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Foreign Direct Investment in United States Real Estate: Xenophobic or Principled Reaction?

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106.27 Determinations by commission; legal disposition by Department of Legal Affairs

(1) If the Commission determines that probable cause exists to believe a violation of this chapter has occurred, the Commission shall immediately transmit such determination to the Department of Legal Affairs for disposition pursuant to this section. The Commission and the Department of State *Division of Elections* shall forthwith transmit to the Department of Legal Affairs all available information concerning the alleged violation.

(a) ...

(b) ...

(2) If the Commission determines that probable cause exists to believe a violation of this chapter has occurred by a candidate for the office of attorney general, the Commission shall immediately transmit such determination to the state attorney in the circuit in which the violation occurred for disposition, pursuant to this section. The Commission and the Department of State shall forthwith transmit to the state attorney in the circuit in which the violation occurred all available information concerning the alleged violation.

(3) ...

(4) ...

Section 9. This act shall take effect upon becoming law.

FOREIGN DIRECT INVESTMENT IN UNITED STATES REAL ESTATE: XENOPHOBIC OR PRINCIPLED REACTION?

> ALIEN — "is derived from the *Latine* word *alienus*, and according to the etymologie of the word, it signifieth one borne in a strange country, under the obedience of a strange prince. . . ."[1]

In November 1974, President Ford signed the Foreign Investment Study Act of 1974,[2] directing the Secretaries of Commerce and Treasury to conduct a comprehensive study of foreign direct and portfolio investments in the United States. Foreign direct investments (F.D.I.) are investments in a host country by a foreign investor having the ability to control the operation of the investment.[3] Included in this directive is a requirement that these departments analyze the effects of F.D.I. in United States real property holdings.[4] The Act further required an analysis of the effects of federal, regional, state, and local laws, rules, and regulations on F.D.I.[5] Congress, responding to

1. 1 E. COKE, COMMENTARY UPON LITTLETON 129a (Butler & Hargraves 1853).

2. Act of Oct. 26, 1974, Pub. L. No. 93-748, 88 Stat. 1450.

3. *Id.* §§2-3 *Foreign portfolio investment* is simply noncontrol purchases of United States securities; the investor holds these securities but does not have a significant voice in the management or control. For statistical purposes, the United States Commerce Department uses 25% or greater foreign ownership of voting stock as the test for "control." Statement of Peter M. Flanigan, in *Hearings on Foreign Direct Investment in the United States Before the Subcomm. on Internat'l Finance of the Senate Comm. on Banking, Housing, and Urban Affairs*, 93d Cong., 2d Sess., at 4 (1974) [hereinafter cited as *Senate Hearings*]. The Department of Commerce, however, reportedly plans to tighten this test to 10% foreign ownership for its future determinations of F.D.I. 1974 NAT'L J. REP. 1311. In light of recent attempts by foreign investors to aid ailing American corporations with massive loans, a test of control limited to voting stock does not seem to recognize the business realities of such a debtor-creditor relationship.

4. Act of Oct. 26, 1974, Pub. L. No. 93-478, §5(b), 88 Stat. 1450.

5. *Id.* §5(3).

recent large F.D.I. in the United States,[6] stated that the act's purpose is to "increase the understanding of the implications of [F.D.I.] both within the United States Government and among the public at large, and thus to help lay the foundation for a national policy concerning foreign investments in the United States."[7]

Foreign direct investment in real estate occupies a unique position in the array of F.D.I. possibilities. Because the ownership of land in the United States has traditionally been regulated by the several states, foreign investors are faced with a hodgepodge of laws regulating their real property investments.[8] In addition to state regulation, the federal government concurrently acts in this area when exercising its power to enter into treaties and executive agreements.[9] Although in several recent cases the constitutional rights of aliens have been expanded by the United States Supreme Court,[10] these cases address only the rights of resident aliens, leaving the rights of nonresident alien investors unclearly defined.[11] Yet, despite this complexity and uncertainty, F.D.I. in United States realty is becoming increasingly lucrative to foreign investors.

It is well settled in international law that each country has the right to prescribe who may own property within its borders.[12] This note will examine the extent of United States regulation of F.D.I. in real estate and comment on the propriety and effectiveness of such regulation in light of the American legal system and national economic and political objectives. In exploring F.D.I. in realty, several issues arise. State regulation naturally invites a discussion of Federalism and the extent of the federal preemptive power. Because of international interaction by treaty and executive agreement, reciprocity becomes an issue and a discussion of foreign treatment of the United States direct investment in realty abroad is thus relevant. Finally, the constitutional rights of aliens must be considered in the regulation of F.D.I. This note will first survey recent F.D.I. in United States real estate and current methods of domestic regulation; a discussion of several foreign countries' methods of control will be followed by a treatment of the federal constitutional issues.

RECENT F.D.I. IN UNITED STATES REAL ESTATE

The threshold issue in F.D.I. is the meaning of the term "alien" or "foreign." An individual alien investor is "one born out of the jurisdiction

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6. See text accompanying notes 20-29 *infra*.

7. H.R. REP. No. 1183, 93d Cong., 2d Sess., in 3 U.S. CODE CONG. & AD. NEWS 5957 (1974).

8. See note 73 *infra*.

9. See note 81 *infra*.

10. *See, e.g., In re* Griffiths, 413 U.S. 717 (1973); Graham v. Richardson, 403 U.S. 365 (1971).

11. See text accompanying notes 139-171 *infra*.

12. *See, e.g.*, 42 U.S.C. §1982 (1970): "All citizens of the United States shall have the same right, in every State or Territory, as is enjoyed by white citizens thereof to inherit, purchase, lease, sell, hold, and convey real and personal property."

of the United States, and who has not been naturalized. . . ."[13] The traditional term describing individual foreign investors has been alien, while business entities have been referred to as *foreign*;[14] however, these terms will be used interchangeably herein. The focus of this note is on alien investors who would probably stipulate their alienage and would continue to retain allegiance to their home country.

Aliens are further classified as resident or nonresident;[15] a classification that may be crucial in determining such issues as constitutional rights[16] and tax liabilities.[17] Broadly speaking, a nonresident alien is one who is residing out of the country; however, the territorial limits of residency vary according to the nature of the dispute and the applicable law.[18] Consequently, the foreign direct investor may be declared resident or nonresident depending on the nature of his investment and the context in which the issue arises. For purposes of this discussion, the investor in realty will be assumed to be a nonresident alien individual.[19]

During 1972 the largest foreign direct investors in this country were the Japanese, who, with an investment of $105 million, increased their annual rate of investment fivefold over that of 1971.[20] Japanese holdings of real estate, predominately resort properties in Hawaii, have reportedly surpassed $350 million in value.[21] It is believed, however, that a catalyst for the sudden

13. *Cf.* note 70 *infra*, for statutes demonstrating the different terms used in defining a foreign direct investor.

14. Low Wah Suey v. Backus, 225 U.S. 460, 473 (1912). Alien is defined under the Immigration and Nationality Act as any person not a citizen or national of the United States. 8 U.S.C. §1101(a)(3) (1970). Generally, the status of persons as aliens in the United States is to be determined by the applicable laws of the United States. *See* United States v. Gancy, 54 F. Supp. 755 (D. Minn.), *aff'd.*, 149 F.2d 788 (8th Cir.), *cert. denied*, 326 U.S. 767 (1945).

15. See note 18 *infra.*

16. See text accompanying notes 139-182 *infra.*

17. See text accompanying notes 82-93 *infra.*

18. The Immigration and Nationality Act defines residence as the place of general abode, without regard to intent. *See* 8 U.S.C. §1101(33) (1970). The states have generally defined nonresident aliens as those who are neither citizens of the United States nor residents of their state. *See, e.g.*, State v. Smith, 70 Cal. 153, 12 P. 121 (1886); *In re* Gill's Estate, 79 Iowa 296, 44 N.W. 553 (1890). For purposes of federal income taxation, a nonresident alien individual is one whose residence is not within the United States and who is not a citizen of the United States. INT. REV. CODE OF 1954, §871; Treas. Reg. §1.871-2(a). *See also* Johansson v. United States, 376 F.2d 809 (5th Cir. 1964); C.I.R. v. Nubar, 185 F.2d 584 (5th Cir.), *cert. denied*, 341 U.S. 925 (1950).

19. Foreign corporations are generally defined as those not incorporated in the forum. Again, the context of the dispute usually defines the territorial limits. Because foreign corporations have, for the most part, received more favorable treatment than foreign individual investors, especially from the states, this note will emphasize the foreign individual investor and discuss the foreign corporate investor only when such a distinction is relevant. See note 73 *infra* for the state statutes that regulate individual and corporate F.D.I. in realty.

20. 1973 NAT'L J. REP. 1755.

21. *See, e.g.*, FORTUNE, Sept. 1975, at 130, 144; Wall Street Journal, March 5, 1974, at 1, col. 6, Jan. 22, 1974, at 1, col. 2. Because real estate prices are so high in land-scarce Japan, Japanese investors seem grateful to be able to purchase real property even at prices that seem too high for United States investors. For example, 1974 property in downtown

concern over F.D.I. in the United States was the recent fourfold increase in the price of oil charged by members of the Organization of Petroleum Exporting Countries (OPEC).[22]

With Arab oil producing nations' foreign currency reserves predicted to reach $400 billion by 1980,[23] it is apparent that these funds must be invested. The investment of this surplus capital in American real estate ranks high on the "economic agenda" of the Arab countries.[24] Several reasons exist for this high priority: (1) the political and economic stability of the United States; (2) the low price of United States real estate compared with the price of realty in other parts of the world; and (3) the considerable tax advantage allowed foreign investment in United States realty.[25] Thus, the Mideast OPEC members have excess reserves they need to invest, and they appear to have a direct investment preference for United States real estate. With such large reserves, however, it would be economically and politically unwise for them to invest solely in American real estate. Accordingly, a United States Treasury Department study of Arab investment, issued in September 1974, estimated that "only a few hundred million dollars may have gone into corporate securities and real estate."[26]

Los Angeles sold at $50 per square foot, but similar land in Tokyo sold for $900 per square foot. *Id.* January 21, 1974, at 6, col. 2; see note 118 *infra.* Japanese land investment has emphasized resort and leisure properties; for example, Japanese reportedly own one-third of the hotel rooms in Honolulu, Hawaii. When the price of oil quadrupled in 1974, however, the Japanese, almost totally dependent on imported petroleum, not only shifted their investment emphasis but also faced Japanese governmental regulation of investment abroad. It appears that industrial properties and real estate, including natural resources, have become more tempting to Japanese investors. *See* DUN'S REV. May 1974, at 58-59. The Japanese Government, responding to a dwindling balance of payments surplus due to increased oil prices, stated that overseas investment in realty would require case-by-case governmental approval. FORTUNE, Sept. 1975, at 135. The Japanese Government approved investment in United States real property amounting to over $47 million between July 1971 and March 1973. Statement of Nelson A. Stitt, in *Hearings on Foreign Investment in the United States Before the Subcomm. on Foreign Economic Policy of the House Comm. on Foreign Affairs,* 93d Cong., 2d Sess., at 41 (1974) [hereinafter cited as *House Hearings*]. Japanese corporations holding offshore reserves, however, are not subject to this regulation. For example, in July 1974, a Japanese corporation paid over $100 million for three hotels on Waikiki Beach, Hawaii; the sale was financed through the London eurodollar market. FORTUNE, Sept. 1975, at 139.

22. On March 15, 1974, the posted price of crude oil stood at approximately $11.63 per barrel, a 400% increase from a year earlier. N.Y. Times, March 16, 1974, at 1, col. 6.

23. Wall Street Journal, March 5, 1974, at 1, col. 6. Estimates of Arab reserves, commonly known as petrodollars, have proliferated and divergent views have become the rule. *Compare* Wall Street Journal, April 16, 1975, at 18, col. 1, *with* Wall Street Journal, June 20, 1975, at 1, col. 5.

24. N.Y. Times, Nov. 24, 1974, §III, at 5, col. 6. Investment in American realty follows industrial development in their home country, defense programs, and some foreign aid. *Id.*

25. *Id.* Further reasons given for favoring investment in United States realty are: the Mideastern countries' insistence on preservation of capital and their consideration of real estate as a lasting asset, their desire for productive land, and their preference for investments that attract publicity. *Id.* For a discussion of tax advantages of F.D.I. in realty, see text accompanying notes 82-93 *infra.*

26. CONG. RESEARCH SERV., Memo No. HG4501 For., October 18, 1974. A survey of recent investment is helpful in determining the scope of Mideast F.D.I. in United States

Japan and the countries of the Mideast are not the only actual or potential foreign direct investors in United States property. In Florida, for instance, the I.T.T. Community Development Corporation is spearheading a drive to sell part of its 92,000 acre Palm Coast development to European investors.[27] Of particular interest is the recent purchase of $11 million worth of property in the central Florida area by a French controlled chemical company for phosphate mining;[28] phosphate is an essential ingredient in chemical fertilizers and, according to the Florida Phosphate Council, "Florida provides 75% of America's urgent need for phosphate."[29]

Thus far, American reaction to F.D.I. in realty has been primarily local. For example, in response to the Kuwait Investment Company's purchase of Kiawah Island, South Carolina,[30] several environmental groups have protested the possible harm to turtle nesting grounds from resort development.[31] Likewise, the Hawaiian populace has strenuously objected to the Japanese practice of buying resort properties, which are then made accessible exclusively to participants in package tours from Japan.[32] Congressional reaction has been minimal so far, and only recently did Congress appropriate $3 million to study the problem.[33] There are, however, several bills pending in Congress that propose to act affirmatively in this area.[34]

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realty. The Kuwait Investment Company (owned half by the Kuwait government and half by private Arab investors) purchased Kiawah Island, South Carolina, for $17.4 million, planning to build a $100 million residential resort. Wall Street Journal, Feb. 26, 1975, at 38, col. 1; Miami Herald, Sept. 13, 1974, at 5, col. 1. Further purchases include a $25 million industrial complex and Kuwaiti investment in a $100 million Atlanta hotel-commercial complex, with $10 million down and a mortgage for a one-half interest in the complex. Miami Herald, Sept. 13, 1974, at 5, col. 1. Chase Manhattan Bank has handled about fifty deals for a single Mideast client; types of purchases included income producing property, joint ventures in industrial buildings, shopping centers, downtown office buildings, and sites for large industrial parks for an aggregate investment of over $100 million. N.Y. Times, Nov. 25, 1974, at 5, col. 1.

27. DUN'S REV., May 1974, at 51, col. 1.

28. Wauchula (Fla.) Herald Advocate, April 24, 1975, at 1, col. 3.

29. *Id.*, April 25, 1975, §3, at 1, col. 3. See text accompanying note 43 *infra*.

30. See note 26 *supra*.

31. Wall Street Journal, Feb. 26, 1975, at 38, col. 1. The Kuwaitis have spent approximately $20,000 annually to find a solution to the environmental impact of resort development on these turtle nesting grounds. A collateral problem arose because Kuwaiti purchases caused surrounding property values and taxes to soar, and the local population could not afford the increased taxes. The Kuwaitis hired tax consultants to ameliorate this result. Because the Kuwaitis have regarded this project as a showcase of Arab direct investment potential in the United States, the local reaction to this purchase and the Kuwaiti response to the problems created by their investment may indicate the future course of F.D.I. in United States realty. *Id.*

32. 1973 NAT'L J. REP. 1758.

33. Act of Oct. 26, 1974, Pub. L. No. 93-478, §11, 88 Stat. 1450.

34. Senator Harrison A. Williams, Jr. (D-N.J.) has sponsored a bill, the Foreign Investors Limitation Act, S. 425, 94th Cong., 1st Sess. (1975), that would: (1) authorize, though not require, the President to prevent specific takeover attempts by foreign countries or governments; (2) require disclosure of beneficial ownership of stocks of publicly traded corporations; (3) require foreign investors to notify the United States Government, in advance, of any purchase of 5% or more of the stock of a United States corporation; and (4)

The Nixon Administration's pro-F.D.I. position was definitively stated before a Senate Hearing,[35] and President Ford has continued this position, stating:

> My Administration will oppose any new restriction on foreign investment in the United States, except where absolutely necessary on national security grounds or to protect essential national interests.[36]

The book value of F.D.I. (25 percent foreign ownership)[37] in the United States reached $17.7 billion at the end of 1973 (an increase of 24 percent over the previous year),[38] compared with a total of $3.4 billion at the end of 1950.[39] Yet overseas direct investments by American investors (defined as 10 percent or more of American ownership) totaled $107.3 billion at the conclusion of 1973 (up 14 percent over 1972),[40] compared with a total of $11.8 billion.[41] With this stake in the free flow of investment dollars, the Administration was apparently unwilling to restrict direct investment in the United States and chance retaliation.

Executive and congressional reactions to F.D.I. appear to result, in part, from an inadequacy of data on such investments in realty. Foreign investors

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authorize the President to bar any such acquisition in the interest of national security, foreign policy, or protection of the economy. 1975 NAT'L J. REP. 477.

The Foreign Investors Limitation Act proposes to prohibit any noncitizen from acquiring, directly or indirectly, more than 5% of the voting securities (or 35% of the nonvoting securities) of any issuer registered under §12 of the Securities and Exchange Act of 1934, 15 U.S.C. §78*l* (1970). Further, under one proposed bill, foreign direct investors would have to register with the Securities and Exchange Commission prior to their acquisition of the securities of any registered American issuer. H.R. 8951, 93d Cong., 1st Sess. (1973).

The Energy and Defense Industry Production Act, although less restrictive than the above legislation, would make it illegal for any noncitizen, or entity owned or controlled by a noncitizen, to control any American issuer who is both registered under §12 of the Securities and Exchange Act of 1934 and engaged in an energy or defense industry. H.R. 12040, 93d Cong., 1st Sess. (1973).

At least 14 bills have been introduced in the 93d and 94th Congresses to regulate or monitor F.D.I. in the United States. Lewis, *Economic Report — Welcome Mat Still Out for Foreign Investors in the U.S.*, 1976 NAT'L J. REP. 31, 32. The House seems to be waiting for Senate action and the results of the administration's Foreign Investment Study (scheduled for presentation to Congress on April 29, 1976) before introducing comprehensive regulatory legislation. Senator Stevenson (D-Ill.) has introduced the Anti-Boycott and Foreign Investment Bill, S. 953, 95th Cong., 1st Sess. (1975), which would prohibit discriminatory boycotting and regulate F.D.I. The F.D.I. section basically incorporates Senator Williams' Foreign Investment Limitation Act. *Id.* at 41. *See generally* Note, *An Evaluation of the Need for Further Statutory Controls on Foreign Direct Investment in the United States*, 8 VAND. J. TRANSNAT'L L. 147, 181-87 (1974) [hereinafter cited as *Statutory Controls*].

35. "While there have been bills introducing such restrictions [on foreign investment], the Administration will, consistent with an overall policy of letting the free market allocate the flow of investment, oppose this legislation unless absolutely necessary to protect our national security." *Senate Hearings*, *supra* note 3, at 8.

36. Lewis, *supra* note 34, at 33.

37. See note 3 *supra*.

38. 1974 NAT'L J. REP. 1311.

39. *House Hearings*, *supra* note 21, at 270.

40. See note 38 *supra*.

41. See note 39 *supra*.

are usually absentee landowners who typically engage a property management firm to look after their investments; identifying land ownership is difficult because it involves checking local land records at the county level; furthermore, real estate investment is usually highly leveraged, and thus minimal capital investment, easily disguised, may control the investment.[42]

Another concern over F.D.I. in real estate is the fear of foreign control over essential raw materials. The Chamber of Commerce of the United States reported that "[i]t does appear from information available that the adverse reaction to foreign investment in the United States comes about when investment is directed toward 'non-productive' or the more speculative assets such as real estate, timberland and other natural resource assets."[43] Moreover, Arab efforts to boycott American firms doing business with Israel and financial institutions having Jewish connections certainly exacerbates the issue of Mideast F.D.I. in the United States and undermines the Administration's pro-F.D.I. position.[44] Running throughout these various adverse reactions to F.D.I. is also a thread of xenophobia — the fear of foreigners — that must be recognized and ameliorated.

DOMESTIC METHODS OF REGULATING F.D.I. IN REAL ESTATE

One commentator on F.D.I. believes that restrictions on alien landholding are the most significant legal impediment to all investment from abroad under either federal or state law.[45] Clearly, state restrictions on alien landholding are potentially the foremost legal impediment to F.D.I. in United States realty because the majority of United States land that would attract F.D.I. is under private title, and the several states currently dominate the regulation of private land ownership.[46] A brief review of the evolution of the state

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42. Statement of Sidney L. Jones, in *Senate Hearings, supra* note 3, at 29. Leverage is a method of financing whereby the investor puts in as little cash as possible and borrows the remainder. The key to success is the differential between the interest rate on the borrowed funds and the rate of return on the investment on disposition. Because of the ability to borrow more money against realty than against other investments and because of the tax advantages associated with realty, leverage is a common and highly desirable method of real estate financing. *See* W. BEATON, REAL ESTATE INVESTMENT 126-27 (1971). For example, leverage financing can cause an investment purchased with 10% cash and 90% borrowed funds that sold for double its purchase price to realize a gain to the investor on disposition equal to 14.25 times his initial investment. S. ROULAC, REAL ESTATE SYNDICATION DIGEST: PRINCIPLES AND APPLICATIONS 106, 108 tab. 12 (1972).

43. Statement of the United States Chamber of Commerce, in *Senate Hearings, supra* note 3, at 143. See also text accompanying notes 28-29 *supra*.

44. 1975 NAT'L. J. REP. 477.

45. Sullivan, *Alien Land Laws: A Re-Evaluation*, 36 TEMP. L.Q. 15, 39 (1962). This statement seems rather broad today because most F.D.I. is in portfolio form, which puts it beyond restrictions on alien land ownership. See CONG. RESEARCH SERV., *supra* note 26.

46. A letter from the United States Secretary of State to the Ambassador of Ireland stated that: "[R]egulation of the ownership of land under private title is a matter of State rather than Federal jurisdiction. . . . Information of this character would have to be obtained from the Attorney General or comparable officer of each State." 8 DIGEST OF INT'L L. 487, 497 (1967).

alien land laws is necessary to fully illuminate the current application of such regulation.[47]

State Alien Land Laws

In 1813 Justice Story outlined the common law disabilities concerning alien land ownership in *Fairfax's Devisee v. Hunter's Lessee*:[48]

> It is clear by the common law, that an alien can [take] lands by purchase, though not by descent; or in other words . . . he may take by the act of the party. . . . [I]n the language of the ancient law, the alien has the capacity to *take*, but not to *hold* lands, and they may be seized into the hands of the sovereign.[49]

Thus, the alien may acquire real property by purchase and hold it against all but the state, which can proceed against him by an action known as "inquest of office" and thereby divest him of his property.[50]

Although the present system of state alien regulations is the result of almost 200 years of lawmaking, it appears to have developed within four distinct phases: (1) common law disabilities during the colonial and Revolutionary periods, (2) legislation substantially modifying the common law in the nineteenth century, (3) anti-alien legislation in the midwestern states during the late nineteenth century, and (4) anti-Japanese legislation during the 1920's and again during the Second World War.[51]

During the colonial period and following independence, the states retained the alien disabilities and modified the common law as seemed appropriate.[52] The post-Revolutionary tendency, however, was to remove these disabilities, and by 1880, perhaps due to the stimulus of the fourteenth amendment, over half of the states allowed aliens to hold land on equal terms with citizens.[53] This trend ended abruptly in the 1880's and 1890's[54] when the Populist Party movement of this period vigorously attacked large alien landholdings, principally those of the immense British cattle companies.[55] It was also during

47. *See* Sullivan, *supra* note 45, at 26-34.

48. 11 U.S. (7 Cranch) 603 (1813).

49. *Id.* at 619.

50. *See generally* 2 W. BLACKSTONE, COMMENTARIES *249, *293; Sullivan, *supra* note 45, at 16. Sir Edward Coke revealed a xenophobic side of the common law in noting several reasons for having alien disabilities: first, the secrets of the realm might be taken and enjoyed by strangers; second, "[i]t should tend to the destruction of the realm"; Coke's third reason has a more current ring, "[that] [t]he revenues of the realm (the sinews of war, & ornaments of peace) should be taken and enjoyed by strangers born." Calvin's Case, 7 Co. Rep. 1a, 18b (1607). Also, Blackstone states that "[the common law] seems to be intended by way of punishment for the aliens' presumption, in attempting to acquire any landed property. . . ." 1 W. BLACKSTONE, COMMENTARIES *372.

51. *See* Sullivan, *supra* note 45, at 26.

52. Ohio was the first state to give aliens equal treatment in landholding matters in Ohio Laws 1804, at 123. Sullivan, *supra* note 45, at 29 n.63.

53. *See* Sullivan, *supra* note 45, at 29.

54. *Id.* at 30.

55. *See generally* Note, *Restrictions on Corporate Holdings of Real Estate*, 21 N.Y.U.L.

this period that precursors of many current alien restrictions such as the Alien Land Bill[56] were passed.[57] As Populism died out, local resentment to alien landholding waned. Nevertheless, this resentment of foreign presence was soon rekindled by the great Japanese immigration during the 1900's. California, bearing the brunt of this immigration, passed an alien land law in 1920.[58] This statute stimulated another wave of anti-alien legislation; the target, this time, was predominantly Japanese immigrants rather than all aliens.[59] In the 1923 decision of *Porterfield v. Webb*,[60] the United States Supreme Court held the California statute constitutional. The discrimination, the Court said, was based on a reasonable classification, and thus there was no violation of the due process or equal protection clauses of the fourteenth amendment.[61] This anti-alien sentiment diminished as the Great Depression approached, presumably because of the assimilation of the previous Japanese immigrants or because of the exclusion of any more Japanese by the Immigration Act of 1924.[62] As World War II revived anti-Japanese sentiment, the alien land laws proved to be an effective vehicle for discrimination, and they were revived or expanded.[63]

The postwar reaction, surprisingly, was not the historical slow progression to equality. In 1948 the United States Supreme Court held that the escheat of real property recorded in the name of a minor United States citizen but paid for by his father, a Japanese citizen ineligible for American citizenship,

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REV. 299 (1946) (discussion of state restrictions on corporate land holdings). *See also* L. NORDYKE, CATTLE EMPIRE (1949) (discussion of the large British cattle companies) (*cited in* Sullivan, *supra* note 45, at 31 n.71); J. WARREN & C. WARREN, THE MATADORS, 1879-1951 (1952).

56. Territorial Land Act of 1887, *as amended*, 48 U.S.C. §§1501 *et seq.* (1970). This act, originally adopted by Congress to restrict land transfers to aliens in the territories of the Great Plains and Rocky Mountains, lays down a complex pattern of restrictions on nonresident aliens.

57. During this period, eight states that had granted aliens equal treatment adopted restrictions. They were Colorado, Illinois, Iowa, Kansas, Minnesota, Missouri, Nebraska, and Wisconsin. *See* Sullivan, *supra* note 45, at 31 n.68.

58. Cal. Stat. 1921, lxxxiii.

59. *See* Sullivan, *supra* note 45, at 33. This group of alien land laws did not discriminate per se; they were based on a vagary of the Immigration Act, 39 Stat. 874, *as amended*, Act of May 25, 1924, 43 Stat. 153, which, prior to 1952, precluded persons of the oriental race from naturalization. The California statute and others patterned after it based alien land ownership on the ability of an alien to be naturalized. These statutes provided that no alien ineligible for citizenship could take or hold legal or equitable title to land. Land conveyed to or for the use of such aliens in violation of the statute would escheat. To knowingly transfer land or the right to the control, possession, or use of land to ineligible aliens was a misdemeanor punishable by fine and imprisonment. *Id.* This group of alien land laws is clearly distinguishable from those laws following the Territorial Land Act of 1887, which precluded persons from owning land who neither were citizens of the United States, nor had declared their intent to become citizens. See note 54 *supra*. *See also* McGovney, *The Anti-Japanese Land Laws of California and Ten Other States*, 35 CALIF. L. REV. 7 (1947).

60. 263 U.S. 225 (1923).

61. *Id.* at 233. For an analysis of this decision and its impact on current F.D.I. in United States realty, see text accompanying notes 149-151 *infra*.

62. The Quota Law of 1924, 43 Stat. 153, *amending* the Immigration Act of 1917, 39 Stat. 874.

63. *See* Sullivan, *supra* note 45, at 34.

deprived the child of equal protection of the law.[64] Moreover, in 1949 the Oregon supreme court was the first state court to invalidate its alien land law,[65] which precluded all persons who were not eligible for citizenship from owning or leasing real property.[66] The court, finding no valid reason why ineligible resident aliens should be precluded as a class from ownership of interests in real property, held that the Oregon Alien Land Law was repugnant to the equal protection clause of the fourteenth amendment.[67] The death knell of the California Alien Land Law tolled in 1952 when the California supreme court, in a four to three decision, determined the act violative of the equal protection clause of the fourteenth amendment.[68] During that same year, the Immigration and Naturalization Act of 1952[69] was amended to provide that "[t]he right of a person to become a naturalized citizen of the United States shall not be abridged because of race. . . ."[70] Consequently, these alien land laws, founded on anti-Japanese sentiment, became moot.

State restriction of alien land ownership, however, has survived these major challenges to its constitutionality.[71] The most notable feature of any current analysis of the states' alien land laws is the crazy quilt of legislation. In a benchmark survey of state alien land laws prepared in 1962, Charles Sullivan grouped these statutes into five classifications based on the degree to which common law disabilities had been modified toward equal treatment: (1) full national treatment; (2) national treatment except for certain numerically unimportant categories of aliens; (3) national treatment for resident aliens only; (4) statutory restrictions on all aliens; and (5) retention of some common law disabilities.[72]

An update of this survey reveals that only a minor shift has occurred since 1962 toward full national treatment of alien land ownership.[73] While

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64. Oyama v. California, 332 U.S. 633 (1948), *rev'g sub nom.* People v. Oyama, 29 Cal. 2d 164, 173 P.2d 794 (1946).

65. Kenji Namba v. McCourt, 185 Ore. 579, 204 P.2d 569 (1949).

66. Ore. Laws §61-108 (1945).

67. 185 Ore. at 614 P.2d at 579.

68. Sei Fujii v. State, 38 Cal. 2d 718, 242 617 (1952). The court stated that "[t]he California Alien Land Law is obviously designed and administered as an instrument for effectuating racial discrimination . . . . There is nothing to indicate that those alien *residents* . . . as a class, might use the land for purposes injurious to public morals, safety or welfare." *Id.* at 737-38, 242 P.2d at 630 (emphasis added).

69. 8 U.S.C. §1101 *et. seq.* (1970).

70. *Id.* §1422.

71. See text accompanying notes 140-172 *infra.*

72. *See* Sullivan, *supra* note 45, at 17.

73. *Group I.* In the following 25 jurisdictions, all aliens receive full national treatment: Alabama, ALA. CODE tit. 47, §1 (1958); Arkansas, ARK. STAT. ANN. §50-301 (1971); California, CAL. CIV. CODE §671 (West 1954); Canal Zone, C.Z. CODE tit. 4, §152 (1963); Delaware, DEL. CODE ANN. tit. 25, §308 (1953); District of Columbia, D.C. CODE ANN. §45-1501 (1973) (*But see* Larkin v. Washington Loan & Trust, 31 F.2d 635 (D.C. Cir. 1929), holding this statute inapplicable to realty within the District of Columbia); Florida, FLA. CONST. art. I, §2, *cf.* FLA. STAT. §732.1101 (1975); Idaho, IDAHO CODE §55-103 (1957); Maine, ME. REV. STAT. ANN. tit. 33, §451 (1964); Massachusetts, MASS. GEN. LAWS ANN. ch. 184, §1 (1969); Michigan, MICH. COMP. LAWS ANN. §554.135 (1967); Missouri, MO. ANN. STAT. §442.560 (Vernon Supp. 1974); Nevada, NEV. REV. STAT. §111.055 (1973); New Mexico, N.M. STAT.

ANN. §70-1-24 (1953); New York, N.Y. REAL PROP. LAW §10(2) (McKinney 1968); North Carolina, N.C. GEN. STAT. §64-1 (1975); North Dakota, N.D. CENT. CODE §47-01-11 (1960); Ohio, OHIO REV. CODE ANN. §2105.16 (Page 1968); Rhode Island, R.I. GEN. LAWS ANN. §34-2-1 (1956); South Dakota, S.D. COMPILED LAWS ANN. §43-2-9 (1967); Tennessee, TENN. CODE ANN. §64-201 (1955); Texas, TEX. REV. CIV. STAT. ANN. art. 166a (1969); Vermont, VT. CONST. ch. II, §62 (*But see* State v. Boston, C. & M. R.R., 25 Vt. 433 (1853), holding that there is no proper procedure for forfeiting property held by aliens, resident or nonresident, under state law); Washington, WASH. REV. CODE ANN. §64.16.005 (Supp. 1973); West Virginia, W. VA. CODE ANN. §36-1-21 (1966).

Group II. The following three jurisdictions restrict the ownership of realty to aliens eligible for citizenship. Because the Immigration and Nationality Act of 1952, 8 U.S.C. §1422 (1970), eliminated racial restrictions to eligibility, only three classes of aliens remain ineligible: (1) those opposed to organized government or favoring totalitarian forms of government; (2) deserters from the armed forces; and (3) persons relieved from service in the armed forces due to alienage; Arizona, ARIZ. REV. STAT. ANN. §33-1201 (1974); Colorado, COLO. CONST. art. II, §27; Louisiana, LA. CONST. art. 19, §21. The following three jurisdictions restrict aliens' realty ownership to those aliens who are the subjects of governments at peace with the United States: Georgia, GA. CODE ANN. §79-301 (1973); Maryland, MD. ANN. REAL PROP. CODE §14-101 (1974); Virginia, VA. CODE ANN. §55-1 (1969).

Group III. The following nine jurisdictions allow only resident aliens to own property: Alaska, the Alien Land Law, 48 U.S.C. §§1501 *et seq.* (1974) (in effect at statehood and never repealed); *see* Sullivan, *supra* note 43, at 20 n.26; Connecticut, CONN. GEN. STAT. ANN. §47-57 (1958); Hawaii, The Alien Land Law, 48 U.S.C. §§1501 *et seq.* (1970) (in effect at statehood and never repealed); Iowa, IOWA CODE ANN. §567.1 (Supp. 1974); Mississippi MISS. CODE ANN. §89-1-23 (1972); New Hampshire, N.H. REV. STAT. ANN. §477:20 (1968); New Jersey, N.J. STAT. ANN. §46:3-18 (Supp. 1974) (*but see* Caparell v. Goodbody, 132 N.J. Eq. 559, 29 A.2d 563 (1942), defining alien friends as subjects of a foreign state at peace with the United States. *But see also* an amendment to §46:3-18 in 1943, N.J. Laws 1943, ch. 145, §1, at 395, wherein friendly alien was defined to exclude nonresident aliens); Oklahoma, OKLA. STAT. ANN. tit. 60, §§121-22 (1971); Wisconsin, WIS. STAT. ANN. §710.02 (Spec. Pamphlet 1975) (limits nonresident alien ownership to a maximum of 640 acres).

Group IV. The following seven jurisdictions impose statutory limitations on resident and nonresident aliens: Illinois, ILL. ANN. STAT. ch. 6, §§1-2 (Smith-Hurd 1966) (limits aliens' right to hold realty to six years or until alien reaches majority); Indiana, IND. ANN. STAT. CODE §§32-1-8-1, -2 (Burns 1973) (limits aliens' right to hold realty in excess of 320 acres to five years from date of acquisition); Kentucky, KY. REV. STAT. ANN. §381.300 (Baldwin 1969) (limits aliens' right to hold realty to eight years after acquisition); Minnesota, MINN. STAT. ANN. §500.22 (Supp. 1974) (limits aliens' right to hold realty in excess of 90,000 square feet); Nebraska, NEB. REV. STAT. §§76-402 *et seq.* (1971) (limits aliens' right to hold realty in excess of five years unless the property is within the corporate limits of a village or city, or within three miles of the corporate limits of a village or city, or necessary for the operation of certain manufacturing, industrial, or petroleum establishments); Pennsylvania, PA. STAT. ANN. tit. 68, §32 (1965) (limits aliens' right to hold realty in excess of 5,000 acres or net annual income of $20,000); South Carolina, S.C. CODE ANN. §57-103 (1962) (limits aliens' right to hold realty in excess of 500,000 acres).

Group V. The following five jurisdictions have apparently allowed the common law to prevail: Kansas, Montana, Oregon, Utah, and Wyoming. WYO. STAT. ANN. §34-151 (1959), precludes nonresident aliens, ineligible for citizenship, from holding real property unless the ineligible alien's country allows a reciprocal right of ownership. Consequently, nonresident aliens eligible for citizenship are governed by the common law and take a defeasible title.

While a survey of state restrictions on alien ownership is useful in discerning trends in the law and in establishing the law's current position, the investigator should be aware that opposition to alien ownership will not disappear merely because a state does not actively preclude foreign investment in realty. For example, the hostility to the Kuwaiti purchase of Kiawah Island, South Carolina, was manifested by environmental and tax com-

several states have relaxed or repealed their laws, it is apparent that others have used wide latitude acting in this area. There is little or no continuity in the various statutes and little apparent rationale for the diverse restrictions.[74] Moreover, it is clear that in many cases the causes for alien restriction have been cyclical, topical reactions and that such reactions when addressed to resident aliens have been strongly attacked on equal protection grounds.[75]

Because some legislative restrictions on alien land ownership have been invalidated as improperly motivated does not necessarily imply that all response is unconstitutional or undesirable; however, divergent actions by the several states at different intensities do generate overwhelming confusion to foreign direct investors, legislators, and the executive branch. As a result, the inertia of these separate laws has inhibited the development of a national policy and a consistent foreign relations position in the area of F.D.I. in realty.[76]

Federal Regulation

Although the federal government has not acted in the area of privately titled real estate per se, several federal activities have a great effect on F.D.I. in realty. The treaty power, for example, affects F.D.I. because a treaty will control whenever it comes into conflict with state law.[77] The standard vehicle for regulating foreign investment between nations is the Treaty of Friendship, Commerce, and Navigation (F.C.N. treaties). The United States has entered into 130 treaties of this type since 1778.[78]

The touchstone of an F.C.N. treaty is reciprocity. The basic approach is to guarantee that, with respect to a certain activity, the nationals of each signator will receive either equal national treatment or the treatment accorded

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plaints. See note 31 *supra*. Of course, that a state does not preclude alien ownership of realty does not imply that it cannot. The maximum regulation might be established by common law disabilities as evidenced in *Group V*, *supra*, or by state constitution. Florida, for example, has no statute that directly addresses the right of a nonresident to purchase realty. The Florida constitution, however, provides that: "All natural persons . . . have inalienable rights, among which are the right to . . . acquire, possess, and protect property; except that the ownership, inheritance, disposition, and possession of real property by aliens ineligible for citizenship may be regulated or prohibited by law." FLA. CONST. art. I, §2. Thus, the maximum regulation in Florida for aliens ineligible for citizenship would be a move to *Group II*, *supra*.

74. *See, e.g.*, IND. ANN. STAT. CODE §§32-1-8-1, -2 (Burns 1973) (limiting alien ownership to 320 acres); MINN. STAT. ANN. §500.22 (Supp. 1974) (limiting alien ownership to 90,000 square feet); PA. STAT. ANN. tit. 68 §§28, 32 (1965) (limiting alien ownership to 5,000 acres or a net annual income of $20,000).

75. *See, e.g.*, *In re* Griffiths, 413 U.S. 717 (1973); note 68 *supra*.

76. Although the conclusion drawn in the 1962 survey that the circumstances surrounding alien real property regulation were no longer meaningful has not necessarily been proven, the view of alien land laws as anachronistic vehicles in reacting to such circumstances appears correct. *See* Sullivan, *supra* note 45, at 34.

77. *E.g.*, Terrace v. Thompson, 263 U.S. 197 (1923). Any doubt that state policies concerning aliens must yield to a valid exercise of the treaty power was put to rest in Kolovrat v. Oregon, 366 U.S. 187 (1961).

78. *Senate Hearings*, *supra* note 3, at 68.

a most favored nation.[79] A problem arises, however, in negotiating a treaty's provisions in the F.D.I. area because of the diversity in state laws. The federal government has been hesitant to abrogate the states' laws, yet it desires to negotiate treaties that will allow United States investment to expand overseas. The solution has been that, in the more recent treaties, "the United States has not accorded nationals of foreign states the privilege of acquiring lands within American territory if such acquisition is opposed by local state law."[80] This "solution" has forced foreign signatories to apply a treatment to American F.D.I analogous to that which the domicile state of the American investor would apply to the signatory's F.D.I.[81]

Another significant federal effect over F.D.I. in United States real estate lies in the area of federal income taxation. The present structure for taxing nonresident aliens and foreign corporations has its genesis in the Foreign Investor's Tax Act of 1966[82] passed, in part, to promote F.D.I. in the United States.[83] One of the most notable features of this Act was to create the concept of "effectively connected with a United States trade or business." This principle classified F.D.I. as business oriented (investment found effectively connected) or investment oriented (investment determined not effectively connected).[84] Thus F.D.I. income (fixed or determinable, annual or periodic income), whether corporate or individual, not effectively connected with United States trade or business, is taxed at a flat rate of 30 percent unless a lower treaty rate applies.[85] This tax is imposed on gross income from United

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79. *National treatment* results from a bilateral agreement to treat investors of the signatory countries as domestic investors. *Most favored nation treatment* gives to the foreign investor the most favorable treatment that is extended by the signatory to any other foreign country; this treatment may be less favorable than national treatment. See *Senate Hearings, supra* note 3, at 68. For example, the F.C.N. Treaty of March 27, 1956, with the Netherlands, art. VII, ¶1, gives national treatment to certain classes of investment activity; ¶2 excepts the exploitation of land and other natural resources from national treatment; ¶4, however, states that even in those areas where national treatment is not required, the countries will still extend most favored national treatment. *Id.* at 69.

80. 8 DIGEST INT'L L. 487 (1967).

81. *See, e.g.*, Treaty with Italy on commerce and navigation, Feb. 2, 1948, 63 Stat. 2255. Article VII, ¶1 provides that Italian investors are dependent on the laws and regulations in force within the American state or territory wherein the property is situated. This has been interpreted to mean that Italy would have the right to deny national treatment to United States investors if their domicile state denied national treatment to Italian investors. 8 DIGEST INT'L L. 489. In the Convention of Establishment with France, Nov. 25, 1959, 11 U.S.T. 2398, §§10, 11 of a protocol provide that France may apply treatment to American investors analogous to that with which the Americans' state of domicile will apply to French investors. *Id.* at 2422.

82. INT. REV. CODE OF 1954, §§871 *et seq.*

83. S. REP. NO. 1707, 89th Cong., 2d Sess., in 1966 U.S. CONG. & AD. NEWS 4446, 4454. See *House Hearings, supra* note 21, at 241. *See generally* Farrell, *Strategies for Foreign Corporations in the U.S. Realty Market*, 3 REAL EST. REV. Winter 1974, at 28, 28-37. Rosignoli & Landy, *Tax Planning for Non-Resident Alien Investors in U.S. Income-Producing Properties*, 3 THE TAX ADVISOR 551-57 (1972) (discussion of other methods of F.D.I. in United States realty, such as partnerships, trusts, and offshore funds).

84. *See* B. BITTKER & J. EUSTICE, FEDERAL INCOME TAXATION OF CORPORATIONS AND SHAREHOLDERS ¶17.02 at 17-13 (3d ed. 1971).

85. INT. REV. CODE OF 1954, §871(a)(1) (individual taxpayers), §881(a)(1) (corporations).

States sources, and no business deductions are allowed.[86] Income derived from an investment deemed effectively connected with American trade or business, however, will be taxed at the appropriate domestic, graduated corporate or individual rates on taxable income (recognizing appropriate deductions).[87]

The treatment of recognized capital gains from F.D.I. is more complicated, depending not only on whether gain is "effectively connected" but also on whether the F.D.I. is in corporate or individual form. If effectively connected with United States trade or business, capital gains are taxable to both individual and corporate taxpayers at domestic graduated rates.[88] If their gain is not effectively connected, individual foreign direct investors present in the United States for 183 days or more will be taxed at a flat rate of 30 percent on recognized capital gain.[89] If the investment is *not* effectively connected with United States trade or business, however, capital gains of foreign direct corporate investors and individual investors not present in the United States for 183 days or more are *tax free*.[90]

If income derived from F.D.I. in United States realty is effectively connected, thus taxable at progressive rates with allowable deductions, then gain recognized on the disposition of this realty should also be effectively connected and subject to taxation. Conversely, if the attendant income is not effectively connected and the taxpayer is not an individual present in the United States for 183 days or more, recognized gain on this disposition should be tax free.

A feature more important to F.D.I. in American realty is that both corporate and individual foreign direct investors may elect to have income and capital gains derived from real property investment determined not effectively connected with United States trade or business treated as if it were from effectively connected realty.[91] The taxpayer can choose the treatment that will give him the greatest benefit, which in some cases will be no taxation at all.[92]

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86. *Id.* For individuals, three deductions exist regardless of their connection: (1) casualty or loss deductions, *id.* §873(b)(1) (*see also* §165(c)(3)); (2) deductions for charitable contributions, *id.* §170; and (3) one personal exemption, *id.* §§151, 142(b)(1).

87. INT. REV. CODE OF 1954, §§871(b), 882(a). The terms "resident-nonresident" and "effectively connected" are terms of art. *See generally* Alexander, *U.S. Taxation of Real Estate Owned by Non-Resident Aliens and Foreign Corporations*, 21 U. MIAMI L. REV. 651 (1967); Crockett & Ashwell, *Federal Taxation of Non-Resident Aliens and Foreign Corporations*, 13 DUQUESNE L. REV. 37 (1974); Feinschreiber & Feinschreiber, *Foreign Investment in U.S. Real Estate: The Federal Tax Considerations*, 3 REAL EST. L.J. 144 (1974), for a discussion of these terms and this area of taxation.

88. INT. REV. CODE OF 1954, §§871(b), 882(a).

89. *Id.* §871(a)(2).

90. INT. REV. CODE OF 1954, §§871(a)(2), (b)(2); see Feinschreiber & Feinschreiber, *supra* note 82, at 146.

91. *See* INT. REV. CODE OF 1954, §§871(d), 882(d).

92. The election, once made, is generally revokable only by consent of the Commissioner, although tax treaties may provide a year by year election. Because gain from the sale of realty may be tax free if no election is taken, there is a significant advantage to being able to terminate the election. There also may be a significant advantage in electing to treat income from realty investment as effectively connected, thus taxable on a net income base, and then terminating the election for a tax-free capital gain on the realty's sale. A clear example of such an advantage to foreign direct investors is found in art. V and art. X of the

This election provision should promote F.D.I. in real property and natural resources.[93]

OTHER COUNTRIES' METHODS OF REGULATING F.D.I.

A thread which appears to run throughout national policies in F.D.I. is the notion of reciprocity or, perhaps, the fear of foreign retaliation.[94] This concept is notably absent in the states' legislation in this area.[95] Consequently, in order to evaluate the concept of reciprocity, a review of several other countries' methods of regulating F.D.I. in real estate is appropriate.

Canada

In the twentieth century, foreign capital has played a greater role in the Canadian economy than it has in the economy of any other advanced nation. Over the past decade, however, there have been noticeable changes in public and official attitudes toward this high level of foreign ownership.[96] In 1972 the Canadian government published an exhaustive study, commonly known as the *Grey Report*,[97] concerning the role of foreign investment in the Canadian economy. In response to this study, the Canadian government passed the Foreign Investment Review Act in 1973[98] to review each proposed foreign

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Netherlands Antilles-United States income tax treaty. For any taxable year these provisions allow an election to treat income and gain as "effectively connected" and thus taxable on a net income base. *See* Langer, *Analysis of the Netherlands Antilles-U.S. Income Tax Treaty* in FOREIGN TAX HAVENS 3D 57, 65 (1974). A case study prepared for the Practicing Law Institute cogently demonstrates how this treaty may be used by foreign direct investors to purchase United States realty at a minimal tax cost. Langer, *Case Study: How Nonresident Aliens Use Netherlands Antilles Companies to Buy U.S. Real Estate* in FOREIGN TAX HAVENS 3D 103 (1973). *See also* Feinschreiber & Feinschreiber *supra* note 87, at 150. It has further been noted that "in almost every conceivable case, it will be advantageous to form a foreign corporation to make the investment in United States real property." Ross, *United States Taxation of Aliens and Foreign Corporations: The Foreign Investors Tax Act and Related Developments*, 22 TAX L. REV. 279, 318 (1967).

93. At least one commentator has noted that such promotion of F.D.I. might not be wise. "While such a policy might be termed 'neo-isolationism,' when viewed in light of the current fervor over growing foreign control over natural resources and energy reserves [encouragement of domestic investment] could well merit consideration." Crockett & Ashwell, *supra* note 87, at 40. It is interesting to note that INT. REV. CODE OF 1954, §892, exempts from taxation the income of foreign governments received from investments from any source in the United States. As OPEC monetary reserves grow, this Code provision will become increasingly significant to these foreign direct investors.

94. See text following note 41 *supra*.

95. See note 73 *supra* for the states' legislation.

96. In 1964, 46% of the people felt that Canada had enough United States capital, while 33% wanted more. By 1972, 67% thought Canada had enough, while only 22% welcomed more United States investment. Fayerweather, *Nationalism or Continentalism? Canada Reacts to U.S. Investment*, CHALLENGE, (SEPT-OCT. 1973) (*cited in* Crain, *The Regulation of Foreign Direct Investment in Australia, Canada, France, Japan, and Mexico*, CONG. RESEARCH SERV. Multilith No. 74-52 E. (1974), at 7).

97. THE GOVERNMENT OF CANADA, FOREIGN DIRECT INVESTMENT IN CANADA (1972).

98. Foreign Investment Review Act of 1973, 21-22 Eliz. II, c. 46 (Can.).

equity investment in Canada in order to determine whether the investment is consonant with Canada's long-run economic plans.[99]

The most significant change in the Canadian view of F.D.I. has come at the provincial level, where there has been a developing concern over the foreign ownership of land. The response to foreign ownership has taken the form of provincial laws that place severe restrictions on the transfer of land to foreigners. Several examples are illustrative. In Ontario Province, an alien purchasing vacation property is subject to a heavy land transfer tax amounting to 20 percent of the purchase price, and anyone selling to a foreigner is taxed up to 50 percent of his profit.[100] Prince Edward Island requires government approval for sales to aliens of tracts larger than ten acres or of more than 330 feet of shore front.[101] Sasketchewan prohibits the sale of realty valued at more than $15,000 to any nonresidents of the province.[102] Nova Scotia has taken the most drastic action by expropriating American owned property. Moreover, this province has compiled a list of land parcels that it wishes to reacquire, either by negotiated settlements or by expropriation.[103]

There are several apparent reasons for provincial reaction to F.D.I. in Canadian realty. Feelings of nationalism lead to the belief that local Canadians, not foreigners, should own Canadian land. An Ontario study revealed that foreign ownership in parts of the Great Lakes region is as high as 90 percent.[104] In some areas of Nova Scotia, foreigners own over half of the available vacation land.[105] Another reason is that foreign money is driving land prices out of the reach of Canadians.[106] Although such legislation restricting nonresident direct investment in Canadian realty is being tested in the Canadian courts, the Canadian Supreme Court upheld the restriction limiting aliens' purchases by holding that Prince Edward Island's regulation of all landowners who are aliens to the Province (both Canadian and non-Canadian citizens) did not invade the exclusive authority of Parliament and only conferred on aliens to Canada the same rights and restrictions as all Canadian citizens concerning the legitimate regulation of property ownership in Prince Edward Island Province.[107] Notably, there is no Canadian federal law in this area.[108]

99. *See* Comment, *Foreign Investment*, 7 VAND. J. TRANSNAT'L L. 725 (1974). *See also* Lamont, *Emerging Neo-Mercantilism in Canadian Policy Toward State Enterprises and Foreign Direct Investment*, 8 VAND. J. TRANSNAT'L L. 121 (1974); *Statutory Controls*, *supra* note 34, at 166-67.

100. *See* Lamont, *supra* note 99, at 123; MacIntosh, *Foreign Investment in Canada — Recent Trends*, in PRIVATE INVESTORS ABROAD — PROBLEMS AND SOLUTIONS IN INTERNATIONAL BUSINESS IN 1974 113-14 (V. Cameron ed. 1975); Wall Street Journal, Sept. 9, 1974, at 28, col. 1.

101. See note 100 *supra*.

102. *Id.*

103. *Id.*

104. Wall Street Journal, Sept. 9, 1974, at 28, col. 2.

105. *Id.*

106. *Id*

107. Morgan v. Attorney-General, 42 D.L.R.3d 603 (U.E.I. Sup. Ct. 1973), *aff'd*, 55 D.L.R.3d 527 (Can. Sup. Ct. 1975); *see* Toronto Star, Feb. 22, 1975, at B6, col. 1.

108. See Toronto Star, note 107 *supra*. It is ironic that 1.5 million Canadians own

The similarity between the Canadian experience and current development in the United States is striking. Both countries are politically stable, consist of large land masses, and have greatly benefited from foreign direct investments in the past. Both have a state-federal system of government and derive their land laws from the common law. There is, however, one crucial difference: Canada has a large amount of F.D.I. occurring within Canada compared to her direct investment abroad.[109] The United States position is the reverse — greater investment abroad rather than foreign investment at home.[110] Thus, Canada has a much smaller exposure to retaliatory restrictions on F.D.I. from countries affected by her restrictions than has the United States.

Japan

For most of the post-World War II era, Japanese policy on foreign investment was severely restrictive.[111] Since 1967, however, Japan has been liberalizing her regulation of F.D.I. The liberalization involved several important policy decisions: (1) to vary the degree of liberalization among industries; (2) to discriminate according to the degree of foreign ownership; and (3) to distinguish between the establishment of new firms and the acquisition of existing firms.[112] These policies were effected primarily by the creation and regulation of three groups of industries: *Category I* — foreign investment was permitted, without individual screening, if foreigners acquired no more than 50 percent ownership; *Category II* — investment was open to 100 percent foreign ownership; *unliberalized* investment in industries not assigned to either category, as well as investment exceeding 50 percent in *Category I* industries, still required individual validation.[113] This liberalization consisted of movements of industries into the more unrestricted categories. Four rounds of liberalization were planned in 1967 to be completed within five years.[114] The fourth round was completed in 1971, one year ahead of schedule.[115]

In 1971 the real estate industry moved into *Category I*.[116] A fifth round of liberalization was initiated in 1973 moving real estate to *Category II* and allowing 100 percent foreign ownership. This phase-over to complete

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property in Florida and that Ontario Premier William Davis has a winter home in Ft. Lauderdale, Florida. Wall Street Journal, Sept. 9, 1974, at 28, col. 3.

109. *See, e.g.*, Dunn, *Canada and Its Economic Discontents*, 52 FOREIGN AFFAIRS, Oct. 1973, at 119-40; Gibson, *Canada's Declaration of Less Independence*, 51 HARV. BUS. REV., Sept.-Oct. 1973, at 69-79.

110. See text accompanying note 38-40 *supra*.

111. *See generally* Furuhashi, *New Policy Toward Foreign Investment Issues in the Japanese Capital Liberalization*, MICH. ST. UNIV. BUS. TOPICS, Spring 1972, at 2.

112. Crain, *supra* note 96, at 44.

113. *Id.* at 45.

114. *See generally Statutory Controls, supra* note 34, at 163-65.

115. *See generally* CURRENT LEGAL ASPECTS OF DOING BUSINESS IN THE FAR EAST (R. Allison ed. 1972); Furuhashi, *Foreign Capital in Japan*, COL. J. WORLD BUS., Mar.-Apr. 1972, at 50; Furushashi, *supra note* 111; King, *Restrictions on U.S. Investment*, 11 SAN DIEGO L. REV. 27, 56-57 (1973); *Statutory Controls, supra* note 34; at 163-65.

116. See note 114 *supra*.

ownership is to be completed by 1976.[117] It must be noted, however, that Japan's realty prices are among the highest in the world.[118] Japan may have been motivated to liberalize its regulations in this comparatively nonlucrative investment area in order to protect from retaliation its substantial investments in real estate abroad.[119]

Latin America

Under Mexico's recently enacted Foreign Investment Law of 1973,[120] all real property owned by foreigners in Mexico must be registered with the Ministry of Foreign Affairs.[121] These investors must also make an agreement with the Mexican government pursuant to the Calvo Clause, which precludes the foreign investor from involving his country's official assistance in Mexican land disputes.[122] Further, although the Mexican constitution prohibits foreign ownership of land within a "prohibited zone,"[123] the new act will allow foreigners to become beneficiaries of a land trust, with a trust duration of thirty years. Additionally, although transient aliens are precluded from acquiring real estate, resident and nonresident aliens may invest in land trusts and even acquire direct ownership of Mexican land, if not located within the "prohibited zone."[124]

Foreign equity investment in Mexican business enterprises owning legal title to realty outside the "prohibited zone" is allowed, provided such participation does not exceed 49 percent foreign ownership. Although such an investment precludes these businesses from owning property in the "prohibited zone," they may acquire beneficial interests in a land trust.[125] Again, the investment must be registered with the Ministry of Foreign Affairs and must include a Calvo Clause agreement.

Perhaps the most interesting reaction to F.D.I. has been the creation of

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117. *See House Hearings, supra* note 21, at 449; N.Y. Times, April 28, 1973, at 44, col. 4; Wall Street Journal, Apr. 26, 1973, at 4, col. 1.

118. 25 Tokyo Municipal News, Mar. 1975, no. 2, at 1200. A Japanese worker, to purchase a piece of real estate, would have to spend all the wages he had earned in six years and 149 days. An American worker would need only 45 days wages; a West German worker would need 174 days wages. *Id.* See note 21 *supra.*

119. See text accompanying note 21 *supra.*

120. LAW FOR THE PROMOTION OF MEXICAN INVESTMENT AND TO REGULATE FOREIGN INVESTMENT, DIARO OFFICIAL, Mar. 9, 1973.

121. *Id.* art. 17.

122. See note 120 *supra.* The Calvo Clause requires that the foreign investor agree not to invoke official assistance from his country in any questions arising from his ownership of land in Mexico. *See generally* Eder, *Expropriation: Hickenlooper and Hereafter,* 4 INT'L LAW. 611 (1970).

123. FEDERAL CONSTITUTION OF THE UNITED STATES OF MEXICO, art. 27, ¶1. The prohibited zone is all land within 100 kilometers of Mexican land borders and within 50 kilometers of Mexican seacoasts. *Id.*

124. *See* Meek, *Land Transfer and Finance in Mexico,* 4 DENVER J. OF L. & POL. 25, 29 (1974). *See also* Chayet & Sutton, *Mexican Real Estate Transactions by Foreigners,* 4 DENVER J. OF L. & POL. 15 (1974); King, *supra* note 115, at 49-53; Vilaplana, *The Forbidden Zones in Mexico,* 10 CAL. WEST. L. REV. 47 (1973).

125. *See* Meek, *supra* note 124, at 27.

the Andean Common Market and the adoption of the Andean Investment Code.[126] The Code classifies enterprises as national,[127] mixed,[128] and foreign.[129] The heart of the Code is its scheme of divestment or transformation of foreign enterprises. All foreign firms established after July 1, 1971, must divest themselves of sufficient equity so that, eventually, all firms enjoying the benefits of trade liberalization will be held by national investors.[130] In essence, all firms wishing to participate in tariff reductions must transform themselves into national or mixed enterprises. The Code establishes procedures for effectuating this "fade-out" from foreign to mixed or national firms.[131] Bolivia and Ecuador, the most underdeveloped of the six member nations, are allowed a longer period to "fade-out" foreign control than are Chile, Colombia, Peru, and Venezuela.[132] Although the new control may be governmental rather than private, divestment insures local control over F.D.I. for each member of the Andean group. It further provides a systematized procedure for local investors to "phase-into" control of their own economy.[133]

Saudi Arabia

Saudi regulation generally prohibits the ownership of realty by non-Saudis, but it does grant specific exceptions. A non-Saudi, for instance, will not be allowed to purchase real estate located within the limits of the Holy Mosques of Mecca and Medina.[134] The non-Saudi, however, may acquire the right of ownership with regard to arable land, if the acquisition is approved by the Ministers of Agriculture and Interior.[135] Foreign enterprises permitted to operate in Saudi Arabia may own realty necessary to their activity, provided a license is obtained from the Minister of Commerce and Industry.[136] Lying beyond these proscriptions, a non-Saudi direct investor, on Royal approval

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126. Andean Foreign Investment Code, 11 INT'L LEGAL MAT. 126 (1972). The Andean Common Market includes Bolivia, Chile, Colombia, Ecuador, Peru, and Venezuela.

127. *Id.* art. 1. A national enterprise is one more than 80% owned or controlled by national investors. A national investor is defined to include private citizen nationals, non-profit legal persons (also nationals), and foreign nationals who have completed one year of residence and have promised not to remove or transfer profits out of the country.

128. *Id.* A mixed enterprise is one 51 to 80% owned or controlled by national investors. A firm may be classified as mixed despite more than 50% *foreign* ownership, however, if: (a) the state is the minority owner; and (b) the state, despite minority ownership, has a determining voice in the management of the enterprise. *Id.* art. 36.

129. *Id.* art. 1. A foreign enterprise is one in which a foreign national has majority ownership and the minority ownership is not in the state. *See generally* Valdez, *The Andean Investment Code: An Analysis*, 7 J. INT'L L. & ECON. 1, 6-7 (1972).

130. Valdez, *supra* note 129, at 9.

131. *Andean Foreign Investment Code*, 11 INT'L LEGAL MAT. 126, arts. 3(c), 28-31.

132. *Id. See also* Lisocki, *The Andean Investment Code*, 49 NOTRE DAME LAW. 317, 321 (1973).

133. *See generally* King, *supra* note 111, at 53-54; Oliver, *The Andean Foreign Investment Code: A New Phase in the Quest for Normative Order as to Foreign Direct Investment*, 66 AM. J. INT'L 763 (1972); *House Hearings, supra* note 21, at 408-18.

134. Royal Decree No. m/22 of 12/7/1390 (Sept. 13, 1970), ¶1.

135. *Id.* ¶3(b).

136. *Id.* ¶3(c).

and with a recommendation from the Minister of the Interior, may own real estate for his private dwelling or for investment purposes.[137]

It is apparent from an analysis of other countries' F.D.I. proscriptions that strict regulation of F.D.I. is becoming increasingly prevalent around the world. This is in no small part a reaction to the tremendous growth of United States based multinational enterprises involved in overseas direct investment.[138] Therefore, the time has arrived for the United States to recognize the reciprocal nature of transnational investment and to consider the effects of increased United States regulation on F.D.I., whether at state or federal level, on international foreign investment equilibrium.

THE CONSTITUTIONALITY OF REGULATING F.D.I. IN UNITED STATES REAL ESTATE

The need for United States regulation (but not necessarily proscription) of F.D.I. is clear in light of the recent increase in F.D.I. in United States realty as well as the global tendency for other countries to regulate foreign property ownership. The threshold issue, however, is not the need for regulation but whether the United States Constitution allows regulation of nonresident alien investors. Further, assuming that such investment can be regulated, are the states preempted from such regulation by the foreign affairs powers exclusively given to the federal government?[139]

The Due Process and Equal Protection Challenge

The most prevalent constitutional challenges to regulation of F.D.I. in realty have been premised on the due process and equal protection clauses of the fourteenth amendment. In *Shames v. Nebraska*,[140] a federal district court noted that "[t]he Supreme Court has never indicated in unequivocal terms whether a State is required to give due process to nonresident aliens."[141] Holding that a Nebraska statute regulating a nonresident alien's right to inherit real property[142] did not violate due process, the district court relied

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137. *Id.* ¶3(d).

138. *See, e.g.*, Gabriel, *MNC's in The Third World: Is Conflict Unavoidable?*, 50 HARV. BUS. REV., July-Aug. 1972, at 93; *New Era for the Multinationals*, BUS. WEEK, July 6, 1974, at 93.

139. U.S. CONST. art. I, §8. This section grants to Congress certain powers with respect to the conduct of foreign affairs. Article II, §2 grants such powers to the President. Further, article I, §10 prohibits the states from entering into any agreement or compact with a foreign power. These provisions, construed together, have been interpreted to mean that the power over foreign affairs is an exclusive federal power. *See* United States v. Pink, 315 U.S. 203, 223 (1942); United States v. Belmont, 301 U.S. 324, 331 (1937). *See generally* Note, *Alien Inheritance Statutes: An Examination of the Constitutionality of State Laws Restricting the Rights of Non-Resident Aliens to Inherit from American Decedents*, 25 SYRACUSE L. REV. 597 (1974).

140. 323 F. Supp. 1321 (D. Neb.), *aff'd.*, 408 U.S. 901 (1971).

141. *Id.* at 1333.

142. The rights of nonresident aliens to take by inheritance from United States citizens has been extensively litigated and commented on. *See, e.g.*, note 168 *infra*; note 140 *supra*;

heavily on a series of Supreme Court decisions that upheld the validity of alien land laws.

In *Terrace v. Thompson*,[143] the Supreme Court upheld the Washington alien land law,[144] noting that:

> [E]ach state in the absence of any treaty provision to the contrary, has power to deny to aliens the right to hold land within its borders. . . . State legislation applying alike and equally to all aliens, withholding from them the right to own land, cannot be said to be capricious or to amount to an arbitrary deprivation of liberty or property, or to transgress the due process clause."[145]

Terrace further expressly upheld the alien land law against an equal protection challenge, noting that the only aliens excluded from ownership of land were those Congress found ineligible for citizenship (primarily Japanese)[146] and those who had failed to declare their intent to become United States citizens.[147] The Court reasoned that the inclusion of good faith declarants in the same class with citizens did not unjustly discriminate against aliens who were ineligible or who failed to declare their intention to become citizens. The Court further held that "the state act is not repugnant to the equal protection clause and does not contravene the fourteenth amendment."[148] In a line of cases argued the same day,[149] the Court also upheld the California alien land law,[150] citing *Terrace* as controlling and noting that the only distinguishing point between the two statutes was that the California statute did not preclude eligible aliens from purchasing realty because they had failed to declare their intent to become citizens.[151]

It is of crucial importance to a foreign direct investor whether he will be protected by the due process or equal protection clause of the fourteenth amendment. The due process clause provides that "[n]o state shall deprive *any person* of life, liberty or property, without due process of law."[152] Consequently, the threshold due process issue becomes a question of whether a nonresident is a "person" under the fourteenth amendment.[153] The Supreme Court's vacillation on this threshold applicability of due process protection

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Note, *supra* note 139; Note, *Non-Resident Alien Inheritance of Nebraska Land: 1854-1971*, 4 CREIGHTON L. REV. 304 (1971) [hereinafter cited as *Inheritance of Nebraska Land*].

143. 263 U.S. 197 (1923).

144. *Id.* at 213 n.2.

145. *Id.* at 217.

146. See note 73 *supra, Group II.*

147. 263 U.S. at 219-20.

148. *Id.* at 222.

149. Porterfield v. Webb, 263 U.S. 225 (1923); *accord*, Frick v. Webb, 263 U.S. 326 (1923); Webb v. O'Brien, 263 U.S. 313 (1923).

150. *See* Webb v. O'Brien, 263 U.S. 313, 319 n.1.

151. *See* Porterfield v. Webb, 362 U.S. 225, 233.

152. U.S. CONST. art. XIV, §1 (emphasis added).

153. Constitutional challenges on due process and equal protection grounds applicable to the states pursuant to the fourteenth amendment apply as well to federal action either expressed or implied by the fifth amendment due process clause. *See* Bolling v. Sharpe, 347 U.S. 497 (1954).

to nonresident aliens continues to trouble courts faced with this issue.[154] The Court in *Shames* avoided this troublesome area by holding that the Nebraska statute,[155] which provided that under certain circumstances property inherited by a nonresident alien would escheat to the state, did not violate the due process clause.[156] Thus, the Court did not need to decide "whether or not a State must accord nonresident aliens due process."[157] The *Shames* Court reasoned that *Terrace* was still the controlling precedent on the substantive merits of a due process challenge to nonresident alien regulation, stating:

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154. See text accompanying note 141 *supra*. The following are the principle cases marshalled in support of extending due process to nonresident aliens. Russian Volunteer Fleet v. United States, 282 U.S. 481 (1931). The Court, faced with an issue of statutory interpretation in a contract dispute arising before the United States Court of Claims, stated that "petitioner was an alien friend, and as such was entitled to protection of the fifth amendment of the Federal Constitution." *Id.* at 489. United States v. Pink, 315 U.S. 203 (1942). The Court, faced with claims on the State of New York by foreign creditors concerning the distribution of assets of a Russian insurance corporation nationalized by the Soviet Union, stated that "aliens as weli as citizens are entitled to the protection of the fifth amendment." *Id.* at 228. Yet the Court allowed New York to grant priority to local creditors. *Id.* Sardino v. Federal Reserve Bank, 361 F.2d 106 (2d Cir.), *cert. denied*, 385 U.S. 898 (1966). The court cogently presented the argument, noting that "the due process clause speaks in terms not of taking but of deprivation," and held that an argument that "'[t]he Constitution of the United States confers no rights on non-resident aliens' is so patently erroneous in a case involving property in the United States that we are surprised it was made." *Id.* at 111.

The authorities that seem contrary to the vesting of the constitutional rights in nonresident aliens are: Toop v. Ulysses Land Co., 237 U.S. 580 (1915). The Court dismissed an appeal alleging that the Nebraska alien land law was repugnant to the fourteenth amendment and stated that "we think also [that the allegation] is too frivolous to afford a basis for jurisdiction." *Id.* at 583. Bridges v. Wixon, 326 U.S. 135 (1945). In determining the constitutionality of a deportation proceeding, the Court said: "[A]n alien brings with him no constitutional rights . . . . The Bill of Rights is a futile authority for the alien seeking admission for the first time to these shores. But once an alien lawfully enters and resides in this country he becomes invested with the rights guaranteed by the Constitution to all people within our borders. Such rights include . . . the due process clause of the fourteenth amendment." *Id.* at 161 (concurring opinion). Johnson v. Eisentrager, 339 U.S. 763 (1950). Again faced with determining the constitutional propriety of exclusion, the Court stated: "But, in extending Constitutional protection beyond the citizenry, the Court has been at pains to point out that it was the alien's presence within its territorial jurisdiction that gave the Judiciary the power to act." *Id.* at 771. Sam Andrews' Sons v. Mitchell, 457 F.2d 745 (9th Cir. 1972). In determining whether commuter aliens are entitled to full constitutional protection when on jobs within the United States, the court stated that "the resident alien has a constitutionally protected presence. Any person within the United States, citizen or alien, resident or non-resident, is protected by the guarantees of the Constitution." *Id.* at 749. This line of cases, *Bridges*, *Johnson*, and *Mitchell*, seems to develop a territoriality theory of constitutional rights. Such a theory would somewhat ameliorate the views expressed by the dissent in *Shames*, 323 F. Supp. at 1341, and the court in *Sardino*, 361 F.2d at 111, that the taking of a nonresident alien's property without compensation would be repugnant to due process. By making an appearance, the foreign direct investor might recover his investment even if the restrictive law was held valid. For an analysis of the cases, *supra*, in the context of an inheritance statute, see *Inheritance of Nebraska Land*, *supra* note 142, at 313-35.

155. 323 F. Supp. at 1324 nn. 5-7.

156. *Id.* at 1335.

157. *Id.* at 1333.

> [A] state's absolute bar of ownership of land by nonresident aliens has been held by the Supreme Court to be within the valid exercise of that state's police power, and not violative of due process of law under the Fourteenth Amendment.[158]

The Supreme Court's affirmance of *Shames* tends to strengthen that conclusion. Thus, unless the Supreme Court speaks in more definitive terms on the issue of nonresident aliens' right to due process with respect to realty ownership, their F.D.I. in United States realty appears to have no such protection.

The equal protection clause states that "[n]o state shall . . . deny to *any person* within its *jurisdiction*, the equal protection of the laws."[159] Thus, from the view of a foreign direct investor, the qualifications for equal protection coverage are stricter than for due process; not only must the nonresident alien be a person recognizable by law, but he must also be within the jurisdiction of a state. The *Terrace* line of cases dismissed the equal protection argument summarily,[160] and the current trend applies equal protection to aliens in a manner at least implying a resident-nonresident alien dichotomy.[161]

The Supreme Court in *Graham v. Richardson*[162] declared the classification of "aliens" a suspect category and stated that "a 'person' in [a fourteenth amendment context] encompasses lawfully admitted resident aliens, as well as citizens of the United States, and entitles both citizens and aliens to equal protection of the laws of the state in which they reside."[163] Similarly, the Court in *In re Griffiths*[164] noted that "resident aliens, like citizens, pay taxes, support the economy, [and] serve in the Armed Forces. . . . It is appropriate that a state bear a heavy burden [when regulating in this area]. . . ."[165] It is apparent in both cases that the Court did not intend to reach the issue of the includability of nonresident aliens into this suspect category.

The *Shames* Court also summarily dismissed an equal protection argument using the "states' jurisdiction" language to distinguish nonresident aliens.[166]

158. *Id.* at 1335. See also text following note 171 *infra.* Although this court's rationale does not depend on whether the Supreme Court ultimately decides that nonresident aliens have vested due process rights, if this vesting is clearly determined, the penalties for violation of a legitimate state statute precluding nonresident alien ownership of realty will have to be examined. As noted by the dissent in *Shames*, 323 F. Supp. at 1344 and the court in *Sardino*, 361 F.2d at 111, there is a line of cases implying a violation of due process if nonresident alien owned property is confiscated without compensation. See note 154 *supra.* This problem seems easily resolved by shaping a penalty that does not require foreign-owned realty to escheat without compensation. For example, the statute might provide that violators be fined, their illegally purchased realty escheat, and fair compensation be paid to the foreign direct investor. Fair compensation could be set at the lesser of his purchase price or the proceeds from the state's sale of the property, less the fine imposed.

159. U.S. CONST. art. XIV, §1 (emphasis added).

160. See notes 143, 149 *supra.*

161. *But see* note 154 *supra*, discussing a territorial notion in the vesting of constitutional rights.

162. 403 U.S. 365 (1971).

163. *Id.* at 371.

164. 413 U.S. 717 (1973).

165. *Id.* at 722.

166. 323 F. Supp. at 1333.

Yet, while defending its finding that due process and equal protection did not attach to nonresident aliens, the court noted that the California alien land law upheld in *Porterfield v. Webb*[167] was later declared unconstitutional by the California supreme court on equal protection grounds.[168] This apparent non sequitur is resolved by the true purpose of the California statute, which was to preclude Japanese immigration. This racial discrimination was recognized by the California supreme court's holding in *Sei Fujii v. State*.[169] Therein the court stated:

> [T]he California alien land law is obviously designed and administered as an instrument for effectuating *racial* discrimination. . . . There is nothing to indicate that those alien *residents* . . . as a class, might use the land for purposes injurious to public morals, safety, or welfare.[170]

Similarly, as Justice Rehnquist noted in his dissent in *Griffiths*, the thrust of the California alien land law was to discriminate by country of origin and thus "conflicts with the core purpose of the equal protection clause. . . ."[171] Consequently, *Fujii* did not reach the issue of due process at all. Furthermore, it addressed only the racially discriminatory effects of the California statutes on resident aliens and did not reach the fundamental question of whether discrimination against nonresident aliens, as a class, would be repugnant to the fourteenth amendment.

The precise issue of whether the fourteenth amendment will allow a foreign direct investor in United States real estate to be precluded from purchasing land or an interest in land has not come before the Court since *Terrace* and its progeny, and the Court has taken no unequivocal action to overrule those decisions when applied to nonresident aliens. The Court's affirmance of *Shames* has strengthened future reliance on the *Terrace* holding. It thus appears that regulation of F.D.I. in realty, even to the extent of preclusion, falls within the bounds of the fourteenth amendment unless it is based on the investor's race or country of origin.

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167. 263 U.S. 225 (1923).

168. Sei Fujii v. State, 38 Cal. 2d 713, 242 P.2d 617 (1952); *accord*, Haruye Masaoka v. People, 39 Cal. 2d 883, 245 P.2d 1062 (1952). The Oregon alien land law had previously been declared unconstitutional by the Oregon supreme court in Kenji Namba v. McCourt, 204 P.2d 569 (Ore. 1949). Both *Nambe* and *Fujii* relied on Oyama v. California, 332 U.S. 633 (1948), which held the application of the California alien land law in a manner denying a minor citizen the right to hold property because his parents were ineligible aliens to be a violation of the equal protection clause of the fourteenth amendment. The state courts further relied on Takahashi v. Fish & Game Comm'n, 334 U.S. 410 (1948), which held the application of the California law in a manner precluding ineligible alien residents from obtaining commercial fishing licenses (thus denying them the chance to work) to be repugnant to equal protection. *See generally* Note, *Immigrants, Aliens and the Constitution*, 49 NOTRE DAME LAW. 1075 (1974).

169. 38 Cal. 2d 718, 242 P.2d 617 (1952). *See generally* Ferguson, THE CALIFORNIA ALIEN LAND LAW AND THE FOURTEENTH AMENDMENT, 35 CALIF. L. REV. 61 (1947).

170. 38 Cal. 2d at 737-38, 242 P.2d at 630 (emphasis added).

171. 413 U.S. at 665.

Federal Preemption

The most prevalent and potent methods of regulating F.D.I. in realty are state laws. Yet the Constitution has delegated to the federal government the exclusive power to act in the area of foreign affairs.[172] The notion that state regulation of nonresident aliens could improperly infringe on this exclusive power was forcefully established by the Supreme Court in *Zschernig v. Miller*.[173] *Zschernig* concerned an Oregon statute regulating nonresident aliens' right to inheritance that was alleged an invalid intrusion into the federal sphere of foreign affairs. The Court, relying on *Clark v. Allen*,[174] found this type of reciprocity statute[175] constitutional on its face but unconstitutional as applied. The improper intrusions found by the Court consisted of comments on the political systems, ideologies, and administrations of foreign governments in the state court's opinion on the reciprocity required by the Oregon statute.[176] The Supreme Court has continued to follow the *Clark v. Allen* rationale by its affirmance of *Shames*, wherein the court interpreted *Zschernig* as "meaning no more than judicial criticism of foreign governments is constitutionally impermissible."[177] Thus the Court, by its affirmance in *Shames*, has not extended *Zschernig* beyond the "name calling" facts on which it held, still leaving the states free to enact reciprocal inheritance legislation.[178]

There is, however, a critical difference in the consequences of state restrictions on inheritance and restrictions on realty ownership. The effect of a state requirement that reciprocity be accorded its citizens before a nonresident alien could inherit American property would have a minimal impact on the United States as a nation. The country as a whole is not threatened by the possibility that an American individual may lose inheritance rights overseas because of retaliation. The United States economy is critically de-

172. U.S. CONST. art 1, §8; *see* note 139 *supra*.

173. 389 U.S. 429 (1968).

174. 331 U.S. 503 (1947). The Court in *Clark* held that the California statute, requiring reciprocity as a condition precedent to inheritance, was not an unconstitutional infringement on the federal foreign relations power. The Oregon statute's reciprocity provision at issue in *Zschernig* was identical.

175. ORE. REV. STAT. §111.070 (1965). The statute required that several criteria be met before a nonresident alien could inherit from an Oregon citizen: (1) the existence of a reciprocal right in the alien's country to take real and personal property; (2) the reciprocal right to receive money originating from estates within the alien's country; and (3) proof that the foreign recipient would receive "use, benefit, and control" of the estate. *See generally* Comment, *Inheritance by Non-Resident Aliens*, 8 VA. J. TRANSNAT'L L. 419 (1968).

176. 389 U.S. at 503. *See generally Inheritance of Nebraska Land*, *supra* note 142, at 318-20.

177. 323 F. Supp. at 1332; *accord*, Bjarsch v. DiFalco, 314 F. Supp. 127 (S.D.N.Y. 1970); Mora v. Battin, 303 F. Supp. 666 (N.D. Ohio 1969); Goldstein v. Cox, 299 F. Supp. 1389 (S.D.N.Y. 1968).

178. The Court in *Shames* quoted approvingly from *Goldstein*: "We appreciate that the Supreme Court, may eventually, go further than it has thus far gone . . . . But we conceive it to be our duty to enforce the law as it is, and not as it may be in the future." 323 F. Supp. at 1332 (quoting Goldstein v. Cox, 299 F. Supp. 1389, 1394 (S.D.N.Y. 1968)).

pendent on international trade and investment.[179] Retaliation could have a dramatic impact on the entire country. A prime example was the 1973 oil embargo. Adverse effects, however, are not always dramatic or apparent. American reaction to Arab direct investment in the United States has been used to justify, in part, the Arab boycott of firms doing business with Israel.[180] Therefore, even if state alien land laws do not violate the fourteenth amendment, they patently interfere with the federal government's exclusive constitutional right to direct foreign relations. Moreover, the statutes at issue in *Zschernig* and *Shames* guaranteed the nonresident aliens' rights to inherit provided there was reciprocity in his home country.[181] Several states have similar reciprocity provisions in their alien land laws.[182] Nevertheless, these statutes, while analogous to the inheritance statutes, would still act in an area of vital interest to the country as a whole and thus be distinguishable from matters involving individual inheritance rights, which have little effect on American foreign relations.

FUTURE DEVELOPMENTS

One clear alternative to the current hodgepodge of state and federal regulation is for Congress to expressly legislate in this area. A second alternative is federal preemption of the states' regulations. While the current bills before Congress do not directly address regulation of F.D.I. in realty,[183] federal statutes that establish a national scheme of regulation have been broadly construed to preempt state law. The Supreme Court in *Hines v. Davidowitz*[184] acknowledged the preemption of a Pennsylvania statute that required alien registration and held that the Nationality Act of 1940[185] evidenced a congressional intent to form a national scheme for the regulation of aliens. The Court further noted that "[o]ur system of government . . . imperatively requires that federal power in the field affecting foreign relations be left entirely free from local interference. . . ."[186] Another example of federal regulation in F.D.I. is found in the purpose of the Foreign Investors Tax Act of 1966, which is, in part, to increase foreign direct investment in the United States;[187] yet, state alien land laws certainly frustrate this congressional purpose.[188]

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179. See text accompanying note 38 *supra*. *See generally* Statement by Charles P. Kindleberger, in *Senate Hearings*, *supra* note 3, at 126.

180. FORTUNE, July 1975, at 170.

181. See notes 142, 175 *supra*.

182. See note 73 *supra*, *Group II*.

183. See note 34 *supra*.

184. 312 U.S. 52 (1941).

185. Act of Oct. 14, 1940, ch. 876, 54 Stat. 1137, *as amended*, 8 U.S.C. §§1101 *et seq.* (1970).

186. 312 U.S. at 63. The Court had previously stated in United States v. Belmont, 301 U.S. 324 (1937), that "complete power over international affairs is in the national government and is not and cannot be subject to any curtailment or interference on the part of the several states." *Id.* at 331.

187. S. REP. NO. 1707, 89th Cong., 2d Sess., in 1966 U.S. CONG. & AD. NEWS 4446, 4454; *see House Hearings*, *supra* note 21, at 241.

188. See text accompanying note 35 *supra*, for the Administration's position encouraging the free flow of international investment. *See generally* L. HENKIN, FOREIGN AFFAIRS AND THE

A third alternative is for the Supreme Court to extend the rationale established by *Zschernig* that a federal common law regulates the areas of exclusive federal jurisdiction; in this context, foreign relations as affected by F.D.I. in American realty. This solution would preempt state action even if Congress does not speak in this area.[189] However, there exist several other areas where state action has a great potential for affecting foreign relations. The most notable of these are recognition of foreign country judgments and concern over private international law. Although these areas require state courts to evaluate foreign countries' legal systems and have a potential for abuse analogous to such inquiries as those found impermissible by the Supreme Court in *Zschernig*, thus far the states' jurisdiction has not been challenged.[190] Of course, because these state actions affecting foreign relations have not been challenged does not mean that they cannot be preempted. The key question is the encroachment effect of the states' actions on the federal foreign relations power. It is on this issue of the regulation's effect that state regulation of F.D.I. in United States realty is distinguishable from state action in recognition of foreign money judgments or private international law.

While there is good cause to preserve the states' powers to protect their citizens, F.D.I. is still significantly more crucial to the nation as a whole than the recognition of money judgments within a single state. One or more states' restrictions on F.D.I. might well invoke retaliation affecting the entire United States.[191] Even if reciprocal "rights" exist pursuant to an F.C.N. treaty or executive agreement, an affected United States direct investor abroad may not want to force the issue of responding to this retaliation through federal

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CONSTITUTION 203-48 (1972); Moore, *Federalism and Foreign Relations*, 1965 DUKE L.J. 248.

189. This remely introduces the issue of whether there exists a federal judicial power to develop rules for problems bearing on foreign relations. Since Erie R.R. v. Tompkins, 304 U.S. 64 (1938), federal courts have been faced with this issue of developing a specific federal common law. *See, e.g.*, Clearfield Trust Co. v. United States, 318 U.S. 363 (1943); D'Oench Duhme & Co. v. Federal Deposit Ins. Corp., 315 U.S. 447 (1942). The Court addressed this issue in a foreign relations context in Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398 (1964). Justice Harlan, speaking for the Court, stated that: "If federal authority in this instance, this Court, orders the field of judicial competence in this area for the federal courts, and the state courts are left free to formulate their own rules, the purposes behind the doctrine could be as effectively undermined as if there had been no federal pronouncement on the subject." *Id.* at 424. *See generally* Friendly, *In Praise of Erie—and of the New Federal Common Law*, 39 N.Y.U.L. REV. 383 (1964); Hill, *The Law Making Power of the Federal Courts: Constitutional Preemption*, 67 COLO. L. REV. 1024 (1967); Hirsch, *Toward a New View of Federal Preemption*, 1972 U. ILL. L.F. 515 (1972).

190. Private international law concerns the conflict of laws among nations. Currently, the state courts make decisions that touch foreign affairs because they must determine whether a foreign court has exercised due process before honoring the foreign country judgment. *See generally* Peterson, *Foreign Country Judgments and the Second Restatement of Conflicts Laws*, 72 COLUM. L. REV. 220 (1972).

191. The United States is generally treated as a single entity by foreign nations. *See* Bergman, *Soviet Heirs in American Courts*, 62 COLUM. L. REV. 257, 269 (1962). *But see* F.C.N. treaties, *supra* note 81. Even if a treaty provides that the foreign signatory may retaliate reciprocally with a single state, that country, depending on its bargaining position, would still appear to have the option to go against the entire United States.

diplomatic channels for fear of further reprisals by the host government.[192] Further, the United States Government may not wish to raise the matter too forcefully, in order to preserve political and economic relationships with the host country.[193] Whatever conflicts that might arise would, nevertheless, have to be negotiated at the federal level due to the federal government's exclusive jurisdiction over foreign affairs.[194] Therefore, it is crucially important that the right to invest transcend any state's desire to retain power in this field.

There is a fourth possible course of action concerning those statutes that require reciprocity before allowing nonresident aliens to purchase land.[195] This course of action is premised on the *Bernstein*[196] exception to the Act of State doctrine.[197] This approach would allow the judiciary, when required to evaluate a foreign country's political or economic regulation of F.D.I., to defer to the federal executive branch for a determination of the foreign relations impact of these judicial actions. By taking judicial notice of the executive branch's findings, the courts could make a determination that would be consistent with national foreign policy objectives.[198] The Supreme Court, however, has taken a dim view of presidential intervention into judicial affairs. In *Zschernig*, for instance, the Court ignored statements made by both the State and Justice Departments to the effect that state inheritance statutes did not interfere with the conduct of foreign affairs.[199] In the decision of *First National City Bank v. Banco Nacional de Cuba*,[200] six of the Justices expressed an aversion to allowing the executive branch's participation in judicial determinations by way of the *Bernstein* exception.[201] Thus it is unlikely that the Supreme Court would permit such pervasive presidential influence on the judiciary that a case-by-case determination of F.D.I. would require.

CONCLUSION

The history of state alien land laws since the Revolution clearly shows that restrictions on F.D.I. in realty have been topical, cyclical responses to temporal events. The road back to rationality after these reactions has been

192. *See generally* 1965 PROCEEDINGS OF THE SECTION ON INTERNATIONAL LAW OF THE AMERICAN BAR ASSOCIATION (REPORT OF COMMITTEE ON COMMERCIAL TREATIES) 215.

193. *See* King, *supra* note 115, at 64. These factors have led to a conclusion that "the concept of national treatment as set forth in most of these [F.C.N.] treaties has not been a fully effective device for the protection of investors." *Id.*

194. See note 139 *supra.*

195. See note 73 *supra, Group II.*

196. Bernstein v. N.V. Nederlandsche, 210 F.2d 375 (2d Cir. 1954).

197. *See generally* Delson, *The Act of State Doctrine — Judicial Defense or Abstention?*, 66 AM. J. INT'L L. 82 (1972); Metzger, *The State Department's Role in the Judicial Administration of the Act of State Doctrine*, 66 AM. J. INT'L L. 94 (1972).

198. *See* Note, *Reciprocity and Retention Statutes — A New Direction?*, 22 RUTGERS L. REV. 770, 782-86 (1968).

199. Brief for the United States as Amicus Curiae, 36 U.S.L.W. 4120, 4121, 4129.

200. 406 U.S. 759 (1972).

201. *Id. See generally* Lowenfeld, *Act of State and Department of State:* First National City Bank v. Banco Nacional de Cuba, 66 AM. J. INT'L L. 795 (1972).

long and difficult. Regardless of the past, F.D.I. in United States realty has recently been on the increase, a trend that is likely to continue. This rise in F.D.I. is predominately due to five factors: (1) economic advantages of productivity in the American market, (2) the availability of scarce raw materials, (3) the promotion of investment within the United States by state and federal governments,[202] (4) the devaluation of the dollar and world economic disequilibrium, and (5) the abundance of OPEC monetary reserves that require investment.[203] Although these factors may not be permanent shifts in the world investment picture, their effect will be significant even in a short-run application on our economy.

By analyzing Canada's scheme of regulation, insight can be gained into what may occur if short term fears are permitted to control decision making.[204] Congress has taken a significant step by establishing and funding a major analysis of F.D.I.'s impact on the United States;[205] nevertheless, it must be remembered that Canada prepared the *Grey Report*[206] yet failed to prevent a xenophobic reaction in the provinces. As long as the several states have an independent power to regulate the F.D.I. in real estate, they will have a concomitant power to regulate United States foreign policy. In today's world, economic power is arguably more potent than physical strength;[207] with the great United States economic exposure abroad, it is in our best interest to have the federal government regulate F.D.I. This is not a cry for the diminution of federalism or the abrogation of states' rights. It is merely an acknowledgment that the Constitution has delegated the management of our foreign relations to the federal government, and state land laws are contrary to that effectuation.[208]

The federal government must be aware that transnational interaction should be firmly grounded on fairness and reciprocity. Escalating retaliation would not serve any country's long-run economic goals. New restrictions on F.D.I. by the United States might encourage allegations of economic "hypocrisy," undermining United States credibility abroad. Conversely, there are benefits that would accrue from a free flow in international investment

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202. See *House Hearings, supra* note 21, at 249-51.

203. See *Statutory Controls, supra* note 34, at 174.

204. See text accompanying notes 96-110 *supra.*

205. Act of October 26, 1974, Pub. L. No. 93-478, 88 Stat. 1450.

206. THE GOVERNMENT OF CANADA, FOREIGN DIRECT INVESTMENT IN CANADA (1972).

207. The most dramatic use of an economic weapon against the United States was the Arab oil embargo of 1973. After analyzing the legal issues in this economic coercion, a commentator stated: "[I]t may be reasonably concluded that the oil embargo employed by the Arab oil producing states (OAPEC) was not a breach of customary international law, of any international agreement among the participants, or any pertinent United Nations obligations." Boorman, *Economic Coercion in International Law: The Arab Oil Weapon and the Ensuing Juridicial Issues,* 9 J. INT'L L. & ECON. 205, 231 (1974).

208. This acknowledgment is not a novel interpretation of the Constitution. The Vermont supreme court in 1859 stated: "[T]he right to interfere with aliens holding real estate in this country, strictly and appropriately belongs to the national and not to the state sovereignty." State v. Boston C. & M. R.R., 25 Vt. 433, 439 (1859).

capital. For example, investment of Mideast capital reserves in the United States could create a common desire for a stable American economy.[209]

The evidence clearly indicates an increase of F.D.I. in United States real estate, yet the amount of this investment and the identity of the investors remains undisclosed. Congress has moved to ascertain the extent of F.D.I. in realty by enacting the Foreign Investment Study Act,[210] and there are bills currently before Congress that would require disclosure by foreign direct investors.[211] With such information at hand and with an understanding of the interdependence of transnational investment, the federal government will be properly armed to shape a national policy based on economic and legal principles rather than the historical xenophobia.

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209. See *Statutory Controls*, *supra* note 34, at 186.
210. See note 205 *supra*.
211. See note 34 *supra*.