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Foreign Direct Investment in the U.S.: An Analysis of Its Potential Costs and Benefits and a Review of Legislative Tools Available to Shape Its Future Course

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Foreign Direct Investment in the U.S.: An Analysis of Its Potential Costs and Benefits and a Review of Legislative Tools Available to Shape Its Future Course

Terry R. Spencer*
Christian B. Green**

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I. INTRODUCTION

Recovery from the overwhelming infrastructure destruction caused by World War II led to an almost unparalleled explosion of economic growth¹ throughout Europe and the United States. The massive growth in world economic activity was due in part to the United States' laissez-faire policy² toward foreign direct investment (FDI)³ as well as increasing world economic integration.⁴

The dramatic increases in FDI within the United States continued throughout the early 1970s, facilitated in part by the elimination of investment restrictions.⁵ An often cited

1. "Economic growth" is defined as a long term rise in the capacity to supply increasingly diverse economic goods to the country's population. Measurable components of economic growth include: (1) growth in per capita output and population; (2) increasing input factor productivity, especially labor productivity; (3) structural transformation in the economy away from agriculture and toward increased manufacturing and services; and (4) ideological support for increased "modernization." See MICHAEL P. TODARO, *ECONOMIC DEVELOPMENT IN THE THIRD WORLD 93-95* (2d ed. 1981).

2. OFFICE OF THE SECRETARY, U.S. DEP'T OF COMMERCE, *1 FOREIGN DIRECT INVESTMENT IN THE UNITED STATES 1-3* (1976). Secretary Elliot Richardson stated that prior to 1973 the United States was relatively unconcerned about the level of FDI. *Id.* This attitude resulted from the relatively small amount of foreign investment in the United States, and the success of U.S.-based multinational enterprises (MNEs) in their investments abroad. See generally Simon Reich, *Roads to Follow: Regulating Direct Foreign Investment*, 43 INT'L ORG. 543 (1989). See also generally Rachel McCullough, *Why Foreign Corporations Are Buying into U.S. Business*, 516 ANNALS OF THE AM. ACADEMY OF POL. & SOC. SCI. 169, 180 (July 1991) (describing the level of foreign investment in the United States).

3. FDI is defined as: "the ownership or control, directly or indirectly, by one foreign person of 10 per centum or more of the voting securities of an incorporated U.S. business enterprise or an equivalent in an unincorporated U.S. business enterprise, including a branch." 15 C.F.R. § 806.15(a)(1) (1993). FDI is most often measured as the sum total, at book value, of intercompany equity inflows and reinvested corporate earnings.

FDI is calculated by the sum of the net stock existing in the United States and the annual gross flow of such investments. The "stock" of foreign investment is defined as the sum of the yearly flows of foreign investment less depreciation, or:

$$\sum I = dF - \mu K$$

where:

I = net stock of foreign investment

F = annual flow of foreign investment or additions to the stock

μ = the exponential rate of investment depreciation

K = value of foreign investments in real rather than financial sectors.

For additional information on the effect of increases in gross investment on growth in gross domestic product, see EDWIN BURMEISTER, *CAPITAL THEORY AND DYNAMICS 40-43* (1980).

The "flow" of foreign investment is defined as the value adjusted sum of the following components: (1) gross foreign purchases of U.S. corporate bonds, stocks, and other debt inflows; (2) foreign purchases of U.S. Treasury securities; and (3) gross reinvested earnings of foreign operations. See INT'L TRADE ADMIN., U.S. DEP'T OF COMMERCE, *INTERNATIONAL DIRECT INVESTMENT: GLOBAL TRENDS AND THE U.S. ROLE 119* (1988) [hereinafter *GLOBAL TRENDS*]. See generally OFFICE OF THE SECRETARY, U.S. DEP'T OF TREASURY, *Treasury Bulletin*, various issues (defining flow of foreign investment).

4. Increased economic integration occurs when the proportion of a country's gross domestic product generated by the production of goods and services traded internationally increases. See PAN A. YOTOPOULOS & JEFFREY B. NUGENT, *ECONOMICS OF DEVELOPMENT: EMPIRICAL INVESTIGATIONS 314* (1976).

5. BUREAU OF ECONOMIC ANALYSIS, U.S. DEP'T OF COMMERCE, *Surv. of Current Bus.*, various issues (describing increased levels of foreign direct investment) [hereinafter *Current Business*].

example of regulatory reform which took place during this period was the 1971 replacement of the Bretton Woods fixed exchange rate system with a floating exchange rate system.⁶ The institution of the floating exchange rate system allowed the current trade account⁷ to immediately reflect the productivity of domestic production inputs.⁸ This almost instantaneous movement in exchange rates created a volatile world currency market and gave investors additional reasons to invest in the relatively stable U.S. economy.⁹

By the mid-1970s, the laissez-faire policy toward FDI taken by the U.S. government came into serious question due to the short term adjustment costs associated with increased FDI, such as the closing of less efficient facilities.¹⁰ In 1974, Congress passed the Foreign Investment Study Act.¹¹ Under this Act, the Secretary of Commerce and the Secretary of the Treasury investigated the nature, scope, and magnitude of foreign investment in the United States.¹² After receiving unsatisfactory results from the Foreign Investment Study Act, due to the unavailability of adequate investment data, Congress passed the International Investment and Trade in Services Survey Act of 1976.¹³ This Act authorizes the President, in unambiguous language, to "obtain information on the activities of multinational enterprises and other international investors . . ."¹⁴ The purpose of collecting this data is to allow for "assessing the impact of such investment and trade, to authorize the collection and use of information on direct investments owned or controlled . . . by foreign governments or persons, and to provide analyses of such information to the Congress, the executive agencies, and the general public . . ."¹⁵

Notwithstanding the passage of these two acts, the Carter administration officially took a neutral position on increased FDI.¹⁶ The Carter administration stated: "the United States will neither encourage nor discourage the inflow or outflow of international investment."¹⁷

6. See The Bretton Woods Agreement of 1944. The name of this Act was subsequently changed to Special Drawing Rights Act, per Pub. L. 90-349, 82 Stat. 188 (1968) (codified in 22 U.S.C. § 286 (1993)). The floating exchange rate system allowed market forces, rather than government policymakers, to determine the relative value of internationally traded goods and services.

7. The current trade account has two components, the trade balance and the services balance. The trade balance is the difference between the value of goods imported and the value of goods exported. The services balance is the difference between payments for domestic services performed for foreign individuals abroad and foreign services performed for U.S. individuals domestically, without the transfer of a physical product. The services balance includes all interest, dividends, and remittances for the services of capital and labor. See NAT'L ASS'N OF REALTORS, FOREIGN INVESTMENT IN U.S. REAL ESTATE: CURRENT TRENDS AND HISTORICAL PERSPECTIVE 3 (1990) [hereinafter REALTORS].

8. CHARLES P. KINDLEBERGER, INTERNATIONAL ECONOMICS 294-95 (5th ed. 1973).

9. See REALTORS, *supra* note 7, at 2. See also *infra* notes 65-67 and accompanying text (discussing political stability).

10. OFFICE OF THE SECRETARY, U.S. DEP'T OF COMMERCE, 1 FOREIGN DIRECT INVESTMENT IN THE UNITED STATES 1-3 (1976).

11. Pub. L. No. 93-479, 88 Stat. 1450 (1974).

12. *Id.* § 10.

13. 22 U.S.C. §§ 3101-08 (1993).

14. *Id.* § 3101(b).

15. *Id.*

16. James K. Jackson, *Foreign Direct Investment in the United States*, Congressional Research Service, Issue Brief No. IB87226, Aug. 20, 1991, at 6.

17. *Id.*

Following the surge of FDI during 1977-81, Congress became concerned that FDI had no substantially effective controls.¹⁸ The Reagan administration, however, took a more aggressive approach by undertaking to promote rather than limit FDI. The focus of the Reagan administration policy toward FDI is summarized in the following three policy objectives: (1) liberalization of barriers and the reduction of distortion of international investments abroad, (2) encouragement of a greater role for private foreign investment in the economic development of less-developed countries, and (3) maintenance of the maximum degree of foreign investment openness for the United States economy.¹⁹

Many liberal Democrats in the U.S. Congress were opposed to the Reagan administration policy and argued that increases in FDI were nothing more than opportunistic efforts by foreign nationals to take advantage of the relatively weak U.S. economy by purchasing available real estate and other productive factors at overly attractive prices.²⁰ A biting example of this protectionist attitude was provided by Representative Traficant (D-Ohio) when he stated:

Our Soldiers won the war, but Congress is letting Japan win the peace . . . Mr. Speaker, I say this to the Members of Congress: The day will come when America's cash crop will not be soybeans and wheat and corn; [it] will be rice, and we will have a rice paddy on the East Lawn of the White House.²¹

As a result of both public²² and congressional concerns, Congress included the Exon-Florio Amendment, as section 5021 of the Omnibus Trade and Competitiveness Act of 1988.²³ This Amendment gives the President the power to review and determine the "national security" impact of proposed mergers, acquisitions, and takeovers by foreign persons or business enterprises where such actions could result in the foreign control of U.S.-based business enterprises engaged in interstate commerce within the United States. Based on the President's findings, a particular FDI could be prohibited as contrary to the national security of the United States. In the authors' opinion, the purpose behind the passage of the Exon-Florio Amendment was to give the federal government the much needed authority to control the scope and magnitude of FDI where national security might

18. Much of Congress' concern during this period can be attributed to the decline of the United States as a predominant world economic power and a net supplier of FDI to the rest of the world. See *Current Business*, *supra* note 5, at 81 (June 1989 issue). By 1984, the United States became the largest host nation for FDI with 27.3% of the \$602.6 billion of world FDI stock, surpassing the second largest host Canada by \$102.5 billion. *Id.* By 1992, the current net book value of the U.S. FDI account was negative \$35.3 billion. *Id.*

19. *Id.*

20. E.J. Ray, *A Profile of Recent Foreign Investment in the U.S.*, 516 ANNALS OF THE AM. ACADEMY OF POL. & SOC. SCI. 50, 64 (1991).

21. 134 CONG. REC. H9583 (daily ed. Oct. 5, 1988) (containing the statements of Representative Traficant describing protectionist attitude of liberal democrats).

22. Examples of recent and highly publicized investments which support the use of restrictions on FDI include: the purchase of Hawaiian land by various Japanese interests, see THE ECONOMIST, Dec. 8, 1990, at 26, 33; the purchase of the Burger King franchise by Grand Metropolitan Ltd. of Great Britain, see FORBES, July 23, 1990, at 356; and finally the purchase of Twentieth-Century Fox by Australian interests, see N.Y. TIMES, Nov. 27, 1990, at D7.

23. 50 U.S.C. app. § 2170 (1993) (providing an amendment to Title VII, section 721 of the Defense Production Act of 1950) [hereinafter Exon-Florio Amendment].

be jeopardized, and where the current antitrust, securities, and emergency powers acts are not triggered.²⁴

The Bush administration reaffirmed the use of an open door foreign investment policy but without the aggressiveness seen in the Reagan administration. The Bush administration's foreign policy can be summarized as follows:

United States policy toward foreign direct investment is centered on two key tenants: [(1)] the United States welcomes foreign direct investment and [(2)] we seek to liberalize investment regimes abroad. . . . The rationale for our investment policy is plain: It fosters economic efficiency, stimulates economic growth, enhances our international competitiveness[,] and increases employment.²⁵

With the passage of the 1990 deficit reduction language and the economic slowdown caused as a result of its implementation, FDI decreased sharply after more than twelve years of robust growth. Since the 1992 election, the Clinton administration has been "tight-lipped" over the future of FDI controls.²⁶ The only official statement of note from an administration official was made prior to the election by Laura Tyson, later the Chairman of the Council of Economic Advisors, where she stated that foreign government investments in the United States would be restricted.²⁷

Since the debate over FDI is far from over, Part II of this Article concentrates on quantifying both the magnitude and composition of FDI in the United States.²⁸ Part III provides an in-depth discussion of the reasons for the rapid growth of FDI in the United States.²⁹ Part IV discusses the costs and benefits associated with increased FDI.³⁰ Part V discusses legislative and regulatory controls which can be used to limit future FDI, including the Exon-Florio Amendment.³¹ Finally, Part VI provides an analysis of the problems associated with the Exon-Florio Amendment.³²

II. MAGNITUDE OF FDI IN THE UNITED STATES

FDI in the United States can be traced back to the seventeenth century, when European trading companies invested in the American manufacturing sector and in the infrastructure of many of the original thirteen colonies.³³ Projects such as the Erie

24. *Id.* § 2170(b) (1993).

25. TREASURY NEWS, Feb. 26, 1991, at 1.

26. *Industrial Policy: Set of Principles on S&T Cooperation Would Be Valuable*, 10 Int'l Trade Rep. (BNA) No. 10, at 663 (Apr. 21, 1993) (statements of Thomas Kalil, technology specials, White House National Economic Council, responding to questions about the definition of national security under the Exon-Florio Amendment).

27. *French Government Ownership of Thompson Should Bar LTV Acquisition*, 9 Int'l Trade Rep. (BNA) No. 24, at 1018 (June 10, 1992).

28. See *infra* notes 33-52 and accompanying text.

29. See *infra* notes 53-77 and accompanying text.

30. See *infra* notes 78-108 and accompanying text.

31. See *infra* notes 109-28 and accompanying text.

32. See *infra* notes 229-76 and accompanying text.

33. Jeffery M. Schaefer & David G. Strongin, *Why All the Fuss About Foreign Investment*, 32 CHALLENGE 31 (May-June 1989).

Canal, the interstate railroad system, and even the purchase of the Louisiana Territory from France in 1803 were completed using foreign investment.³⁴

Modern measurement of FDI began in the late nineteenth century and has been measured in three different ways. The first and most widely reported approach is the "balance of payments" approach. Under this approach, intercompany and equity inflows, reinvested corporate earnings, and value adjustments to account for changes in the market value of existing financial assets are measured at book value. The resulting amount is the value and equity held by FDI in, and outstanding loans to, their affiliates in the United States.³⁵

The second measure is the "total assets" approach. Under this approach, the total value of assets controlled by foreign persons is considered foreign investment. This measure is flawed because it does not distinguish between investment wholly owned by foreign persons and investments in which foreign persons are only minority shareholders. Thereby the actual value of foreign investment is overstated.

The third measure of FDI reported by the U.S. Department of Commerce is the book value of property, plants, and equipment. In the benchmark survey, U.S. affiliates³⁶ were required to disaggregate the gross book value of property, plant, and equipment used in their U.S. operations. These disaggregated values were calculated separately for manufacturing operations, other commercial operations, and remaining operations.³⁷ These various disaggregated measures of FDI also tend to overestimate FDI in the United States because they are gross values and because they do not differentiate between companies which are wholly owned subsidiaries and those in which the foreign investors are only minority shareholders. For example, in 1987, the gross value of property, plant and equipment FDI was \$353,278 million, compared to \$271,788 million under the net book value approach.³⁸

Under the balance of payments approach, the cumulative book value of FDI stock in the United States exceeded \$700,200 million by 1914, as various European manufacturing companies began investing in chemicals, electronics, and automobiles.³⁹ The magnitude and scope of FDI in the United States followed a roller-coaster path from the 1920s to the 1940s.⁴⁰ Investment was heavily influenced during this period by the expansive

34. See Mark L. Hanson, *The Regulation of Foreign Investment in the United States Defense Industry*, 9 NW. J. INT'L L. & BUS. 658, 659-60 (1989).

35. See GLOBAL TRENDS, *supra* note 3, at 119 (describing the balance of payments approach). During this time, U.S. investments abroad were growing rapidly and amounted to \$3.5 billion. *Id.* By 1919, the United States had become a net supplier of capital to world markets and began a great period of net foreign investments which did not end until 1988. *Id.* In 1989, the net book value of United States FDI abroad was \$373.4 billion compared to FDI in the United States of \$400.8 billion, a deficit of \$27.4 billion. *Id.* See also Russell B. Scholl, *The International Investment Position of the United States in 1988*, in 69 *Current Business*, *supra* note 5, at 41, 59 (June 1989).

36. A U.S. affiliate is defined as a U.S. business enterprise in which there is foreign direct investment; a business enterprise is as an organization, association, branch, or venture that exists for making profit or to otherwise secure an economic advantage. See GLOBAL TRENDS, *supra* note 3, app. M, 4-5 (discussing in greater detail U.S. affiliates and business enterprises).

37. *Id.* app. M, at 13.

38. *Id.* at 41.

39. See Scholl, *supra* note 35, at 48 (describing the amount of FDI stock in the United States).

40. See *Current Business*, *supra* note 5.

monetary policy of the early 1920s, the overly contractionary monetary policy of the late 1920s and 1930s, and the subsequent depression.⁴¹

As stated in the introductory section, from the post-World War II period until the mid-1970s, there was an increase in economic growth and world economic integration.⁴² FDI in the United States increased during this period from \$3.39 billion to over \$13.27 billion in 1975.⁴³ These increases, although massive, were out-shadowed by the increase in United States investment abroad, which reached \$52.21 billion in 1975 and \$96.39 billion in 1979.⁴⁴ The United States was a strong supplier of funds to the world market as late as 1979.⁴⁵

As stated above, the 1980s ushered in concerns over the nature, scope, and course of future FDI in the United States. During this period, U.S.-based multinationals (MNEs) weakened; the position of the United States as a net supplier of capital to foreign markets came to an abrupt halt with the rapid increase in FDI in the United States.⁴⁶ The growth in book value of FDI in the United States during the 1980s, in comparison to U.S. investment abroad, is shown in table 1 below:

TABLE 1
BOOK VALUE OF THE STOCK OF FDI, 1980-89 (IN MILLIONS)⁴⁷

Year	U.S. FDI Abroad	FDI in the U.S.	Net U.S. Position
1980	215,375	83,046	132,329
1981	228,348	108,714	119,634
1982	207,752	124,677	83,075
1983	207,203	137,061	70,142
1984	211,480	164,583	46,897
1985	230,250	184,615	45,635
1986	259,562	220,414	39,148
1987	314,307	263,394	50,913
1988	333,501	314,754	18,747
1989	373,436	373,763	-327

In comparison to the information in table 1, under the balance of payments approach, total FDI in the United States in 1992 was \$430,397 million, a decrease of \$3,948 million over the 1991 level.⁴⁸ As shown in table 1, the foreign investment practices of the 1980s resulted in near parity between the book value of FDI in the United States and the book

41. *Id.*

42. *Id.*

43. *See id.* (Aug. 1985, Aug. 1986, and Aug. 1987 issues).

44. *Id.*

45. *Id.*

46. *See Current Business*, *supra* note 5 (1982-91 various issues).

47. Amounts represented are the net total book value of FDI stock in millions of U.S. dollars. *Id.* (1982-91 various issues).

48. *Id.* at 81 (Mar. 1993 issue).

value of U.S. FDI abroad.⁴⁹ While U.S. FDI abroad increased by 51.8 percent in nominal terms during the 1980s, but only 4.5 percent in real terms, FDI in the United States increased by 296 percent and 172.5 percent in nominal and real terms respectively.⁵⁰

Using the book value approach, table 2 below provides a comparison of the magnitude of FDI in the United States with the annual United States gross national product. This approach presents a complete picture of the magnitude of FDI, not from an internal growth perspective, but from its contribution to the total output of goods and services in the United States.

TABLE 2
A COMPARISON OF THE STOCK OF FDI IN THE U.S. WITH U.S.
GROSS NATIONAL PRODUCT (GNP), 1980-89 (IN MILLIONS)⁵¹

<u>Year</u>	<u>U.S. GNP</u>	<u>FDI in the U.S.</u>	<u>FDI as % of GNP</u>
1980	2,732,000	83,046	3.04%
1981	3,052,000	108,714	3.56
1982	3,166,000	124,677	3.94
1983	3,045,700	137,061	4.50
1984	3,772,200	164,583	4.36
1985	4,014,900	184,615	4.60
1986	4,231,600	220,414	5.20
1987	4,515,600	263,394	5.83
1988	4,873,700	314,754	6.64
1989	5,200,800	373,763	7.19

Regardless of which measure of FDI is chosen, the 1980s produced significant increases in the flow and stock of FDI in the United States as well as a relatively modest increase in FDI as a percentage of U.S. gross national product. These increases in FDI in the United States can be traced to nearly all of the United States' major European and Asian trading partners.⁵²

49. NORMAN J. GLICKMAN & DOUGLAS P. WOODWARD, *THE NEW COMPETITORS: HOW FOREIGN INVESTORS ARE CHANGING THE U.S. ECONOMY* 30 (1989). These authors provide a cautionary note concerning the use of the this data. Most of the U.S. investments were booked during the 1950s and 1960s and would therefore underestimate the current value of these assets. *Id.*

50. *See Current Business, supra* note 5 (1982-91 various issues) (calculating the increase of FDI abroad). The numbers presented provide a less than accurate comparison of U.S. FDI abroad and FDI in the United States because this approach tends to undervalue U.S. FDI abroad. *Id.* Many of the U.S. investments abroad are underestimated. *Id. See supra* note 49 (discussing this data).

51. *Id.* (Aug. 1991 issue). The GNP and FDI amounts shown are in millions of U.S. dollars. *See Current Business, supra* note 5, at 20 (1982-91 various issues). The percentages were calculated by the authors.

52. As shown in the table below, Japanese investment, as measured by the standard balance of payments approach, increased dramatically during the 1980s. From 1987 to 1990, total Japanese investment increased at an annual rate of 34.36%, far outpacing increases in German, British, and French investment.

III. REASONS FOR RAPID GROWTH OF FDI DURING THE 1980S

The reasons behind the rapid growth in FDI in the United States during the 1980s have been widely discussed. We have found it advantageous to categorize these reasons into two theoretical categories, "ownership-specific" advantages and "location-based" advantages.

A. Ownership-Specific Advantages

The advantages a business owner or investor can reap from FDI often depend upon the size of the investor's operation. For established MNEs, which often invest from a position of relative economic strength, investment decisions are influenced by micro-economic factors, such as: (1) access to new technology, (2) increased capacity, (3) the need to exploit a newly patented technology, and (4) global diversification and product expansion.⁵³ The proper exploitation of these factors can give a foreign firm an advantage against an existing domestic competitor in a given national market, such as the United States. Many of these ownership-specific advantages are seen as market share expansion efforts rather than short-run profit maximization or cost minimization efforts.⁵⁴

Increased productive capacity can be gained domestically or internationally by a foreign investor through licensing agreements, joint ventures, establishment of wholly owned subsidiaries, acquisition of existing facilities, or the purchase of stock. The form FDI takes will depend upon the purpose behind the investment. For example, if the investor is trying to compete on factors other than cost, such as customer service or customization, the purchase of an existing facility near the target market must be equal to peak demand rather than average experienced demand. If the investor wants to market

However, Japanese investment in the United States was still 22.73% below the net book value of British FDI in the United States in 1990.

TABLE 3
FDI IN THE UNITED STATES BY U.S. TRADING PARTNERS
ON A HISTORICAL COST BASIS, 1987-90

Country	1987	1988	1989	1990
Belgium	3,371	3,471	3,972	4,230
France	10,137	13,233	16,822	19,550
Germany	21,095	25,250	29,015	27,770
Japan	34,421	51,126	67,319	83,498
Sweden	4,910	4,713	5,303	5,450
Switzerland	13,772	14,372	18,772	17,512
United Kingdom	75,519	95,698	105,511	108,055

Note: The amounts shown are in millions of U.S. dollars.

Current Business, supra note 5, at 51-54 (Aug. 1991 issue).

53. Kang-tsung Chang, *Japan's Direct Manufacturing Investment in the United States*, 41 PROF. GEOGRAPHER 314, 315 (1989).

54. Erica Schoenberger, *Foreign Manufacturing Investment in the United States: Competitive Strategies and International Location*, 61 ECON. GEOGRAPHY 241, 242-243 (1985).

a newly patented product, a licensing agreement will likely result because the financial risks of FDI to the foreign patent holder are at a minimum.

Access to new technology is the most often cited reason for increased FDI in the United States.⁵⁵ The category of new technology includes not only engineering and scientific knowledge, but also market strategies information unavailable or unknown in the investment source country. A foreign investor will often strive for access to new technological information in order to avoid many of the start-up costs associated with a new venture in an unfamiliar market.⁵⁶ FDI in the U.S. technology sectors of chemical products, metal fabrication, and electronics grew from \$25,810 million in 1985 to \$68,394 million by 1990, an annual increase of 21.52 percent.⁵⁷

Notwithstanding the substantial increase in FDI in the high-technology sector, a recent study of Japanese investment patterns in the United States seriously questioned the role that access to new technology has played as a force behind increased FDI.⁵⁸ The study concluded that the spatial clustering of Japanese high-technology FDI in certain areas within the United States which have an abundance of skilled labor, weak organized labor, and public research facilities, mirrors the investment pattern of U.S. manufacturers—evidencing that such investors are no longer net providers of new manufacturing technology.⁵⁹ Implicitly the study concluded that the Japanese are currently net providers of technology to investment host countries such as the United States.⁶⁰ While Japanese investors are current net providers of new technology to the United States, other industrialized countries and lesser developed countries will likely still base future FDI decisions on the availability of U.S. technology.⁶¹

Global expansion of foreign-based MNEs into the United States offers access to the world's largest and most homogenous markets. The United States does not require extensive infrastructure investment or extensive language accommodations in order to take advantage of marketing opportunities.⁶² Investment in such a large and homogeneous market offers foreign investors an opportunity to use scale economies in production if their individual production operation is characterized by declining marginal costs.⁶³ Even without economies of scale, MNEs may have advantages over their competitors because

55. See, e.g., *French Government Ownership of Thompson Should Bar LTV Acquisition*, 10 Int'l Trade Rep. (BNA) No. 9, at 1018 (June 10, 1992).

56. See Scholl, *supra* note 35, at 48.

57. See *Current Business*, *supra* note 5, at 54, 77 (Aug. 1991 issue).

58. See Chang, *supra* note 53, at 314-28.

59. *Id.* at 325. The results of the Chang study are supported by a similar study by the General Accounting Office. See *Foreign Investment in the United States: Hearings Before the House Subcommittee on International Economic Policy and Trade*, 100th Cong., 2nd Sess. 32 (1988) [hereinafter *Foreign Investment Hearings*] (statement by A.I. Mendelowitz, Senior Associate Director, National Security and International Affairs Division, General Accounting Office) (discussing Japanese Investment in the U.S. automobile industry in which the flow of technology is into the United States).

60. Chang, *supra* note 53, at 326.

61. *Id.* at 326.

62. HARVEY A. PONIACHEK, *DIRECT FOREIGN INVESTMENT IN THE UNITED STATES* 15-20 (1986).

63. Declining marginal costs mean that the additional cost associated with the production of each additional unit is falling. When declining marginal costs exist, the average cost of production also declines allowing larger plants or operations to drive smaller competitors out of business. See JACK HIRSHLEIFER, *PRICE THEORY AND APPLICATIONS* 313-14 (2nd ed. 1980) (emphasis added).

of their size—allowing greater access to capital markets, increased risk spread, better information, and greater state and federal political influence.

Closely related to the factors of size and economies of scale, the United States also offers a more stable political climate⁶⁴ than many lesser developed countries, and even European countries.⁶⁵ A recent study by Safizadeh on the importance of the political climate indicates that MNEs consider the political stability of the host country one of the most important considerations in allocating funds to foreign investment projects. The importance of this factor is due to the belief that absent some measure of political stability, existing foreign investments may be subject to noneconomic forces beyond the investor's control, such as investment nationalization.⁶⁶

While access to new technology and political stability are general benefits obtained by all foreign investors, advantages such as scale economies and increased capacity are firm-specific and are not captured by all foreign investors. In the case of a future analysis of these firm-specific advantages, the structure of the domestic market should be taken into account.

B. Location-Based Advantages

The advantages an investor can reap from FDI depend not only upon firm-specific advantages, but also upon the host country's general economic climate. The often cited locational advantages of FDI in the United States include economic and political variables such as: (1) economic size and growth rates, (2) productivity level changes, (3) exchange rate movements, (4) the possibility of current and future trade restrictions, and (5) the generally favorable business climate.⁶⁷

In the decade immediately following World War II, the United States laid claim to having the largest and fastest growing economy and the highest level of productivity.⁶⁸ In the 1980s, both the overall economic growth rate and the productivity growth rate slowed. This allowed many major trading partners to surpass the United States in growth percentage terms.⁶⁹ However, in terms of the total increase in goods and services produced, the United States still ranked as one of the most expansive world economies. Consequently, this factor likely had a great influence on FDI increases during the 1980s.

Another reason for the increase in FDI in the United States during the 1980s was the dramatic exchange rate movements engineered by the U.S. government as a means to

64. Political stability is defined as: "Positive perceptions emanating from internal intergovernmental relationships, and anticipated or unanticipated governmental actions brought about by social, economic, and political variables existing in a country's internal or external environment." This definition was developed from a definition of political risk by Safizadeh. See K. Fatehi-Sedeh & M.H. Safizadeh, *The Association Between Political Instability and Flow of Foreign Direct Investment*, 29 MGMT. INT'L REV. 4, 10 (1989).

65. Barney Warf, *US Employment in Foreign-Owned High Technology Firms*, 42 PROF. GEOGRAPHER 421, 423 (1990).

66. See Fatehi-Sedeh & Safizadeh, *supra* note 64, at 4.

67. Chang, *supra* note 53, at 315-16.

68. *Current Business*, *supra* note 5 (various issues).

69. *Id.*

quell inflation, making U.S. products relatively more expensive on world markets.⁷⁰ For instance, the value of the dollar against the Japanese yen increased from 210.44 yen per dollar in 1978 to 238.54 yen per dollar in 1985.⁷¹ These exchange rate movements are an important determinant of rates of return on many types of internationally traded assets. Increases in value of the yen and other major currencies against the dollar made the United States more attractive as a production site by lowering U.S. production costs relative to those in Europe or Japan. The exchange rates, therefore, have played a significant role in increasing FDI in the United States.⁷²

A long-standing proposition of international trade theory is that artificially restricting trade flows stimulates compensating factor flows. Countries experiencing slower economic growth, inflation, or high unemployment often place restrictions on imports as a means of maintaining a relatively stable balance of trade and protecting domestic industries. The manufacturing and service operations owned by foreign MNEs in such an import-restricted country are often unaffected by such policies. It is therefore attractive to invest in countries which have or will likely use protective measures as a means to obtain access to the domestic market in the United States. While theoretically correct, according to McCulloch, a statistical analysis of Canadian and U.S. data has failed to confirm a systematic relationship between FDI and the adoption of protectionist policies.⁷³ The hypothesis used by McCulloch to explain the lack of a statistically significant link between increased FDI and protectionism is that protectionism creates a locational advantage by raising the cost of serving the market through trade.⁷⁴ In other words, protectionism leads to barriers to entry against future market entrants, as opposed to increasing the overall FDI.⁷⁵ These policy barriers are a likely decisive investment factor in low technology market segments where the cost of protectionism cannot be overcome by investor-specific advantages such as patent exploitation.

The final and most general locational advantage associated with increased FDI in the United States is its generally favorable business climate.⁷⁶ While the business climate is hard to measure, it generally encompasses factors such as: (1) the tax structure, (2) environmental policy, (3) the proximity to and promotion of university research centers, (4) a skilled and educated labor force, and (5) an adequate existing infrastructure.⁷⁷

IV. COSTS AND BENEFITS ASSOCIATED WITH INCREASED FDI

A large number of law review and business journal articles from differing economic and political viewpoints discuss either the theoretical costs or the theoretical benefits

70. Contraction of the domestic money supply increased the exchange rate, thus increasing U.S. interest rates. This increase in interest rates and the subsequent increase in international capital to the United States provided Congress with the ability to finance the ever-increasing U.S. domestic budget deficit by increasing interest rates and thus enticing additional foreign investors.

71. INT'L MONETARY FUND, INTERNATIONAL FINANCIAL STATISTICS 442 (1988).

72. McCullough, *supra* note 2, at 178-79.

73. *Id.* at 179-80.

74. *Id.*

75. *Id.*

76. See Warf, *supra* note 65, at 422.

77. *Id.*

associated with growth in FDI in the United States.⁷⁸ A review of these articles would lead one to conclude that an objective discussion of both the costs and benefits associated with FDI in the United States is warranted.

A. Costs Associated with Increased FDI

A discussion of the costs associated with increased FDI in the United States includes those costs normally discussed from a particular political point of view and those costs for which a more objective view is appropriate. Viewpoint-based costs include the negative effects of increased FDI on national security, employment, and land ownership. These three factors lack of objective factors from which to measure the impacts on the cost category (without making assumptions). The non-viewpoint-based costs associated with increased FDI are foreign capital dependence, technology transfer, and inflation.

1. Viewpoint-Based Costs of Increased FDI

The first of the three viewpoint-based costs associated with increased FDI in the United States is its potential negative impact on "national security." National security is defined in broad terms as the "national defense or foreign relations of the United States."⁷⁹ Included within this definition is the concept of "economic security."⁸⁰ An interpretation of the economic security component of national security has led some in Congress and the national media to believe that the protection of jobs in *all* domestic sectors should be included within the definition of national security.

From this viewpoint, increased FDI in the United States, via joint ventures or the acquisition of an existing production facility, could negatively affect the economic security component of the national security in a variety of ways. First, opponents of FDI may argue that the purchase of an existing facility by a foreign national adds nothing to U.S. productive capacity, and is simply a transfer of assets to persons who must eventually answer to a foreign government.⁸¹ These opponents further argue that allowing increased FDI entices foreign governments to engage in political influence peddling, thus weakening the economic and social structure of the United States.⁸²

Second, where foreign investors have purchased an existing U.S. facility, opponents argue that the repatriation of business profits back to the investment source country could lead to a decrease in investment in the U.S. economy.⁸³ Finally, FDI proponents argue

78. See, e.g., Michael Ulan, *Should the United States Restrict Foreign Investment*, 516 ANNALS OF THE AM. ACADEMY OF POL. & SOC. SCI. 117, 122 (1991).

79. 50 U.S.C. § 401, Exec. Order No. 12356, pt. 6, § 6.1 (1993).

80. Economic security includes, e.g., the capability of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services. See Defense Production Act of 1950, 50 U.S.C. app. § 2170(e), para. 2 (1993).

81. Ulan, *supra* note 78, at 122.

82. See *Foreign Investment Hearings*, *supra* note 59, at 32 (statement by A.I. Mendelowitz, Senior Associate Director, National Security and International Affairs Division, General Accounting Office).

83. Jackson, *supra* note 16, at 5-6. The argument that foreign investors would likely engage in influence peddling is further weakened by recognizing that investors are generally in business to generate profits, and unless the influence peddling is either in their best financial interests or foreign investors are being subsidized by their governments, such is unlikely to take place. See Ulan, *supra* note 78, at 123.

that if foreign nationals are in control of future research and development spending, foreign governments could influence a shift of U.S. domestic production away from products necessary in a national defense emergency, such as semiconductors and other high-technology items, thereby having a negative impact on future U.S. aggression deterrence capabilities.⁸⁴

The proponents of increased FDI would argue that such investment can actually increase domestic productivity by utilizing otherwise idle physical, financial, and human capital.⁸⁵ FDI in the form of new plants, joint ventures, or stock purchases imports productive assets located outside the United States and adds to existing capital to increase both the gross domestic product and the tax base.⁸⁶ Even where the FDI results in the purchase of an existing facility, it is rarely done in isolation without additional investments in human or financial capital.⁸⁷

FDI opponents claim the possibility of influence peddling by foreign nationals and their governments as a national security justification to limit increased future FDI.⁸⁸ This position assumes that influence only flows one way, from the parent foreign investor to its U.S. subsidiary.⁸⁹ This argument appears to be suspect because it is just as likely that the U.S. subsidiary could pressure the foreign parent to adopt policies favorable to U.S. interests.

Opponents of increased FDI also charge that negative impacts on national security will result from the future FDI research and development spending decisions that move production away from goods which could be utilized in a national security emergency.⁹⁰ However, U.S. national security can be adequately protected by direct government funding of research projects it deems most appropriate. The government would thereby avoid placing restrictions on increased FDI, which may only result in reciprocal restrictions on U.S. investments abroad. Foreign control of research and development spending seems to be even more of a smoke screen because of the poor record of domestic firm spending on research and development, especially given the U.S. Congress' drain of domestic financial capital via the huge federal budget deficit. This draining effect on domestic financial markets should itself be a more prominent national security issue.

The second viewpoint-based cost of increased FDI in the United States is the adverse impact on employment.⁹¹ Critics of increased FDI, such as the AFL-CIO, argue that when FDI is used to purchase an existing U.S. firm, the new foreign owners frequently reduce the number of employees.⁹² These critics further argue that when FDI does

84. See Robert E. Lipsey, *Foreign Direct Investment in the United States and U.S. Trade*, 516 ANNALS OF THE AM. ACADEMY OF POL. & SOC. SCI. 76, 77-79 (1991) (discussing the consequences of foreign investment).

85. Ulan, *supra* note 78, at 118-20.

86. *Id.*

87. *Id.*

88. Jackson, *supra* note 16, at 5-6.

89. *Id.*

90. Ulan, *supra* note 78, at 120-24.

91. *Id.*

92. *Id.* at 122. See also GLICKMAN & WOODWARD, *supra* note 49, at 15-18. Businesses controlled by foreign investment employ approximately three million U.S. citizens. Employment estimates for "Greenfield" investments (investments which do not replace other U.S. investments through buyout, merger, or takeover) are in the 50,000 to 100,000 range. Even using the smaller of the two presented employment

create jobs, these jobs are generally low-skilled jobs in comparison to those created by domestic companies.⁹³

These employment arguments are flawed for two reasons. First, the argument assumes the U.S. worker is faced with a choice between working for an existing U.S. manufacturer or working for a foreign-owned U.S. subsidiary. In reality, the United States owned operation may be poorly managed and may have been shut down if not sold to foreign investors.⁹⁴ Furthermore, increased FDI has actually increased domestic job opportunities.⁹⁵ Second, although FDI from many countries with inferior technology might create only low-skilled jobs, because of the Japanese superiority in many technological fields,⁹⁶ it is unlikely that jobs created by Japanese-based investment in these sectors would always equate to low-skilled jobs.⁹⁷

As stated in the introduction to this article, some congressional FDI opponents have argued that FDI increases are simply opportunistic efforts to purchase real estate at attractive prices.⁹⁸ FDI in U.S. real property, other than agricultural land,⁹⁹ increased dramatically during the 1980s. This is evidenced by increases in the real estate portion of the foreign investment portfolio, which increased from three percent in 1974 to seven percent in 1980, and finally to ten percent by 1986.¹⁰⁰ Regardless of whether future studies demonstrate that FDI has a negative impact on the economy, uncertainty over divestiture will ultimately lead to lower levels of investment both in real property and

numbers, the impact of foreign investment cannot be dismissed as unimportant. Under the export theory of regional development, each employee of a firm which exports goods and services to another region or country will create multiple final sector jobs in the economy. An example of this phenomenon is seen in the increasing numbers of fast food restaurants which occur near manufacturing plants or government centers. Additionally, there is no clear estimate as to how many of the more than two million non-Greenfield jobs may have been lost without the infusion of foreign capital. See generally *Foreign Investment in the United States: Hearings Before the House Committee on International Economic Policy and Trade of the House Committee on Foreign Affairs*, 100th Cong. 2nd Sess. 76-77 (1988) (statement by E.L. Richardson, Association for Investment in America).

93. Jackson, *supra* note 16, at 5-6. See GLICKMAN & WOODWARD, *supra* note 49, at 15-18.

94. Ulan, *supra* note 78, at 122.

95. *Id.* at 123.

96. See *supra* notes 58-61 and accompanying text (discussing Japanese technology).

97. See *supra* notes 58-66 and accompanying text (discussing the transfer of technology from Japan to the United States).

98. See *supra* notes 20-24 and accompanying text (discussing opportunistic motives to engage in FDI).

99. The agricultural sector has not traditionally been a large recipient of foreign direct investment. In 1982, foreign direct investment in agriculture amounted to only \$4 million. By 1988, foreign investment had risen to only \$226 million, a very small amount in comparison to other segments of the economy. See INT'L TRADE ADMIN., U.S. DEP'T OF COMMERCE, FOREIGN DIRECT INVESTMENTS IN THE UNITED STATES (December 1983 and September 1988). While the increase during this six-year period was 5550%, one would think the total amount would not produce a political uproar, but the political controversy generated has been not greater than the controversy associated with corporate farm ownership.

A possible source of negative economic effects from foreign ownership of farm land is the possibility that such land may be taken out of production. Assuming the foreign owners choose to keep the land idle, crop and land prices would tend to rise for the farmer and the consumer as the supplies were reduced. However, the economic reality of foreign investment in agricultural land during the 1980s does not support such a supply reduction scenario.

100. See GLOBAL TRENDS, *supra* note 3, at 40.

securities, as foreign investors seek to maximize investment profits while simultaneously seeking to minimize investment risk.

2. Non-Viewpoint-Based Costs of Increased FDI

Dependence on foreign financial capital is often cited as a reason for limiting FDI. Prior to the 1980s, foreign investors held thirty percent of U.S. securities, and the percentage declined to around twenty percent during the first six years of the Reagan administration.¹⁰¹ Notwithstanding the decline in the percentage of U.S. securities held by foreign investors, the total value of these securities increased from \$136.6 billion in 1981 to \$425.1 billion in 1990, an annual increase of 13.44 percent.¹⁰² This was the result of the increasing budget deficit.¹⁰³ An example of the potential impact foreign investors can have on the U.S. economy can be taken from the results of a study on the October 1987 stock market crash. This 1988 study, administered by Nicholas Brady, the head of the presidential task force that studied the crash, concluded that the record drop in the New York Stock Exchange was triggered in part by the heavy Japanese selling of U.S. government bonds on October 14, 1987, following the release of the U.S. trade

101. Schaefer & Strongin, *supra* note 33, at 33.

102. *Id.*

103. FEDERAL RESERVE, BULLETIN (1986-92 various issues).

TABLE 4
A COMPARISON OF THE STOCK OF FDI IN THE U.S. WITH U.S.
GROSS NATIONAL PRODUCT (GNP), 1980-89 (IN MILLIONS)

Year	Total U.S. Debt	Debt Held in Foreign Hands	Percent of Debt Held by Foreign MNEs
1955	223.9	6.8	3.04%
1960	231.2	12.3	5.32
1965	259.5	16.7	6.44
1970	275.7	14.8	5.37
1975	437.3	66.5	15.21
1980	737.7	134.3	18.21
1981	825.4	141.4	17.13
1982	987.7	149.5	15.14
1983	1,174.5	166.3	14.16
1984	1,373.4	205.9	14.99
1985	1,598.5	224.8	14.06
1986	1,813.3	263.4	14.53
1987	1,953.9	299.7	15.34
1988	2,091.2	362.2	17.27
1989	2,244.2	392.9	17.51

The numbers provided above are in billions of U.S. dollars from data contained in INTERNATIONAL MONETARY FUND, INTERNATIONAL FINANCIAL STATISTICS (1960-89 various issues). The authors generated the percentages. The debt held by foreign investors consists of U.S. treasuries, corporate bonds, and corporate equities. The net foreign investor purchases of U.S. securities during the 1980s exceeded \$215 billion. These purchases increased foreign ownership from less than 3.04% in 1955 to 17.51% in 1989, an annual increase of more than 5%.

deficit figures for August 1987.¹⁰⁴ Whether U.S. economic policy has been affected by the large foreign holdings of government debt remains an open question, but as the results of the study by the presidential task force demonstrate, the possible exertion of direct or indirect foreign influence exists.

The loss of control over inflation is also cited as a cost associated with increased FDI which does not require a particular ideological reference point. In order for increased FDI to increase domestic inflationary pressures the economy must be operating at full employment and the FDI must not add to the productive capacity of the domestic economy.¹⁰⁵ The economy is operating at full employment when all of the labor offered by workers at the current real wage rate is taken by employers and all employers are able to obtain the amount of labor preferred at the wage rate.¹⁰⁶ This occurs when published unemployment statistics are in the neighborhood of four to six percent, due to voluntary job changes. Therefore, in order for FDI to have a possible inflationary impact, unemployment must be below six percent. While this level of unemployment has been achieved in recent years, its return in the near future is not likely. Thus, any inflationary pressure from increased FDI does not currently exist.

B. Benefits Associated with Increased FDI

The benefits to the domestic economy from increased FDI include: increased capital-to-labor ratios, which may give rise to increased employment; domestic interest rate controls; and the promotion of openness for U.S. investment abroad. Capital-to-labor ratios, and thus real wages, will increase as foreign investments are used to purchase or upgrade plants and equipment and new technology is introduced from foreign technologically advanced countries.¹⁰⁷ Therefore, increased FDI indirectly adds to gross domestic product (GDP), increases demand for U.S. labor, and increases the domestic standard of living.¹⁰⁸

104. Thomas E. Ricks, *Task Force's Brady Says Japanese Sales of U.S. Bonds Touched Off Oct. 19 Crash*, WALL ST. J., Apr. 22, 1988, at 18.

105. *Foreign Investment Hearings*, *supra* note 59, at 14 (statement by R. Ortner, Undersecretary for Economic Affairs, U.S. Dept. of Commerce). FDI will add to productive capacity when additional human or financial capital is developed or acquired as a result of the investment. The availability of FDI increases available financial capital and lowers the cost of business expansion in new or existing markets. The additional supply of investment funds and the corresponding increase in physical and human capital allows the domestic economy to control inflation by increasing the supply of goods rather than acting as a catalyst for future inflation.

106. PAUL BURROWS & THEODORE HITIRIS, *MACROECONOMIC THEORY: A MATHEMATICAL INTRODUCTION* 81 (1983).

107. *See supra* notes: 58-61 and accompanying text (discussing Japanese technology).

108. MICHAEL E. PORTER, *THE COMPETITIVE ADVANTAGE OF NATIONS* 8 (1990). A side benefit of increased FDI in this area is that international standards of competitiveness are brought to bear in local and national markets, increasing overall economic efficiency.

The increase in standard of living caused by increasing capital-labor ratios is offset by the drain on financial capital and thus physical capital formation by the increasing U.S. budget deficit. Financial capital that would ordinarily have gone to the private sector to purchase capital equipment goes instead to finance ever-increasing social program levels. If the resources needed to finance this deficit had to come from domestic sources alone, interest rates would rise 3.5 to 5.5 percentage points. *See Foreign Investment Hearings*, *supra* note 59, at 75 (statement by E.L. Richardson, Association for Foreign Investment in

V. LEGISLATIVE AND REGULATORY CONTROLS ON FDI

A. Indirect FDI Controls

Prior to the passage of the Exon-Florio Amendment in 1988,¹⁰⁹ control over the scope of permissible FDI in the United States was controlled by a hodgepodge of absolute legislative bars to investment in numerous locations and sectors of the economy. In an article by Almond and Goldstein,¹¹⁰ it was noted that FDI was prohibited in the following areas: mining and energy,¹¹¹ broadcasting and communications,¹¹² inter-coastal transportation,¹¹³ banking,¹¹⁴ investment companies,¹¹⁵ domestic air transportation,¹¹⁶ and military weapons technology.¹¹⁷

America). Such an increase in interest rates would have a devastating effect on domestic capital formation in the United States and would likely have been the catalyst for another serious economic downturn.

109. 50 U.S.C. app. § 2170 (1993). This section was an amendment to title VII, section 721 of the Defense Production Act of 1950.

110. Michael A. Almond & Shelly M. Goldstein, *Foreign Direct Investment in the United States: An Overview*, 7 N.C. J. INT'L L. & COM. REG. 153, 158 (1982).

111. *See, e.g.*, Atomic Energy Act of 1954, 42 U.S.C. § 2133(d) (1993) (prohibiting the issuance of licenses to manufacture, acquire, or transport atomic energy components to aliens or any corporation known to be controlled by an alien); General Mining Law of 1872, 30 U.S.C. § 24 (1993) (limiting the purchase of lands containing valuable mineral deposits to citizens of the United States or to those who have declared their intention to become citizens); Water Power Act, 16 U.S.C. § 797(e) (1993) (limiting persons who could receive a license to construct, operate, or maintain dams to citizens); Mineral Leasing Act of 1920, 30 U.S.C. § 181 (1993) (limiting the ownership of any interest in a lease concerning mineral deposits to citizens of the United States if the foreign country from which the person originates has a prohibition against U.S. citizens obtaining similar leases); Geothermal Steam Act of 1970, 30 U.S.C. § 1015 (1993) (limiting to citizens, or corporations organized under the laws of the United States, the right to obtain a geothermal lease).

112. *See* Communications Act of 1934, 47 U.S.C. §§ 151-613 (1993) (section 310(b)(1) provides a license ownership restriction under which "no broadcast or common carrier or aeronautical en route or aeronautical fixed radio station license can be granted to or held by an alien or any representative of an alien").

113. *See* Merchant Marine Act of 1920, 46 U.S.C. app. § 883 (1993) (limiting the right of noncitizens to engage in coastal shipping).

114. *See, e.g.*, Depository Institutions Deregulation and Monetary Control Act of 1980, 12 U.S.C. § 72 (1993) (requiring that every director of a national bank be a citizen of the United States during his term); International Banking Act of 1978, 12 U.S.C. § 3102 (1993) (setting out the regulations applicable to establishment of branches by foreign banks).

115. *See, e.g.*, Investment Company Act of 1940, 15 U.S.C. §§ 80a-7 & -8 (1993) (restricting the use of interstate commerce to investment companies organized under the laws of the United States or any state).

116. *See* Federal Aviation Act of 1958, 49 U.S.C. App. § 1378(a)(4) (1993) (prohibiting any foreign air carrier or person controlling a foreign air carrier from acquiring control of an air carrier established under the laws of the United States).

117. *See* Arms Export Control Act, 22 U.S.C. § 2751 (1993) (limiting foreign access to U.S. military weapons technology by limiting the source of weapons financing where the sale of weapons would be inconsistent with U.S. foreign policy). *See also* Dep't of Defense Directive 5220.22-R, § 2-102(a) (noneligibility for security clearances for facilities which are under foreign ownership or control), cited in Hanson, *supra* note 34, at 665.

The level of FDI may further be prohibited or eliminated by the antitrust laws where it is perceived to interfere with free economic competition.¹¹⁸ The potentially useful antitrust laws include the Sherman Act of 1890,¹¹⁹ section 7 of the Clayton Act of 1914,¹²⁰ and section 5 of the Federal Trade Commission Act (FTCA).¹²¹ As interpreted by the courts, the antitrust laws provide a good first-line defense against harmful FDI where market destabilization would occur. Enforcement of the antitrust law provisions is vested primarily in the Antitrust Division of the Justice Department and additionally in the Federal Trade Commission.¹²² State officials and private citizens, however, need not rely on federal enforcement of the antitrust laws. By federal statute, states have the authority to enforce both state and federal antitrust provisions.¹²³

118. Antitrust laws are designed to promote a vigorous competitive economy in which each business enterprise has an opportunity to compete on the basis of price, quality, and service. See *Northern Pac. Ry. v. United States*, 356 U.S. 1, 4-5 (1958).

119. 15 U.S.C. §§ 1-7 (1993). The Sherman Act prevents the aggregation of economic power and promotes competition through two main prohibitions: (1) "Every contract, combination in the form of a trust or otherwise, or conspiracy, in the restraint of trade or commerce among the several States or with foreign nations is hereby declared to be illegal." 15 U.S.C. § 1 (1993). (2) "Every person who shall monopolize or attempt to monopolize or combine or conspire with any other person or persons to monopolize any part of trade or commerce among the several States or with foreign nations, shall be deemed guilty of a felony." *Id.* § 2.

The Sherman Act prohibitions are almost unconstitutionally broad in their language and applications. Thus, the Act can be used by the U.S. government to prohibit any particular FDI if it would lead to further monopolization of a given market. In order to make a successful case that a particular FDI would lead to further monopolization of the relevant market, the government would have to demonstrate the following prima facie elements: (1) the investment will result in possession of monopoly power in the relevant market, as defined by either the cross-elasticity of demand, the cross-elasticity of supply, or reasonable interchangeability of the relevant market goods; and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product. See *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966); *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391 (1956).

120. 15 U.S.C. § 18 (1993). This section prohibits mergers, joint ventures, consolidations, or acquisitions of stock or assets where the effect may be to substantially lessen competition. To prohibit FDI under section 7, the U.S. government is required to define and substantiate the relevant product and geographic markets and then show that the particular foreign investment would likely substantially lessen competition in that particular market. There is no specific definition of what "substantially lessen" means, but if competition has been substantially lessened, a court can require divestiture. See *RSR Corp. v. F.T.C.*, 602 F.2d 1317 (1979).

121. 15 U.S.C. § 45(a)(1) (1993). First, the FTCA prohibits all "unfair methods of competition." *Id.* This prohibition has been interpreted by the U.S. Supreme Court to encompass not only Sherman Act violations but also restraints of trade contrary to the spirit of the antitrust laws. See *F.T.C. v. Brown Shoe Co.*, 384 U.S. 316 (1966). Second, the FTCA prohibits "unfair or deceptive acts or practices," prohibiting representations that are unfair to consumers. See *F.T.C. v. Sperry & Hutchinson Co.*, 405 U.S. 233 (1972). Included within the scope of the FTCA are prohibitions against misrepresenting the origin of the product. *Id.* Thus, foreign persons who do not manufacture goods in the U.S. cannot use the "Made in the U.S.A." label.

122. 15 U.S.C. § 45 (c) (1993).

123. *Id.* § 15(a). Additionally, section 4 of the Clayton Act provides that "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue . . . and shall recover three fold damages." *Id.* This provision authorizes the recovery of treble damages against any foreign government when it is acting in a commercial capacity. See *Pfizer, Inc. v. Government of India*, 434 U.S. 308 (1978).

The securities laws may also be used to limit or curtail FDI in the United States where such investment would violate the following basic economic protections: (1) safeguarding the economy from the operation of the securities sector, and (2) providing adequate disclosure of both the issuer and the purchaser of the securities.¹²⁴ The Securities Act of 1933¹²⁵ requires all entities, foreign or domestic, issuing stock or reissuing a controlling block of stock to file a registration statement which includes the name of the issuer, state or sovereign power under which the issuer is organized, and the names and addresses of all persons owning more than ten percent of any stock class.¹²⁶ Those foreign entities who do not fully comply with the registration requirements risk having their FDI activity halted by the issuance of a stop order by the Securities and Exchange Commission.¹²⁷

The Securities Exchange Act of 1934¹²⁸ can also be used to restrict FDI. The 1934 Act heavily regulates the proxy gathering process, which can be a method to prohibit foreign entities from secretly gaining control of both sensitive and nonsensitive business entities.¹²⁹ Congress amended the 1934 Act with the enactment of the Domestic and Foreign Investment Improved Disclosure Act of 1977.¹³⁰ As part of an effort to monitor the frequency of large stock purchases, the 1934 Act, as amended, requires foreign investors holding more than five percent of any class of stock to comply with increased disclosure requirements.¹³¹ These requirements include the disclosure of nationality¹³² and the magnitude of the interest held.¹³³ Thus, the 1933 and 1934 Acts allow the U.S. government to closely monitor FDI flows as they relate to the purchase and sale of securities.

The Export Administration Act of 1979¹³⁴ can also be used to curtail FDI in the United States. Under the Act, the President may eliminate or curtail exports from the United States if: (1) national security is threatened, (2) there is an excessive drain of resources, (3) there is serious domestic inflationary pressure as a result of foreign demand, or (4) controls are necessary to further foreign policy objectives.¹³⁵ This Act can control future FDI where the intended recipient of the FDI is controlled by a foreign person operating within the United States and is exporting items such as military information or hardware, natural resources, or energy.¹³⁶

124. See LOUIS LOSS, *FUNDAMENTALS OF SECURITIES REGULATION* (1988) (discussing securities disclosures).

125. 15 U.S.C. §§ 77a-77aa (1993) [hereinafter 1933 Act].

126. *Id.* § 77aa.

127. *Id.* § 77h-1.

128. 15 U.S.C. §§ 77b-77kkk (1993) [hereinafter 1934 Act].

129. *Id.* § 78n(d).

130. *Id.* §§ 78m(d), (e), (h); *id.* § 78o.

131. *Id.*

132. *Id.* § 78m(h)(1).

133. *Id.* § 78m(f)(1)(a).

134. 50 U.S.C. app. §§ 2401-20 (1993).

135. *Id.*

136. See *The Adequacy of the Federal Response to Foreign Investment in the United States*, House Committee on Government Operations, H.R. REP. NO. 1216, 96th Cong., 2nd Sess. 133-34 (1980) [hereinafter *Adequacy Hearings*].

Additionally, under the International Emergency Economic Powers Act,¹³⁷ the President has the authority to act upon any transaction involving property which is owned or will be immediately owned by foreign investors. Included within the Act are the powers to stop foreign acquisitions and expropriate private property, subject to the constitutional requirement of just compensation. Although the powers under this Act are extremely broad, the President must declare a national emergency in order to invoke any of its provisions.¹³⁸

B. Direct FDI Controls Prior to Exon-Florio

Direct controls target FDI specifically. Their objective is to channel FDI away from or selectively prohibit FDI above a certain level in certain sensitive, domestic economic sectors by imposing reporting and monitoring requirements on foreign investors. By the mid-1970s, Congress had become increasingly aware of the relatively large increase in FDI in the United States and was concerned that statistical data used to track the existing scope of FDI and to formulate future foreign investment policy was unavailable. Congress responded by enacting the Foreign Investment Study Act of 1974 (FISA).¹³⁹ The conclusion of this study was that the United States had inadequate data collection procedures and therefore was unable to formulate a coherent foreign investment policy.¹⁴⁰ With the amount of foreign investment increasing rapidly during the early 1970s, both the legislature and the executive branches began to review the possible foreign policy implications of uncontrolled FDI flows.¹⁴¹

On May 9, 1975, President Ford issued Executive Order 11,858 establishing the Committee on Foreign Investment in the United States (CFIUS).¹⁴² The language of Executive Order 11,858 gives CFIUS the continuing responsibility for monitoring the impacts of FDI and foreign portfolio investments in the United States and coordinating the implementation of U.S. policy on these investments. To fulfill the responsibilities given to CFIUS, the Committee was directed to analyze trends in foreign investment, arrange for advance consultations with foreign governments seeking to invest in the United States, review proposed direct investments which might have major national

137. 50 U.S.C. §§ 1701-06 (1993).

138. See *Adequacy Hearings*, *supra* note 136, at 134.

139. Pub. L. No. 93-479, 88 Stat. 1450 (1974). Under FISA, the Secretary of Commerce and the Secretary of the Treasury were directed to investigate the nature, scope, and magnitude of foreign investment in the United States. *Id.* § 10.

140. Peter T. Butterfield, *Who Owns America? The Adequacy of Foreign Investment Disclosure Requirements*, 24 COLUM. J.L. & SOC. PROBS. 79, 83 (1990).

141. Hanson, *supra* note 34, at 668.

142. Exec. Order No. 11,858, 40 Fed. Reg. 20,263 (1975). CFIUS is chaired by the Treasury Department and includes Assistant Secretary or higher membership from the Departments of Defense, Commerce, State, the United States Trade Representative, and the Council of Economic Advisors. Other entities that have subsequently joined CFIUS include the Attorney General and the Director of Management and Budget. See generally Thomas W. Hoseman, Comment, *International Law—The Exon-Florio Amendment to the 1988 Trade Bill: A Guardian of National Security or a Protectionist Weapon*, 15 J. CORP. L. 597, 602-03 (1990).

interest implications, and consider proposals for new legislation or regulations relating to foreign investment.¹⁴³

To provide access to foreign investment data necessary to develop a coherent FDI policy, Congress enacted the International Investment and Trade in Services Act of 1976 (IITSA).¹⁴⁴ When enacting the Agricultural Foreign Investment Disclosure Act of 1978 (AFIDA),¹⁴⁵ Congress began to focus its attention on exactly which economic sectors were receiving FDI. Congress subsequently set forth two additional acts to determine the scope of FDI in the United States: the Foreign Investment in Real Property Tax Act

143. *Id.* See generally *infra* notes 197-228 and accompanying text (discussing CFIUS in connection with the Exon-Florio provisions).

144. 22 U.S.C. §§ 3101-08 (1993). The accompanying regulations to this Act are found in 15 C.F.R. § 806.15 (1991). Under IITSA, Congress defined both direct and portfolio investment (the two components of total foreign investment in the U.S.) and authorized the President to collect limited amounts of foreign investment data. *Id.* Portfolio investment is defined as "any international investment which is not direct investment." 22 U.S.C. § 3102(11) (1993). Examples of portfolio investments are the purchase by foreign persons of: U.S. Treasury securities, corporate bonds, or corporate stocks where less than 10% of the total amount of stock is held. FDI is defined by IITSA as: "[T]he ownership or control, directly or indirectly, by one foreign person of 10 per centum or more of the voting securities of an incorporated business enterprise or an equivalent in an unincorporated U.S. business enterprise, including a branch." 15 C.F.R. § 806.15(a)(1) (1993).

Included within the definition of FDI are joint American-foreign ventures, the construction and establishment of a wholly owned foreign subsidiary or the acquisition of an existing domestic facility by a foreign person. Examples of recent foreign investment which are classified as direct include the November 1989 purchase of Columbia Pictures by Sony Corporation, the January 1988 purchase of CBS Records by Sony, and the May 1988 purchase of Firestone Tires by Bridgestone. See Richard Turner, *Matsushita to Buy MCA for \$6.59 Billion, Largest U.S. Purchase by a Japanese Firm*, WALL ST. J., Nov. 27, 1990, at A3.

Under the statutory definition of FDI, the annual flow of FDI into the United States increased from \$0.33 billion in 1950 to \$11.99 billion by 1979, an annual increase of 13.69%. See GLOBAL TRENDS, *supra* note 3, at 119 (the percentage increase in the flow of FDI was calculated by the authors). The net book value of the FDI stock existing in the United States increased from \$3.39 billion in 1950 to \$54.46 billion by 1979, an annual increase of 10.42%. *Id.* (percentage increase in the stock of FDI was calculated by the authors). Notwithstanding these dramatic yearly increases in both the stock and flow of FDI, Congress and the American public remained relatively unconcerned about growth in foreign direct investment. This attitude was due in part to the fact that, in 1979, the United States was still the predominant world economic power and a net supplier of FDI to the rest of the world. In 1979, the United States had \$187.86 billion in FDI's abroad compared to the \$54.46 billion of FDI's in the United States. *Id.* at 107, 119.

145. 7 U.S.C. §§ 3501-08 (1993). AFIDA requires foreign persons who acquire, dispose of, or hold an interest in agricultural land to disclose all transactions and holdings to the U.S. Secretary of Agriculture. Agricultural land is defined as "land in the United States currently used for, or, if currently idle, land last used within the past five years, for farming, ranching, forestry, timber production, except land not exceeding ten acres in the aggregate if the annual gross receipts from the sale of the farm, ranch, forestry, or timber products produced thereon do not exceed \$1,000." 7 C.F.R. § 781.2(b) (1993). While AFIDA does not in any way control the scope or magnitude of future FDI, it does provide useful information from which policy analysts can evaluate the impact of FDI on the agricultural sector and on the aggregate economy.

(FIRPTA)¹⁴⁶ in 1980 and the International Trade and Investment Act of 1984 (ITIA).¹⁴⁷

The various direct FDI laws passed by Congress, as well as Executive Order 11,858,¹⁴⁸ do not provide the necessary investment scope prohibitions, or level controls to manage the course of future FDI flows. These laws merely provide a structure for data collection, which is essential in developing a meaningful FDI policy. Like the securities laws, export control laws are only marginally useful in controlling the scope and magnitude of future FDI. Only the International Emergency Economic Powers Act¹⁴⁹ and the antitrust acts¹⁵⁰ provide even a modicum of protection.

The existing legal structure does not, however, provide adequate protection against particular FDIs, which may compromise a narrower and more traditional definition of national security.¹⁵¹ For example, FDI in a company producing computer chips would

146. 26 U.S.C. § 6039C (1993). Under FIRPTA, any foreign person whose "real property interest" in the United States has a fair market value in excess of \$50,000 at any time during the calendar year must file a return setting forth their name and address and a description of the real property interest held. *Id.*

147. Pub L. No. 98-573, 98 Stat. 2948 (1984) (codified in scattered sections of 19 U.S.C.). The purpose of ITIA, as applied to FDI, is to enhance the free flow of U.S. direct investment abroad through the negotiation of trade agreements which reduce or eliminate trade distortion effects of investment-related measures. Specifically, ITIA requires the U.S. Trade Representative to identify and analyze trade barriers related to performance requirements and authorizes the U.S. Trade Representative to impose import duties as a negotiation tactic. GLOBAL TRENDS, *supra* note 3, at 155. ITIA assists FDI in the U.S. by removing trade barriers which foreign countries may impose on external investment.

148. Exec. Order No. 11,858, 40 Fed. Reg. 20,263 (1975).

149. See notes 136-38 and accompanying text. Under the International Emergency Economic Powers Act, the President has a wide array of powers which could be used to completely control any property in the United States which is, or will immediately be, owned by foreign investors. However, these vast powers are only available if the President declares a national state of emergency. This would naturally include the power to stop an acquisition, to condemn and expropriate (subject to the payment of just compensation under the Fifth Amendment to the U.S. Constitution), and to require priority defense production or other uses. See *Adequacy Hearings*, *supra* note 136, at 134.

150. See *supra* notes 118-23 and accompanying text. The antitrust acts provide significant protection against both the scope and magnitude of a particular FDI where such an investment could negatively impact market competition. The Sherman Act could be used to limit or prohibit the sale of Japanese-made consumer goods if the sales were made at below hard cost, if such sales tended to restrain future trade in particular consumer goods in a particular geographic area by driving current competitors out of business, or establishing cost-based barriers to entry by future competitors. More than 15 "blocking" statutes designed to impede the extraterritorial application of U.S. antitrust laws have been enacted by major trading partners of the United States such as Canada, England, and Germany. See Joseph P. Griffin, *United States Antitrust Laws and Transnational Business Transactions: An Introduction*, 21 INT'L LAW. 307, 308-09 (1987). Thus, notwithstanding problems associated with the extraterritorial application of the antitrust laws, these laws are a powerful weapon to protect the economic security component of U.S. national security by allowing for the control of those FDIs that might cause further concentration of market power. While there is no standard definition, economic security is a broad concept often included within the traditional concept of national security. See *infra* note 151 (discussing the sanctioned definition of national security).

151. "National security" is defined as "the national defense or foreign relations of the United States." 50 U.S.C. § 401, Exec. Order No. 12,356, pt. 6, § 6.1 (1993). The factors to consider in determining if a particular FDI involves a national security threat are: (1) domestic production needed for projected national defense requirements; (2) the capability and capacity of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services; and (3) the control of domestic industries and commercial activities by foreign citizens as it affects the capability and capacity of the United States to meet the requirements of national security.

not be prohibited by the antitrust laws unless the investment would “substantially lessen” competition in the computer chip market. Control of this technology by companies clearly answerable solely to the U.S. government is essential in order to maintain future military superiority. Therefore, the Exon-Florio Amendment is a necessary control over future FDI in economic sectors with traditional national security significance.

C. Exon-Florio Amendment

The cost-benefit discussion of increased FDI contained in Part IV¹⁵² leads to the conclusion that the benefits of increased FDI likely outweigh its costs. This suggests that special interest group politics rather than economics are behind the lobbying effort to restrict both the stock and flow of future FDI. However, Congress in recent years has become increasingly worried that the existing structure of antitrust, securities, and emergency powers laws is inadequate to stem the loss of high-technology, and, should the trend continue, national security may be breached by United States’ reliance on foreign sources for military technology and hardware.

To curb these trade worries, Congress included the Exon-Florio Amendment in the Omnibus Trade and Competitiveness Act of 1988, amending title VII, section 721 of the Defense Production Act of 1950.¹⁵³ Because the Exon-Florio Amendment was meant to bridge the statutory gap left by the previous legislative or regulatory scheme, the remainder of this section closely evaluates the political process surrounding passage of the Exon-Florio Amendment, its specific provisions, and the implementing regulations that the Department of the Treasury (Treasury) has promulgated.

1. The Setting

From the end of World War II until the late 1970s, the United States had almost unrestricted openness to FDI. During this period, U.S.-based MNEs stood as dominant leaders of world FDI.¹⁵⁴ Beginning in the early 1980s, U.S. dominance began to fade due to increasing international competition and heightened levels of congressional economic mismanagement, which resulted in a growing trade deficit problem.¹⁵⁵ During this period, the annual trade deficit grew from \$25.5 billion in 1980 to a staggering \$159 billion in 1987; in 1992, the last year for which complete statistics are available, the trade deficit decreased to \$96.3 billion as the U.S. economy weakened.¹⁵⁶

See Defense Production Act of 1950, *Id.* app. § 2170(e) & (f) (1993) (describing national security threat).

152. See *supra* notes 78-108 and accompanying text (discussing the theoretical costs and benefits associated with growth in FDI in the United States).

153. 50 U.S.C. app. § 2170 (1993).

154. See *supra* notes 42-45 and accompanying text (discussing the U.S. share of the global FDI market).

155. A simplified analysis of the correlation between the trade and budget deficits completed by this author produced a correlation coefficient of 0.7303, which provides evidence that up to 73.03% of the trade deficit is a direct result of the U.S. domestic budget deficit (analysis by authors). The money flowing into foreign hands as a result of the budget deficit is being recycled into the purchase of U.S. defense-related companies. See generally 135 CONG. REC. H903 (daily ed., Apr. 3, 1989) (citing SCHWARTZ, JOHNS HOPKINS FOREIGN POL’Y INST., FOREIGN OWNERSHIP IN DEFENSE RELATED COMPANIES (Feb. 1989)).

156. *Current Business*, *supra* note 5 (1990-93 various issues).

With pessimistic trade deficit news repeated monthly, there was a general feeling on Capitol Hill that something must be done to reduce the massive red ink. Acting on this general sentiment, Senator John Danforth (R-Mo.) initiated hearings in 1981 which eventually generated the 1984 Trade and Tariff Act.¹⁵⁷ Debate over this Act eventually played an important role in the development of various sections of the Omnibus Trade and Competitiveness Act of 1988.¹⁵⁸

While downplaying the importance of the federal budget deficit as a determinant of the U.S. trade deficit, many in Congress favored the "leveling of the export playing field" as a solution to the trade deficit crisis.¹⁵⁹ These congresspeople pointed to the increasing FDI flows and foreign trade barriers erected by many trading partners of the U.S. as the source of the trade deficit crisis.¹⁶⁰ Support for their position came from a 1984 report compiled by the U.S. Trade Representative, who listed some 300 pages of foreign trade barriers faced by U.S. exporters.¹⁶¹ Nearly thirty pages of the trade restrictions were imposed by Japan, the source of nearly thirty-three percent of the trade deficit problems in 1984.¹⁶²

The General Accounting Office (GAO), in a 1987 study on the effects of trade restrictions on the trade deficit, took the wind from the sails of this theory. The GAO study concluded that these overt trade barriers accounted for only a negligible percentage of the trade deficit.¹⁶³ As for the politically charged trade deficit with Japan, the study concluded that if the trade barriers were completely removed, exports to Japan would increase by \$5 billion to \$8 billion, an amount far short of closing the 1987 \$66.57 billion trade deficit with Japan.¹⁶⁴ The results of this GAO report clearly demonstrate that the trade deficit problem lies squarely on the shoulders of Congress.

As the 1980s progressed and Congress was unable or unwilling to deal with the domestic budget and trade deficits, public pressure for a reassessment of the U.S. open-door policy to FDI increased. This increased pressure resulted from U.S. citizens fearing that funds transferred to Japan, as a result of the trade deficit, would now return to the in

157. Trade & Tariff Act of 1984 (Update of 1974 Act), 19 U.S.C. §§ 2101 *et seq.* (1993).

158. Steven R. Phillips, *The New Section 301 of the Omnibus Trade and Competitiveness Act of 1988: Trade Wars or Open Markets?*, 22 VAND. J. TRANSNAT'L L. 491, 496 (1989).

159. An example of the actions taken by those Congressmen who were proponents of the level playing field theory was the introduction of the Reciprocal Trade and Investment Act of 1982. See 128 CONG. REC. S678 (daily ed. Feb. 10, 1982).

160. *Id.*

161. Phillips, *supra* note 158, at 500 (citing OFFICE OF THE U.S. TRADE REPRESENTATIVE, REPORT TO CONGRESS ON FOREIGN TRADE BARRIERS, 1986 NATIONAL TRADE ESTIMATES 171-93 (1986)). In addition to Japan's overt trade protectionism, member states of the European Common Market and many of the lesser developed countries have erected reciprocal trading requirements, which decreased the amount of U.S. exports that could be used to offset the U.S. trade deficit with Japan. S.L. GORDON & F.A. LEES, FOREIGN MULTINATIONAL INVESTMENT IN THE UNITED STATES 10-13 (1986). The most often used restrictions are: (1) local content requirements, (2) restriction on FDI in certain sectors of the economy, (3) limits on foreign acquisition of domestic firms, (4) limits on the size of new foreign investment projects, (5) local equity participation requirements, (6) limits on profit repatriation, and (7) limits on local borrowing. *Id.*

162. Phillips, *supra* note 158, at 500.

163. GENERAL ACCOUNTING OFFICE, THE U.S. TRADE DEFICIT: CAUSES AND POLICY OPTIONS FOR SOLUTIONS 28-29 (1987).

164. *Id.*

United States the form of U.S. asset purchases.¹⁶⁵ Publicity of foreign takeovers of U.S. industries fueled both citizen and Congressional pressure. In particular, the hearings before the House and Senate during the two years prior to passage of the final version of Exon-Florio excitedly discussed the following proposed takeovers: (1) the takeover of Newmont Mining, the largest U.S. gold producer, by Consolidated Gold Fields of Great Britain,¹⁶⁶ (2) the takeover of Fairchild Semiconductor Corporation, a California based chip manufacturer, by Fujitsu Limited of Japan,¹⁶⁷ and (3) the attempted hostile takeover of Goodyear Tire and Rubber Company by Sir James Goldsmith, also of Great Britain.¹⁶⁸

Congress passed the Exon-Florio Amendment based on a perception that the executive branch lacked the authority to prohibit those FDIs that impact the broadly defined notion of national security, but where such investments meet the requirements of the current antitrust and securities laws,¹⁶⁹ and fearing the likely political backlash from a failure to protect the economically important defense, gold, and semiconductor industries.¹⁷⁰

165. *Foreign Direct Investment: Effects on the United States*, Subcommittee on Economic Stabilization of the Committee on Banking, Finance and Urban Affairs, 101st Cong., 1st Sess. at 199 (citing THOMAS, AMERICAN PUBLIC OPINION TOWARDS FOREIGN INVESTMENT).

166. In the case of Newmont Mining, Ivanhoe, a limited partnership involving U.S. citizen T. Boone Pickens, began acquiring Newmont Mining shares in the open market and had extended a tender offer for existing shares. Consolidated Gold Fields, a British concern, and holder of 26.2% of Newmont Mining stock increased its share to 49.7% to block the takeover by Ivanhoe. *Foreign Takeovers and National Security: Hearings Before the House Subcommittee on Commerce, Consumer Protection, and Competitiveness, and Committee on Energy and Commerce*, 100th Cong., 1st Sess. 33 (Oct. 20, 1987) (hearings on Section 905, H.R. 3, House version statement by T. Boone Pickens). Congressional members were of the opinion that the consolidation of a large portion of the free world's gold supply in the hand of one entity may impair national economic security, and that the laws presently in place were ill-equipped to prevent such a national security impairment. *Id.* at 53.

167. The other high profile proposed takeover impacting on the eventual Exon-Florio Amendment language involved Fujitsu, one of Japan's largest computer and chip manufacturers, attempted takeover of American-based (but French-controlled) Fairchild Semiconductor Corporation. Hanson, *supra* note 34, at 670-75. Because of Fairchild's extensive work for the Department of Defense and opposition from the Reagan administration and Congress, CFIUS became involved in the transaction. Because of the Reagan administration opposition, Fujitsu eventually withdrew its proposal to acquire controlling interest in Fairchild. *Id.* However, it was recognized by many in Congress that the law as it existed before the passage of the Exon-Florio Amendment was ill-equipped to block such a takeover in the absence of questionable antitrust implications. *Id.*

168. Goodyear is an important defense contractor and producer of items such as synthetic rubbers, chemicals, adhesives, and fabrics. Prior to the Goldsmith raid, Goodyear also had an aerospace division which produced aircraft and missile hardware. See Hoseman, *supra* note 142, at 599 n.23.

169. See 134 CONG. REC. E905 (daily ed. Mar. 30, 1988). Senator Exon stated:

When I called [the proposed acquisitions of Goodyear Tire and Fairchild Semiconductor] to the attention of the Administration, I was told: "We can't do anything because they're not [sic] violations of the antitrust law. The only way we can do anything is to declare a national emergency and we think that would be overreacting."

Id. See also Wm. Gregory Turner, Comment, *Exon-Florio: The Little Statute that Could Become a Big Headache for Foreign Investors*, 4 TRANSNAT'L LAW. 701, 713 n.62 (1991) (restating Senator Exon's speech).

170. Note that neither the Fairchild nor the Goodyear takeovers were ultimately consummated. Turner, *supra* note 169, at 712-13.

2. The Legislation

The catalyst of the Exon-Florio Amendment emanated from the fear associated with the potential magnitude of future FDI flows into the United States. The Exon-Florio Amendment, which is a single section in title V of the Omnibus Trade and Competitiveness Act of 1988, is contained in section 5021 and amends section 721 of the Defense Production Act of 1950.¹⁷¹ Section 5021 contains eight paragraphs and outlines the following three-step procedure: step 1, a thirty-day phase, is a review stage; step 2, a forty-five-day phase, is an investigation stage; and step 3, a fifteen-day phase, is an intervention stage.

Paragraph (a) delegates to the President, or the President's designee, through a long string of "magic words," the authority to undertake investigations to determine the effects on "national security" of "proposed or pending" mergers, acquisitions, or takeovers "by or with foreign persons which could result in foreign control of persons engaged in interstate commerce in the United States."¹⁷² The exercise of this authority is discretionary rather than mandatory.¹⁷³ If an investigation is warranted, it must commence within thirty days after receipt of written notification of the proposed transaction.¹⁷⁴ The investigation itself must be completed within forty-five days after the notification.¹⁷⁵

Paragraph (c) provides that any information or documentary material filed with the President or designee is exempt from disclosure under the Freedom of Information Act.¹⁷⁶ Neither the information nor the documentary material filed can be made public, except in administrative or judicial proceedings.¹⁷⁷ This prohibition, however, does not prevent disclosure to Congress or its duly authorized committees or subcommittees.¹⁷⁸

Paragraph (d) authorizes certain actions, either by the President or Attorney General. Presidential actions include suspension or prohibition of a transaction of "a person engaged in interstate commerce"¹⁷⁹ by or with "foreign persons"¹⁸⁰ that threatens to impair national security.¹⁸¹ If Presidential action is taken, the decision must be announced within fifteen days after the investigation has been completed.¹⁸² The President or designee also can direct the Attorney General "to seek appropriate relief, including divestment relief" in district courts where necessary.¹⁸³ Under paragraph (d), the actions set out in paragraph (c) can only be taken if the President or designee has made two

171. 50 U.S.C. app. § 2170 (1993).

172. *Id.* § 2170(a).

173. *Id.*

174. *Id.*

175. *Id.*

176. The Freedom of Information Act disclosure requirements are found in 5 U.S.C. § 552 (1993).

177. 50 U.S.C. app. § 2170(c) (1993).

178. *Id.*

179. A United States person is defined as "any person resident in the United States or subject to the jurisdiction of the United States." 22 U.S.C. § 3102(4) (1993).

180. The term foreign person means any person residing outside the United States or subject to the jurisdiction of a country other than the United States. *Id.* § 3102(5) (1993).

181. *Id.* § 2170(d).

182. *Id.*

183. *Id.*

findings.¹⁸⁴ First, a “credible evidence finding” must be made.¹⁸⁵ Second, an “inadequacy finding” must be made.¹⁸⁶ The findings are conjunctive, so both must occur before action can be taken.¹⁸⁷ Additionally, paragraph (e) provides that these findings are not subject to judicial review.¹⁸⁸

Paragraph (f) contains an illustrative list of the factors to be considered in determining whether national security has been impaired.¹⁸⁹

- (1) domestic production needed for projected national defense requirements;
- (2) the capability and capacity of domestic industries to meet national defense requirements, including the availability of human resources, products, technology, materials, and other supplies and services; and
- (3) the control of domestic industries and commercial activities by foreign citizens as it affects the capability and capacity of the United States to meet the requirements of national security.¹⁹⁰

If the President or designee intends to take action under paragraph (d), paragraph (g) requires a written report of the action that the President or designee proposes to take to be filed with the Secretary of the Senate and the Clerk of the House of Representatives.¹⁹¹ The report must include “a detailed explanation of [paragraph (e)] findings.”¹⁹² Paragraph (h) mandates implementing regulations.¹⁹³ They should “minimize paperwork burdens” and “coordinate reporting requirements” under Exon-Florio and other federal laws.¹⁹⁴ Paragraph (i) addresses the question of how the Exon-Florio Amendment affects other laws.¹⁹⁵ This paragraph states that “[n]othing in this section shall be construed to alter or affect any existing power, process, regulation, investigation, enforcement measure, or review provided by any other provision of law.”¹⁹⁶

184. *Id.*

185. *Id.* “There is credible evidence . . . to believe that the foreign interest exercising control might take action that threatens to impair the national security.” *Id.*

186. *Id.* “Provisions of law [other than the International Emergency Economic Powers Act and the Defense Production Act of 1950, as amended,] do not . . . provide adequate and appropriate authority . . . to protect the national security . . .” *Id.*

187. 50 U.S.C. app. § 2170(d) (1993).

188. *Id.* § 2170(e).

189. These factors were briefly mentioned in connection with the discussion of antitrust law protection of national security. See *supra* notes 118-23 and accompanying text (discussing the application of antitrust laws to FDI).

190. 50 U.S.C. app. § 2170(f) (1993).

191. *Id.* § 2170(g).

192. *Id.*

193. *Id.* § 2170(h).

194. *Id.*

195. *Id.* § 2170(i).

196. *Id.*

3. *Developments Between Enactment of the Exon-Florio Amendment and Promulgation of Its Implementing Regulations*

President Reagan designated CFIUS¹⁹⁷ as his designee for purposes of the Exon-Florio Amendment in Executive Order 12,661 on December 27, 1988.¹⁹⁸ When created, CFIUS merely monitored the impact of FDI and coordinated U.S. policy toward FDI. Executive Order 12,661 greatly expanded CFIUS' role.¹⁹⁹ CFIUS had the authority to investigate, implement, and enforce the provisions of the Exon-Florio Amendment, subject to presidential approval.

The Exon-Florio Amendment amended section 721 of the Defense Production Act of 1950. Section 721 contained a sunset provision under which the authority to review foreign investments, pursuant to the Exon-Florio Amendment, lapsed on October 20, 1990.²⁰⁰

When this authority lapsed, the Treasury announced on November 6, 1990, that CFIUS would continue to review new proposed foreign investments on an informal basis under temporary CFIUS criteria in accordance with the original Exon-Florio criteria.²⁰¹ Under the temporary CFIUS criteria, if no agency believed there were national security concerns that warranted further review within thirty days, the parties were advised to proceed with the transaction.²⁰² However, if problems were later discovered, or other aspects of the transaction required additional research, a forty-five-day investigation period was initiated.²⁰³ Even though during the lapse period the President did not have the authority to prohibit the transaction, parties to the transaction still had an incentive, possible future divestment, to cooperate with CFIUS.²⁰⁴

Subsequent to the lapse of Exon-Florio authority, various bills were introduced to strengthen the laws governing foreign investment acquisition. One such bill, H.R. 2642, was the Technology and Preservation Act of 1991.²⁰⁵ H.R. 2642 was offered by Representative Cardiss Collins (D-Ill.) and sponsored by majority leader Richard Gephardt (D-Mo.), among others.²⁰⁶ None of these bills was adopted.

On August 2, 1991, both the House and the Senate approved a conference report on H.R. 991, the Defense Production Act Extension and Amendments of 1991 (DPAEA),

197. See *supra* notes 142-43 (discussing CFIUS as having the continuing responsibility of monitoring the impacts of FDI).

198. 54 Fed. Reg. 779 (1988).

199. Through this executive order, former President Ronald Reagan delegated his investigative authority under Exon-Florio to CFIUS and the Secretary of the Treasury pursuant to § 2170(a).

200. Memorandum of the President, 53 Fed. Reg. 43,999 (1988).

201. See *CFIUS to Continue Reviewing Acquisitions Despite Lapse of Exon-Florio Provision*, 7 Int'l Trade Rep. (BNA) No. 45, at 1739 (Nov. 14, 1990) [hereinafter *Reviewing Despite Lapse*]. The Department of the Treasury made this announcement because the Secretary of the Treasury chairs CFIUS which, as the President's designee under Executive Order 12,661, exercised the Defense Production Act, § 721 authority.

202. Pub. L. No. 88-774, 64 Stat. 798 (1988).

203. *Id.*

204. *Reviewing Despite Lapse*, *supra* note 201, at 1739.

205. *Id.*

206. *Bill Offered to Strengthen Law Governing Foreign Acquisitions*, 8 Int'l Trade Rep. (BNA) No. 25, at 947 (June 19, 1991).

making the Exon-Florio provision permanent.²⁰⁷ President Bush signed DPAA into law on August 17, 1991.²⁰⁸

4. The Implementing Regulations

Since President Reagan designated CFIUS as his designee under the Exon-Florio Amendment,²⁰⁹ and since the Secretary of the Treasury chairs CFIUS,²¹⁰ the U.S. Treasury assumed responsibility for promulgating and implementing regulations under Exon-Florio. Regulations under the Defense Production Act, as amended by Exon-Florio, are exempt from the provisions of the Administrative Procedure Act.²¹¹ Nevertheless, the Treasury decided to use a notice-and-comment approach to the promulgation process, "elect[ing] to do so as a means of soliciting public comment, given the complexity of the subject area covered by the regulations and their potential impact on commerce."²¹² The Treasury published proposed regulations in the Federal Register on July 14, 1989.²¹³ The proposed regulations provided for a sixty-day comment period.²¹⁴ During the sixty-day period, over seventy parties—private and public, domestic and foreign—filed approximately 500 pages of comments.²¹⁵

As a result of suggestions made in the comments and CFIUS' own experience in reviewing FDI since the proposed regulations were published, the Treasury made certain "substantive"²¹⁶ changes before promulgating the final regulations on November 21, 1991.²¹⁷ The second section of the preamble to the final regulations identifies nine major substantive issues that were raised during the public comment period. These are:

- (1) definition of national security;
- (2) scope of coverage;
- (3) definition of foreign control;
- (4) effect on foreign lenders;
- (5) internal fast track mechanism;
- (6) hostile takeovers;
- (7) remedies for material omissions and errors;

207. *Congress Clears Legislation to Make Exon-Florio Permanent*, 8 Int'l Trade Rep. (BNA) No. 32, at 1172 (Aug. 7, 1991).

208. *Bush Signs Defense Measure Making Exon-Florio Permanent*, 8 Int'l Trade Rep. (BNA) No. 34, at 1248 (Aug. 21, 1991).

209. See *supra* notes 142-43, 199 and accompanying text (discussing CFIUS).

210. *Id.*

211. Section 709 of the Defense Production Act (codified at 50 App. U.S.C. § 2159), contains an exemption from the Administrative Procedure Act (APA) (codified at 5 U.S.C., pt. I, ch. 5, subch. II) for functions exercised under the Defense Production Act. Although regulations promulgated under the Defense Production Act need not comply with the APA, they must be accompanied by a statement that industry representatives were consulted in formulating the regulations. *Id.*

212. 56 Fed. Reg. 58,774 (1991).

213. 54 Fed. Reg. 29,744 (1989).

214. *Id.*

215. Defense Production Act, 56 Fed. Reg. 58,774 (1991) (to be codified at 31 C.F.R. pt. 800).

216. *Id.*

217. *Id.*

- (8) CFIUS procedures; and
- (9) "Sunset of Presidential Authority" under section 721 of the Defense Production Act.²¹⁸

Other changes, which were characterized as "technical,"²¹⁹ included clarifications of terms and changes in format,²²⁰ and may be found in the third section of the preamble of the final regulations.²²¹

The final regulations consist of seven subparts, lettered A through G. Subpart A contains general provisions addressing questions of scope, the effect of the Exon-Florio Amendment and its implementing regulations on other laws, prior acquisitions, and transactions or devices used to avoid the Exon-Florio Amendment and its promulgated regulations.²²² Twenty-one different terms or concepts are defined in subpart B.²²³ The definitional subpart is as important for those terms that are not defined as for those that are defined. Subpart C speaks to the issue of coverage.²²⁴ Lending transactions are dealt with separately. All other transactions either are or are not section 721 transactions. Actions by CFIUS are covered by subparts D and E.²²⁵ Subpart D discusses notice provisions, while subpart E outlines the procedures CFIUS will use in reviewing and investigating transactions.²²⁶ Presidential action is covered by subpart F.²²⁷ Subpart G states that parties have an obligation to provide information and imposes a duty of confidentiality.²²⁸

VI. ANALYSIS

A. Introduction

It appears that the intent of Congress in passing the Exon-Florio Amendment was not to impose additional barriers to FDI flows unless there was clear interference with national security concerns.²²⁹ Given this legislative intent, proposed and final regulations were developed by the Treasury to implement Exon-Florio. The proposed regulations provided for a system of voluntary notice by any or all parties to a proposed transaction.²³⁰ Pursuant to paragraph (g) of the Exon-Florio Amendment, the Department

218. See 56 Fed. Reg. 58,774-78 (1991) (discussing the second section of the preamble to the final regulations).

219. 56 Fed. Reg. 58,774 (1991).

220. *Id.*

221. See 56 Fed. Reg. 58,778-80 (1991) (discussing the third section of the preamble to the final regulations).

222. *Id.* subpart (a).

223. *Id.* subpart (b).

224. *Id.* subpart (c).

225. *Id.* subparts (d) & (e).

226. *Id.* subpart (d).

227. *Id.* subpart (f).

228. *Id.* subpart (g).

229. S. REP. NO. 80, 100th Cong., 1st Sess. 25 (1987). However, as discussed below, the term "national security" was not defined and has various meanings based on ideological points of view.

230. 54 Fed. Reg. 29,748 (1989).

of the Treasury published a proposed set of regulations with a request for public comment.²³¹ The proposed regulations contain seven topical areas forwarded to the public with the intent to clarify and implement the Exon-Florio Amendment as passed by Congress. The topical areas include: definitions, coverage, notice, CFIUS committee procedures, confidentiality, and presidential actions.²³²

In response to a Federal Register request for public comments to the proposed Exon-Florio regulations, the Department of the Treasury, Office of International Investment received forty-seven written comments.²³³ From these responses, a statistical sample of twenty-one responses was selected to determine the problems existing in the proposed regulations. The results of the sample analysis are provided in table 5.

TABLE 5
PROBLEMS WITH THE LANGUAGE OF THE EXON-FLORIO REGULATIONS²³⁴

<u>Problem Cited</u>	<u>Percent of Sample Citing Problem</u>
Definition of National Security	61.9%
Definition of Control	57.1
Scope of Items Covered	52.4
Coverage of Small Investments	52.4
Nature and Scope of Materials to be Submitted to CFIUS	33.3

B. Existing Problems

The remainder of this section discusses the major Exon-Florio Amendment problems as identified through a review of the submitted public comments and through CFIUS response to those comments in the final regulations.²³⁵

1. Defining "National Security"

"National security" is defined as the national defense or foreign relations of the United States.²³⁶ Neither the 1988 conference report, the proposed regulations, nor the Exon-Florio Amendment itself define national security.²³⁷ The Conferees' explanation

231. 54 Fed. Reg. 29,744-49 (1989).

232. *Id.*

233. These comments are on record at the Department of Treasury, and the statistical sample is a product of the authors' independent research.

234. OFFICE OF INT'L INV., DEP'T OF TREASURY, PUBLIC COMMENTS ON THE PROPOSED EXON-FLORIO REGULATIONS (1989). The percentages were generated by the authors.

235. The final regulations were published in 56 Fed. Reg. 58,774-88 (1991) (to be codified at 31 C.F.R. pt. 800).

236. *See supra* note 151 and accompanying text (defining national security).

237. 54 Fed. Reg. 29,744 (1989). *See* H.R. Conf. Rep. No. 576, 100th Cong., 2d Sess. 924-25 (1988) [hereinafter House Report] (discussing the scope of and areas of concern of the Exon-Florio Amendment).

for the obvious oversight is that the term is to be broadly interpreted.²³⁸ According to the legislative history of the Senate version of the Exon-Florio Amendment, the standard for determining whether a particular FDI involves national security is whether “essential commerce” is affected.²³⁹ Although the “essential commerce” language was later deleted and replaced with broad policy factors, these factors can be interpreted in such a way as to encompass all forms of economic security²⁴⁰ and to allow any U.S. business entity who is the target of a potential foreign takeover to approach CFIUS and request the initiation of a national security-based investigation. According to testimony given before Congress, defining national security in such broad terms would be a giant step backward by placing the government in the position of reviewing every marketplace transaction.²⁴¹

In the final regulations issued on November 21, 1991, CFIUS found it imprudent to further define national security, despite that over sixty-one percent of those responding to the proposed regulations identified the lack of such a definition as a problem.²⁴² CFIUS rejected all proposed definitions of national security found in the comments to the proposed regulations because “they could improperly curtail the President’s broad authority to protect the national security.”²⁴³

2. Defining “Control”

While no specific definition of “control” was provided in the legislative history of either the House, Senate, or the final version of the Exon-Florio Amendment, section 800.213 of the proposed regulations attempt to partially correct this oversight by focusing the test of control on whether the power exists to “formulate, determine, direct, or decide important matters relating to the entity.”²⁴⁴ Under this definition, control could be exercised by significant stock ownership, contractual arrangements, or other means. This overly broad definition of control presents a wide array of problems both for those foreign firms wishing to invest in the United States, but not wishing to be exposed to the possibility of post investment divestiture, and for persons working in the securities industry within the United States who are now bombarded with a new concept of control,

238. House Report, *supra* note 237, at 926.

239. See 54 Fed. Reg. 29,744 (1989). See also House Report, *supra* note 237, at 926 (discussing the scope of the Exon-Florio Amendment).

240. See *supra* note 151 and accompanying text (defining national security). See also *Foreign Acquisitions and National Security: Hearings Before the Subcommittee on Commerce, Consumer Protection, and Competitiveness of the House Committee on Energy and Commerce*, 101st Cong., 2d Sess. 16 (1990) (statement of Michael Skarzynski: “national security . . . is ultimately dependent upon economic security”).

241. *Acquisitions by Foreign Companies, Hearings Before the Senate Committee on Commerce, Science and Transportation*, 100th Cong., 1st Sess. 9 (1987).

242. This sampling is a product of the authors’ independent research.

243. 56 Fed. Reg. 58,775 (1991).

244. 54 Fed. Reg. 27,744 & 29,751 (1989). The term “formulation” was dropped from the final published regulations in an attempt to provide some level of clarification. 56 Fed. Reg. 58,778 (1991).

different from that implicitly utilized in the Securities Act of 1933²⁴⁵ and in the Securities Exchange Act of 1934.²⁴⁶

The broad definition of control under the Exon-Florio provisions creates additional problems because of the varying forms of foreign investment. If the investment is purely one of the purchase of stock (portfolio investment), each share of preferred stock contains voting rights which by definition would give the foreign investor some measure of control such that he may fall within the power of the Exon-Florio Amendment.²⁴⁷ It is not clear if portfolio investments are intended to be covered by Exon-Florio, or if only those direct investments in which operational management is or could be exercised by the foreign investor are covered. Finally, it is not clear from the Amendment how control by foreign persons is to be measured.²⁴⁸ If unaffiliated foreign investors in aggregation have purchased sufficient shares in the company to have a controlling interest, is there control? Or must the investors act in concert in the purchase of stock to be within the realm of the Exon-Florio Amendment?

In the final regulations, CFIUS noted that it would be inappropriate for control to be defined by a bright-line test such as a particular stock ownership percentage or the nature of the composition of the board of directors.²⁴⁹ CFIUS did, however, clarify some of the ambiguities in the control standard by conforming more closely to the definition found in the Investment Company Act of 1940.²⁵⁰ The definition of control has been modified with the addition of section 800.204(b) to clarify that a U.S. business entity will not automatically be deemed to be under foreign control when a number of unrelated foreign investors hold an interest in the U.S. business entity.²⁵¹

3. Defining "Material Information"

The fifth item on the list of identified problems with the Exon-Florio proposed regulations concerns the breadth of the information which must be "voluntarily" supplied by the parties to a transaction in order to avoid the possibility of a post-investment divestiture.²⁵² Several reasons support a clarification of what is "material" evidence and who can provide it. First, without a clear definition of the information required for

245. 15 U.S.C. §§ 77a-77aa (1993).

246. *Id.* §§ 77b-77kkk. In neither the Securities Act of 1933 nor the Securities Exchange Act of 1934 is "control" explicitly defined. However, in the related Investment Company Act of 1940, control is defined as "the power to exercise a controlling influence over the management or policies of a company, unless such power is solely the result of an official position with such company." *Id.* § 80a-2(9).

247. 50 U.S.C. app. § 2170(b) (1993).

248. A definition of control which has no specific guidelines allows for a flexible application of a particular statute at the cost of increasing uncertainty. One definition of control which may be useful to regulators is the definition of "direct investment" found in the International Investment and Trade in Services Act of 1976, 22 U.S.C. § 3102(10) (1993). *See supra* note 144 (defining control under this Act).

249. 56 Fed. Reg. 58,776 (1991).

250. *See supra* note 246 (defining control under the Investment Company Act of 1940).

251. 56 Fed. Reg. 58,778 (1991).

252. The term voluntary is used in the proposed regulations at § 800.401. The term, however, is a misnomer because persons who do not supply information for a CFIUS review risk divestiture. *See* 54 Fed. Reg. 29,748 (1989). Any person, including nonparties, to a proposed investment transaction may contact CFIUS and supply information. *Id.*

approval of a given FDI, the process could be used by a third person interested in stopping a particular FDI or even future Democratic administrations as a bureaucratic weapon or protectionist device to slow future FDI.²⁵³ This prediction could materialize because many investment decisions have a short window of feasibility, and the interference by marginally affected or unaffected parties may stop the investment opportunity. Second, without a provision for financial sanctions against third parties who provide CFIUS with false or misleading information, third party competitors will have the opportunity to inflict oppressive burdens of proof on the parties to the proposed foreign investment as they try to undo the damage caused by the false or misleading statements. Finally, without informational guidelines, the review process will obviously become slow and more burdensome, thus increasing the possibility that the system could be used as a takeover defense and further reduce FDI.

In the final regulations, in response to public comments that CFIUS should adopt a more narrow definition of material, CFIUS did not directly discuss the issue of what information is material to the CFIUS review or investigation. CFIUS did, however, discuss procedures to be implemented in the case of a material omission²⁵⁴ and procedures for handling unsolicited information from third parties.²⁵⁵ On the issue of omissions, CFIUS did not accept public suggestions that an investment review only be reopened if a party deliberately withheld material information.²⁵⁶ On the issue of handling third party unsolicited communications, CFIUS did recognize that there was a problem and directed that such communications should be given to CFIUS itself or to a designated member, rather than to individual members, in order to avoid confusion.²⁵⁷

4. The Scope of the Amendment's Coverage

The third and fourth most cited problems with the proposed Exon-Florio regulations concern the Amendment's coverage of nonmilitary items, small dollar investments, and joint ventures.²⁵⁸ While reasons for the coverage of some of these items were suspect at best, reasons for the exclusion of these items depended on the individual business perspective from which comments were made. The one clear theme from the public comments supplied to the Department of Commerce by law firms, foreign multinational corporations, domestic multinational corporations, and trade associations, is that more attention should have been paid by the drafters of the Amendment to limiting its potential scope.²⁵⁹ Each time uncertainty creeps into the investment decision process of a foreign entity, aggregate FDI declines. A decline in capital investment from whatever source reduces the marginal product of labor and real wage rates.

253. See Hoseman, *supra* note 168, at 611.

254. 56 Fed. Reg. 58,777 (1991).

255. *Id.*

256. *Id.*

257. *Id.*

258. Coverage is discussed in the proposed regulations at § 800.301. See 54 Fed. Reg. 29,747 (1989).

259. This is a conclusion drawn from the authors' independent sampling of concerns expressed by those responding to the Federal Register's request for public comments regarding the proposed Exon-Florio Amendment. See *supra* notes 78-108 and accompanying text.

In the portion of the final regulations pertaining to Exon-Florio coverage, CFIUS recognized that many of the public comments suggested a minimum dollar threshold or some other bright-line test established which proposed foreign investments would not be reviewed by CFIUS.²⁶⁰ In response to these suggestions, CFIUS found it inappropriate to establish such criteria because even a very small transaction could have a meaningful impact on national security.²⁶¹

C. Potential Problems

The costs associated with increased FDI²⁶² include the following categories: national security, future employment, capital dependence, and technology transfer.²⁶³ Each of these four cost categories is revisited below to determine what effect, if any, passage of the Exon-Florio provisions has on the reduction of possible costs.

1. National Security

A review of the Exon-Florio provisions clearly shows that they provide excellent protection against increased FDI. In fact, as previously stated, the term national security has no definition under the Exon-Florio legislation or under the final implementing regulations and it can be interpreted to mean whatever CFIUS says it means at any moment. Although section (e) of Exon-Florio clearly provides three factors to be used in the President's decision on possible national security impairment, these factors leave open the possibility that the President may consider economic security in making his decision.²⁶⁴ The ability to take into account other factors, such as economic security, changes the provision from an objective to a subjective standard and invites future influence peddling, an identified national security cost.²⁶⁵ Such a discretionary decision process, which includes the lack of a clear evidentiary standard, will ultimately lead to the misuse of power, even if misuse is unintended. Therefore, because the President is allowed to take economic security into account, and the possibility of political influence is not eliminated, the Exon-Florio provisions eliminate only part of the national security associated costs. The increased level of uncertainty will, in the long run, lead to a lower level of investment and a lower level of domestic capital formation.²⁶⁶

260. 56 Fed. Reg. 58,775 (1991).

261. *Id.*

262. *See supra* notes 78-108 and accompanying text.

263. *See id.* (discussing other FDI-based costs). The remaining costs associated with increased FDI were relatively unaffected by the passage of the Exon-Florio Amendment and its accompanying regulations and, therefore, are not again discussed herein.

264. *See supra* note 190 and accompanying text (presenting a list of the factors to be used by the President in his Exon-Florio investment decision).

265. *See supra* note 88 and accompanying text (discussing influence peddling).

266. An example of the concerns foreign investors are having with the broad definition of national security found in the Exon-Florio Amendment and its accompanying regulations was raised by the European Economic Community. *Highlights*, 9 Int'l Trade Daily (BNA) No. 8, at 293 (Feb. 19, 1992). The EEC warned that the national security definition is causing uncertainty among many European companies. *Id.* An EEC declaration called on the Bush Administration to find a way to safeguard U.S. national security while ensuring investor confidence. *Id.* The EEC stated that it would take any Exon-Florio abuses to the

On the question of whether Exon-Florio adds to the protection provided by the antitrust laws against FDI harmful to national security, Exon-Florio does add a modicum of protection by allowing divestiture in cases where the antitrust laws were not violated. This would likely only occur where the proposed investment pierced the narrowest definition of national security.²⁶⁷ For FDIs that involve a breach of economic security, the Exon-Florio Amendment and its implementing regulations provide no additional protection to U.S. businesses, unless protectionism is behind the exercise of the Exon-Florio power. In such protectionist cases, the power to prohibit future FDI is exercised at the expense of the domestic producers and consumers.

Even without defining national security itself, the problem could partially be solved if a list of companies or industries that are susceptible to a national security breach from FDI was compiled and utilized. One such list has already been compiled as a result of Public Law 100-456, section 823, which requires the Department of Defense to submit a "Critical Technologies Plan" to Congress each year.²⁶⁸ This plan is to contain a list of those items which are critical to national security or defense.²⁶⁹ Additionally, if the concept of economic security²⁷⁰ was clearly defined not to be within the definition of national security, the factors listed in the Amendment would have definable meanings,²⁷¹ and the Critical Technologies Plan could serve as an objective standard from which to judge the national security implication of a prospective FDI. However, as discussed above, CFIUS rejected the use of a narrowly tailored definition of national security in the final version of the implementing regulations.²⁷²

2. Future Employment

Future employment will also likely be negatively affected by implementation of the final Exon-Florio regulations.²⁷³ Under generally accepted principles of economic theory, the level of employment is directly related to various factors, one being the level of capital formation. Increased uncertainty, due to the failure of CFIUS to define terms, such as national security, decreases the likelihood of increased future FDI in capital goods. This, in turn, reduces the availability of domestic capital and, over time, reduces the capital-to-labor ratio and the marginal product of labor over what it otherwise would

Organization for Economic Cooperation and Development. *Id.*

Investor uncertainty is increased by statements, such as those by Representative Mel Levine (D-Cal.), where he stated the Exon-Florio Amendment is being too narrowly interpreted and the term national security means more than military security. *Foreign Investment: Narrow Interpretation of Statute Hobbles Exon-Florio Reviews, Lawyers Told*, 9 Int'l Trade Rep. (BNA) No. 8, at 325 (Feb. 19, 1992).

267. See *supra* notes 236-43 and accompanying text (discussing national security).

268. National Defense Authorization Act, Fiscal Year 1989, Pub. L. No. 100-456, § 823, 102 Stat. 1918 (1988).

269. *Id.*

270. *Foreign Takeovers and National Security: Hearings on H.R. 3, Section 905 Before the House Subcommittee on Commerce, Consumer Protection and Competitiveness, Committee on Energy and Commerce*, 100th Cong., 1st Sess. 1 (1988) (statement by Representative Florio).

271. See *supra* notes 236-43 and accompanying text (discussing the concept of national security).

272. *Id.*

273. See 134 CONG. REC. H2321 (daily ed. Apr. 21, 1988) (statement of Representative Craig discussing the negative impact of the Exon-Florio Amendment's plant closing provision on U.S. businesses).

have been. A reduction in the marginal product of labor leads directly to a decrease in the real wage level. Therefore, the failure of the Exon-Florio provision to identify "national security" and "control" will, among other things, lead to a decrease in the number of high-paying jobs as a percentage of total employment, given the continued existence of a U.S. budget deficit.

3. Capital Dependence

As previously discussed, the introduction of uncertainty will lead to a reduction in FDI (or at least in the growth of FDI). If a simple reduction in capital dependence is the goal, the Exon-Florio Amendment was brilliantly crafted. However, freeing the U.S. economy from dependence on foreign capital has its side effects. First, reducing foreign capital will increase domestic interest rates.²⁷⁴ Second, if the United States continues to run a budget deficit, most of the domestically available capital will be withdrawn from the private sector to finance the budget deficit. The reduction of private sector capital will lead to a reduction in the capital-to-labor ratio and to a reduction in the marginal product of labor and finally to a reduction in real wages. Therefore, while a position of capital dependence is not the optimal alternative, until Congress has the political will to deal with the budget deficit, capital dependence is preferred to the alternative.

4. Technology Transfer

As previously stated, assumptions pertaining to the transfer of U.S. technology to foreign investors were made at a time when the United States was in a position of technical dominance.²⁷⁵ Passage of the Exon-Florio Amendment is an adequate protection against the foreign acquisition of U.S. technology. This is evidenced by the ordered divestiture of China National Aero-Technology Import and Export Corp.'s purchase of MAMCO, Inc.²⁷⁶ However, as written, industries seeking market protection, and labor unions who fear additional technology will reduce their bargaining power will likely use the lack of national security and material information standards of the Exon-Florio Amendment to either slow down or to prohibit FDIs that attempt to introduce superior foreign technology into the United States.

VII. CONCLUSIONS

The lack of definitions for the key elements of the Exon-Florio Amendment, as well as the lack of negative economic effects associated with the overwhelming majority of FDIs, support the conclusion that the Exon-Florio Amendment as currently drafted will have an overall negative impact on the U.S. economy. Perhaps most frightening is the possibility that unscrupulous U.S. persons, through the filing of misleading statements to

274. See *supra* note 70 and accompanying text (discussing the effects of FDI on U.S. interest rates and exchange rates).

275. See *supra* notes 58-61 and accompanying text (discussing the net importation of Japanese technology).

276. *Bush Orders Divestiture of Chinese Acquisition on National Security Grounds*, 7 Int'l Trade Rep. (BNA) No. 6, at 178 (Feb. 7, 1990).

the CFIUS, and foreign investors, through stepped-up influence peddling, could use the Exon-Florio provisions to make the average American worker worse off than if the legislation had not been passed.

However, any specific potential problems with the Exon-Florio Amendment will pale in comparison to the economic problems created by the U.S. domestic budget deficit. If progress is made in controlling federal spending, most problems with FDI will evaporate overnight, given the link between the budget deficit and the trade deficit. However, if the Democratic Party, which is now in control of both houses of Congress and the White House, is either unwilling or unable to curb federal spending, the U.S. economy will continue to hemorrhage until FDI will not be a problem because foreign investors will no longer be willing to invest in the United States.