469</sup> but this bill stalled as the president indicated he was inclined to block the transaction. The results of the CFIUS investigation, strong congressional scrutiny, and broad public awareness made the acquisition much too risky and controversial. Then, towards the end of the legislative session, Senator Byrd introduced Amendment 3077 to the National Defense Authorization Act for Fiscal Year 1993. The cosponsors were Senators Exon, Riegle, Sarbanes, Bingaman and Dixon.

Although debate was limited, it was passionate due to the fact that it was introduced subsequent to an attempt to block the Thomson-CSF transaction. One of the main concerns about the Thomson-CSF proposal was the issue of French government control over Thomson-CSF's parent company and sensitive LTV technology. This concern was consistent with Congress's long history of disapproval over France's third-party transactions involving the transfer of military equipment. Ultimately, Thomson-CSF withdrew its proposal in response to the politicization of the transaction and anticipation of the outcome. After restructuring its proposal to include joint acquisition with U.S.-based defense contractor, Loral Group, which agreed to purchase the LTV

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<sup>469</sup> See S. 2704, 102<sup>nd</sup> Cong., 2<sup>nd</sup> sess., 1992 stating that "no foreign person may purchase or otherwise acquire the LTV Aerospace and Defense Company." Foreign person is defined in the bill as "any foreign organization, corporation, or individual resident in a foreign country, or any domestic or foreign organization, corporation, or individual, that is owned or controlled by the foreign organization, corporation, or individual."

Missile Division and thereby reduce Thomson-CSF's interest to less than ten percent, Thomson-CSF was able to get the acquisition approved.<sup>470</sup>

Regardless of the outcome of the LTV case, Senator Byrd had successfully introduced Amendment 3077 ("Byrd Amendment") which inserted a new subsection 721(a) to the DPA requiring mandatory investigations of foreign mergers, acquisitions, or takeovers when the acquirer is "controlled by or acting on behalf of a foreign government" and the merger, acquisition, or take over "could affect the national security of the United States." The amendment provided that such investigation "shall commence not later than 30 days after receipt by the President or the President's designee of written notification," and the investigation "shall be completed not later than 45 days after its commencement."<sup>471</sup>

The redesignated subsection 721(f) was amended to add two additional factors for the president to consider when making a decision to block a foreign merger, acquisition, or takeover:

- (1) 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

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<sup>470</sup> W. Robert Shearer, Comment, "The Exon-Florio Amendment: Protectionist Legislation Susceptible to Abuse," *Houston Law Review* 30 (1993) 1729.

<sup>471</sup> *National Defense Authorization Act for Fiscal Year 1993*, Section 837(a), Public Law 102-484, *U.S. Statutes at Large* 106 (1993) 2315, § 837(a), (enacted bill 102 HR 5006), *U.S. Code* 50 (1993), app. §2170(b).

(2) the potential effects of the transaction on U.S. technological leadership in areas affecting U.S. national security.<sup>472</sup>

The amendment also added the requirement that the “President shall immediately transmit to the secretary of the Senate and the Clerk of the House of Representatives a written report of the President’s determination of whether or not to take action” to include a “detailed explanation of the findings and factors considered in making the determination.”<sup>473</sup> Finally, the amendment added the “sense of the Congress” that the president should include the director of the Office of Science and Technology Policy and the assistant to the president for National Security in the membership of the CFIUS.

The comments of the Byrd Amendment sponsors are particularly instructive for understanding Congress’s concerns about CNOOC’s bid for Unocal. “We face the dilemma of how to prevent foreign companies, particularly those controlled by their governments, from raiding the U.S. economy and snatching up the prized jewels of America’s industrial base without discouraging legitimate foreign investment in our economy,” said Senator Byrd.<sup>474</sup> Even though global defense spending was dramatically reduced since the end of the Cold War, there were negative side effects on the industry;

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<sup>472</sup> *National Defense Authorization Act for Fiscal Year 1993*, Section 837(a), Public Law 102-484, 106 Stat. 2315, (1993) (enacted bill 102 HR 5006), *U.S. Code 50* (1993), app. §1270(f).

<sup>473</sup> *National Defense Authorization Act for Fiscal Year 1993*, Section 837(a), Public Law 102-484, 106 Stat. 2315, (1993) (enacted bill 102 HR 5006), *U.S. Code 50* (1993). app. § 2170(g).

<sup>474</sup> Senator Robert Byrd of Virginia speaking on the *National Defense Authorization Act for Fiscal Year 1993*, on September 18, 1992, 102<sup>nd</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.* 138, no. 128: S14195.

one of which was the failure of weaker defense firms making them ripe for acquisition. In Senator Byrd's opinion, although the Exon-Florio Amendment provides the executive branch with "all the tools" it needs "to ensure the stability and safety of our industrial base," presidents have not chosen to use these tools. Senator Byrd feared that "we have established a pattern where only the most blatantly risky cases receive scrutiny and even then they are likely to get the go-ahead."<sup>475</sup>

Senator Exon echoed Senator Byrd's concerns, emphasizing that President George H.W. Bush had used his powers under Exon-Florio Amendment "rather conservatively." He did not fault the president, but suggested that changes in "what can be expected in the post cold war era" required updating the law. Of course, it is not surprising that Senator Exon would shy away from criticizing the statute that he had authored.<sup>476</sup> By way of contrast, Senator Riegle (D-MI) emphasized that the Reagan/Bush Administration was "blinded by its free trade and open investment ideology." Reigle suggested that the presidents' narrow interpretation of the authority Congress gave them kept them from seeing the "cumulative impact" of foreign takeovers.<sup>477</sup>

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<sup>475</sup> Senator Byrd of West Virginia speaking on the Senate on the *National Defense Authorization Act for Fiscal Year 1993*, on September 18, 1992 102<sup>nd</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.* 138, no. 128: S14195.

<sup>476</sup> Senator Exon of Nebraska speaking on the *National Defense Authorization Act for Fiscal Year 1993*, September 18, 1992, 102<sup>nd</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.* 138, no. 128: S14195.

<sup>477</sup> Senator Riegle of Michigan speaking on *National Defense Authorization Act for Fiscal Year 1993*, on September 18, 1992, 102<sup>nd</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.*, 138, no. 128: S14195.

Senator Sarbanes (D-MA) emphasized that cases involving foreign-owned companies fall into a different category “by definition ... because they are not dictated strictly by market forces.” He also expressed concern about the “generic issue of foreign government ownership of U.S. defense contractors.”<sup>478</sup> Emphasizing that even the U.S. government did not own its own defense contractors, he questioned whether it would be a good idea to let foreign governments own them. Mr. Sarbanes concluded that the changes proposed by the amendment would allow the president to consider additional factors in considering whether to block a transaction. In addition, the new reporting requirements would increase transparency. In the past, presidents were not required to provide an explanation as to why they made the decisions they did. As a result, it has been “virtually impossible for Congress and the public to know what policy had been developed by the administration in applying the Exon-Florio provision or to hold the administration accountable.”<sup>479</sup>

In short, the Byrd Amendment made three significant changes to the original 1988 Exon-Florio Amendment. First, it shifted the focus from the intended use of the acquired assets to national origin of the entity acquiring the assets. Review was mandatory if an acquiring entity was controlled by or acting on behalf of a foreign entity. Second, it lowered the threshold for determining when review should occur. No longer did the

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<sup>478</sup> Senator Sarbanes of Maryland speaking on *National Defense Authorization Act for Fiscal Year*, on September 18, 1992, 102<sup>nd</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.* 138, no. 128: S14195.

<sup>479</sup> *Ibid.*

CFIUS need to find that the transaction “*threatens to impair* national security,” instead the CFIUS only needed to find that the transaction “*could affect* national security.”<sup>480</sup> Finally, it expanded the scope of factors that the president was to consider and emphasized technological leadership in maintaining national security.

Even though the Byrd Amendment improved the statute, it was not the panacea for handling foreign mergers; rather, it was a compromise. The first compromise was that reporting of a merger was still voluntary. Voluntary filing by foreign entities was included in the original Exon-Florio Amendment to demonstrate the U.S. government’s support of open trade. The reporting option was based on the “safe harbor” principle, that is, if parties to a merger were to notify CFIUS of a proposed or completed merger, and the CFIUS were to determine that a transaction did not pose a threat to national security, then the foreign entity could rest assured that the president would not order divestiture at a later time. But if the parties failed to notify the CFIUS of the transaction, it would leave the door open for future investigation and remedies. The risk of nondisclosure was heightened by the fact that any remedies imposed by the president were not subject to judicial review, leaving the foreign entity with no legal recourse once the president makes a decision. In spite of the incentive for voluntary notification, some members of Congress continued to believe voluntary notification was a flaw in the statute

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<sup>480</sup> Byrd Amendment to the *National Defense Authorization Act for Fiscal Year 1993*, Public Law 102-484, *U.S. Statutes at Large* 106 (1993) 2315-16, § 837(a), *U.S. Code* 50, app. § 2170(a)(b) [emphasis added]. For further discussion of this distinction see Christopher R. Fenton, “U.S. Policy towards Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security,” *Columbia Journal of Transnational Law* 41 (2002-2003): 207-208.



because sensitive information could exchange hands before any CFIUS review or presidential decision.

A second improvement in the statute was to require mandatory investigations in certain circumstances. The compromise language stipulates that CFIUS had responsibility for making the determination that national security “could” be affected by the transaction, that the subject U.S. company would be under foreign "control," and possibly, that a foreign company was "acting on behalf of" a foreign government. Without clear definitions of terms, the Byrd Amendment still left a lot of room for interpretation and, consequently, a lot of room for disagreement as to that interpretation.

Third, even though the Byrd Amendment specified additional factors for CFIUS to consider regarding sales of military goods and technology to countries supporting terrorist activities, some analysts have noted that the CFIUS already considered these factors as part of the review.<sup>481</sup> But even if the changes were minor, or redundant, by identifying specific factors in the statute, Congress was attempting to ensure that those factors would be given greater political weight during the review process.<sup>482</sup> This research into the CNOOC case and other bids proposed by Chinese corporations confirms that the CFIUS did give these statutorily defined factors more careful consideration in subsequent reviews.

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<sup>481</sup> Christopher F. Corr, “A Survey of United States Controls on Foreign Investment and Operations: How Much is Enough?” *The American University Journal of International Law & Policy* 9 (Winter 1994): 432.

<sup>482</sup> *Ibid.*, 431.

Fourth, the Byrd Amendment addressed Congress's concern about the lack of transparency in how presidents had been implementing Exon-Florio in the CFIUS investigative process. The amendment required specific guidelines for initiation of the process and milestones for each stage of the review, that is, the review must begin within 30 days of written notice, the review must be completed and a recommendation made to the president within 45 days, and the president must make a decision within 15 days. In addition, the president was required to report to Congress immediately regarding any decisions after undertaking an investigation, and a Quadrennial Report was required to provide details as to any credible evidence concerning industrial espionage or attempted control over leading technology.<sup>483</sup> Even though some have argued that the Byrd Amendment had little legal consequence, the message that Congress sent to the president and the CFIUS had political consequences. That is, it was clear that Congress would review CFIUS consideration of investments proposed by foreign government-owned entities more assiduously.

On February 16, 1994, pursuant to amendments to the Defense Production Act, the Treasury Department issued proposed implementing regulations. Treasury defined "foreign government" broadly to include any government body exercising governmental functions, such as state and local authorities.<sup>484</sup> The regulations also specified that a

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<sup>483</sup> *National Defense Authorization Act for Fiscal Year 1993*, § 837(a), Public Law 102-484, *U.S. Statutes at Large* 106 (1993): 2315 (enacted bill 102 HR 5006), *U.S. Code* 50, app. § 2170.

<sup>484</sup> *Code of Federal Regulations*, title 31, § 800, 210; *Federal Register* 59, no. 7 (1994): 666.

mandatory investigation would not be required where the foreign government entity was merely a "passive participant in an acquisition by a foreign person."<sup>485</sup> The inclusion of this language demonstrates how administrative agencies are able to assume control over how laws and statutes are implemented, especially when Congress does not provide clear definitions or statutory guidance.

In short, the Byrd Amendment to Exon-Florio was “designed to serve as a surgical instrument to prevent control of critical defense-related industries by hostile governments or transfer of sensitive technologies to strategic competitors” by focusing on the origin of capital in determining whether a transaction threatened national security.<sup>486</sup> But in 2000, the GAO published its report and concluded that the process for identifying foreign acquisitions which affect national security still could be improved.<sup>487</sup> Some of the weaknesses identified by the report are as follows: First, the reporting process still did not ensure that all national security-related acquisitions were reviewed. The CFIUS continued to rely upon voluntary reporting and Congress assumed that companies would report contemplated foreign acquisition to the CFIUS early in the process because the

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<sup>485</sup> See *Code of Federal Regulations*, title 31, § 800, 210, *Federal Register* 59, no. 7 (1994): 666.

<sup>486</sup> Christopher R. Fenton, “U.S. Policy towards Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security,” *Columbia Journal of Transnational Law* 41 (2002-2003): 198.

<sup>487</sup> U.S. Government Accounting Office, “Defense Trade: Identifying Foreign Acquisitions Affection National Security Can Be Improved,” Report to the Honorable Chuck Hagel, U.S. Senate, GAO/NSIAD-00-144, Washington, D.C.: Government Printing Office, June 2000.

president retained authority to force divestiture for acquisitions that were not reported.<sup>488</sup> Second, the CFIUS still did not know the extent to which foreign acquisitions of U.S. companies might have an effect on national security. This was because no records were kept of acquisitions identified by member agencies or contacts made with parties to the acquisitions to encourage voluntary reporting.<sup>489</sup> Third, even though other laws and regulations required the reporting of some security-related acquisitions to individual agencies, the agencies were not required to report this information to the CFIUS.<sup>490</sup> Instead, Treasury officials reported that the CFIUS member agencies continued to obtain information about acquisitions of potential concern by reviewing business media sources.<sup>491</sup> This resulted in inconsistent reporting from one agency to the next. Fourth, since agency referrals to the CFIUS were informal, agencies did not maintain formal records of contacts and agency actions pertaining to the contracts, resulting in little to no follow-up regarding the referrals.<sup>492</sup>

Over the years, foreign countries, and their investors, have expressed concerns that American presidents would interpret the Exon-Florio provisions too broadly and there would be a trend towards more protectionist policies. In fact, presidents have been reluctant to apply the statute too broadly for fear of interfering with foreign trade and

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<sup>488</sup> Ibid., 5.

<sup>489</sup> Ibid., 7.

<sup>490</sup> Ibid., 7.

<sup>491</sup> Ibid., 9.

<sup>492</sup> Ibid., 13.

investment opportunities. This reluctance is documented in the 2000 GAO Report indicating that only seventeen percent of 7,371 foreign acquisitions reported to the Commerce Department Bureau of Economic Analysis from 1988 to 1999 were reported to the CFIUS.<sup>493</sup> [See Table 5] Of those reported, only seventeen were investigated, seven were withdrawn, and only one was blocked by the president.

In spite of these weaknesses, according to McLean, the Exon-Florio Amendment has not failed. “Before the law was enacted, presidents had very few tools to protect the national security when a foreign entity took control of an important security asset of the United States,” he said. “The test of the law is not how many transactions that have been stopped, but that transactions involving foreign purchasers are scrutinized to ensure that the national security is protected.”<sup>494</sup>

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<sup>493</sup> Ibid., 8.

<sup>494</sup> Christopher A. McLean, “Exon Florio – The Spirit of Late Senator Jim Exon Still Soars,” e-Copernicus, accessed at [www.e-copernicus.com/Press20%Releases/Exon Florio.pdf](http://www.e-copernicus.com/Press20%Releases/Exon%Florio.pdf) on 6/27/09. McLean served as legal counsel to U.S. Senator Jim Exon and was a staff co-author of the Exon-Florio law.

**TABLE 5: Foreign Acquisitions, Voluntary Reports, and Dispositions** <sup>495</sup>

Year	Foreign Acquisitions	Reports to CFIUS	Reports Investigated	Offers Withdrawn	President Decision	President Blocked
1988	869	14 <sup>a</sup>	1	0	1	0
1989	837	204	5	2	3	1
1990	839	295	6	2	4	0
1991	561	152	1	0	1	0
1992	463	106	2	1	1	0
1993	554	82	0	0	0	0
1994	605	69	0	0	0	0
1995	644	81	0	0	0	0
1996	686	55	0	0	0	0
1997	640	62	0	0	0	0
1998	673 <sup>b</sup>	65	2	2	0	0
1999	c	79	0	0	0	0
2000	c	72	1	0	1	1
2001	c	55	1	1	0	0
2002	c	43	0	0	0	0
2003	c	41	2	1	1	1
2004	c	53	2	2	0	0
2005	c	65	2	2	0	0

<sup>a</sup> Filings began in September 1988

<sup>b</sup> Data not complete

<sup>c</sup> Data not available

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<sup>495</sup> Department of Treasury; Department of Commerce; Bureau of Economic Analysis; and Institute for International Economics, *U.S. National Security and Foreign Investment*, “Chapter 2: The Exon-Florio Amendment,” 57, available at [www.iie.com](http://www.iie.com).

### III. POST 9/11 IMPLEMENTATION OF EXON-FLORIO

September 11, 2001 marked a major shift in the international world order. Previously, national security threats were state-based and foreign trade policies reflected that world order. After the terrorist attacks on American soil in 2001, the focus of national security was no longer on nation-states, but on non-state actors, and their relationships to different nation-states. Along these lines, President Bush added the Department of Homeland Security to the CFIUS which had the effect of shifting the balance of power on the committee from agencies that focused on the economic benefits of foreign direct investment to agencies that focused on the complexities of providing national security.<sup>496</sup>

Consistent with the heightened concern about national security and the authorities provided to the president under the Homeland Security Act, many in Congress believed that President Bush's post 9/11 interpretation of the Exon-Florio Amendment would change.<sup>497</sup> This would have been consistent with the popular belief that a more expansive view of national security is required when threats by non-state actors are considered. Analysts such as Christopher Fenton suggested that the changed global environment required an expansion of new relationships

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<sup>496</sup> *Homeland Security Presidential Directive 7 (HSPD-7)* (December 17, 2003) sets forth government policy for protecting critical infrastructure and key resources, identifies critical infrastructure sectors, and assigns responsibilities to various agencies for protecting those sectors. Available at [www.whitehouse.gov](http://www.whitehouse.gov) (accessed December 8, 2009).

<sup>497</sup> *United and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act*, §1016(e) codified at *U.S. Code* 42 (2001), §5195c (e) (commonly known as *The Patriot Act*).

to preclude terrorist access to the international financial system and mainly include: the protection of industries required for the execution of the global anti-terror campaign, security threats posed by foreign control of particular domestic industries, and potential third-party transactions between foreign entities that acquire these industries.<sup>498</sup>

In spite of past efforts to increase congressional oversight of CFIUS investigations, foreign transactions continued to be reviewed in a “highly secretive” manner.<sup>499</sup> Although intended to protect sensitive proprietary information, Senator Richard Shelby (R-AL) emphasized that this secretive process made congressional oversight difficult. For example, some of the CFIUS-reviewed cases that continued to raise congressional concerns were: (1) the proposed acquisition of Silicon Valley Group, Inc. (SVG), a manufacturer of computer semiconductor lithography with military applications, by ASM Lithography (ASML), a Netherlands company; (2) the 2003 proposed acquisition of a majority stake in the bankrupt Global Crossing Ltd, a fiber optic network provider, by Singapore Technologies Telemedia and Hutchison Whampoa Ltd. of Hong Kong;<sup>500</sup> and (3) the purchase of Magnequench, Inc., a high-precision magnet manufacturer by a Chinese consortium.

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<sup>498</sup> Christopher R. Fenton, “U.S. Policy towards Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security,” 200.

<sup>499</sup> Report by Senator Shelby of Alabama, Foreign Investment and National Security Act of 2006, on June 21, 2006, to the Committee on Banking, Housing and Urban Affairs, Calendar No. 474, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess.: 109-264.

<sup>500</sup> Although heightened sensitivity to acts of terrorism, led the CFIUS to impose conditions on the Global Crossing acquisition so as to preserve the CIA’s and FBI’s ability to conduct surveillance through fiber optic networks, and the Hong Kong conglomerate dropped out of the deal, congressional leaders were still concerned about their lack of oversight over foreign acquisitions. See Stephen J. Norton, “A Bid to ‘Buy



The proposed acquisition of the SVG had been set for review under President Clinton, but SVG withdrew its proposal after intervention by the Department of Defense and some members of Congress. When ASML reapplied under the George W. Bush Administration, the CFIUS was deadlocked at the end of the 45-day review and had to work overtime to reach a consensus. Finally, the CFIUS issued a formal recommendation in which it conditioned approval on restructuring which included ASML agreeing to sell SVG's Tinsley Laboratories, a manufacturer of optical components for spy satellites.<sup>501</sup>

The Bush Administration was criticized for how it handled the ASML-SVG deal. Fenton suggests the “most legitimate and relevant” reasons for the criticism were that : (1) the CFIUS was overstepping its bounds by evaluating both direct and indirect effects of an acquisition; (2) the Department of Defense was seeking to expand its influence by insisting upon “performance requirements” rather than agreeing to informal guarantees which had been acceptable in the past; (3) the Bush Administration preferred to require restructuring of foreign acquisitions rather than deny business opportunities; and (4) the committee’s decision making stalemate was caused by irreconcilable ideological differences.<sup>502</sup>

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American’ Under Security Spotlight, *Congressional Quarterly Weekly*, July 8, 2005, 1953).

<sup>501</sup> Jaret Seiberg and Shanon D. Murray, “Antitrust Alert,” *The Daily Deal*, May 1, 2001.

<sup>502</sup> Christopher R. Fenton, “U.S. Policy towards Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security,” 195-249.

Accordingly, on February 20, 2004, Senator Richard Shelby (R-AL), chairman of the Committee on Banking, Housing, and Urban Affairs, and Senator Sarbanes (D-MD), ranking member of the committee, requested another Government Accountability Office (GAO) study of the implementation of Exon-Florio.<sup>503</sup> While the GAO was conducting its study, and prior to the release of its findings, the Chinese-controlled CNOOC was secretly contemplating a proposal to acquire Unocal.

Early in 2005, when rumors surfaced that CNOOC was preparing a bid, executive investigation of a proposed merger still was not mandatory. Specifically, the statute stated,

The President or the President's designee *may* make an investigation to determine the effects on national security of mergers, acquisitions, and takeovers proposed or pending . . . by or with *foreign persons* which could result in foreign control of persons engaged in interstate commerce in the United States.<sup>504</sup>

A few months later, when CNOOC formally announced its interest in Unocal, members of Congress were still awaiting the results of the GAO report. General questions about administrative review of foreign acquisitions, uncertainty stemming from the secret review process, and heightened concern about national security following September 11 contributed to the elevation of the CNOOC proposal on the congressional policy agenda.

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<sup>503</sup> S. Rep. 109-264, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., 2006.

<sup>504</sup> *U.S. Code* 50, app. § 2170(a) (emphasis added).

#### IV: THE UNOCAL ACQUISITION CASE

##### A. FTC Review of ChevronTexaco's Proposed Merger

ChevronTexaco submitted its plan for the proposed merger to the FTC on April 4, 2005 while the FTC was involved in an administrative hearing with Unocal over a previous charge that Unocal unlawfully monopolized the market for reformulated gasoline meeting the specifications of the California Air Resources Board (CARB).<sup>505</sup> According to the FTC, the alleged monopolization resulted from Unocal misrepresenting its research regarding the reformulated gasoline as nonproprietary while also pursuing a patent on the technology.<sup>506</sup>

In reviewing the proposed Chevron-Unocal merger, the FTC acknowledged that ChevronTexaco and Unocal both had extensive oil and gas operations. But since Unocal did not have any refineries or gasoline stations, and few other downstream operations, the FTC determined “virtually all of the competitive overlaps between the two firms are in unconcentrated upstream markets, and the merger thus creates no competitive risk.”<sup>507</sup> However, the FTC warned, if ChevronTexaco acquired Unocal, and Union Oil’s questionably obtained patents, then ChevronTexaco would be in a position to “obtain

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<sup>505</sup> The FTC had filed the charge against Unocal with its complaint, *In the Matter of Union Oil Company of California*, File No. 011-0214, Docket No. 9305 (March 4, 2003); available at [www.ftc.gov/os/2003/03/unocalcmp.htm](http://www.ftc.gov/os/2003/03/unocalcmp.htm) (accessed 3/18/2007).

<sup>506</sup> *In re: Union Oil Co. Calif.*, File No. 011-0214, Docket No. 9305 (April 4, 2003) available at [www.ftc.gov/os/2003/03/unocalcmp.htm](http://www.ftc.gov/os/2003/03/unocalcmp.htm), accessed 3/18/2007.

<sup>507</sup> Statement of Federal Trade Commission, *In the Matter of Union Oil Co. of California*, Docket No. 9305 and *In the Matter of Chevron Corporation and Unocal Corporation*, File No. 51-0125, Docket No. C-4144 (August 2, 2005); available at <http://www.ftc.gov/os/caselist/0510125/050802statement0510125.pdf> (accessed March 18, 2007).

sensitive information and to claim royalties from its own horizontal downstream competitors.” This, the FTC believed, would “have an adverse effect on competition” and “would inevitably have required an extensive inquiry and possible litigation.”<sup>508</sup>

This concern was resolved by executing an Agreement Containing Consent Order (Consent Agreement) which became final after a 30-day public comment period.<sup>509</sup> The Consent Agreement mandated that upon merging, neither ChevronTexaco nor Unocal take any action to enforce the patents or collect royalties, including pending litigation; the order also required that Unocal would disclaim its reformulated-gasoline patents and release the patent information to the public.<sup>510</sup> Because resolution of the patent/monopolization matter was predicated upon the ChevronTexaco-Unocal merger, a successful bid from another entity would require FTC to reopen the administrative hearing on the issue. Since reopening the hearing would involve additional legal costs, many assumed it was in Unocal’s best interest to complete the merger with ChevronTexaco.

The next section turns to discussion of the legal obligations ChevronTexaco had as a corporate entity to its shareholders, and how these obligations imposed another formal constraint upon the congressional reaction to the CNOOC proposed takeover.

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<sup>508</sup> Ibid., 2.

<sup>509</sup> Decision and Order, *In the Matter of Chevron Corporation and Unocal Corp.*, Docket No. C-4144, <http://www.ftc.gov/os/caselist/0510125/050802do0510125.pdf>, (accessed March 18, 2007).

<sup>510</sup> Ibid.

## **B. ChevronTexaco Corporate Obligations to Shareholders**

The operations of business associations and corporations are largely governed by statutory law.<sup>511</sup> The Uniform Partnership Act of 1914 received almost unanimous acceptance and has been adopted in forty-nine states, with the exception of Louisiana. Since then, very few amendments have been made. This consistency, along with decades of litigation, has given corporations a good sense of the kinds of legal issues that may arise and how the courts may interpret those issues. A second statute, the Model Business Corporation Act, was very influential in the development of state corporation statutes. The difference between “uniform” statutes and “model statutes is that uniform statutes are designed to create nationwide uniformity of provisions applicable to the corporations, whereas model statutes suggest that jurisdictions may pick and choose from a template and make amendments or changes as desired. As a result, there is considerable variation in the state corporation statutes.

Unocal’s board of directors was obligated to comply with the corporation law of Delaware where Unocal was legally incorporated.<sup>512</sup> Unocal was also subject to the Federal laws, such as the Securities Act of 1933, *U.S. Code* 15, § 77a *et seq.* which imposes specific requirements on corporations engaged in the public sale of securities. While discussion of the specific details of these statutes goes beyond the scope of this dissertation, it is important to understand that Unocal’s directors were bound by the duty of care and the business judgment rule adopted in Delaware.

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<sup>511</sup> This study refers to both corporations and business associations, in general, as corporations throughout the remainder of this dissertation.

<sup>512</sup> See *Delaware Code Annotated*, title 8 (1974 and supp. 2000).

In general, the standard of due care is met under corporate law if two tests are met: (1) due care must be used in “ascertaining relevant facts and law before making the decision,” and (2) the decision must be made after reasonable deliberation.<sup>513</sup> The American Law Institute has defined the duty of care and business judgment rule as follows:

A director or officer has a duty to the corporation to perform the director’s or officer’s functions in good faith, in a manner that he or she reasonably believes to be in the best interests of the corporation, and with the care that an ordinarily prudent person would reasonably be expected to exercise in a like position and under similar circumstances. . . .<sup>514</sup>

A director fulfills the duty of making a business judgment in good faith if he is “informed with respect to the subject of the business judgment to the extent the director reasonably believes to be appropriate under the circumstances” and the director “rationally believes that the business judgment is in the best interests of the corporation.”<sup>515</sup>

Under Delaware law, directors are charged with an “unyielding fiduciary duty to the corporation and its shareholders.”<sup>516</sup> The rule itself is “a presumption that in making a business decision, the directors of a corporation acted on an informed basis, in good

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<sup>513</sup> Robert W. Hamilton, *Corporations Including Partnerships and Limited Partnerships: Cases and Materials*, (St. Paul, MN: West Publishing Co., 1990), 752.

<sup>514</sup> The American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations*, § 4.01 (1994) cited in Robert W. Hamilton, *Corporations Including Partnerships and Limited Partnerships: Cases and Materials*, (St Paul, MN: West Publishing Co., 1990), 754.

<sup>515</sup> *Ibid.*

<sup>516</sup> Robert W. Hamilton, *Corporations Including Partnerships and Limited Partnerships: Cases and Materials*, (St Paul, MN: West Publishing Co., 1990), 766.

faith and in the honest belief that the action taken was in the best interests of the company.”<sup>517</sup> In regards to acquisitions, whether directors make an informed decision, in good faith, includes how they timed the acquisition, how it was initiated, structured, negotiated, disclosed to directors, and how approvals were obtained from directors and shareholders. An informed decision also includes financial considerations of the proposed acquisition, including assets, market value, earnings, future prospects, and any other factors that affect the intrinsic or inherent value of the company’s stock.<sup>518</sup>

Directors may be held liable for taking actions that are so improvident, or risky, as to be contrary to fundamental conceptions of prudent business practices. However, courts are reluctant to interfere with corporate affairs, “except in the egregious case of bad judgment or when there is evidence of bad faith.”<sup>519</sup>

Although deliberations concerning the CNOOC proposed acquisition were not made public, the directors had a duty to give the CNOOC offer detailed and judicious consideration before bringing the ChevronTexaco proposal to the stockholders for a vote. Because the directors were obligated to bargain for a fair price, and to make an informed decision based upon the information that was available to them, they would have to weigh the pros and cons, the costs and benefits, of both the ChevronTexaco and CNOOC

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<sup>517</sup> *Aronson v. Lewis*, Del. Supr., 473 A.2d 805, 812 (1984).

<sup>518</sup> Robert W. Hamilton, *Corporations Including Partnerships and Limited Partnerships: Cases and Materials*, St Paul, MN: West Publishing Co., 1990), 858-59. See 8 Del.C § 262(h).

<sup>519</sup> Hansen, “The ALI Corporate Governance Project: Of the Duty of Due Care and the Business Judgment Rule,” *Business Law* 41 (1986); 1237, 1238-42, 1247.

proposals. This duty of care played into the unfolding of events surrounding the Unocal case.

### **C. CNOOC's Proposed Acquisition of Unocal**

There has been a great deal of speculation as to why CNOOC would choose to enter the U.S. market through a takeover rather than by building a new subsidiary. Assuming that CNOOC was interested in profits, like most investors, it would be attracted to the most profitable option. The advantage of an acquisition is that it would allow “relatively quick entry into a foreign market.”<sup>520</sup> By being the first to enter a foreign market, investors may avoid barriers that are created by prior entry of other investors. In addition, when markets are growing slowly, there is an advantage to being able to enter a market rapidly through an acquisition instead of forming a subsidiary.<sup>521</sup>

Globerman and Shapiro note that corporations are motivated to invest abroad because of the opportunity for “enhance[ing] the efficiency and competitiveness of the investor.”<sup>522</sup> Foreign investment provides “complementary assets” which “include marketing and distribution networks in the host country and technological and managerial knowledge resident in the host country.”<sup>523</sup> Another motive is “to exploit the investing firm’s competitive advantages in the host market. Where those advantages are rooted in

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<sup>520</sup> Steven Globerman and Daniel Shapiro, “Economic and Strategic Considerations Surrounding Chinese FDI in the United States,” *Asia Pacific Journal of Management* 26 (2009): 166.

<sup>521</sup> Ibid.

<sup>522</sup> Ibid.

<sup>523</sup> Ibid.



firm-specific knowledge or other intangible assets, they are typically best exploited by internalizing their utilization within a wholly owned affiliate.”<sup>524</sup> But this usually requires knowledge of the host market conditions and the host country environment.

Considering the net advantages of acquisitions, Globerman and Shapiro conclude that the Chinese companies are more likely to find acquisitions to be the most advantageous way to enter the U.S. market.<sup>525</sup> Early in 2005, prior to the FTC hearing discussed above, CNOOC had commissioned a review of Unocal’s assets, and rumors had begun to surface that CNOOC was interested in purchasing Unocal.<sup>526</sup> Although neither CNOOC nor Unocal would comment on the reports, Unocal’s stock jumped and analysts began to speculate as to whether CNOOC had the financial ability or managerial expertise to pull off such an ambitious deal.<sup>527</sup> The possibility of a petroleum company in a developing country purchasing a western petroleum company with a hundred year history was “hot news” in the energy industry.<sup>528</sup>

In the meantime, a number of bills which were working their way through Congress helped set the stage for politicizing any offer made by CNOOC. For example, eleven bills had been introduced in the 108<sup>th</sup> Congress to address China’s currency peg,

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<sup>524</sup> Ibid.

<sup>525</sup> Ibid.

<sup>526</sup> *New York Times*, January 7, 2005.

<sup>527</sup> Christopher Palmeri, “On a Fast Boat to China?” *Business Week*, (3917) (January 24, 2005): 62-63.

<sup>528</sup> *China Chemical Reporter*, March 6, 2005, 7.

and these bills reappeared in the 109<sup>th</sup> Congress: S. 14 (Stabenow, D-MI), S. 295 (Schumer, D-NY), and H.R. 1575 proposed to raise U.S. tariffs on Chinese goods by an additional 27.5% unless China appreciated its currency; S. 277 (Lieberman, D-CT) directed the president to negotiate with countries that manipulate their currency; and HR 1216 (English, R-PN) and S. 593 (Collins, R-ME) would apply U.S. countervailing laws dealing with government subsidies to nonmarket economies such as China. Early in April, the Senate approved Amendment 309 to S. 600, the Foreign Affairs Authorization Act, which would impose an additional 27.5 percent tariff on Chinese goods if China did not appreciate its currency to market levels. In response to this amendment, the Senate leadership moved to allow a vote on S. 295, with the same language, no later than July 27, 2005 on the condition that the sponsors of the amendment would not sponsor similar amendments for the rest of the 109<sup>th</sup> congressional session.<sup>529</sup>

Later in the month, the U.S. Trade Representative announced that he had placed China on the Special 301 Priority Watch List due to failure to increase protection of U.S. intellectual property rights. The Trade Representative urged China to prosecute criminal piracy cases and to improve market access to products with intellectual property rights protection; and it warned China that it may bring a case against it to the World Trade Organization for failure to enforce the intellectual property right laws.

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<sup>529</sup> Later on June 30, 2005 Senator Schumer and other sponsors of S. 295 agreed to delay consideration of the bill until they received a briefing from the Bush administration which would provide assurances that China would make progress on currency reform in the next few months.

The political environment surrounding U.S.-China trade issues was made worse for the CNOOC bid when the Treasury Department released its International Economic and Exchange Rate Report on May 17, 2005. The report reinforced legislators' fears regarding China's currency by concluding that China was substantially distorting world markets by pegging its currency to the U.S. dollar. The report stressed that China should move towards a more flexible exchange rate and that Treasury would closely monitor progress in this area over the next six months.

While Congress was debating China's trade policies, CNOOC Executive Chairman Fu Chengyu's plans to submit a bid were delayed when CNOOC's non-executive directors decided to hire independent advisors to review his proposal.<sup>530</sup> Then, while the review was taking place, ChevronTexaco finally announced its own offer for Unocal on May 27, 2005.<sup>531</sup> At that time, the possibility of a CNOOC bid was still not off the table. Congressional reaction to this possibility seemed unnecessary to many observers given that the offer had not yet been made and CFIUS review had not yet been triggered under the Exon-Florio Amendment. But by the time that the CNOOC board voted on June 22, 2005 to counter-offer an \$18.5 billion cash offer for Unocal,<sup>532</sup>

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<sup>530</sup> *Financial Times*, May 9, 2005.

<sup>531</sup> *Financial Times*, May 27, 2005.

<sup>532</sup> *The Times* (London Edition), June 23, 2005.

lawmakers in Washington had already begun questioning whether the Bush Administration should intervene and the issue was heating up.<sup>533</sup>

On the day following the announced bid, the Bush Administration held to the position that the question of a national security review was “hypothetical” because the transaction had not yet occurred.<sup>534</sup> While the administration did not appear unduly concerned, the question permeated the media which certainly played a role in stirring up the controversy. Perceiving the upcoming rivalry with CNOOC, ChevronTexaco may have added fuel to the debate by focusing on the fact that CNOOC is controlled and financed by the Chinese government and playing on fears that China would divert oil to China on a non-commercial basis.<sup>535</sup>

Meanwhile, the idea that CNOOC’s bid was politically motivated, or would have an effect on U.S. security, was immediately rejected by most members of the financial community and China specialists.<sup>536</sup> There are benefits to the domestic owners of assets acquired by foreign investors, as well as by the host country consumers. If foreign owners can operate acquired assets more efficiently than the domestic owners, they can

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<sup>533</sup> David Barboza and Andrew Ross Sorkin, “Chinese Oil Giant in Takeover Bid for U.S. Company,” *New York Times*, June, 23 2005.

<sup>534</sup> See Treasury Secretary John Snow’s statement to the Senate Finance Committee, cited in Edmund L. Andrews, “Capital Nearly Speechless on Big China Bid,” *New York Times*, June 24, 2005.

<sup>535</sup> Peter Robinson, vice chairman, quoted in *Economist* 376, no. 8433 (July 2, 2005): 54-56.

<sup>536</sup> See for example, Lee Raymond, Exxon Mobile, cited in *Economist*, 376, no. 8433 (July 2, 2005): 54-56; James Dorn, Cato Institute, cited in *Economist* 376, no. 8442, (September 3, 2005): 24-26.

afford to bid higher prices for the assets. It is also assumed that productivity gains associated with the acquisition will be passed on to the domestic consumers in the form of lower prices. The stronger the domestic competition, the more likely that consumers will benefit.<sup>537</sup> In spite of these advantages, the issues of political motives and threats to national security continued to heat up as members scrambled to draft legislation to block the Chinese proposal.

#### **D. Bills Introduced and Debated in Congress**

The socio-historical approach of institutional theory requires examining the relationships of individuals and institutions. This considers the bills which were introduced in Congress after it was rumored that CNOOC was preparing a bid to purchase Unocal. Examination of the legislative history gives insight into why members of Congress politicized this particular business transaction.

At the end of 2004, the U.S. Trade Representative had issued its third annual China WTO compliance report. Although the report stated that China's efforts had been "impressive" it reiterated that China's performance in certain areas was less than satisfactory and the country had a long way to go to reach compliance.<sup>538</sup> The main areas of concern included failure to protect U.S. intellectual property rights, undervaluing of the Chinese currency by pegging it to the U.S. dollar, and lack of transparency of trade laws. These deficiencies continued to persist while the trade imbalance between the U.S.

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<sup>537</sup> Steven Globerman and Daniel Shapiro, "Economic and Strategic Considerations Surrounding Chinese FDI in the United States," *Asia Pacific Journal of Management* 26 (2009): 168.

<sup>538</sup> *Congressional Research Service Report*, "China-U.S. Trade Issues," by Wayne M. Morrison, (Washington, D.C.: Library of Congress, July 1, 2005).

and China continued to grow. This caused several members of Congress to call upon the Bush Administration to take a more aggressive stance against China's "unfair" trade policies. At the same time, fearing a lack of executive action, a number of bills were introduced to mandate changes in U.S.-China trade policy. A few of these bills are relevant to the mood of Congress towards both the administration and China in 2005.

Representative Kirkpatrick (D-AZ) staged a direct attack against the Bush Administration by introducing an amendment to H.R. 3055 (the FY2006 Appropriations Act for various agencies) which prohibited the Department of Treasury from using funds to recommend approval of the sale of Unocal to CNOOC.<sup>539</sup> But the language was rather extreme and was deleted by the Senate. It was not included in the Conference Report which passed the House and Senate and was eventually signed into law, but Kirkpatrick did make her point.<sup>540</sup>

Several other bills addressing the currency issue were introduced in the 109<sup>th</sup> Congress. For example, S. 14 (Stabenow, D-MI), S. 295 (Schumer, D-NY), and H.R. 1575 (Myrick, R-NC) directed the Treasury secretary to negotiate with China to accept a market-based system of currency valuation. These bills went so far as to impose a duty on Chinese goods if the president were unable to certify to Congress that China had stopped manipulating the exchange rate and was complying with accepted market-based trade policies. Although President Bush had been known to criticize China's currency

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<sup>539</sup> Amendment to *Transportation, Treasury, Housing and Urban Development, the Judiciary, the District of Columbia and Independent Agencies Appropriations Act for FY 2006*, HR 3055, Section 951.

<sup>540</sup> H. Rept. 109-307.

peg, he had not made any progress with the issue. On April 6, 2005, the Senate leadership moved to allow a vote on S. 295 later in the session, and it may have passed, but on June 30<sup>th</sup> Senator Schumer and the other sponsors agreed to delay consideration of the bill after the Bush Administration informed them that China was expected to make progress on the reforming its currency. These promises, however, did not assuage all the members of Congress from wanting to send a strong message to the Chinese (and the Bush Administration) about China's trade policies, especially after news of the CNOOC bid hit the press.

On June 17, 2005, two Republican members of Congress from California, Representatives Richard W. Pombo and Duncan Hunter, wrote a letter to President Bush stating that American companies would continue to have difficulty competing against the Chinese and urged the president to initiate a review based on the Defense Production Act. Then, on July 24, 2005, another group from the House of Representatives directed a letter to the administration's Secretary of Treasury Snow expressing concern about China's "ongoing and proposed acquisition of energy assets around the world, including assets of U.S.-based energy and oil companies." The letter stated specific issues for CFIUS to review in order to protect U.S. energy security.

While ChevronTexaco may have been lobbying the California congressional delegation to intervene in the hostile bid, Exxon Mobil Chief Executive Lee Raymond warned against legislative interference. "To the extent that they preclude the Chinese from buying assets here, it could easily come back and reflect that we won't be able to

buy assets in a foreign country.”<sup>541</sup> According to Vice President for International Economic Affairs for the National Association of Manufacturers Frank Vargo, American businesses “have our issues with China, but investing in the U.S. is not one of them.”<sup>542</sup> Similarly, Liu Jianchao, spokesman for the Chinese Foreign Ministry, claimed that it was a “corporate issue” and that he could not comment on the case, however he “encourage[d] the U.S. to allow normal trade relations to take place without political interference.”<sup>543</sup> In fact, Beijing energy consultant, He Jun, warned that if the United States “treats China as a threat, it will inevitably have to find its own path to meet its energy needs.”<sup>544</sup> This, of course, would be contrary to the Bush Administration’s interest in discouraging China from cultivating energy deals with “rogue” states.

On the other hand, Peter Robertson, Chevron-Texaco’s vice-chairman, accused the Chinese of not competing fairly. “Clearly, this is not a commercial competition,” he stated. “We are competing with the Chinese government, and I think that is wrong.”<sup>545</sup> Robertson also contended that Chevron was in a better position to develop Unocal’s

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<sup>541</sup> Quoted in Heather Timmons, “China Oil Chang Expected to Vote Today on Unocal Bid,” *The New York Times*, June 22, 2005.

<sup>542</sup> Quoted in Dan Roberts, Richard McGregor and Stephanie Kirchgaessner, “A New Asian Invasion: China’s Champions Bid High for American Brands and Resources.” *Financial Times* (London Edition), June 24, 2005.

<sup>543</sup> David Barboza and Andrew Ross Sorkin, “Chinese Oil Giant in Takeover Bid for U.S. Company,” *New York Times*, June 23, 2005.

<sup>544</sup> Quoted in Joseph Kahn, “Behind China’s Bid for Unocal: A Costly Quest for Energy Control,” *New York Times*, June 27, 2005.

<sup>545</sup> Quoted by Alexei Barrionuevo and Andrew Ross Sorkin, “Chevron Criticizes Rival Suitor,” *New York Times*, June 25, 2005.



assets than CNOOC. He also hinted that CNOOC had less than honorable intentions and might “steer natural gas produced in Indonesia to the Chinese market” rather than the broader Asian market.<sup>546</sup> Of course, this kind of comment from a rival company in a merger and acquisition is not surprising. Todd M. Malan, executive director of the Organization for International Investment, a Washington association that represents U.S. subsidiaries of foreign companies, warned

If our process is viewed as merely a proxy for Chevron’s views or subject to political intervention, and not a true national security review, then we ought to be prepared for that to happen when a U.S. company wants to make an investment in China.<sup>547</sup>

Meanwhile, the Bush Administration continued to avoid taking a position on the issue. Secretary John W. Snow told the Senate Finance Committee that the question of a national security review was “hypothetical” because the transaction had not yet occurred, and Chairman of the Federal Reserve, Alan Greenspan, made no comment.<sup>548</sup> This perceived lack of interest, or support, from the administration was not well received by Finance Committee members from both political parties. For example, Senator Ron Weyden (D-OR) was put off by the administration’s diffidence, while Senator Jim

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<sup>546</sup> Quoted by Alexei Barrionuevo and Andrew Ross Sorkin, “Chevron Criticizes Rival Suitor,” *New York Times*, June 25, 2005.

<sup>547</sup> Justin Blum, “CNOOC Requests U.S. Security Scrutiny,” *Washington Post*, June 28, 2005.

<sup>548</sup> Edmund L. Andrews, “Capital Nearly Speechless on Big China Oil,” *New York Times*, June 24, 2005.

Bunning (R-KY) said that the administration had made little progress in negotiations over China trade policy, complaining that the CFIUS told them “to take a hike.”<sup>549</sup>

In spite of the sentiments of those on the Senate Finance Committee, it is unlikely that the president was just brushing the issue aside. In fact, the proposed acquisition put the Bush Administration in a difficult position. Responding to a push by conservatives, President Bush had been taking a harder line toward China than previous presidents. At the same time that the CNOOC bid had become a hot issue, the Pentagon and Defense Department had been criticizing China for increasing its military spending while failing to use economic pressure to convince North Korea to end its nuclear program. On the economic front, Secretary Snow had already informed Congress about negotiations to convince the Chinese to change their currency policy. In the administration’s view, it would be counterproductive to take punitive action against China.<sup>550</sup>

Congress was not convinced and on June 30, 2005 the House passed H.Res. 344<sup>551</sup> The resolution expressed the sense of the House of Representatives “that a Chinese state-owned energy company exercising control of critical United States energy infrastructure and energy production capacity could take action that would threaten to

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<sup>549</sup> Edmund L. Andrews, “Capital Nearly Speechless on Big China Oil,” *New York Times*, June 24, 2005.

<sup>550</sup> Richard W. Stevenson with David E. Sanger and Jeff Gerth contributing, “In Unocal Bid, U.S. Struggles with China Policies,” *New York Times*, June 26, 2005.

<sup>551</sup> H.Res. 344 was introduced on Wednesday, June 29, 2005, *Cong. Rec.*, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., 151 (2005): H5434. It was referred to the Committee on Financial Services, and the Committee on International Relations.

impair the national security of the United States.”<sup>552</sup> Pursuant to the House rules, Mr. Ney (R-OH) and Ms. Kilpatrick (D-AZ) each controlled 20 minutes on the floor. Mr. Ney supported the immediate adoption of the resolution which asked that the president initiate a thorough review of any potential takeover of Unocal by CNOOC “as soon as any agreement of such a takeover is announced.”<sup>553</sup> He justified the action on the grounds that in times of rising energy prices “ready access to energy resources is a vital element” to economic and national security. Furthermore, he cited differences in how a “Communist government” and the U.S. government interpret trade agreements. He suggested that the Chinese government sees treaties as “the starting point for negotiation” whereas the U.S. government views treaties as “documents that must be adhered to.”<sup>554</sup> As a consequence, Mr. Ney was “skeptical” that CNOOC would honor assurances to dedicate regional oil production to American consumption. In his view, CNOOC’s proposal was a means of perpetuating China’s unfair trade practices which would threaten security “by holding out the prospect that every drop of oil, every unit of natural gas produced by that company could end up being shipped to China.”<sup>555</sup>

Ms. Kilpatrick testified to her bipartisan support for not spending any money for a “Communist-owned” company and not supporting further loss of technology to the

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<sup>552</sup> The bill was sponsored by Rep. Richard W. Pombo (CA). Co-sponsors included Representatives Joe Barton (TX), Henry J. Hyde (IL), Michael G. Oxley (OH), Duncan Hunter (CA), and Robert W. Ney (OH).

<sup>553</sup> Statements by Representative Ney on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5571.

<sup>554</sup> *Ibid.*

<sup>555</sup> *Ibid.*

Chinese when they do not protect intellectual property rights. Her primary concern was protecting American business.<sup>556</sup> Similarly, the chairman of the Committee on Energy and Commerce, Mr. Barton (R-TX), supported the resolution because of the lack of reciprocity in Chinese law which “does not allow a foreign company to have a controlling interest in a company in China.” He was also concerned that the money for the purchase was coming from a government loan which would more than double the debt.<sup>557</sup>

On the other hand, Mr. Moran (D-VA) stated he did not oppose CFIUS review of the contract. Although he said he “[could] not stand State-controlled economies,” he opposed Congress taking actions that would encourage the Chinese to invest in governments that are a threat to the U.S. He also expressed the opinion that Chinese acquisition of Unocal, which produced only one percent of U.S. oil and gas, would not constitute a threat to national security. Furthermore, he reminded Congress that the U.S. oil companies have drilling rights in China, off the coast, and “all over the world.” If Congress were to pass this resolution and others like it, it would interfere with free enterprise and the free global economy. He suggested that CNOOC’s American educated CEO understood the market system, CNOOC had a good track record, and unlike its competitor, ChevronTexaco, would preserve American jobs.<sup>558</sup>

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<sup>556</sup> Statements by Representative Kilpatrick on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5571.

<sup>557</sup> Statements by Representative Barton on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5571.

<sup>558</sup> Statements by Representative Moran on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5570.

Mr. Paul (R-TX) indicated reservations over legislation in which the federal government was “involving itself in the sale of a private American company” with shareholders and a board of directors. Rather than creating security problems, he argued that “international trade and economic activity tends to diminish tensions.”<sup>559</sup> Similarly, Mr. Pete Stark (D-CA) opposed the resolution, claiming that the Republican Majority which “has already sold the entire farm to foreign central banks and multinational corporations” was now trying to blame the Chinese for our dependence on foreign oil. He used his time to boast that he had “proudly voted for renewable energy” and legislation that supported American workers.<sup>560</sup> This was an important statement to interject since California voters were heavily dependent upon positive trade relationship with China, but were also suffering from increasing gasoline prices.

The Chairman of the Committee on Armed Services, Mr. Duncan Hunter (R-CA), supported the attempt to block the sale because it involved “a strategic asset and a strategic lever for Communist China.”<sup>561</sup> Mr. Michael Capuano (D-MA) stated that it was a good resolution, but pointed out that CNOOC’s bid for Unocal was not the “elephant in the room.” The real issue, he felt, was the exponential increase in the debt owed to China, and the jobs, money and economic power we were sending overseas. Mr. Robin Hayes (R-NC) emphasized the “strong signal” the legislation would send to China

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<sup>559</sup> Statements by Representative Paul on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5576.

<sup>560</sup> Statements by Representative Stark on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5576.

<sup>561</sup> Statements by Representative Hunter on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5572.

– that the U.S. would no longer stand for the loss of jobs, currency manipulation, and violation of intellectual property rights that were harming American business.<sup>562</sup> Mr. Earl Blumenauer (D-OR) also stressed the need to get our “fiscal house in order” and stop making loans to the Chinese. He voiced the fear held by others that the Chinese might start dumping our bonds and cause havoc with fiscal policy.<sup>563</sup>

Mr. J.D. Hayworth (R-AZ) called on his peers to put aside “campaign screed that would criticize the opposing party” and “find some common agreement, apart from the grandstanding and campaigning that is so easily enjoined.”<sup>564</sup> Yet, Ms. Marcy Kaptur (D-OH) could not resist the temptation to state that “America has lost her independence” and the economy is worse under the current president.<sup>565</sup> Mr. Bill Jefferson (D-LA) took this opportunity to praise the fact that he had “supported free trade” since he had been in Congress and was continuing to do so with this resolution. He stated that the more China seeks control over assets for themselves, the more difficult it will become for the U.S. to claim it is a free, market-based economy.<sup>566</sup>

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<sup>562</sup> Statements by Representative Capuano on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5572.

<sup>563</sup> Statements by Mr. Blumenauer on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5572.

<sup>564</sup> Statements by Mr. Hayworth on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5573.

<sup>565</sup> Statements by Mr. Kaptur on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5573.

<sup>566</sup> Statements by Mr. Jefferson on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5574.

Mr. Michael Oxley (R-OH) refocused the debate on the fact that CFIUS review was a slow process and that as chairman of the committee with jurisdiction over the Defense Production Act,<sup>567</sup> he felt it was critical that the administration act quickly. He then recited a number of statistics relating to China's increased oil consumption and emphasis on "owning the import oil at the production point" which threatens the free market.<sup>568</sup> This concluded the debate and the vote was taken. The measure passed by a vote of 398 to 15. The speed with which the resolution moved through the House and the strong majority vote was testimony to the skill of the sponsors as well as to the timeliness of the issue.

Less than two weeks later, the House Armed Services Committee held a hearing on the proposed CNOOC-Unocal merger. In his opening remarks on July 13th, Duncan Hunter (R-CA) addressed the issue of whether review of the CNOOC-Unocal merger was outside the scope of national security reviews normally conducted by Congress. He said it was within their jurisdiction because "energy is a strategic commodity" and the infrastructure, drilling rights, and exploration capabilities that Unocal uses to bring energy to the open market represent strategic assets. Even though Unocal was a small producer in the U.S., Hunter said that the fact that the company was a major provider of

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<sup>567</sup> The Committee on Financial Services has jurisdiction over the DPA.

<sup>568</sup> Statements by Mr. Oxley on June 30, 2005, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., *Cong. Rec.* 151, no. 90: H5576 (emphasis added).

natural gas in South East Asia and a primary investor in Central Asian oil pipelines contributed to its strategic importance.<sup>569</sup>

In addition, Hunter seemed offended by the Chinese Foreign Ministry's "*demand* that the U.S. Congress correct its mistaken ways of politicizing economic and trade issues and stop interfering in the normal commercial exchanges between enterprises of the two countries."<sup>570</sup> On the other hand, ranking minority member Ike Skelton (D-MO) noted that the hearing was taking the committee into uncharted territory and even though he was sure no one wanted to impair the nation's security, he cautioned committee members that the CNOOC acquisition was just a "theoretical possibility" not an inevitability since Unocal could accept ChevronTexaco's offer.<sup>571</sup>

Emphasizing that Congress is accountable to the American people, not the Chinese government, Hunter called upon the first witness, R. James Woolsey, former director of Central Intelligence, for his testimony. Woolsey stated that China is the most dominant dictatorship in the world and the strategic task of the Communist Party is "to

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<sup>569</sup> Representative Duncan Hunter speaking at the hearing before the Committee on Armed Services of the House of Representatives, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., in "National Implications of the Possible Merger of the Chinese National Offshore Oil Corporation with Unocal Corporation," (Washington D.C., U.S. Government Printing Office, 2007), 1

<sup>570</sup> Representative Duncan Hunter quoting statement issued by Chinese Foreign Ministry in hearing before the Committee on Armed Services of the House of Representatives, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., in "National Implications of the Possible Merger of the Chinese National Offshore Oil Corporation with Unocal Corporation," (Washington D.C., U.S. Government Printing Office, 2007), 2.

<sup>571</sup> Representative Ike Skelton speaking at the hearing before the Committee on Armed Services of the House of Representatives, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., in "National Implications of the Possible Merger of the Chinese National Offshore Oil Corporation with Unocal Corporation," (Washington D.C., U.S. Government Printing Office, 2007), 3.



secure a coordinated development of national defense and the economy to build modernized, regularized, revolutionary armed forces.”<sup>572</sup>

Mr. Frank Gaffney, Jr., President and CEO of the neoconservative Center for Security Policy, followed by stating that it would be “folly to abet” Communist China’s efforts to acquire more of the world’s finite resources. If demand for oil were to grow at the projected rate of 60 percent, then the U.S. and China are on a “collision course.” Although the Chinese said the proposal was a “purely commercial transaction,” Gaffney saw it as an “ominous” long-term, global strategy to dominate strategic energy resources.<sup>573</sup> To support his case, Gaffney suggested that CNOOC’s willingness to pay above market prices only makes sense from a strategic perspective. In advising Congress, Gaffney indicated that the strategic nature of Unocal’s business and the legislative intent of Exon-Florio to interpret the statute broadly made CFIUS review mandatory. However, Gaffney reiterated that review should not take place until the issue is ripe, which in this case would be after the August 10, 2005 shareholder decision.

Gaffney also reiterated the flaws in Exon-Florio, including lack of transparency in the process and Congress’s failure to give itself oversight power. Since Congress has exclusive power over commerce with foreign states under the Constitution, Gaffney

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<sup>572</sup> Testimony of R. James Woolsey paraphrasing the White Paper put forth by China’s Ministry of National Defense, in the House Armed Services Committee Hearing, on July 13, 2005, China Quarterly Transcripts.

<sup>573</sup> Testimony of Frank J. Gaffney, Jr. at the hearing before the Committee on Armed Services of the House of Representatives, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., in “ National Implications of the Possible Merger of the Chinese National Offshore Oil Corporation with Unocal Corporation,” (Washington D.C., U.S. Government Printing Office, 2007), 6.

recommended that Congress proceed to change the statute. On the other hand, Mr. Jerry Taylor, Director of Natural Resources Studies at the libertarian Cato Institute, argued that fears are “ill-founded” that the CNOOC transaction would harm national security by making the U.S. more dependent upon foreign oil or by giving China a weapon to use against the U.S.<sup>574</sup> As an economist, he suggested that supply disruptions would increase prices regardless of where they occur. Physical access to oil is irrelevant because oil is available in world spot and futures markets. There are very few long-term contracts, and even if there were, long-term contracts provide no guarantees that they may not be broken, or that assets may be nationalized. If physical access were important, Mr. Taylor suggested, other oil companies would have gotten into a bidding war against CNOOC. But Mr. Taylor identified several reasons why they did not. First, the oil that might be diverted to China would only displace what would have been imported otherwise. Second, Unocal’s production was only about 0.23% of global production and would have very little impact on the world market. Third, China and the U.S. have the same interest in low prices, and in fact, high prices would hurt China more than the U.S. because its economy cannot respond to price spikes as efficiently as the U.S. economy.<sup>575</sup>

When asked whether Mr. Taylor believed any of China’s acquisitions of foreign corporations were strategic, Mr. Taylor responded that they were economically strategic. He did not find it surprising that the Chinese government would want to diversify its

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<sup>574</sup> Testimony of Jerry Taylor at the hearing before the Committee on Armed Services of the House of Representatives, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., in “ National Implications of the Possible Merger of the Chinese National Offshore Oil Corporation with Unocal Corporation,” (Washington D.C., U.S. Government Printing Office, 2007), 16.

<sup>575</sup> *Ibid.*, 17-18.

investments away from U.S. debt and move towards investing in U.S. assets. In support of his belief that the Unocal acquisition would not be a threat, Mr. Taylor stated that the U.S. holds \$105 billion worth of China's assets while China only has \$8 billion of U.S. assets. Purely economic arguments led others to challenge Mr. Taylor's assumptions and expertise. Mr. Hunter argued that even though this one acquisition would only impact "a quarter of one percent of world production" additional acquisitions could approach 5 percent or 10 percent and that could cause a spike in price. Admitting that 5 percent would be significant, Mr. Taylor expressed the opinion that "It's hard to imagine [CNOOC] putting together that kind of portfolio." "Historically," he said, "reserves are primarily controlled by producer states regardless of contract, and they're not generally controlled by those with contractual rights to exploit and sell."<sup>576</sup>

Mr. Woolsey then commented that Mr. Taylor was an energy analyst with "blinders on" and not a defense analyst. This led Mr. Weldon to interject that the real concern in the CNOOC-Unocal debate was China's growing military capability. In fact, the Cox Commission on which he served several years earlier concluded by a 9-0 vote that U.S. security was being harmed severely by China's acquisition of American technology. Mr. Taylor agreed that "acquisition of military technology would be worrisome," but to his knowledge Unocal technology did not have any military application and nothing was proprietary – anything Unocal had in the oil sector was

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<sup>576</sup> Testimony of Jerry Taylor at the hearing before the Committee on Armed Services of the House of Representatives, 109<sup>th</sup> Cong., 1<sup>st</sup> sess., in "National Implications of the Possible Merger of the Chinese National Offshore Oil Corporation with Unocal Corporation," (Washington D.C., U.S. Government Printing Office, 2007), 18.

available through contractors and private vendors. If there were any military applications or proprietary technology, he said that a security review would provide restrictions.

The Armed Services Committee hearing turned into a heated debate regarding U.S.-China trade policy and whether America was making progress towards democracy, openness and transparency in China by assuming such a large trade deficit. Mr. Taylor continued to emphasize that only “marginal producers can affect world price” for oil and the only scenario he could conceive in which China would be a marginal producer would be if it physically occupies Middle East oil reserves or developed an unknown field. But Mr. Woolsey stressed that the U.S. may be on a “collision course” with China – depending upon China’s domestic situation, Chinese leaders may “look for a foreign enemy.” Mr. Gaffney agreed saying that Chinese leaders have been saying for years that “war with the U.S. is inevitable.” Senator D’Amato agreed with what come called an “alarmist view” and reiterated that little progress had been made between the U.S. and China on major issues such as currency, intellectual property rights, subsidization, and arms proliferation.

Mr. Taylor countered that military analysts have a history of overestimating capabilities of other countries, just as the CIA did with the Soviet Union. He stressed that “every country on the planet” has similar goals of “a robust economy,” and they will “use their military and their national self-interest” to achieve it. Attempting perhaps to lower the intensity of the debate, Representative Vic Snyder (D-AR) quoted Dr. Schlessinger who said “If you call someone an enemy often enough, they will become your enemy.” “And China is not our enemy today,” said Snyder.

Woolsey continued to take the stance that China's economic growth was dependent upon an aggressive military strategy. He quoted Zhu Feng, security expert at Beijing University, to make his point:

Many people argue that oil interests are the driving force behind the Iraq war. For China, it has been a reminder and a warning about how geopolitical changes can affect its energy issues. So China has decided to focus much more intently to address its security.

Walter Jones (D-NC) brought up a *Washington Times* article which quoted an unidentified energy advisor to the Chinese government as saying, "No matter if it's a rogue oil or a friend's oil, we don't care. . . . Anyone who helps China with energy is our friend."<sup>577</sup> Bringing the hearing back to the issue of the role of CFIUS in the proposed Unocal bid, Jones' stated his opinion that Congress had abdicated its constitutional authority too many times. He emphasized how the loss of 1.5 million jobs to China demonstrates that Congress and the administration need to "do what we can to influence this sale if it comes about."

Mr. D'Amato agreed. "The most important thing we can do is defend our own interests." He went on to say that "Congress has exclusive and complete power to regulate these transactions if it so chose, because it has the sole authority under the constitution to do so." In his opinion, "the behavior of CFIUS over the years needs complete review and I think that the power over foreign commerce needs to be re-exerted by this body." This statement sums up the issue underlying the Committee's four hour debate and points to the primary reason behind Congress's politicization of the Unocal

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<sup>577</sup> "Unocal Purchase is Part of China's Brand New Oil Plan," *Washington Times*, July 13, 2005.

bid. That is, members of Congress were concerned about the efficacy of the Exon-Florio Amendment and whether it was being implemented in a manner that would balance the opposing interests of maintaining an open trade policy while protecting the nation's security.

While the House was debating its concerns about CNOOC's bid for Unocal and the issues surrounding presidential interpretation of the Exon-Florio Amendment, the Senate was working on its own legislation. On July 15, 2005, Senator Byron Dorgan (D-ND) introduced Senate Bill 1412. Some of the highlights of the debate included concerns that CNOOC was a state-controlled corporation, the Chinese government provided CNOOC with deep subsidies which diminished competitiveness of American corporations, the Chinese government did not grant U.S. businesses reciprocal treatment regarding acquisitions of Chinese companies, the CFIUS review process was inadequate, and that, in spite of all these concerns, free trade with China should remain a priority.<sup>578</sup>

The rhetoric in Congress was intense, but perhaps the most decisive factor for the Chinese was when Congress passed the Energy Policy Act of 2005 towards the end of July. As enacted, section 1837 required a national security review of international energy requirements. Specifically relating to the CNOOC offer was a clause that the findings concerning China's growing energy needs were to be reported to both Congress and the President not more than 120 days after enactment of the Energy Policy Act. This provision prevented any instrumentality, including CFIUS, from concluding a national security review concerning an investment in energy assets of any U.S. owned corporation

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<sup>578</sup> *Cong. Rec.*, 109<sup>th</sup> Cong. 1<sup>st</sup> Sess., July 17, 2005: S8384.

by any entity owned or controlled by China until 21 days after the report was submitted and the President had certified receipt of the report.<sup>579</sup> This restriction was so prohibitive that CNOOC could not compete with ChevronTexaco, even with the offer of more money. With no other recourse, CNOOC withdrew its bid on August 2, 2005.

Afterwards, Senator Charles E. Schumer (D-NY) released the following statement.

There was nothing wrong with CNOOC taking over Unocal and for that reason I didn't oppose the merger. But the furor over China treating American companies and workers unfairly up and down the line is real. And while it led to an incorrect result in this case, it must be dealt with. For instance China likely wouldn't allow an American company to buy a similarly situated Chinese company. If China were open to American companies buying Chinese companies, I think CNOOC would have had a much easier time of it.<sup>580</sup>

Speaking from the House, Representative Pombo (R-CA) issued a statement that "CNOOC's withdrawal from this bidding process is good news for the free market, the American consumer and U.S. national security."<sup>581</sup> He stated that it was "pure irony that Congress expressed near-unanimous concern" over the CNOOC bid while many legislators continue to oppose efforts such as development in ANWR, to increase our domestic energy supplies. It was clear that Mr. Pombo used this opportunity to promote

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<sup>579</sup> *Energy Policy Act of 2005*, Public Law 109-58. See *Congressional Research Service Report*, "Unocal: Legal Implications of Acquisition Bids by Chevron Corporation and China National Offshore Oil Corporation," by Janice E. Rubin and Michael V. Seitzinger, (Washington, D.C.: Library of Congress, updated August 3, 2005): 4.

<sup>580</sup> Senator Schumer, "CNOOC Nixes Bid for Unocal," U.S. Federal News Service, Washington, D.C. (August 2, 2005).

<sup>581</sup> U.S. Federal News Service, *Representative Pombo Issues Statement on CNOOC Bid Withdrawal* (Washington, D.C: U.S. Government Printing Office, August 2, 2005).

his own political agenda, but it is unclear as to whether his personal interests were in the best interest of U.S.-China foreign policy.

#### **E. How Politicization of CNOOC Bid Helped Expedite Exon-Florio Reform**

Pursuant to law, the U.S.-China Economic and Security Review Commission released its Third Annual Report to Congress on November 9, 2005. The statute mandates that the Commission “monitor and investigate and report to Congress on the national security implications of the bilateral trade and economic relationship between the United States and the People’s Republic of China.”<sup>582</sup> In doing so, the Commission adhered to the central principle that “economic health and well-being are a fundamental national security matter” and that during the year, the CNOOC proposed acquisition of Unocal highlighted that linkage.<sup>583</sup> The report further states that “far too little, if any” progress was made in balancing economic and security issues during 2005.

On February 28, 2007, the House of Representatives passed H.R. 556

to ensure national security while promoting foreign investment and the creation and maintenance of jobs, to reform the process by which such investments are examined for any effect they may have on national security, to establish the Committee on Foreign Investment in the United States, and for other purposes.<sup>584</sup>

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<sup>582</sup> See Public Law 106-398, October 30, 2000, as amended by Division P of Public Law 108-7, February 20, 2003. The Commission was established in response to the debate in Congress over Permanent Normal Trade Relations (PNTR) for China and China’s admission to the WTO.

<sup>583</sup> U.S.-China Economic and Security Review Commission, *2005 Report to Congress* (Washington, D.C.: U.S. Government Printing Office, 2005); iv. Available at <http://www.uscc.gov>.

<sup>584</sup> H.R. 556, 110<sup>th</sup> Cong., 1<sup>st</sup> sess., *National Security Foreign Investment Reform and Strengthened Transparency Act of 2007*, Public Law 110-49.



The requirement to report on U.S-China trade relations was in place years before Congress passed the 2005 Energy Policy Act with the more explicit requirement concerning review of U.S. energy assets owned or controlled by China. For this reason, some might argue that the stipulation in the Energy Policy Act was unnecessary, that is, if it were not for the fact that Congress felt powerless to force the President to act expeditiously on the proposed CNOOC bid.

## V. CONCLUSION

“Foreign policy issues are most pronounced when there is a serious conflict between domestic and international interests.”<sup>585</sup> In the CNOOC case, heightened concern about America’s vulnerability and the concern for increased national security efforts conflicted with business interests in free trade and the potential impact of trade restrictions on the domestic economy. Legislators took advantage of this conflict in 2005 to politicize the CNOOC bid for Unocal and make long-sought changes in the president’s authority under the Exon-Florio Amendment. Congress’s political strength ruled the day, in spite of CNOOC’s extensive planning and reliance upon experienced American strategists.

Most analysts agree that American-educated CNOOC Chairman and Chief Executive Officer Fu Chengyu was the motivating force behind the bid for Unocal. Of China’s three oil companies, CNOOC was in the best position to take on Wall Street.

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<sup>585</sup> Barbara Farnham, “Impact of the Political Context on Foreign Policy Decision-Making,” *Political Psychology* 25, no. 3 (2004): 458.

The company was not too large, but had a number of exploration and production joint ventures with foreign oil companies, including Chevron, operating off the China coast. Half of its eight board members were non-executive directors and were foreigners. According to Fu, even though a state-owned parent owned the majority interest in the company, it was run “no differently than Western companies” whose motivations “are purely commercial.”<sup>586</sup>

But not all the CNOOC board members were one hundred percent behind the proposed acquisition. When the acquisition was first conceptualized, executive board members consisted of CEO Fu Chengyu, CFO Mark Qiu (an investment banker), CNOOC President Zhou Shouwei, and CNOOC Vice President Luo Han. Zhou started as an engineer in 1982 before being appointed to the board in 1999 and becoming president in 2002. Luo represented CNOOC in its offshore production joint venture with Chevron and Eni.

The board also included four independent nonexecutive directors in accordance with Hong Kong stock market regulations where CNOOC, Ltd. is listed. The independents were Kenneth Curtis, professor of economics and Asia vice chairman at Goldman Sachs; Erwin Schurtenberger, former ambassador to China who resigned in April and was replaced by Aloysius Tse, former partner at KPMG; Royal Dutch/Shell executive Evert Henkes; and Australian solicitor Chiu Hong Sung.

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<sup>586</sup> Kate Linebaugh, Matt Pottinger, Jason Singer, and Greg Hitt, “CNOOC’s Unocal Bid Sheds Light on Revised Strategy: After Failed IPO, Oil Firm Resolved to Play to Win,” *Asian Wall Street Journal*, June 27, 2005.

Mr. Fu selected Charles Li, a senior banker at J.P. Morgan who had worked at CNOOC in the 1970s and had assisted with tapping into Western capital markets, as a key player in planning the Unocal bid. After learning English as a young man, Mr. Li received a scholarship to attend the University of Alabama where he earned a Masters degree in journalism. Then after earning a law degree at Columbia University, he was hired by Brown & Wood which had a China practice. While working at Brown & Wood, Mr. Li did some work for Merrill Lynch & Co. and was later recruited to join Merrill as a banker. During this time he worked on a secondary offering of China Mobile, a landmark deal, which caught the attention of J.P Morgan. It was after moving to J.P. Morgan, that Mr. Li first thought about putting together CNOOC's bid for Unocal.<sup>587</sup>

With his experience, Mr. Li recognized that there are hurdles to cross in putting together mergers and acquisitions, and Washington is one hurdle that must be considered. CNOOC's team consisted of foreign advisors, including Akin Gump Strauss Hauer & Field, a Dallas law firm with ties to both political parties, which was selected to lead the effort in Washington. Late in 2004, Goldman Sachs joined the CNOOC team with Bill Wicker, the new head of Asian investment banking, leading the charge. The Brunswick Group, a media-strategy firm, was hired for its specialization in mergers and acquisitions. Public Strategies Inc. of Austin was selected to handle communications because of its close ties to the Bush Administration. The "point person" for Public Strategies, Mark Palmer, was an expert in crisis communications and emphasized the importance of

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<sup>587</sup> Kate Linebaugh, Matt Pottinger, Jason Singer, and Greg Hitt, "CNOOC's Unocal Bid Sheds Light on Revised Strategy: After Failed IPO, Oil Firm Resolved to Play to Win," *Asian Wall Street Journal*, June 27, 2005.

“getting people to see the business rational for this proposed merger.”<sup>588</sup> In addition to the communications advisors, CNOOC hired two law firms, Davis Polk & Wardwell and Herbert Smith of Hong Kong. The independent directors, who expressed concerns about the proposal, were advised by investment bank N.M. Rothschild & Sons, consulting firm CRA International, and law firm Skadden, Arps, Slate, Meagher & Flom.<sup>589</sup>

In spite of the heavy hitters and the ties to the Bush Administration, the CNOOC team was not able to overcome the political backlash in Congress. The timing might have been better if it had not been for ChevronTexaco’s announced bid. This action forced CNOOC to go public with a hostile bid during a politically volatile time. Just as the Senate Finance Committee was holding its hearings on U.S.-China economic relations, the Bush Administration was pushing Congress to pass the 2005 Energy Policy Act. U.S.-China trade relations and security policies were at the center of the legislative agenda and the CNOOC bid was being introduced as an example in debate after debate.

In this way, the timing of the CNOOC bid for Unocal played into the hands of key legislators, some of whom had been trying for years to muster support for strengthening the Exxon-Florio. After 41 members of Congress called for CFIUS review of the proposal, Fu Chengyu attempted to neutralize opposition to the bid by writing a letter to Congress stating:

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<sup>588</sup> Ibid.

<sup>589</sup> “CNOOC Jumps through U.S. Hoops,” *Energy Compass* (London), June 30, 2005.

We know this bid is historic for both companies and will be closely scrutinized by everyone involved. I want you to know we encourage that review and welcome opportunity to participate.<sup>590</sup>

But CNOOC's effort to go through the CFIUS process was not enough to overcome the anger and mistrust that had been brewing among various legislators and within different congressional committees. Not only did CNOOC have the disadvantage of taking the brunt of criticism for all of the perceived shortcomings in U.S.-China trade negotiations, it also suffered from misunderstanding and mistrust of a political and economic system based on different assumptions and values.

Even those legislators who were supportive of the achievements that China had made in opening up to the West, modernizing its society, and integrating into the global economy, found a common platform for opposing the CNOOC acquisition. They were united in their concern that the Exon-Florio Amendment was no longer effective in the post-9/11 world. By failing to define national security, granting the president broad discretionary powers to interpret the amendment, and being complacent about reporting responsibilities, Congress had abdicated its powers under the Commerce Clause. The combination of Congress's desire to take back power from the executive branch and strengthen its oversight authority, along with political pressure to mandate that China adopt democratic values and the rule of law, and fears that the Chinese government was scheming to overtake the U.S. as a world hegemony created a "perfect storm" resulting in the demise of CNOOC's first foray into the U.S. oil industry.

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<sup>590</sup> Jad Mouawad, "Unocal's Chinese Suitor Wants U.S. Review," *New York Times*, June 28, 2005.

## **CHAPTER 5**

### **IMPLICATIONS OF THE UNOCAL CASE FOR FUTURE POLICY MAKING**

In 2005, when Chinese-owned CNOOC proposed a hostile bid to acquire American-owned Unocal it sparked an unexpected clash of events analogous to a “perfect storm” in Washington. The expediency with which Congress reacted to CNOOC’s bid provided a unique opportunity for observing and analyzing how U.S. foreign policy is made and implemented. This study adopted the theoretical approach of new institutionalism as a means of understanding and explaining the roles that executive and legislative branches play in forming, implementing, and overseeing foreign policy initiatives.

New institutionalism emerged in response to the shortcomings of the realist approach which focuses on the interaction of nation-states and diminishes the significance of political values and collective choice in making foreign policy. In adopting the institutional approach, the analysis is redirected to the interaction between institutions and institutional actors. The study assumes that institutions are infused with values over time and the consistency provided by society’s acceptance of these values creates both a sense of security for the populace as well as an obstacle for policy makers who are confronted with the need to adapt to changing global environments. The theory’s explanatory power is particularly applicable in a new millennium characterized by China’s explosive growth and increased influence over the global economy,

America's phobia about China's potential for global dominance, and an unprecedented sense of vulnerability to terrorist attacks.

Although there have been efforts within the institutional school to bifurcate the theory, this study focused on an integrated approach by adopting core elements of the historical, rational choice, and sociological approaches to new institutionalism. The basic premises were as follows:

(1) An institution's history is important because it creates values which become imbedded in the system.

(2) Actors attempt to make rational decisions but the maximization of utility is often compromised by the democratic decision making process.

(3) Due to formal constraints, political actors will try to identify informal mechanisms for accomplishing their policy goals.

(4) The success of a policy initiative in the U.S. Congress is dependent upon a variety of factors, including public awareness, constituent support, party support, presidential support, and timing.

In the American system of governance, the Constitution is fundamental. It grants separate powers to Congress, the president, and the judiciary. It also incorporates a system of "checks and balances" to keep any one of the three institutions from becoming too powerful. As a result, policy making is often fragmented, inefficient, and difficult to predict. This was the case in 2005 when Congress was struggling with drafting legislation that would balance conflicting objectives in the areas of open trade,

comparative advantage in a global economy, intellectual property rights protection, natural resource development, and national security.

Achieving balance in the American political system is complicated by the separation of powers among the institutionalizations of the president, the legislature, and the judiciary. Over the years, both the presidency and Congress have gained autonomy and have become more complex while preserving coherence and the ability to adapt to change — elements that have strengthened the institutions without diminishing the possibility that at any point in time one institution may dominate policy making. The struggle between the institutions of the presidency and Congress is an on-going process. At the same time, exogenous factors may arise that create windows of opportunity for one of the institutions to assert its authority over the other. But the system constantly seeks balance. Therefore, whenever the power is weighted towards one institution, actors in the less dominant institution will look for a window of opportunity to rebalance the system. Since windows of opportunity are temporary moments in time, political actors must be prepared to act when the conditions are ripe.

After 9/11, the president was in a position of strength for implementing foreign policy initiatives. The shock of the terrorist attacks combined with President Bush's strong rhetoric and decisive actions elevated his popularity to unprecedented levels in American politics. This gave him a clear advantage in pushing his political agenda through Congress, especially when the policies were concerned national security. President Bush's managerial style also served to place the White House and his cabinet in a position to gain strong control over foreign policy decision making. Strong control



over communications networks and relationships with the media also contributed to the President Bush's political success.

However, by 2005, when the CNOOC bid leaked to the press, the president's ratings were beginning to fall and support for him in Congress was no longer unconditional. Political capital earned after 9/11 had been spent and Americans were questioning policies that did not accomplish their stated goals, such as the failure to find the weapons of mass destruction which had provided the rationale for the war in Iraq and failure of the Office of Homeland Security to provide first responder relief to victims of Hurricane Katrina. It was amid events such as these that key legislators in Congress found an opportunity in the CNOOC bid for demonstrating how presidents had misinterpreted the 1988 Exon-Florio Amendment and the 1992 Byrd Amendment and thereby failed to comply with the statutory intent of protecting Americans, their resources, their economy, and their national security.

Senators Shelby (R) and Sarbanes (D) had suspected these shortcomings when they asked for a GAO study of the president's implementation of Exon-Florio a year earlier in 2004. This type of request would not have been unusual coming from the opposite party as the president's. However, in this case, it was a bipartisan request symbolizing an informal mechanism, permitted rather than required by the law, which could serve to undermine the president's performance and give Congress a political advantage in shaping foreign investment decisions.

It is significant to this analysis that key Republicans joined with Democrats to introduce legislation that would force the president's hand in blocking the CNOOC

transaction. House Resolution 344 was purely a political move. It was a non-binding resolution on the part of one chamber in Congress to take a foreign policy stand, to make a statement to the administration about how the United States should handle foreign acquisitions of American corporations. The sponsors of the bill played on the public's heightened awareness of the nation's vulnerabilities in an effort to intimidate the Chinese to drop their proposal and consider making other foreign policy concessions. Support for the resolution was overwhelming and it did make an impression on the Chinese government – at least to the extent that Beijing expressed indignation over political intervention in the business transaction even though Chinese leaders were loath to admit that inexperience in capitalist markets may have contributed to the failed hostile takeover.

Although H.R. 344 received the most attention in the media, various other bills debated in the 109<sup>th</sup> Congress focused on China. In analyzing the debates, it was obvious that individual members in Congress had varying concerns about China's foreign policies, ranging from human rights to currency pegs and from intellectual property rights to a military build-up. It also became obvious that the CNOOC acquisition was being used as an example of the weaknesses in the Exon-Florio process, the need to reform the statute, and the need for Congress to rein in the discretionary powers granted to the president. Some of the changes members were suggesting were to specify timelines for presidential action, to increasing agency reporting requirements, and to improve opportunities for overall congressional oversight of CFIUS implementation of the president's statutory authority.

Another reason for members to support legislation blocking the CNOOC deal was revealed through analysis of the hearings and testimony. This was the desire to support American businesses and American jobs and to discourage economic competition with China. Even if CNOOC's acquisition of Unocal was based on purely economic, rather than political motives, the outcome was to the benefit of American-owned ChevronTexaco. In its 2005 Annual Report, ChevronTexaco announced that the company had achieved annual earnings of \$14.1 billion, the highest in its history. This achievement was partially due to successful integration of Unocal's exploration and production operations which enhanced the company's portfolio of assets in areas of strategic importance.

In the previous two years, ChevronTexaco's portfolio had declined at a higher rate. The company claimed this had been due to damage to facilities and infrastructure by hurricanes and tropical storms and to the sale of nonstrategic properties. This downward trend was offset by acquiring Unocal and properties that complimented and enhanced ChevronTexaco's position in the Gulf of Mexico and Permian Basin. During the first five months after the acquisition, ChevronTexaco reported the net daily production from former Unocal properties, averaged 53,000 barrels of crude oil and natural gas liquids and 360 million cubic feet natural gas, or 113,000 barrels on an oil equivalent basis.<sup>591</sup>

ChevronTexaco claims its U.S. portfolio was "anchored by mature assets" in the United States and Gulf of Mexico and was improved by disposing of nonstrategic assets

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<sup>591</sup> Chevron Corporation, *2005 Supplement to the Annual Report*, 14. Available at [www.chevron.com/documents.pdf](http://www.chevron.com/documents.pdf) (accessed September 23, 2009).

such as Unocal's offshore assets in Canada. Already the largest holder of natural gas resources in Australia, ChevronTexaco gained additional exploration blocks through the Unocal acquisition. There were other benefits of the acquisition. For instance, ChevronTexaco held 10.3% working interest in Azerbaijan International Operating Company (AIOC) and acquired 8.9% equity interest in the pipeline which transports AIOC production from Baku Azerbaijan through Georgia to deep water port facilities in Ceyhan, Turkey. ChevronTexaco also acquired interest in 3 production sharing contracts in Bangladesh encompassing more than 3.5 million acres and by early 2006 ChevronTexaco supplied 20% of Bangladesh's natural gas market.<sup>592</sup>

These downstream acquisitions complimented ChevronTexaco's strategies for upstream businesses, that is, to "grow profitability in core areas, build new legacy positions, and commercialize natural resource base by targeting North American and Asian Markets."<sup>593</sup> Unocal's upstream portfolio of assets bolstered ChevronTexaco's position in the Asian-Pacific, Gulf of Mexico and Caspian regions.

From the perspective of ChevronTexaco, the politicization of CNOOC's proposed acquisition in 2005 certainly benefited the American corporation's business interests. Yet, the efforts of so many members of the 109<sup>th</sup> Congress to politicize the Unocal case so as to facilitate reform of the 1988 Exon-Florio Amendment stalled after CNOOC withdrew its bid in August of 2005. Nonetheless, the actions of key legislators were not in vain as the stage was set for the proponents of reform to continue their mission during

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<sup>592</sup> Chevron Corporation, *2005 Supplement to the Annual Report*, 23-26. Available at [www.chevron.com/documents.pdf](http://www.chevron.com/documents.pdf) (accessed September 23, 2009).

<sup>593</sup> *Ibid.*, 10.

the second session in 2006. Advocates for Exon-Florio reform had stirred up the necessary momentum for mandating institutional change by shifting foreign policy decision making powers back toward the legislative arena while giving Congress greater oversight over foreign acquisitions of American corporations.

The coup de grâce for overcoming institutional resistance to change in the balance of power between the presidency and Congress came when Congress learned through the media, rather than the president, that United Arab Emirates-owned Dubai Ports World was in the process of purchasing Peninsular and Oriental Steam Navigation Company (P&O). The London-based P&O was the world's fourth largest port operator with operations in over twenty U.S. ports from Maine to Texas. The port operator was responsible for securing cargo coming in and out of ports, the port facilities themselves, and the hiring of security personnel. The proposed transaction would transfer control of substantial terminal functions at America's major East and Gulf Coast ports to Dubai Ports World.

In consideration of the port operator's critical functions, on Monday, February 13, 2006, Senators Chuck Schumer (D-NY), Tom Coburn (R-OK), Frank Lautenberg (D-NJ), and Chris Dodd (D-CT) joined Representatives Chris Shays (R-CT), Vito Fosselia (R-NY), and Mark Foley (R-FL) in sending a bipartisan letter to Treasury Secretary John Snow urging immediate CFIUS review and scrutiny of security issues as required by law. The letter cited the requirement that "the President or his designee investigate the impact on national security of a foreign acquisition if the acquisition 'could result in control of a person engaged in interstate commerce in the United States that could affect the national

security of the United States.” It emphasized that the “country’s maritime ports are critical to our national security, vital to our military capability, and essential to our economy. Some ninety-five percent of all goods imported to the U.S. arrive through our ports.” Furthermore, the letter noted that Dubai “has been named as a key transfer point for shipments of nuclear components that were shipped to Iran, North Korea, and Libya . . . and the UAE was one of only 3 countries (including Pakistan and Saudi Arabia) that recognized the Taliban as the legitimate government of Afghanistan.” On February 27, 2006, Senator Schumer introduced legislation, with five Democrats and five Republicans as sponsors, to deal with the Dubai Ports issue. Stating that “homeland security is a number one priority,” Mr. Schumer raised the following questions: (1) whether CFIUS is the right committee to conduct reviews since it was set up more than 20 years ago to justify economic deals, (2) whether a report would serve a purpose if it is kept secret and only provided to the President, and (3) whether Congress could be able to find a constitutional way to disapprove the deal.<sup>594</sup> Ms. Collins followed by introducing a joint resolution disapproving the conclusion of the CFIUS regarding the Dubai Ports acquisition.<sup>595</sup>

The next day, Ms. Harmon (D-CA), member of the House Intelligence Committee and Homeland Security Committee introduced S.J. Res. 32 in the House and called for the CFIUS to rescind the decision, conduct a formal 45-day investigation, and brief

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<sup>594</sup> Mr. Schumer speaking before the U.S. Senate on February 27, 2006, 109<sup>th</sup> Congress, 2<sup>nd</sup> sess., *Cong. Rec.* 152, no. 22: S1504.

<sup>595</sup> Ms. Collins speaking for S.J. Res. 32, on February 27, 2006, before the U.S. Senate, 109<sup>th</sup> Congress, 2<sup>nd</sup> sess., *Cong. Rec.* 152, no. 22: S1504.

Congress before allowing the deal to proceed.<sup>596</sup> On March 1<sup>st</sup>, Representative Corrine Brown (D-FL) was one of many representatives to testify. She stated that she had been lobbying the President for additional funds for the nation's port and infrastructure, especially in Florida. "This is absolutely the wrong time for our government to make a decision that could give the impression of vulnerability," stated Brown.<sup>597</sup> Mr. Feeney (R-FL) also from Florida had stated the previous day that homeland security is the number one issue facing the nation and that the administration has a strong record, but "Americans throughout my district expressed deep concern that this fast track deal has not been given the type of scrutiny that all of us took an oath to do when we said we would protect our country."<sup>598</sup>

In March 2006, the Senate Banking, Housing, and Urban Affairs Committee held a hearing on the Exon-Florio Amendment with a focus on Dubai Ports World's proposed acquisition of P&O.<sup>599</sup> Chairman Richard Shelby opened the hearing by remarking that the "credibility and integrity" of the CFIUS process is vital to American national

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<sup>596</sup> Ms. Harmon speaking for S.J. 32 in the House, on February 28, 2006, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess. *Cong. Rec.* 152, no. 23: E214.

<sup>597</sup> Representative Brown speaking before the House, on March 1, 2006, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., *Cong. Rec.* 152, no. 24: H476.

<sup>598</sup> Representative Feeney speaking before the House, on February 28, 2006, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess. *Cong. Rec.* 152, no. 23: H392.

<sup>599</sup> In addition to members of the committee, witnesses included Robert M. Kimmitt, Deputy Secretary of Treasury; Eric Edelman, Under Secretary for Policy, Department of Defense; Stewart Baker, Assistant Secretary for Policy, Department of Homeland Security; and Robert Joseph, Under Secretary for Nonproliferation, Department of State.

security.<sup>600</sup> In his opinion, the Dubai Ports World case once again raised the concerns that Congress expressed over the 2005 CNOOC case. Mr. Shelby reiterated that there were serious gaps in the CFIUS review process that prevented full assessment of acquisitions, that the process lacked transparency and avoided congressional oversight.

Senator Sarbanes said he had long been concerned about how foreign purchases of U.S. assets are evaluated which is why he and Senator Bayh had requested a GAO report to address these concerns. What amazed Mr. Sarbanes was that the GAO report had been delivered in September 2005 and the Banking, Housing, and Urban Affairs Committee had held two hearings to discuss weaknesses in the CFIUS process before the Dubai controversy arose; and yet, CFIUS did not appear to have heeded any of the advice in the report when allowing the Dubai Ports World transaction to move forward.

Every other member of the committee that spoke during the hearing expressed similar concerns. Senator Allard (R-CO) opposed the transaction for security reasons but, he said, the “much broader concern [is] how we even got to this point and the answer lies in a flawed CFIUS process.”<sup>601</sup> Senator Debbie Stabenow (D-MI) was emphatic that the issue of homeland security “should not be negotiated, sidestepped, or ignored in any of the processes that have been developed.” She was appalled that the importance of port security was “ignored” and said that it would not have mattered what foreign company

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<sup>600</sup> Senator Richard Shelby speaking before the Senate Committee on Banking, Housing and Urban Affairs, U.S. Senate, on March 2, 2006, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., published in “Examination of the Exon-Florio Amendment: Focus on Dubai Ports World’s Acquisition of P&O,” Washington, D.C.: Government Printing Office (2007): 1-2.

<sup>601</sup> Senator Allard speaking before the Senate Committee on Banking, Housing and Urban Affairs, U.S. Senate, on March 2, 2006, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., published in “Examination of the Exon-Florio Amendment: Focus on Dubai Ports World’s Acquisition of P&O,” Washington, D.C.: Government Printing Office (2007): 6.



was involved. “I believe American companies accountable to the American people should manage the operations of these vital national security interests,” Stabenow added.<sup>602</sup>

The realization that the Dubai Ports World transaction had been in the works just as Washington was settling down from the passionate debates over the CNOOC-Unocal transaction and while Congress was deliberating over the GAO report was shocking to these Committee members as well as others in Congress. It was all that the proponents of reform needed to convince their peers that the CFIUS process was broken and needed to be fixed.

During the second session of the 109<sup>th</sup> Congress, members introduced over two dozen measures to address the various concerns that arose from the CNOOC and Dubai Ports World acquisition bids. Some of the deficiencies addressed in these bills included:

- (1) CFIUS uses too much discretion in determining which transactions to investigate;
- (2) CFIUS members incorrectly interpreted statutory requirements for investigations of transactions involving firms owned or controlled by foreign governments;
- (3) Commonly accepted definitions of national security were no longer applicable in a post-9/11 world;

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<sup>602</sup> Senator Debbie Stabenow speaking before the Senate Committee on Banking, Housing and Urban Affairs, U.S. Senate, on March 2, 2006, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., 2006), published in “Examination of the Exon-Florio Amendment: Focus on Dubai Ports World’s Acquisition of P&O,” Washington, D.C.: Government Printing Office (2007): 8-9.

(4) Time constraints on CFIUS to complete reviews did not provide adequate time for conducting thorough reviews and completing the necessary tasks;

(5) Members of the CFIUS did not appear to be well-informed of the outcomes of reviews and investigations regarding pending transactions; and

(6) Reporting requirements did not provide Congress enough time to fulfill its oversight responsibilities.<sup>603</sup>

The most prominent bills introduced in the second session of the 109<sup>th</sup> Congress were H.R. 5337 and S. 3549. The stated purpose of H.R. 5337 was to ensure national security while promoting foreign investment, creation of and maintenance of jobs, and to establish the Committee on Foreign Investment in the United States.<sup>604</sup> The stated purpose of S.B. 3549 was “to strengthen government review and oversight of foreign investment in the United States, to provide for enhanced Congressional oversight with respect thereto. . . .”<sup>605</sup>

Both bills called for statutory establishment of the CFIUS. While H.R. 5337 would have retained the basic committee structure, S.B. 3549 would have added the Director of National Intelligence and eliminated the members from the White House staff. Both bills sought to clarify significant definitions. For

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<sup>603</sup> “Exon-Florio After 9-11,” *CRS Report to Congress*, Washington D.C.: U.S. Government Printing Office, January 23, 2007.

<sup>604</sup> *National Security Foreign Investment Reform and Strengthening Transparency Act of 2006*, H.R. 5337, Union Calendar No. 329, Report No. 109-523, I and II, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess., May 10, 2006.

<sup>605</sup> S.B. 3549, introduced by Senator Shelby, on June 21, 2006, in the 109<sup>th</sup> Cong., 2<sup>nd</sup> sess. *Cong. Rec.*, S8317-S8321.

example, the House bill defined “covered transactions” as any transaction which could result in the control by any person engaged in interstate commerce in the U.S. by a foreign government or entity acting by or on behalf of a foreign government.” National security was to include issues relating to homeland security, including “critical infrastructure.”<sup>606</sup>

Although the bills gave CFIUS more authority to negotiate, they both also sought more congressional oversight of the committee. While the House bill required semi-annual reports, the Senate bill only required an annual report, but specified the content of the report in great detail. In addition to tightening up reporting requirements, the bills provided for greater intelligence review. The Senate bill provided that governors of relevant states shall be notified in the review process, while the House bill required that the departments of Treasury and Homeland Security must agree on all decisions. The Senate bill also added factors for the president to consider, such as “long term projections of U.S. requirements for sources of energy and other critical resources and materials” and the “effect on U.S. technology leadership in areas affecting national security.”<sup>607</sup>

Both House and Senate bills garnered support on July 26, 2006, and even though

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<sup>606</sup> H.B. 5337, *Reform of National Security Reviews of Foreign Direct Investments Act*, introduced by Representative Blunt, on May 10, 2006, 109<sup>th</sup> Cong., 2<sup>nd</sup> sess. Hearings were held on March 1, 2006, April 27, 2006, and May 17, 2006 by the Subcommittee on Domestic and International Monetary Policy, Trade and Technology of the House Financial Services Committee; approved unanimously with an amendment by the House Financial Services Committee on June 14, 2006; passed the House as amended, July 26, 2006. See *Cong. Rec.*, July 26, 2006: H5863-H5873.

<sup>607</sup> S.B. 3549, introduced by Senator Shelby, on June 21, 2006, in the 109<sup>th</sup> Congress, 2<sup>nd</sup> sess.

there were details to work out in conference, the 109<sup>th</sup> Congress adjourned before the Conference Committee had time to convene.<sup>608</sup>

The issue was picked up again in the 110<sup>th</sup> Congress where Exon-Florio was finally revised.<sup>609</sup> As modified, the statute preserved the basic elements of the 1988 Exon-Florio Amendment, such as voluntary reporting and confidentiality, but made significant changes regarding implementation and congressional oversight. The most notable changes accomplished by the 2007 amendment are as follows:

(1) The statute provided more structure and clarity to the process by requiring Treasury to designate a lead agency for conducting the investigation, and by giving CFIUS explicit authority to negotiate and enter into mitigation agreements with the acquiring company based on risk analysis.

(2) The scope of Exon-Florio review was expanded to include transactions involving “critical infrastructure,” which was defined as any vital system or asset, physical or virtual, whose destruction or incapacity would have a “debilitating impact” on national security.

(3) CFIUS was mandated to consider a country’s relationship with the United States and record in supporting nonproliferation of arms and counterterrorism. This

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<sup>608</sup> U.S. Congressional Research Service, *Exon-Florio Foreign Investment Provision: Comparison of H.R. 5337 and S. 3549*, January 24, 2007, by James K. Jackson, (Washington, D.C., 2007), summary.

<sup>609</sup> The *Foreign Investment and National Security Act of 2007* (FINSIA) was enacted on October 24, 2007 to amend Section 721 of the Defense Production Act.

included consideration of whether the country in question sells military goods to countries which the Department of Defense has identified as a regional military threat.

(4) The previous focus on national defense was expanded to include factors which impact the nation's ability to protect homeland security. This includes consideration of long-term energy supplies and the potential diversion of technology by the acquiring company to military applications.

(5) The statute closed the loophole in the Byrd Amendment by requiring CFIUS perform an investigation within 45 days unless the Department of Treasury and the head of the lead agency on the transaction jointly determine that the transaction would not have an impact on national security.

(6) CFIUS was given the authority to reopen review of previously approved transactions based upon intentional or material breach of a mitigation agreement.

(7) The secrecy issue was addressed by requiring that officials give Congress prompt notice of approved transactions with an explanation of the rationale behind the committee's actions. Congress was authorized to request classified briefings from CFIUS.

Even after politicizing two major foreign investment cases – CNOOC's proposed acquisition of U.S.-based Unocal and the proposed acquisition of London-based P&O by Dubai Ports World – it took two congressional sessions to revise the 1988 Exon-Florio Amendment. It may seem that the passage of time and failure of the 109<sup>th</sup> Congress to finalize the bill diminishes the impact of the two events. But time is relative, and the accomplishment of the 110<sup>th</sup> Congress was significant when one considers that members

had been trying to modify the 1988 Exon-Florio Amendment ever since the 102<sup>nd</sup> Congress had realized the shortcomings of the 1992 Byrd Amendment.

Ushering legislation through Congress is difficult at best, and the process is complicated by the constraints of formal rules and values, the political dynamics between the president and Congress, the intervention of political parties and special interest groups, and expectations of constituents. The more complex the system and the players, the more difficult it is to develop effective policies. This is the dilemma that government institutions face.

This study shows how the Constitution provided the foundation for conflict between the executive and legislative branches by institutionalizing the system of “checks and balances.” The founding fathers accomplished their goal of preventing any one branch from becoming too powerful, but they did not foresee the complexity of drafting and implementing policy in twenty-first century America. The institutions have become more complex and have developed a life of their own. Today, it takes an experienced politician to maneuver his or her way through formal rules and traditional resistance to change to accomplish a policy goal. Long-time members of Congress have a political edge over an incoming president, especially one that has not had extensive experience in Washington, as it is not as easy to move a ship of hundreds of individually-minded legislators. Every member comes to Washington with their own values and personal commitments to their party and their constituents.

President Bush’s managerial style created an additional challenge for reformists. While we might expect a unified Congress to be able to overcome the influence of a weak

president over the policy making agenda, it was a different matter under the strong Bush Administration. However, members of the 109<sup>th</sup> Congress were able to overcome the obstacles of a tightly controlled cabinet and administrative staff, and a constituency that was loyal to the president and his party, to unify Congress against the CNOOC's acquisition of Unocal in spite of executive preference for nonintervention.

Fortunately for the proponents of legislative reform, the timing of the CNOOC proposal helped elevate concerns about implementation of the Exon-Florio Amendment to the top of the policy agenda in 2005. What had seemed like a perfect storm to the CNOOC directors was a fortuitous set of events for members of Congress yearning to reform the 1988 Exon-Florio Amendment, impose more restrictive requirements for the president and CFIUS in reviewing foreign acquisitions, and mandate more stringent reporting requirements so that Congress could exercise its oversight authority.

Although Americans had long supported free and open trade policies, the events of 9/11 had created a sense of vulnerability and urgency for developing and implementing national security policies. At the same time, members who had been struggling with China's trade policies, and perceived violations of the rule of law, found a venue for voicing their concerns, and hoped to make headway with new trade legislation.

The research shows how the Speaker of the House controls the legislative agenda with the suspension of rules; how bills may or may not get to the floor through the gate keeping Rules Committee; and how committee chairs play a critical role in manipulating the content and tone of testimony in hearings. Getting legislation through all these

obstacles requires more than an understanding of the formal process; it requires the ability to finesse informal mechanisms that will create coalitions of power and support.

Members of the 109<sup>th</sup> Congress formed bipartisan coalitions to support legislative reform so as to rebalance the power between the legislative and executive branches. The tendency for members to support a president from their own party was clearly diminished by the perception that the president was sidestepping his authority to promote free trade at the expense of protecting national security, energy resources, and critical technology. The real victory came in the 110<sup>th</sup> Congress when Republicans joined Democrats to oppose the Republican president's preference for avoiding additional legislative constraints. Congressional members coalesced to provide the statutory basis under the 2007 modifications to the 1988 Exon-Florio Amendment for greater legislative oversight of CFIUS review of foreign direct investments.

The difficulty of getting bills through each house of Congress and then reaching consensus between the two houses cannot be overstated. The process is complicated by the large number of participants and the preferences of their constituents, the multiplicity of formal procedures and informal relationships within Congress, and interactions with and loyalty to the administration. How members vote is often clouded by their personal values, the information they receive, and trade-offs that must be made with regard to other policy issues.

The ability of Congress to develop effective policies is diminished because compromise is necessary to create winning coalitions. An open, democratic process may increase responsiveness to the public and interest groups but it diminishes the potential



for passing responsible legislation. Members often have short-term constituency preferences and re-election takes precedence over long-term policy interests. Debates have become platforms for gaining political support and often lack substantive solutions. Therefore, in analyzing hearings and debates it is important to go beyond political motives and innuendos to identify real policy concerns. In this study, that meant looking beyond posturing vis-à-vis foreign trade with a “communist regime” in order to identify common issues of concern. Here, the common thread was not just that China bases its development on principles that are different from the capitalist West, but that the U.S. executive office had failed repeatedly to implement safeguards against acquisitions of U.S. corporations by a foreign government-owned corporations, such as CNOOC, which may pose a threat to national security and the economic well being of American enterprise.

In a post-9/11 world, business may no longer be “as usual” but will require additional protection against the unforeseen perils which are bound to arise in a global economy. This study shows how an overwhelming majority of legislators were able to agree that the American predilection towards an open trade policy, which has contributed so much to economic growth and prosperity, must be tempered with an element of caution. In this case, this element of caution was accomplished by reforming the 1988 Exon-Florio Amendment to require that the president be more accountable to Congress and the public for how he implements the policy governing foreign acquisitions of American corporations.

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**TABLE 4: AGENCIES REPRESENTED ON THE COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES<sup>610</sup>**

<b>Agencies Represented</b>	<b>Year Added</b>	<b>Lead Office Mission</b>
<b>Department of the Treasury</b>	1975	Office of International Investment: Coordinates policies toward foreign investments in the U.S. and U.S. investments abroad
<b>Department of Commerce</b>	1975	International Trade Administration: Coordinates Issues concerning trade promotion, international commercial policy, market access, and trade law enforcement
<b>Department of Defense</b>	1975	Defense Technology Security Administration: Administers the development and implementation of Defense technology security policies on international transfers of defense-related goods, services, and technologies
<b>Department of State</b>	1975	Bureau of Economic and Business Affairs: Formulates and implements policy regarding foreign economic matters, including trade and international finance and development
<b>Office of U.S Trade Representative</b>	1980	Directs all trade negotiations of and formulates trade policy for the United States
<b>Council of Economic Advisors</b>	1980	Performs analyses and appraisals of the national economy for the purpose of providing policy recommendations to the President
<b>Department of Justice</b>	1988	Criminal Division: Develops, enforces, and supervises the application of all federal criminal laws, except for those assigned to other Justice Department divisions
<b>Office of Management and Budget</b>	1988	Evaluates, formulates, and coordinates management procedures and program objectives within and among federal departments and agencies, and controls administration of the federal budget
<b>Office of Science and Technology Policy</b>	1993	Provides scientific, engineering, technological analyses for the President with respect to federal policies, plans, and programs
<b>National Economic Council</b>	1993	Coordinates the economic policymaking process and provides economic policy advice to the President
<b>National Security Council</b>	1993	Advises and assists the President in integrating all aspects of national security policy as it affects the United States
<b>Department of Homeland Security</b>	2003	Information Analysis and Infrastructure Protection: Identifies and assesses current and future threats to the homeland, maps those threats against vulnerabilities, issues warnings, and takes preventative and protective action

<sup>610</sup> U.S. Government Accountability Office, Report to Congressional Requesters (GAO-05-686), “Defense Trade: Enhancements to the Implementation of Exon-Florio Could Strengthen the Law’s Effectiveness, (September 2005); 6.

**TABLE 5: LIST OF ABBREVIATIONS**

AIOC	Azerbaijan International Operation Company
ANWR	Arctic National Wildlife Refuge
APA	Administrative Procedure Act
ASEAN	Association of South East Asian Nations
ASML	ASM Lithography
BBL/D	Billion barrels per day
BEA	Bureau of Economic Analysis
BOB	Bureau of Budget
BTU	British Thermal Units
CATIC	China National Aero-Technology Import and Export Corporation
CEO	Chief Executive Officer
CFIUS	Committee on Foreign Investment in the United States
CIA	Central Intelligence Agency
CNOOC	Chinese National Offshore Oil Corporation
CNPC	Chinese National Petroleum Corporation
DOE/EIA	Department of Energy/Energy Information Administration
DOJ	Department of Justice
DPA	Defense Production Act
EOP	Executive Office of the President
FBI	Federal Bureau of Investigation
FDI	Foreign direct investment

FDR	Franklin D. Roosevelt
FTC	Foreign Trade Commission
GAO	Government Accountability Office
GDP	Gross Domestic Product
GOP	Republican (“Grand Old”) Party
G-7	Group of Seven
HSAC	Homeland Security Advisory Council
IDA	International Development Association
IEA	International Energy Administration
IEEPA	International Emergency Economic Powers Act
IIE	Institute for International Economics
IMF	International Monetary Fund
INS	Immigration and Naturalization Service
LNG	Liquid Natural Gas
LRA	Legislative Reorganization Act
MFN	Most Favored Nation
NEPDG	National Energy Policy Development Group
NGO	Nongovernmental Organization
NDRC	National Development and Reform Commission
NSA	National Security Advisor
NSC	National Security Council
OECD	Organization for Economic Cooperation and Development



OHS	Office of Homeland Security
OMB	Office of Management and Budget
OSI	Office for Strategic Initiatives
PNA	Premerger Notification Act
SEZ	Special Economic Zone
SETC	State Economic and Trade Commission
SINOPEC	China National Petrochemical Corporation
SVG	Silicon Valley Group, Inc.
UN	United Nations
WB	World Bank
WHO	White House Office
WTO	World Trade Organization
WWI	World War One
WWII	World War Two