

Closing the Open Door to Foreign Direct Investment

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Recommended Citation

Kubota, Carolyn J. (1982) "Closing the Open Door to Foreign Direct Investment," *Cornell International Law Journal*: Vol. 15: Iss. 1, Article 4.
Available at: <http://scholarship.law.cornell.edu/cilj/vol15/iss1/4>

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CLOSING THE OPEN DOOR TO FOREIGN DIRECT INVESTMENT

The United States traditionally has neither encouraged nor discouraged foreign direct investment.¹ In fact, the United States, as a means of attaining its goal of maximizing freedom for trade, investment, and capital flows in the world economy, has long urged that other countries adopt this policy of neutrality, the so-called open door policy, towards foreign direct investment.² In the early 1970's, however, the United States discovered that the appeal of the open door approach to foreign direct investment varied as economic conditions changed. Before the 1970's, firms based in the United States were rapidly expanding abroad, while foreign investment in the United States remained inconsequential.³ Changes in the international economy triggered an influx of foreign investment into the

1. In 1977, the Economic Policy Group issued a policy statement for the Carter Administration that upheld the long-standing United States commitment to an open international economic system. The policy statement concluded that

"[t]he fundamental policy of the U.S. Government toward international investment is to neither promote nor discourage inward or outward investment flows or activities. . . .

The Government, therefore, should normally avoid measures which would give special incentives or disincentives to investment flows or activities and should not normally intervene in the activities of individual companies regarding international investment."

The Operations of Federal Agencies in Monitoring, Reporting on, and Analyzing Foreign Investments in the United States: Hearings before the Subcomm. on Commerce, Consumer, and Monetary Affairs of the House Comm. on Government Operations, 96th Cong., 1st Sess. pt. 3, 328 (1979) [hereinafter cited as 1979 Hearings], reprinting Economic Policy Group statement (July 6, 1977).

The policy statement also confirmed the commitment of the United States to neutral treatment by stating that governments "should not discriminate against established firms on the basis of nationality or deprive such firms of their rights under international law." *Id.* at 328, *reprinting* Economic Policy Group statement (July 6, 1977). *See also* Niehuss, *Foreign Investment in the United States: A Review of Government Policy*, 16 VA. J. INT'L L. 65, 67-69 (1975).

2. *See 1979 Hearings, supra* note 1, pt. 2, at 199 (statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

3. In 1975, Professor Benjamin Cohen testified before the Subcommittee on Foreign Commerce and Tourism of the Senate Committee on Commerce as follows:

This growth of American concern about foreign investment in our country is not without its irony. For decades, when the United States was by far the largest exporter of capital in the world, American officials and business leaders traditionally preached just the benefits of international investment, advocating full reliance on the operation of free-market forces to determine the direction of capital flows throughout the world. Little attention was paid or credence given to concerns expressed in capital-importing countries about the potential costs, at least to them, of foreign investments. . . .

United States,⁴ exciting public concern and precipitating two administrative policy reviews. These reviews reaffirmed the open door policy and called for more empirical data.⁵ United States policymakers still maintain that the economic and political costs of foreign direct investment are insufficient to warrant a change in United States policy.⁶

Following the second policy review, conducted in 1975, foreign direct investment in the United States expanded at an ever-increasing rate.⁷ Because of this persistent increase, policy questions regarding foreign direct investment have acquired new significance. Foreign direct investment has become a permanent factor in the economy of the United States, rather than a transient economic phenomenon.

This Note examines the adequacy of the response of the United States to foreign direct investment and concludes that the United States should reconsider its present policy of neutrality. The present indiscriminate treatment of foreign direct investments ignores the complexity of the matter, and fails to take into account the costs of foreign direct investment. In order to evaluate the available policy choices, one must understand the impact of foreign direct investment on the United States economy and upon the political scene. Accordingly, this Note first examines the reasons for foreign direct investment and its economic and political effects.

This Note then considers two approaches to foreign direct investment. House bill 7750⁸ presents one version of the first approach. The bill sought to amend the Securities Exchange Act of

. . . Yet now that the shoe is on the other foot, and it is we who are increasingly the host of international investment flows, many Americans would have us do what previously this country criticized others for doing.

Foreign Investment Legislation: Hearings on S. 329, S. 995, S. 1303, and Amendment No. 393 Before the Subcomm. on Foreign Commerce and Tourism of the Senate Comm. on Commerce, 94th Cong., 1st Sess. 141-42 (1975) (testimony of Professor Benjamin J. Cohen) [hereinafter cited as 1975 Hearings], reprinted in 1979 Hearings, supra note 1, pt. 3, at 17. See H. STEPHENSON, THE COMING CLASH 12 (1972).

4. See *infra* notes 19-20 and accompanying text.

5. See *infra* notes 65-77 and accompanying text.

6. See *infra* notes 78-82 and accompanying text.

7. At the end of 1975, foreign direct investment in the United States amounted to \$27,662 million. Chung & Fouch, *Foreign Direct Investment in the United States, 1977*, SURV. CURRENT BUS., Aug. 1978, at 39, 46. This amount represented approximately a 10% increase over the previous year. Foreign direct investment rose approximately 23% to a total of \$52,260 million by the end of the year. Chung & Fouch, *Foreign Direct Investment in the United States in 1979*, SURV. CURRENT BUS., Aug. 1980, at 38, 38. Thus, both the rate of growth and the total amount of foreign direct investment nearly doubled within this four-year period.

8. H.R. 7750, 96th Cong., 2d Sess. (1980). The bill has now died from inattention.

1934⁹ to create reciprocal limitations on foreign investment. Specifically, the bill would have made it unlawful for a foreign corporation to acquire the beneficial ownership of equity securities, unless the laws and regulations of the incorporating country had been no more restrictive than United States Federal law with respect to like investments by United States corporations in the incorporating country.¹⁰ Proponents of the bill apparently believed that its enactment would have reduced the barriers to foreign direct investment that United States investors encountered abroad by inducing foreign nations to reduce the restrictions they placed on inflows of investment capital in order to secure investment privileges for their nationals in the United States.¹¹ Moreover, the proposed statute would have prevented those countries unwilling to admit United States investors on terms equivalent to those offered by the United States from taking advantage of the lenient open door policy.¹²

9. 15 U.S.C. §§ 77b-77e, 77j-77k, 77m, 77o, 77s, 78a-78d, 78e-78l, 78m-78o, 78o-3 to 78hh, 78ii-78jj (1976), amended by 15 U.S.C. §§ 77(b)(15), 77c(a)(2), (6)-(7), (9)-(10), (b), 77(d)(6), 77s(c), 78c(a)(12), (40), 78k(a)(3), 78m(b), (d)(1), (g)-(h), 78o(d), 78u(g), 78ff (Supp. IV 1980).

10. The bill provided in full as follows:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 13(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(d)) is amended by adding at the end thereof the following new paragraph:

"(7) It shall be unlawful for any person incorporated in a foreign country to acquire, directly or indirectly, the beneficial ownership of equity securities of the type and in the amount described in paragraph (1) of this subsection unless the laws and regulations of the country in which such person is incorporated are no more restrictive than the provisions of this title and other Federal law with respect to the acquisition, by a person incorporated in a State of the United States, of a like amount of equity securities issued by a person incorporated in such foreign country. The President may waive the application of this paragraph in any case in which he determines such waiver is required by a national emergency."

H.R. 7750, 96th Cong., 2d Sess. (1980).

11. Apart from other doubts concerning the success of this quid pro quo approach in bringing about the desired reduction in other nations' restrictions on foreign direct investment, *see infra* text accompanying notes 123-24, the limited scope of House Report 7750 would have handicapped the effectiveness of the proposed statute. The proposed statute apparently would have applied only to the acquisition of the beneficial ownership of equity securities by foreign corporations. *See supra* note 10. Moreover, the proposed statute would have tested a corporate investor's eligibility only by examining the laws and regulations of the incorporating nation. *Id.* The nationality of a corporation's owners, however, often differs from the nationality of the corporation itself. Consequently, foreigners might have avoided the apparent intent of the proposed statute by shopping for an incorporating country that subscribes to an open door policy concerning foreign direct investment. This Note concerns not so much the particular provisions of House bill 7750, however, as the bill's general quid pro quo approach to foreign direct investment.

12. This is the standard rationale for reciprocal limitations. For a discussion of the merits of reciprocal limitations on foreign direct investment, see D.F. LAMONT, FOREIGN STATE ENTERPRISES 23-25, 43-47, 193-202 (1979); see also 1979 Hearings, *supra* note 1,

The second approach to foreign direct investment is a case by case screening procedure. It is the thesis of this Note that a screening procedure deserves consideration as a policy device that will permit the United States to regulate future foreign direct investment in accord with its national interests, without significantly hampering the international flow of investment capital.

I. AN OVERVIEW OF FOREIGN DIRECT INVESTMENT

At the end of 1979, the aggregate of foreign direct investment¹³ in the United States was \$52,260 million.¹⁴ This represented a twenty-three percent increase over the previous year, following a similar increase in 1978.¹⁵ These increases were more than double the average accretions in the years 1975 to 1977,¹⁶ and the pace of growth in foreign direct investment shows no signs of slackening.¹⁷

As with domestic investors, the prospect of economic gain is the

pt. 3, at 21-30 (testimony of Douglas F. Lamont, Dean, Walter E. Heller School of Business Administration, Roosevelt University).

13. The conventional definition of foreign direct investment is the ownership of a partial or total controlling interest in an enterprise. This definition distinguishes a direct investment from an indirect or portfolio investment, *i.e.*, an investment that does not provide the investor with operating control of the enterprise involved. Note, *U.S. Regulation of Foreign Direct Investment: Current Developments and the Congressional Response*, 15 VA. J. INT'L L. 611, 613-15 (1975). For instance, the International Investment Survey Act of 1976, 22 U.S.C. §§ 3101-3108 (1976), amended by 22 U.S.C.A. §§ 3108 (West 1979), and by 22 U.S.C. §§ 3103(a)(3), (d), 3107(b), 3108 (Supp. III 1979), defines direct investment as "the ownership or control, directly or indirectly, by one person of 10 per centum or more of the voting securities of an incorporated business enterprise or an equivalent interest in an unincorporated business enterprise." 22 U.S.C. § 3102(10) (1976). The Act defines portfolio investment as "any international investment which is not direct investment." *Id.* § 1302(11). The Act's definition of direct investment principally concerns the ownership or control of profitmaking organizations, but also covers the ownership of real estate. *Id.* § 3102(6).

Of course, the quality of being foreign is the second major part of any definition of foreign direct investment. Any law on foreign direct investment must include some standard by which to test the foreignness of the investment capital or the investor or both. In the case of foreign corporate investment and investors, any such standard is often elusive and problematic. See generally Kronstein, *The Nationality of International Enterprises*, 52 COLUM. L. REV. 983 (1952); Vagts, *The Corporate Alien: Definitional Questions on Federal Restraints on Foreign Enterprises*, 74 HARV. L. REV. 1489 (1961).

Finally, because it suggests only capital movements for the purpose of establishing lasting economic relations, the word investment may supply some substantive content to the definition of foreign direct investment. See, *e.g.*, ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT (OECD), INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISES, REVIEW OF THE 1976 DECLARATION AND DECISIONS, 45 n. 7 (1979) [hereinafter cited as 1979 OECD REVIEW].

14. Chung & Fouch (Aug. 1980), *supra* note 7, at 38.

15. See *supra* note 7.

16. See Chung & Fouch (Aug. 1978), *supra* note 7, at 46; Chung & Fouch (Aug. 1980), *supra* note 7, at 38.

17. U.S. NEWS & WORLD REP., Feb. 13, 1978, at 79, 79.

foreign investor's primary motivation.¹⁸ Commentators generally attribute the currently favorable foreign investment climate in the United States to six factors: first, the depreciation of the United States dollar in foreign exchange markets; second, and closely related, the depressed value of the United States stock and real estate markets; third, the economic and political stability of the United States; fourth, the size and homogeneity of many markets within the United States; fifth, possible access to United States technological innovations; and sixth, the availability of raw materials and scarce natural resources.¹⁹ In addition, fear of future protectionism and

18. 1979 Hearings, *supra* note 1, pt. 1, at 8 (testimony of Professor Jeffrey S. Arpan). The pertinence of this proposition for most foreign investors was never in dispute. In the mid-1970's, however, many members of the Organization of Petroleum Exporting Countries (OPEC) began making large-scale investments in the United States. Many Americans feared that political rather than economic goals motivated these government-controlled investments. See Note, *supra* note 13, at 611-13, 618, 621-26, 629, 633-47. Such fears notwithstanding, OPEC governments generally behave like other large institutional investors. Indeed, sophisticated and conservative Western investment advisers manage the vast bulk of OPEC government funds and exercise considerable discretion over their clients' accounts. Niehuss, *supra* note 1, at 99-102.

19. H.R. REP. NO. 1216, 96th Cong., 2d Sess. 9-10 (1980) [hereinafter cited as H.R. REP. NO. 1216]; Chung & Fouch, (Aug. 1980), *supra* note 7, at 40-41.

The depreciation of the dollar makes investment in the United States cheaper in terms of foreign currency and so increases the purchasing power of foreign investors. The proliferation of dollars abroad creates additional investment incentive. H.R. REP. NO. 1216, *supra*, at 10. The Comptroller of the Currency recently testified: "[T]he result of the U.S. international account deficit position is to place excess dollars in the hands of foreigners, virtually inviting them to invest in the United States." 1979 Hearings, *supra* note 1, pt. 4, at 65 (testimony of John G. Heiman, Comptroller of the Currency).

Because of the depressed value of the United States stock market, many major companies have been selling at below net asset value. H.R. REP. NO. 1216, *supra*, at 10. For a foreign investor, "US common stocks now look the cheapest as well as the fastest way to a stake in America." *Foreign Investment in the USA*, 1978 MULTINATIONAL BUS. 12, 15. *But cf.* Address by Dieter zur Loye, Senior Executive Vice President and Chief Operating Officer of the American Hoechst Corporation, Société de Chimie, American Chapter, New York, New York (May 23, 1980), *printed in* VITAL SPEECHES OF THE DAY, July 15, 1980, at 599, 599-601. (Mr. zur Loye, a West German corporate executive, takes the position that bargain prices are not always the primary motivation for European investment in United States firms. He maintains that, instead, many foreign investors pay high prices for United States acquisitions, because it is often necessary in terms of international corporate strategy to establish a position in the United States market.)

Foreign investors perceive the United States as a politically stable investment environment and relatively free from governmental regulatory controls on the economy. Concerned by an apparent long-run trend toward socialism in many parts of the world, many investors regard the United States as the last bastion of capitalism. U.S. NEWS & WORLD REP., Feb. 13, 1978, at 79, 79. United States attractions also include a large, homogeneous market united by a common language and common laws. The sheer size of the United States market presents greater potential for future growth and profits than its smaller European counterparts. Wall St. J., Aug. 21, 1979, at 1, col. 2. Moreover, many firms believe that successful competition within the United States is a prerequisite to developing an internationally competitive position. H.R. REP. NO. 1216, *supra* note 19, at 9.

By making investments in the United States, foreign firms may acquire access to United States technological innovations, which in turn may be transferred to a parent firm abroad. 1979 Hearings, *supra* note 1, pt. 1, at 48-57 (testimony of Eldon E. Sweezy).

stricter trade restrictions by the United States government has stimulated foreign direct investment in the United States.²⁰

The effects of foreign direct investment on the economy of the United States are too far-reaching to estimate with accuracy. It is apparent, however, that foreign direct investment does not only produce benefits. In gauging the impact and desirability of foreign direct investment, United States policymakers should concentrate on its effect on the United States balance of payments.²¹ Proponents of the policy of neutrality argue that foreign direct investment holds down the balance of payments deficit and bolsters the international value of the United States dollar by increasing capital flows into the United States.²² This, however, is not necessarily true.

Greater foreign direct investment does not necessarily signal the inflow of capital from abroad.²³ Many foreign investors borrow between sixty and eighty percent of their investment funds from the United States credit market.²⁴ By augmenting the demand for domestic funds, these foreign investors exert an upward pressure on United States interest rates.²⁵

See infra notes 44-47 and accompanying text. Similarly, foreign investors may seek a guaranteed source of raw materials or natural resources. 1979 *Hearings, supra* note 1, pt. 1, at 9 (testimony of Professor Jeffrey S. Arpan).

20. Chung & Fouch (Aug. 1980), *supra* note 7, at 41.

21. As a general proposition, foreign direct investment will benefit the United States balance of payments if it generates greater demand for dollars abroad, and thereby causes the value of the dollar to appreciate—or to depreciate less rapidly. If the investment results in a net outflow of dollars, the supply of dollars abroad will increase and thereby cause their value to fall. 1979 *Hearings, supra* note 1, pt. 3, at 213.

22. For an expression of this point of view, see 1979 *Hearings, supra* note 1, pt. 2, at 198-204 (statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

23. In 1976, the Department of Commerce reported that, although capital inflows were significant in 1974, banks and other sources in the United States were the largest suppliers of capital for foreign-owned firms in the United States. 1 U.S. DEP'T OF COMMERCE, FOREIGN DIRECT INVESTMENT IN THE UNITED STATES 235-36 (1976). In 1978, a Chase Manhattan Bank study noted that foreign subsidiaries in the United States were financed primarily by United States commercial banks. CHASE MANHATTAN BANK, FOREIGN DIRECT INVESTMENT IN THE UNITED STATES 40 (1978).

24. *Id.* The experience of United States firms that invest abroad indicates that domestic credit markets are commonly the source of funds for foreign direct investment. For example, a study of the activities of multinational corporations in Brazil and Mexico made this finding:

Of the net sources of funds used by U.S. manufacturing subsidiaries in the 1958-68 period, only 20 percent represented new capital inflows from the parent. . . .

(This includes funds borrowed internationally by the U.S. parent and then invested in the foreign affiliate.) The remaining 80 percent was produced internally by the subsidiary itself or borrowed locally

R. NEWFARMER & W. MUELLER, MULTINATIONAL CORPORATIONS IN BRAZIL AND MEXICO: STRUCTURAL SOURCES OF ECONOMIC AND NONECONOMIC POWER, REPORT TO THE SUBCOMM. ON MULTINAT'L CORPS. OF THE SENATE COMM. ON FOREIGN RELATIONS, 94TH CONG., 1ST SESS. 16 (Comm. Print 1975).

25. Domestic borrowing by foreign-owned firms has the same effect on the United States credit market as does domestic borrowing by United States firms: the demand for

Although highly leveraged²⁶ foreign investments in the United States may not initially harm the United States balance of payments, the long-term repatriation²⁷ of profits earned on such investments may ultimately produce a net outflow of capital.²⁸ In the late 1960's, when they faced domestic opposition to large scale exportation of investment capital,²⁹ firms based in the United States used this possibility to justify outflows of investment capital. United States corporations maintained that they repatriated dividends and profits from their foreign investments in amounts greater than the capital outflows to host countries.³⁰ As one American businessman stated: "It is simply a matter of economics that foreign investments ultimately return a lot more dollars than they siphon off."³¹ The profits generated by foreign direct investment in the United States may follow a similar course and flow back to the investors' home countries.

Foreign direct investment indirectly affects the United States balance of payments through its impact on United States trade accounts. If foreign direct investment displaces imports—*e.g.*, when an investment is responsible for the domestic manufacture of a pre-

funds increases, and to the extent that money markets become tighter, interest rates tend to rise. 1979 Hearings, *supra* note 1, pt. 3, at 214.

26. A leveraged investment is an investment that the investor finances in part by debt. Such an investor usually pays for his purchase with a small capital outlay and a large percentage of borrowed funds. The investor is thus able to earn a relatively high rate of return while putting at risk a relatively small amount of his own capital.

27. The term repatriation generally refers to the return of foreign investment capital, or profits or other income derived from it, to the country from which it originally came. At a minimum, the term refers to the removal of such money from the country where it was invested.

28. The General Accounting Office recently noted:

"Theoretically, if investment capital comes from abroad, the host country has an immediate short-term benefit from the balance-of-payments standpoint. However, as profits and interest are repatriated to the home country and exceed vested capital, the balance-of-payments effects ultimately become adverse. The United States, according to this theory, thus stands to face future balance-of-payments problems."

H.R. REP. NO. 1216, *supra* note 19, at 15, quoting GEN. ACCOUNTING OFFICE, EMERGING CONCERNS OVER FOREIGN INVESTMENT IN THE UNITED STATES 33 (1975). See also 1979 Hearings, *supra* note 1, pt. 1, at 142 (testimony of Professor Robert G. Hawkins).

As an example, assume that a foreign investor acquires a United States corporation for \$10 million, paying \$2 million in cash and borrowing the remainder from a United States bank. If this investor repatriates \$4 million of profits from the investment, the United States will experience a net outflow of \$2 million—not accounting for the time value of money—and a corresponding intertemporal debit in its balance of payments.

29. See U.S. TARIFF COMM'N, REPORT TO THE SUBCOMM. ON INT'L TRADE OF THE SENATE COMM. ON FINANCE, 93D CONG., 1ST SESS. 21-23 (Comm. Print 1973).

30. See *id.* at 29-30.

The term home country refers to the country from which the foreign investor comes, and the term host country refers to the state where the foreign investor makes an investment.

31. R. NEWFARMER & W. MUELLER, *supra* note 24, at 12, quoting Eugene Latham, president of Mexletter Investment.

viously imported good—the trade accounts and the balance of payments will improve.³² Conversely, an affiliate in the United States may harm the trade accounts and balance of payments by serving as a sales outlet for a foreign parent, or by importing component parts for assembly in the United States.³³ The experience of the foreign affiliates of United States firms also illustrates this point.³⁴ A 1973 report by the United States Tariff Commission examined the impact of the foreign investments of multinational corporations on the economies of home and host countries.³⁵ It stated that “the appropriate conclusion for the seven countries surveyed is that the MNCs [multinational corporations], in their dealings with their parent country, exerted a large and growing negative or adverse influence on host-country balances of payments.”³⁶

Americans generally think that foreign direct investment creates new manufacturing facilities, such as the Honda Motor Company's proposed construction of an automobile assembly plant in Ohio.³⁷ Most foreign direct investment, however, involves the acquisition of healthy, established businesses.³⁸ In 1979, the acquisition of established firms consumed ninety-three percent of the total foreign investment expended in the United States.³⁹ Because they are buying into a new business environment, foreign investors prefer investments with a proven record of performance.⁴⁰ The purchase of a healthy United States business can provide a foreign investor with immediate access to United States marketing, manufacturing, and research facilities that would have been costly and time consuming to develop.⁴¹

32. 1979 Hearings, *supra* note 1, pt. 3, at 213.

33. *Id.*

34. A study conducted by the Department of Commerce in 1972 indicated that United States firms maintaining affiliates abroad were responsible for 25% of all United States exports. The export earnings of United States manufacturers increased because of shipments of goods, including manufacturing components, to affiliates in countries where no market for these United States goods previously existed. H.R. REP. NO. 1216, *supra* note 19, at 15-16. See also R. NEWFARMER & W. MUELLER, *supra* note 24, at 12. If this trend reverses, imports into the United States will increase as a result of foreign direct investment, and the balance of payments and trade accounts will suffer.

35. U.S. TARIFF COMM'N, *supra* note 29, at 78.

36. *Id.* at 30.

37. N.Y. Times, Jan. 12, 1980, at A1, col. 1.

38. H.R. REP. NO. 1216, *supra* note 19, at 16.

39. Int'l Inv. Div., *U.S. Business Enterprises Acquired or Established by Foreign Direct Investors in 1979*, SURV. CURRENT BUS., Jan. 1981, at 28, 36.

40. John L. Gornall, an attorney who represents many foreign investors, recently testified: “I find that foreign investors do not buy anything but the best properties available to them.” 1979 Hearings, *supra* note 1, pt. 1, at 20. See also Wall St. J., Aug. 21, 1979, at 1, col. 2.

41. Address by Dieter zure Loye, *supra* note 19, printed in VITAL SPEECHES OF THE DAY, July 15, 1980, at 599, 600-01; Bus. WK., Mar. 23, 1981, at 40, 41; U.S. NEWS & WORLD REP., Feb. 13, 1978, at 79, 80.

If it establishes new facilities, foreign direct investment offers potential benefits for the economy of the United States. Although the net consequence of this kind of investment may prove harmful as well, it does have the potential for generating capital inflows, creating new jobs, and improving the tax base for the United States. In contrast, acquisitions by foreign investors are not likely to give rise to any of these benefits.⁴²

Acquisitions by foreign investors may serve as a vehicle for obtaining technological innovations.⁴³ An affiliate in the United States may transfer such information to its foreign parent and thereby reduce the competitiveness of the United States overseas.⁴⁴ A different and more subtle shift in competitive advantage occurs when a foreign investor enters a United States market without having its United States affiliate participate in product development.⁴⁵ With reference to foreign direct investment in Canada, the Canadian-American Committee⁴⁶ observed that the Canadian affiliates of foreign firms "do not do as much research or as sophisticated research as their parent companies abroad in most cases."⁴⁷ Thus,

42. The benefits derived from a new plant may be offset if the investor repatriates the profits or imports components for assembly in the United States. Initially, however, such investment has potential for benefiting the United States. Acquisitions by foreign firms stand in contrast: "The major exception, in my view, to the general attitude of *laissez faire* [toward foreign direct investment] may be in instances of foreign takeovers of U.S. firms. In instances of takeovers, there is . . . a reasonable chance of economic cost to the economy . . ." 1979 *Hearings, supra* note 1, pt. 1, at 147 (testimony of Professor Robert G. Hawkins).

43. *Id.* at 142 ("In takeovers of U.S. companies . . . , the foreign firm may be motivated by research facilities or technology owned by the U.S. firm or available through production facilities in the United States."); U.S. NEWS & WORLD REP., Feb. 13, 1978, at 79, 80; *see, e.g.*, BUS. WK., May 5, 1980, at 54, 54; *id.*, Oct. 22, 1979, at 86, 86.

44. Such a transfer took place after Fujitsu, a large Japanese firm, invested in the Amdahl Corporation, a domestic computer manufacturer. Through its investment, Fujitsu obtained access to a new design for a computer system. The United States suffered a corresponding loss of competitive advantage in this field in the international market. 1979 *Hearings, supra* note 1, pt. 3, at 84, 86, *reprinting* Letter from Professor Stefan H. Robock to Congressman Benjamin S. Rasantal (Oct. 12, 1979); 9 U.S. DEP'T OF COMMERCE, *supra* note 23, at app. 0, at 0-34 to -35 (1976).

Most observers appear to agree that foreign direct investment only occasionally generates technology transfers to foreign countries. *See, e.g., id.* app. 0, at 0-60. However, this conclusion does not remove all cause for concern. The participants in a seminar on this topic, conducted by the Department of Commerce in 1976, noted that the acquisition of United States technology may increasingly be a factor in foreign direct investment. "Already some foreign acquisitions of U.S. firms reflect the critical need to move fast in new areas of technology. Digital watches provide a good example, because American technology is way ahead in this field and foreigners (e.g., the Japanese) can hardly hope to catch up by starting from scratch." *Id.* app. 0, at 0-33.

45. 1979 *Hearings, supra* note 1, pt. 1, at 52 (testimony of Eldon E. Sweezy).

46. The Canadian-American Committee draws its members from both Canada and the United States and examines problems arising from the growing interdependence of the two countries. A.E. SAFARIAN, THE PERFORMANCE OF FOREIGN-OWNED FIRMS IN CANADA iii (1969).

47. *Id.* at 53; *see generally id.* at 41-56.

even if foreign direct investment rarely generates technology transfers to foreign countries, it may shift the technology base, the dynamic component of economic growth, outside the United States.

For many foreign investors, the United States is a stable source of abundant natural resources.⁴⁸ In 1975, the General Accounting Office reported: "Faced with today's world shortages . . . , some [foreign] investors [in the United States] are doubtlessly seeking to insure their home countries' access to sources of food, energy, and other scarce commodities."⁴⁹ In contrast to many nations,⁵⁰ the United States imposes few restrictions on foreign direct investment in these sectors of the economy. Given the exhaustible nature of many of these resources, however, this policy seems at odds with long range United States economic interests.⁵¹

The undesirable political effects of foreign direct investment stem simply from the foreignness of the investor. Such companies and individuals operate under the jurisdiction of more than one nation-state. The large scale presence of foreign investors may diminish national autonomy. As foreign investors wield greater influence within the United States economy, the United States Government may gradually surrender some of its ability to shape its own social, economic, and political policies.⁵²

Public concern over foreign direct investment derives in part from the intuition that key domestic industries should remain in the hands of nationals.⁵³ Although the United States restricts foreign direct investment in some key sectors of the economy, such as domestic broadcasting, internal air transport, and nuclear energy

48. 1979 *Hearings*, *supra* note 1, pt. 1, at 9 (testimony of Professor Jeffrey S. Arpan); *see generally* BUS. WK., July 9, 1979, at 50. In 1974, for example, a subsidiary of Veba, a West German enterprise, purchased coal mines in West Virginia for \$24 million. The company ships coal from these mines to Europe to fuel West Germany's electrical generators. D.F. LAMONT, *supra* note 12, at 41, 155-56 (1979).

49. H.R. REP. NO. 1216, *supra* note 19, at 18 (emphasis omitted) *quoting* GEN. ACCOUNTING OFFICE, *supra* note 28, at 34.

50. King, *Foreign Restrictions on U.S. Investment*, 11 SAN DIEGO L. REV. 27, 32 (1973). For summaries of the policies of other major industrialized nations on foreign investment, including their policies on foreign investment in natural resources and raw materials, see 9 U.S. DEP'T OF COMMERCE, *supra* note 23, app. N.

51. Even if the need for some of these restrictions is presently remote, Professor Lamont argues that the United States only encourages more Western European and Japanese dependence on United States resources by delaying their imposition. Consequently, when the need for such restrictions becomes acute, the United States will encounter foreign opposition to their imposition. D.F. LAMONT, *supra* note 12, at 155.

52. 1975 *Hearings*, *supra* note 3, at 141-45 (testimony of Professor Benjamin J. Cohen), *reprinted in* 1979 *Hearings*, *supra* note 1, pt. 3, at 17, 17-19; Ellis, *United States Multinational Corporations: The Impact of Foreign Direct Investment on United States Foreign Relations*, 11 SAN DIEGO L. REV. 1, 10-11 (1973).

53. Ellis, *supra* note 52, at 9-10.

production,⁵⁴ these regulations may be too narrow to effectively protect the interests of the United States.⁵⁵

Investment activities bring the foreign investor partially under the dominion of United States law.⁵⁶ Nevertheless, foreign investors are capable of circumventing or ignoring national policies regarding matters such as employment, prices, regional development, market competition, research and development, and foreign trade.⁵⁷ Moreover, although some foreign investors acquire a global economic and commercial perspective, most retain a national political outlook.⁵⁸ There is often a close relationship between a foreign investor and the home government.⁵⁹ Such an investor may feel compelled to observe the policies of the home government, even when they clash with the objectives of the host government.⁶⁰

II. UNITED STATES POLICY ON FOREIGN DIRECT INVESTMENT

Throughout the postwar era, the United States has energetically promoted an international economic order based on market competition.⁶¹ Towards that end, the United States has supported the

54. Federal law controls foreign investment in, among others, the following areas: aviation, coastal shipping, salvage, the transfer of ships, fishing, domestic radio and television communications, telegraph companies, nuclear energy operations, the purchasing or leasing of public lands and of pipelines and mineral rights on government property, and the directorships of national banks. For specific citations and a discussion, see Niehuss, *supra* note 1, at 82-87.

55. Professor Benjamin Cohen has expressed this view: "[T]hese regulations [restricting foreign direct investment in certain areas] may be far less adequate than [sic] administration spokesmen would have us believe. My reason for suggesting this is simply that the interpretation of national security embodied in these regulations is simply too narrow to be effective." 1975 Hearings, *supra* note 3, at 143, reprinted in 1979 Hearings, *supra* note 1, pt. 3, at 17, 18.

56. Enactments such as the National Labor Relations Act, the Sherman and Clayton Acts, and the Internal Revenue Code, as well as the common law of torts, contracts, and corporations, may all have some application to foreign investors. Problems of jurisdiction and service of process, however, may present obstacles to enforcement. In addition, the substantive scope of United States law does not respond directly to the chief fears raised by foreign investment. For example, no law requires an investor to maintain his investment, and no law limits the size or growth of foreign-held companies. For a discussion of this problem, see Note, *The Rising Tide of Reverse Flow: Would a Legislative Breakwater Violate U.S. Treaty Commitments?*, 72 MICH. L. REV. 551, 556-61 (1974).

57. 1975 Hearings, *supra* note 3, at 142 (testimony of Professor Benjamin J. Cohen), reprinted in 1979 Hearings, *supra* note 1, pt. 3, at 17, 18. See also *supra* 21-36 and accompanying text.

58. 1975 Hearings, *supra* note 3, at 143 (testimony of Professor Benjamin J. Cohen), reprinted in 1979 Hearings, *supra* note 1, at 17, 18.

59. Indeed, foreign governments own 59 of the 500 largest industrial corporations outside the United States. D.F. LAMONT, *supra* note 12, at 30. Nearly all of these firms occupy competitive positions, within their respective industries, in the United States. *Id.*

60. A.E. SAFARIAN, *supra* note 46, at 107.

61. *E.g.*, 1979 Hearings, *supra* note 1, pt. 2, at 199 (statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

unimpeded movement of investment capital among nations.⁶² This open door policy harmonized well with the United States' position as the world's largest exporter of investment capital with little foreign direct investment at home. United States policymakers regarded host countries' resistance to the infusion of United States investment capital as either unfriendly or unsophisticated.⁶³

In the early 1970's, the attitude of the United States public toward foreign direct investment underwent a radical transformation. Two devaluations of the dollar in quick succession, along with a sudden upsurge in foreign direct investment from Western Europe and Japan, excited public concern.⁶⁴ In 1973, the Nixon Administration conducted a review of the policy of the United States toward foreign direct investment.⁶⁵ Even though the survey demonstrated the United States Government's inability to assess the magnitude and significance of foreign investment in the United States,⁶⁶ the study reaffirmed existing policy.⁶⁷ Congress devised the Foreign

62. For example, the United States participated in the drafting of the 1961 Code of Liberalisation of Capital Movements for the Organisation for Economic Co-Operation and Development (OECD). OECD, *THE ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT* app. IV (1963). Since its promulgation, the United States has urged other nations to remove their reservations and derogations under the Code. Niehuss, *supra* note 1, at 68.

63. "Host-country regulations to restrict new investments or the activities of already existing investments were greeted with criticism in this country as being irrational or unfriendly—or both; some were even threatened with retaliation." *1975 Hearings, supra* note 3, at 142 (testimony of Professor Benjamin J. Cohen), *reprinted in 1979 Hearings, note 1, pt. 3, at 17, 17.*

64. Foreign direct investment in the United States rose from \$20.6 billion in 1973 to \$25.1 billion in 1974, an increase of 21.8%. *1979 Hearings, supra* note 1, pt. 3, at 209. For a discussion of other economic and political factors contributing to United States public concern over foreign direct investment, see *1979 Hearings, supra* note 1, pt. 1 at 10-11 (testimony of Professor Jeffrey S. Arpan); COMM. TO STUDY FOREIGN INV. IN THE U.S., SECTION OF CORP., BANKING AND BUSINESS LAW, AM. BAR ASS'N, *A GUIDE TO FOREIGN INVESTMENT UNDER UNITED STATES LAW* 11-12 (1979).

65. U.S. PRESIDENT, *INTERNATIONAL ECONOMIC REPORT OF THE PRESIDENT* 43 (1975). The Council on International Economic Policy (CIEP) conducted the survey, as part of its overall review of the United States' international investment policy, with the assistance of the Interagency Task Force on Foreign Investment in the United States. Niehuss, *supra* note 1, at 71-72.

66. The CIEP found that the system for collecting data on foreign investment in the United States was inadequate. U.S. PRESIDENT, *INTERNATIONAL ECONOMIC REPORT OF THE PRESIDENT* 65 (1974). A subsequent Department of Commerce study confirmed this state of affairs. The Department of Commerce found that over 20 Federal agencies collected data on foreign investment, using 140 report forms. The collection and disclosure of this data was not systematic or standardized. 1 U.S. DEP'T OF COMMERCE, *supra* note 23, at 222-23. The degree of ownership necessary before an agency required a foreign investor to submit a form varied from 1% to 50%. *Id.* at 227; *cf. 1979 Hearings, supra* note 1, pt. 3, at 9 (testimony of Professor William S. Barnes) (comparison to information gathering of other countries).

67. The CIEP concluded that the open door policy should continue in force and that the Administration should oppose any Congressional attempt to impose new restrictions. U.S. PRESIDENT, *supra* note 66, at 65. The CIEP reported that foreign investment was

Investment Study Act of 1974⁶⁸ to remedy the problem of insufficient information. That Act created a mechanism to monitor and study all forms of foreign investment in the United States.⁶⁹

Public interest in foreign direct investment subsided briefly until the oil embargo. The emergence of the Organization of Petroleum Exporting Countries (OPEC) as a major force in the the world economy triggered renewed interest.⁷⁰ Concern over the substantial dollar holdings of the OPEC nations, and their capacity to invest in the United States, led to the 1975 policy review.⁷¹ This study confirmed the conclusions of the 1973 policy review.⁷²

In their reports pursuant to the Foreign Investment Study Act of 1974,⁷³ neither the Department of Commerce nor the Department of the Treasury expressed alarm over the growth of foreign investment in the United States, and neither recommended any departure from the traditional open door policy of the United States.⁷⁴ Both, how-

not a significant factor when compared to the overall size of the United States economy, *id.* at 59, 62, and that there was no evidence of foreign control in any critical sector. *Foreign Investment in the United States: Hearings Before the Subcomm. on Foreign Economic Policy of the House Comm. on Foreign Affairs*, 93d Cong., 2d Sess. 86 (1974) (statement of Peter M. Flanigan, Assistant to the President for International Economic Affairs) [hereinafter cited as *1974 Hearings*]. There was a sharp increase in foreign investment in 1973, but the data indicated that these investment flows were subject to fluctuation from year to year. *Id.* at 80, 86 (testimony and statement of Peter M. Flanigan, Assistant to the President for International Economic Affairs). The CIEP concluded that the figures of one year alone cannot serve as the basis for any dramatic policy change. *Id.*

68. Pub. L. No. 93-479, 88 Stat. 1450 (noted at 15 U.S.C. § 78b (1976)).

69. The Act directed the Departments of Treasury and Commerce to undertake three major activities: first, a survey of the nature, scope, and magnitude of foreign investment in the United States, *id.* §§ 2, 4(1), 5(1), 6(1); second, analysis of a number of matters concerning foreign investment, *id.* §§ 5(2)-(12), 6(2)-(8); and third, a study of the adequacy of reporting and disclosure requirements, accompanied by recommendations for improvements in the data-collecting process, *id.* §§ 5(11), 5(13), 6(9)-(10).

70. Niehuss, *supra* note 1, at 66.

71. *Foreign Investment Act of 1975: Hearings on S. 425 Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 1st Sess. 21, 23-24 (1975) (testimony of Jack F. Bennett, Under Secretary for Monetary Affairs, U.S. Department of the Treasury).

72. Four major conclusions emerged. First, there was no need for any new legislation restricting foreign investment. *Id.* at 22. Second, there was a possible need for legislation devised to reveal the beneficial owner standing behind both foreign and domestic investments made in nominees' names. *Id.* Third, there was a need to create a new interagency committee to supplement existing administration action. *Id.* Fourth, the United States Government would seek advance consultation with principal foreign governmental investors concerning major direct investments in the United States. *Id.* The Committee on Foreign Investment in the United States later became the proposed interagency committee. Exec. Order No. 11,858, 3 C.F.R. §§ 990-92 (1971-1975 Compilation), amended by Exec. Order No. 12,188, 3 C.F.R. §§ 131-35 (1980 Compilation), reprinted in 15 U.S.C. § 78b app. at 1468-69 (Supp. IV 1980).

73. U.S. DEP'T OF COMMERCE, *supra* note 23; U.S. DEP'T OF THE TREASURY, FOREIGN PORTFOLIO INVESTMENT IN THE UNITED STATES (1976).

74. 1 U.S. DEP'T OF COMMERCE, *supra* note 23, at 233-40; 1 U.S. DEP'T OF THE TREASURY, *supra* note 73, at 1-5.

ever, recommended improved information gathering.⁷⁵ Accordingly, Congress enacted the International Investment Survey Act of 1976⁷⁶ "to provide clear and unambiguous authority for the President to collect information on international investment and to provide analyses of such information to the Congress, the executive agencies, and the general public."⁷⁷

Bolstered by the findings of the two policy reviews and the reports under the Foreign Investment Study Act of 1974, United States officials continue to adhere to the open door policy. This policy rests on the premise that the unhindered operation of competitive market forces brings about the most efficient allocation of scarce resources in the world economy.⁷⁸ This theory holds that an uninhibited international market for capital improves employment levels and standards of living, resulting in a net economic benefit for both sending and receiving countries.⁷⁹ One advocate of the current policy summarized the United States' approach as follows: "So long as it [foreign direct investment] takes place in response to market forces, we welcome it."⁸⁰ Consequently, the United States does not

75. 1 U.S. DEP'T OF COMMERCE, *supra* note 23, at 241; 1 U.S. DEP'T OF THE TREASURY, *supra* note 73, at 55-61.

76. 22 U.S.C. §§ 3101-3108 (1976), amended by 22 U.S.C.A. § 3108 (West 1979), and by §§ 3103(a)(3), (d), 3107(b), 3108 (Supp. III 1979). The 1976 Act authorizes the President to conduct, "to the extent he deems necessary and feasible," a regular data collection program on foreign direct and portfolio investment in the United States. *Id.* § 3103(a). The Act also requires the President to make comprehensive benchmark surveys every five years. *Id.* § 3103(b)-(c).

77. *Id.* § 3101(b).

78. For instance, the Assistant Secretary of the Treasury testified in 1975 as follows:

U.S. policy with respect to international investment has generally been based on the premise that we should rely on the private market as the most efficient means to determine the allocation and use of capital in the international economy.

Accordingly, our basic policy toward foreign investment in the United States has reflected an "open door" approach.

*Foreign Investment in the United States: Hearing Before the Subcomm. on Int'l Trade, Investment and Monetary Policy of the House Comm. on Banking, Currency and Housing, 94th Cong., 1st Sess. 155 (1975) (testimony of Gerald L. Parsky, Assistant Secretary of the Treasury) [hereinafter cited as *Hearing on Foreign Investment*], reprinted in 1979 Hearings, *supra* note 1, pt. 3, at 66, 80 (annex to statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).*

79. The world and U.S. economies have benefited greatly from the expansion of world trade and capital flows, in terms of increases in employment and standards of living far greater than would have been possible if we and other nations had raised, rather than lowered, the barriers to international trade and payments. 1979 Hearings, *supra* note 1, pt. 2, at 203 (statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury). Others maintain that unrestricted foreign direct investment also promotes greater competition, higher wages, additional tax revenues, and an overall increase in production. 1974 Hearings, *supra* note 67, at 299, 349-52 (report prepared for use by CIEP).

80. 1979 Hearings, *supra* note 1, pt. 2 at 204 (statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

presently consider whether a particular investment will generate net benefits or net harm.⁸¹ These United States policymakers maintain that the free international exchange of investment capital will produce, on the whole, an improvement in the economic welfare of the world.⁸² This view, however, ignores the fact that this free exchange of investment capital may not distribute the costs and benefits of a foreign direct investment equitably between the home and host countries.⁸³ The question remains as to whether the United States can forge a policy that will reap an adequate share of the benefits associated with foreign direct investment, without assuming a disproportionate share of the harmful consequences.

The present policy does not adequately recognize or respond to the costs of foreign direct investment.⁸⁴ Moreover, this passive policy fails to distinguish between beneficial investments, such as new plant construction financed by investment capital inflows, and possibly harmful investments, such as takeovers. Detrimental investments encounter no obstacles, while clearly beneficial projects meet with indifference.⁸⁵

81. The United States "offer[s] foreigners no special incentives to invest here and, with a few internationally recognized exceptions, ha[s] imposed no special barriers." *Hearing on Foreign Investment, supra* note 78, at 155 (testimony of Gerald L. Parsky, Assistant Secretary of the Treasury), *reprinted in 1979 Hearings, supra* note 1, pt. 3, at 66, 80 (annex to statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

82. *See supra* note 79.

83. On the distinction between the efficient allocation of scarce resources and the distribution of goods and services, see E. MANSFIELD, *MICROECONOMICS: THEORY AND APPLICATIONS* 9-11 (3d ed. 1979). Distribution is an ethical matter for which the science of economics can give no guidance. P. SAMUELSON, *ECONOMICS* 635 (9th ed. 1973).

84. Nor does it respond to the public concern over this issue. "While foreign direct investments always have existed in the United States, their dramatic increase in the early 1970's was noticed more readily and was of more concern to a wider number of parties in this country than ever before." *1979 Hearings, supra* note 1, pt. 1, at 10 (testimony of Professor Jeffrey S. Arpan). The following passage illustrates the tenor of this concern:

As a recently retired Foreign Service Officer, I have lived in several countries where a heavy and rapid infusion of foreign capital has had a negative effect when allowed to dominate especially sensitive sectors of the economy (e.g. banks, public utilities)

Someone obviously has to point out to big business and to big government that investment when carried to an extreme by foreigners is not an unmitigated benefit. . . .

It is no longer sufficient for business and government to declare that such investment in America is a sign of euphoric confidence in our country. Rather, it is a sign that certain astute foreigners can recognize the bargains which can be picked up at a bankruptcy auction.

1979 Hearings, supra note 1, at 116, 116, *reprinting* Letter from Walter M. Bastian, Jr., to Congressman Benjamin S. Rosenthal (July 28, 1979).

85. Many of the United States' trading partners have not hesitated to establish controls on foreign investment. For a description of Canadian and Mexican restrictions, see Barnes, *Foreign Investment in Canada and Mexico: An Agenda for Host Country Screening*, 1 B.C. INT'L & COMP. L. J. 1 (1977). For a discussion of French and West German controls, see Note, *supra* note 56, at 580-84. For a summary and discussion of Latin

Supporters of the open door policy argue that imposing restrictions on foreign direct investment would violate treaty obligations of the United States. The United States has entered treaties of friendship, commerce, and navigation with over forty countries.⁸⁶ The terms of most of these treaties will easily accommodate restrictions on foreign direct investment.⁸⁷ The remainder generally contain sufficient flexibility to permit the United States to enact some restrictions on inflows of investment capital.⁸⁸

Proponents of the existing policy also maintain that the United States' postwar effort to establish an international free market will collapse if the United States appears to hedge on this commitment in any respect.⁸⁹ This argument overstates the significance of United States policy. The United States' example does not establish pat-

American controls, see PERMANENT COUNCIL OF THE ORG. OF AM. STATES, A COMPARATIVE STUDY OF LATIN-AMERICAN LEGISLATION ON THE REGULATION AND CONTROL OF PRIVATE FOREIGN INVESTMENT (1975).

86. H.R. REP. NO. 1216, *supra* note 19, at 38.

87. Approximately one-half of the less restrictive treaties promise most-favored-nation treatment only with regard to the organization of companies, the acquisition of shares, and the holding of executive positions. Note, *supra* note 56, at 575-76. The other half date from an earlier period, before the United States began to promote direct investment abroad. These earlier treaties do not deal explicitly with investment activity and merely impose a most-favored-nation commitment in matters of commerce. The term commerce is nowhere defined. *Id.* at 576. The terms of both types of treaties are sufficiently elastic to accommodate United States restrictions against all foreign investment.

88. Treaties of friendship, commerce, and navigation that incorporate the principle of national treatment are most problematic. Under this principle, the Federal Government may not impose restrictions on the nationals of the other party to the treaty that are stricter than those it imposes on American nationals. *Id.* at 569. Some of these treaties, however, may not prescribe national treatment for investment activities by foreigners. *Id.* at 573-74. Moreover, the protocols accompanying others in this group of treaties may permit exceptions to the principle of national treatment in the case of controls on foreign investment. *Id.* at 571-72. In addition, the treaties of friendship, commerce, and navigation contain escape clauses that authorize activities necessary to protect essential security interests. *Id.* at 591. These clauses might provide a basis for exception to national treatment. *Id.* at 591. Finally, the United States can renegotiate or terminate, if necessary, those treaties whose guarantee of national treatment proves a bar to restrictions on foreign investment. H.R. REP. NO. 1216, *supra* note 19, at 38; Note, *supra* note 56, at 588-89.

Admittedly, controls on foreign investment would violate the spirit of many United States treaty obligations. Nevertheless, none of the United States' partners in these treaties has matched the United States commitment to unrestricted foreign investment. H.R. REP. NO. 1216, *supra* note 19, at 48-55; see also Note, *supra* note 56, at 580-88. If the spirit of these treaties can tolerate other nations' restrictions, reasonable measures by the United States should, likewise, be acceptable.

89. If the United States—the primary “keeper of the faith” for an open international economic system—were to appear to be moving down the road toward restrictions, this would have a major corrosive effect on other countries and tend to legitimize current and new interventions in international investment on their part.

1979 Hearings, *supra* note 1, pt. 3, at 66 (statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

terns of behavior for other countries.⁹⁰ Moreover, the United States' consistent advocacy of free market principles generally has not prevented changing economic conditions from eroding the once cooperative atmosphere in the world economy.⁹¹ In response to these changing conditions, many nations are reexamining their policies toward foreign investment.⁹² The United States should be no less responsive to a changing world economic environment.⁹³

90. Contrary to the United States' example, the rest of the world has adopted a restrictive approach toward foreign investment. *See infra* notes 95-102 and accompanying text. United States policy apparently failed to persuade other countries to relax their foreign investment restraints. Thus, there does not appear to be any reason for those countries to adopt more stringent policies in response to the United States establishing a policy comparable to the milder among those employed by United States trading partners.

91. The staggering jump in the cost of energy and the endless turmoil in the international money markets have wrenched the global economy loose from its postwar moorings and forced it to head into totally unknown waters in the 1980s. . . .

. . . Three decades of open, free trade that permitted the multinationals to blossom are giving way to a period of neo-mercantilism So the cooperative effort to create an interdependent world economy—a hallmark of the postwar period—is being replaced by what often appears to be a free-for-all among industrial nations trying to grab or preserve as much as possible for themselves of the shrinking economic pie.

BUS. WK., July 9, 1979, at 50, 50.

92. H.R. REP. NO. 1216, *supra* note 19, at 148-57; 1974 Hearings, *supra* note 67, at 375, 375-467, reprinting STAFF OF HOUSE COMM. ON FOREIGN AFFAIRS, 93d CONG., 2d SESS., INTERNATIONAL TRENDS IN THE REGULATION OF FOREIGN INVESTMENT (1974) (J. Sanford and J. Costa).

93. For one recommendation for a new United States domestic policy on foreign direct investment, see *supra* notes 125-37 and accompanying text.

The United States employs three general methods to implement its foreign policy on international investment: bilateral accords, multilateral accords, and unilateral action. Bilateral agreements in the form of treaties of friendship, commerce, and navigation have had only limited success. *See supra* note 88. As noted, the United States subscribes to the OECD Code of Liberalisation of Capital Movements. *Supra* note 62. Nevertheless, "[e]ven the OECD Code has fallen into disuse, its escape and derogation clauses being invoked widely by many members." Note, *supra* note 13, at 627.

A more recent multilateral effort concerning, among other things, national treatment and international investment incentives and disincentives is the OECD Declaration on International Investment and Multinational Enterprises. Declaration on International Investment and Multinational Enterprises, OECD Doc. 21(76)04/1 (1976), *reprinted in* OECD, INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISES 7 (1976), *and in* 75 DEP'T ST. BULL. 83 (1976). A related OECD decision authorizes, among other things, consultations on international investment. OECD, *supra*, at 73, 75 DEP'T ST. BULL. 88 (1976), *both reprinting* Decision of the Council on International Investment Incentives and Disincentives. The Declaration and the Decision have three main elements with respect to international investment: first, participating member countries commit themselves "to give due weight to the interests of Member countries affected by specific laws, regulations and administrative practices in this field (hereinafter called 'measures') providing official incentives and disincentives to international direct investment," 75 DEP'T ST. BULL. 83, 83; second, participating member countries commit themselves to "endeavour to make such measures as transparent as possible, so that their importance and purpose can be ascertained and that information on them can be readily available," *id.*; and third, provision for consultations "at the request of a Member coun-

Another rationale for maintaining the open door policy is the fear that if the United States imposes restrictions, foreign countries will retaliate against United States investors.⁹⁴ As the world's largest exporter of investment capital, the United States is vulnerable to the imposition of restrictions on foreign investment. The possibility of retaliation, however, is exaggerated. Most United States investors abroad are already subject to registration and screening requirements, and must meet certain conditions for entry.⁹⁵ Latin American countries, for instance, generally require the registration and authorization of foreign investments,⁹⁶ and designate a government-

try which considers that its interests may be adversely affected by the impact on its flow of international direct investments of measures taken by another Member country specifically designed to provide incentives or disincentives for international direct investment," *id.* at 88. 1979 OECD REVIEW, *supra* note 13, at 55. The Turkish Government did not participate in the Declaration and abstained from the decision. OECD, *supra*, at 9 n. (1976).

The Declaration also states that member countries should, "consistent with their needs to maintain public order, to protect their essential security interests and to fulfill commitments relating to international peace and security," accord national treatment to foreign-controlled enterprises after their establishment. 75 DEP'T ST. BULL. 83. In contrast, the 1961 OECD Code of Liberalisation of Capital Movements, *supra* note 62, does not refer to the treatment of foreign-controlled enterprises after their establishment. 1979 OECD REVIEW, *supra* note 13, at 46. Finally, the Declaration expressly "does not deal with the right of Member countries to regulate the entry of foreign investment or the condition of establishment of foreign enterprises." 75 DEP'T ST. BULL. 83, 83 (1976).

It is perhaps too soon to assess the Declaration's success in liberalizing or retarding the growth of restrictions on international investment. The 1979 ministerial review of the Declaration observed "a growing risk of increased competition in the use of investment incentives by governments." 1979 OECD REVIEW, *supra* note 13, at 56. The United States Government has already expressed its dissatisfaction with the efficacy of the Declaration: "Over the past 3 years, the United States has been disappointed in the inability of OECD member governments to deal effectively with the issue of investment incentives and disincentives." DEP'T ST. BULL., Sept. 1979, at 41, 41, *reprinting* U.S. Department of State, Press Release No. 181 (July 27, 1979).

Finally, Mr. Bergsten intimates, *supra* note 89, that the United States Government intends that its domestic policy on foreign investment within the country should influence international economic policy. One might describe this as a species of unilateral action. The United States' mere example, however, seems ineffective in an era of deteriorating economic cooperation among the industrialized nations of the West and Japan. *See, e.g., supra* note 90. Instead, foreign governments and their nationals are free to exploit investment opportunities in the United States without providing comparable access to their home markets to United States investors. Moreover, United States investors abroad must demonstrate benefits to the host country, while even the least desirable foreign investment finds a receptive host in the United States. This inequity is particularly acute when the foreign investor is a government-controlled or -owned enterprise. For instance, the United States permits the government-controlled British Petroleum Company to mine in United States territory, even though United States firms may not do the same in Great Britain. 1979 Hearings, *supra* note 1, pt. 3, at 23 (testimony of Professor Douglas F. Lamont). For a description of the British Petroleum Company's activities in the United States, see BUS. WK., April 27, 1981, at 42; *id.*, May 8, 1978, at 76.

94. H.R. REP. NO. 1216, *supra* note 19, at 37.

95. *Id.*

96. PERMANENT COUNCIL OF THE ORG. OF AM. STATES, *supra* note 85, at 41-123, 126.

tal agency with a variety of powers to oversee foreign investment.⁹⁷ More importantly, the leading industrialized countries in the West and Japan⁹⁸ generally have some form of compulsory reporting for foreign investment,⁹⁹ limit foreign investment in broad sectors of the economy,¹⁰⁰ and discriminate against acquisitions by foreign investors.¹⁰¹ At least seven of the United States' major trading partners have some form of review for foreign investment,¹⁰² ranging from informal review to regular screening.¹⁰³ In short, the rest of the world already restricts foreign investment, and, consequently, it is unlikely that comparable restrictions by the United States would provoke retaliatory actions by other countries.

Finally, United States policymakers believe that any limitation of foreign direct investment will discourage foreign investors, causing the loss of beneficial inflows of investment capital.¹⁰⁴ This belief is part of a larger, and perhaps the central objection to any change in the open door policy. As a matter of general economic policy and theory, defenders of the open door policy do not want to interfere with the efficient market allocation of scarce resources,¹⁰⁵ even though they recognize that some foreign investments are undesirable.¹⁰⁶ The international market for investment capital is now responding to the investment policy initiatives of foreign governments more than ever before.¹⁰⁷ Moreover, under the open door pol-

97. *Id.* at 41-126.

98. This information is from a Department of Commerce study that examined the treatment of foreign investment in Belgium, Canada, France, West Germany, Italy, the Netherlands, Switzerland, the United Kingdom, and Japan. 9 U.S. DEP'T OF COMMERCE, *supra* note 23, app. N, at N-2.

99. *Id.* at N-2.

100. *Id.* at N-1.

101. *Id.*

102. *Id.* at N-6 to -12 (France), N-17 to -19 (West Germany), N-23 to -28 (Italy), N-32 to -36 (the Netherlands), N-46 to -51 (the United Kingdom), N-57 to -65 (Canada), N-68 to -76 (Japan).

103. Canada, France, and Japan have formal screening procedures. *Id.* at N-1, N-6 to -12, N-57 to -65, N-68 to -76.

104. "The establishment of new authority by law . . . to block foreign investments would be highly visible to potential investors in the United States, and would be taken as a sign that our nation is changing its basic and traditional attitude toward such investment." 1979 *Hearings*, *supra* note 1, pt. 3, at 65 (statement of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

105. *See, e.g., supra* note 78; U.S. PRESIDENT, *supra* note 65, at 43.

Foreign direct investment is sometimes called a win-win situation. *See, e.g., King, supra* note 50, at 6. Even though a particular foreign direct investment may not benefit the host country, international investment augments the wealth of the world generally, because investors presumably employ their capital in the most profitable fashion possible. This is what United States policymakers mean by efficient resource allocation. *See generally supra* note 83.

106. 1979 *Hearings*, *supra* note 1, pt. 3, at 60 (testimony of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

107. *See infra* note 136.

icy, foreign investors need not concern themselves with the so-called spillover costs and benefits of foreign direct investment, those costs and benefits that affect society but not the investor.¹⁰⁸ If, from among equally desirable investment options, a foreign investor fails to select the investment with the most desirable spillover result,¹⁰⁹ then the market will have allocated resources in a fashion that is less efficient than theoretically possible.¹¹⁰ On the other hand, even if each of the foreign investor's options will yield the same spillover result, the open door policy fails to consider whether the international and domestic distribution of these spillover costs and benefits is equitable.¹¹¹ Note that a policy that brings about an equitable distribution of spillover costs and benefits need by no means reject the private market's allocation of scarce resources. For instance, a governmental agency enforcing such a policy need not purport to tell prospective foreign investors what investment option would be most profitable and insist that they select that option or none at all. If the agency did sometimes refuse to approve a proposed foreign investment under a new policy, it would, of course, affect the private market's allocation of resources. The agency would do so, however, only where the spillover costs outweighed the spillover benefits, or the net benefits to the foreign investor, or both. This sort of interference

108. See *supra* notes 21-60 and accompanying text.

Discussion of foreign direct investment frequently employs the term spillover costs and benefits. See, e.g., *1979 Hearings, supra* note 1, pt. 3, at 60 (testimony of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury); King, *supra* note 50, at 4-5. Here the term refers to any cost of foreign direct investment that the associated foreign investor does not incur, and to any benefit of foreign direct investment that the associated foreign investor does not reap.

This definition is synonymous with what economists conventionally call externalities. See, e.g., P. SAMUELSON, *supra* note 83, at 474. The term spillover costs and benefits may be broader, however. Economists attempt to identify external costs, for instance, because they can enhance the efficiency of resource allocation by making the relevant decisionmaker take these costs into account. The problem of pollution is a familiar example. See, e.g., E. MANSFIELD, *supra* note 83, at 373-81. If the economist's externalities refer only to those external costs and benefits the manipulation of which can enhance the efficiency of resource allocation, then the term spillover costs and benefits is broader in meaning. The latter term also refers to costs and benefits that have nothing to do with the efficiency of resource allocation. For instance, when a foreign investor constructs a new plant, the host country reaps the spillover benefit of new jobs. Government cannot, however, enhance the efficiency of resource allocation by bringing this sort of consideration to bear on the foreign investor's selection of a plant site. Instead, whether one country or another reaps the new jobs is a matter of distribution.

109. In the sense of an externality. See *supra* note 108.

110. Such an external diseconomy arises when a foreigner uses a direct investment as a vehicle to transfer technology abroad without compensating those who paid to develop this technology.

111. Distributive schemes do not purport to increase wealth; instead, they concern win-lose situations. Compare *supra* note 105. For instance, if one host country wins the jobs that new plant construction creates, another possible host country loses these jobs. No redistribution of these jobs among countries will produce greater wealth, rather, the matter is simply one of fairness. See generally *supra* note 83.

with the market's allocation is desirable. Consequently, the objections to policies designed to distribute the spillover costs and benefits or to enhance the efficiency of the market's allocation frequently appear to amount to an assertion that governmental regulation would be too burdensome, too costly, or ineffective.¹¹² Without experience, however, one cannot assess the truth of this assertion.

There remains, however, another difficulty. If, in response to purely domestic concerns, the Federal Government were officially to recognize that sound policy on foreign direct investment must at the least accommodate both the market allocation of resources and the distribution of spillover costs and benefits, then the United States could not consistently advocate one goal without also advocating the other. In this sense, the United States would perhaps dilute the rigorous purity of its earlier position. The time has come, however, for the United States to recognize that the practice of other nations, if not their words, demonstrates that fewer and fewer nations subscribe to a rigorous open door policy for international investment.¹¹³ Such a recognition would not require the United States to abandon international investment as an essential component of the free market world economy that the United States still seeks to erect. Indeed, in the long run, the United States might have greater success in the international arena if it were to distinguish among desirable and undesirable types of restrictions on foreign investment,¹¹⁴ instead of simply insisting upon an unrealistic policy of neutrality that many foreign countries can no longer uphold.

III. THE UNITED STATES LEGISLATIVE RESPONSE

Members of Congress have sponsored a wide spectrum of bills, ranging from absolute bans on foreign investments to more moderate proposals that would leave present policy largely unchanged.¹¹⁵

112. See, e.g., *1979 Hearings, supra* note 1, pt. 3, at 59-60 (testimony of C. Fred Bergsten, Assistant Secretary for International Affairs, U.S. Department of the Treasury).

113. See *supra* notes 95-103 and accompanying text.

114. For instance, the practice of most Western industrialized nations accords national treatment to foreign direct investments after their establishment. 9 U.S. DEP'T OF COMMERCE, *supra* note 44, app. N, at N-1. The recent OECD Declaration on International Investment and Multinational Enterprises gives explicit recognition to this principle. See *supra* note 93.

115. From the first session of the ninety-third Congress to the second session of the ninety-fifth Congress, for instance, Members of Congress introduced more than 80 different bills concerning foreign investment. *1979 Hearings, supra* note 1, pt. 1, at 11 (testimony of Professor Jeffrey S. Arpan). For a discussion of a number of these bills, see Note, *supra* note 63, at 634-46. The commentator identifies at least five general types of proposed legislation. One proposal would flatly prohibit foreign investment under certain conditions, usually a certain monetary amount or specified percentage of ownership. Another type proposes selective screening before a prospective investor makes an investment. A third type proposes *pro forma* screening, i.e., a reporting requirement with a

House bill 7750¹¹⁶ proposed reciprocal limitations on foreign investment. The bill would have amended the Securities Exchange Act of 1934¹¹⁷ to make it unlawful for a foreign corporation to acquire the beneficial ownership of equity securities,¹¹⁸ "unless the laws and regulations of the country in which such person is incorporated are no more restrictive than the provisions of this title and other Federal law with respect to the acquisition, by a person incorporated in a State of the United States, of a like amount of equity securities issued by a person incorporated in such foreign country."¹¹⁹

The bill adopted the quid pro quo approach to foreign direct investment. This approach has two purposes. First, it remedies the fundamental inequity of the open door policy that allows foreign investors unimpeded access to the United States, even though the home countries of these investors would place substantial restrictions on the activities of United States investors.¹²⁰ Second, this approach retains the present policy's goal of encouraging other nations to remove restrictions on inflows of investment capital,¹²¹ but it rejects the purely multilateral tendency that characterized United States policy in the 1970's¹²² in favor of unilateral action. This approach presumes that other countries will lower or remove restrictions on foreign investment in order to obtain comparable investment privileges for their nationals in the United States.

The success of House bill 7750 and similar bills adopting the quid pro quo approach would depend on the response they evoke abroad. This approach assumes either that the prospect of greater investment privileges in the United States is sufficiently enticing to cause other countries to lift their foreign investment restrictions, or that other countries can and are willing to accord United States investors treatment different from that given to other foreign investors. Moreover, because each nation's response would depend on its policies toward both inflows and outflows of investment capital, the

provision for closer scrutiny, if certain circumstances arise. A fourth type would provide for monitoring after a foreign investor has made an investment. A final category simply proposes reporting requirements. *Id.* at 634-35.

116. H.R. 7750, 96th Cong., 2d Sess (1980). For the full text of the bill, see *supra* note 10.

117. 15 U.S.C. §§ 77b-77c, 77j-77k, 77m, 77o, 77s, 78a-78d, 78e-78l, 78m-78o, 78o-3 to 78hh, 78ii-78jj (1976), amended by 15 U.S.C. §§ 77(b)(15), 77c(a)(2), (6)-(7), (9)-(10), (b), 77(d)(6), 77s(c), 78c(a)(12), (40), 78k(a)(3), 78m(b), (d)(1), (g)-(h), 78o(d), 78u(g), 78ff (Supp. IV. 1980).

118. The bill followed the definition of equity securities in 15 U.S.C. § 78m(d)(1) (Supp. IV 1980).

119. H.R. 7750, 96th Cong., 2d Sess. (1980).

120. See *supra* notes 95-103 and accompanying text.

121. See *supra* notes 89 & 93.

122. See *supra* note 89.

international reaction is difficult to predict. The quid pro quo approach assumes that other countries generally favor outflows of investment capital, and that this preference outweighs any resistance to inflows of investment capital. This assumption, however, is problematic. Not all countries encourage outflows of investment capital;¹²³ for example, developing countries want to keep investment capital at home.¹²⁴ For such countries, the quid pro quo approach offers little or no inducement to lower restrictions on inflows of investment capital because the prospect of greater investment privileges abroad is not appealing. If the United States were to match restrictiveness with restrictiveness, the approach would result in an overall increase in restrictions on foreign investment.

The major drawback of the quid pro quo approach is its failure to discriminate among prospective investments on the basis of their merits. Identical investments originating in different countries would receive disparate treatment. If a foreigner proposes a highly beneficial investment, but comes from a country with a restrictive policy on inflows of investment capital, the quid pro quo approach would reject the proposed investment, and the United States would have to forego the spillover benefits.

An alternative to the present policy and the quid pro quo approach of House bill 7750 is a case by case screening procedure for inflows of investment capital. Other industrialized countries have instituted such procedures.¹²⁵ In general, an agency uses a screening procedure to determine the net economic and political effect of a prospective foreign investment on the host country. With this information, the agency can approve, reject, or seek modification of a proposal.

Canada, for example, adopted the Foreign Investment Review Act¹²⁶ in 1973. Under the Act, Canada scrutinizes the proposed investments of noneligible persons¹²⁷ (foreigners) under a test that

123. See generally 9 U.S. DEP'T OF COMMERCE, *supra* note 23, app. N, at N-3 to -4, N-8, N-26 to -27, N-32 to -34, N-40, N-46 to -48, N-69 to -70.

124. E. NWOGUGU, *THE LEGAL PROBLEMS OF FOREIGN INVESTMENT IN DEVELOPING COUNTRIES*, 18-21 (1965); see generally *id.* at 2-4.

125. Canada is one such nation. See *infra* notes 126-34 and accompanying text. Australia, Brazil, France, Mexico, and West Germany, among others, have also instituted measures for reviewing foreign investments. King, *supra* note 50, at 44-62.

126. 1973-1974 Can. Stat. ch. 46, amended by 1976-1977 Can. Stat. ch. 52, s. 128(2). For a thorough discussion of the history and provisions of the Act, see G. HUGHES, *FOREIGN INVESTMENT REVIEW ACT (1975)*. The Act is a statute of the Parliament of Canada and received Royal Assent on December 12, 1973. 109 Can. Gaz. 2477 (1975). It came into force on April 9, 1974, with respect to takeovers, 108 *id.* at 1533 (1974), on October 15, 1975, with respect to new businesses, 109 *id.* at 2477 (1975).

127. The Act defines a noneligible person as follows:

(a) an individual who is neither a Canadian citizen nor a permanent resident within the meaning of the *Immigration Act, 1976* and includes

attempts to determine whether an investment will be of "significant benefit"¹²⁸ to Canada. The Act employs a bargaining paradigm¹²⁹—in return for the opportunity to invest in Canada, the responsible officials seek concessions from the prospective foreign investor.¹³⁰ Such concessions might include an agreement to buy more Canadian goods, or an agreement to sell a portion of a proposed Canadian affiliate to Canadian nationals within a specified period of time. These commitments ensure that Canada will obtain a net economic gain from inflows of investment capital. Canada approves roughly ninety percent of the applications submitted.¹³¹

The international reaction to the Canadian screening procedure is unclear. Although some individual decisions have elicited protests

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- (i) a Canadian citizen who is not ordinarily resident in Canada and who is a member of a class of persons prescribed by regulation for the purpose of this definition, and
 - (ii) a permanent resident who has been ordinarily resident in Canada for more than one year after the time at which he first became eligible to apply for Canadian citizenship,
 - (b) the government of a country other than Canada or of a political subdivision of a country other than Canada, or an agency of such a government, or
 - (c) a corporation incorporated in Canada or elsewhere that is controlled in any manner that results in control in fact, whether directly through the ownership of shares or indirectly through a trust, a contract, the ownership of shares of any other corporation or otherwise, by a person described in paragraph (a) or (b) or by a group of persons any member of which is a person described in paragraph (a) or (b)

1973-1974 Can. Stat. ch. 46, s. 3(1), amended by 1976-1977 Can. Stat. ch. 52, s. 128(2); see generally G. HUGHES, *supra* note 126, at 16-23.

128. 1973-1974 Can. Stat. ch. 46, s. 2(2). The Act establishes five factors for assessing whether a proposed foreign investment will be of significant benefit to Canada:

- (a) the effect of the acquisition or establishment on the level and nature of economic activity in Canada, including without limiting the generality of the foregoing, the effect on employment, on resource processing, on the utilization of parts, components and services produced in Canada, and on exports from Canada;
- (b) the degree and significance of participation by Canadians in the business enterprise or new business and in any industry or industries in Canada of which the business enterprise or new business forms or would form a part;
- (c) the effect of the acquisition or establishment on productivity, industrial efficiency, technological development, product innovation and product variety in Canada;
- (d) the effect of the acquisition or establishment on competition within any industry or industries in Canada; and
- (e) the compatibility of the acquisition or establishment with national industrial and economic policies taking into consideration industrial and economic policy objectives enunciated by the government or legislature of any province likely to be significantly affected by the acquisition or establishment.

Id.; see generally G. HUGHES, *supra* note 126, at 53-60.

129. *Id.* at 2, 61, 63, 67-70, 72.

130. See 1979 Hearings, *supra* note 1, pt. 3, at 6, 10 (statement and testimony of Professor William S. Barnes); see generally Barnes, *supra* note 85.

131. 1979 Hearings, *supra* note 1, pt. 3, at 8, 10 (testimony of Professor William S. Barnes); 9 U.S. DEP'T OF COMMERCE, *supra* note 23, app. N, at N-63.

from the investors concerned, there is no evidence that other countries have retaliated against Canadian investors abroad.¹³² Moreover, United States investors have steadily expanded their investments in Canada since the inception of the screening procedure.¹³³ Thus, from a Canadian standpoint, the screening process is successful: without significantly reducing the inflow of investment capital, the Foreign Investment Review Act has ensured that foreign direct investment benefits Canada.¹³⁴

The case by case consideration makes sense in the context of foreign direct investment because the desirability of each investment depends on its particular characteristics.¹³⁵ Through negotiation, the responsible officials and the prospective investor may be able to reduce the detrimental aspects of a proposed investment. Legislation can also empower the screening agency to insulate key sectors of the economy from foreign direct investment. Moreover, a screening agency can encourage particularly beneficial projects by selectively

132. Until 1979, Canada administered the screening process liberally and evenhandedly in all areas of foreign investment. See *NEWSWEEK*, July 13, 1981, at 63. There is no evidence that Canada's administration of the screening procedure before 1979 drew official objections or retaliatory action from other countries. More recently, however, Canada has sought to raise the level of Canadian ownership in the country's oil and gas industry. *BUS. WK.*, Oct. 6, 1980, at 126, 126, 128, 131. Increasingly, Canada uses the screening procedure to effect this goal. *NEWSWEEK*, July 13, 1981, at 63, 63; *BUS. WK.*, Oct. 6, 1980, at 126, 131. This use of the screening procedure has provoked complaints from United States companies with holdings in Canada's energy sector, who claim that restrictions on sales to other foreigners are depressing the value of their investments. *NEWSWEEK*, July 13, 1981, at 63. In response to these complaints, some discussed the possibility of retaliatory action, but the United States has taken no steps in that direction. *Id.*; *BUS. WK.*, June 8, 1981, at 146. Thus, it appears that the United States business community objects not so much to the screening procedure itself, but to the particular and heavyhanded way Canada has applied the procedure to foreign investment in the energy sector. Nevertheless, because of an alleged concern over the screening procedure generally, President Reagan recently decided to seek talks with Canada under the General Agreement on Tariffs and Trade. *N.Y. Times*, Jan. 13, 1982, at D2, col. 4.

133. *BUS. WK.*, Oct. 6, 1980, at 126.

134. A partner at a major Toronto law firm now advises his foreign clients to "make share offerings to increase Canadian ownership, develop a board with Canadian members—and talk to FIRA [Foreign Investment Review Agency], to try to get recognized by it as a Canadian company." *Id.* at 131, quoting Peter R. Hayden. This advice, to increase Canadian ownership and participation in foreign-owned industry, accords with the objectives of the Act. See *supra* note 128.

135.

The reasons leading Canada to introduce a review process could well be applied to other host countries even though they are not experiencing the same degree of foreign presence or predominance: first, that foreign investment has a role to play in future economic development where it contributes to realizing national industrial objectives; second, that special measures to deal with certain problems will be required no matter how rosy the picture in the future; third, that costs and benefits of foreign direct investment vary from industry-to-industry and from case-to-case, thereby requiring flexibility rather than fixed rules; fourth, that good performance is more important than local ownership and control of a firm.

Barnes, *supra* note 85, at 4 (footnotes omitted).

applying investment incentives in the form of tax reductions, accelerated depreciation schedules, or low interest loans.¹³⁶ Foreigners who invest in economically depressed areas, declining industries, or industrial research may be appropriate recipients of such incentives. Finally, a screening procedure creates a current and accurate source of information on foreign direct investment.

Congress should consider establishing a screening agency patterned after those of similarly situated countries. This agency should be empowered to review potential investments with an eye toward significant benefit to the United States.¹³⁷ The agency should attempt to bargain away the harmful effects of proposed investments. The agency should also have the authority to bar investments, if negotiation cannot alleviate the detrimental aspects.

The agency's criteria for screening should address the concerns about foreign direct investment identified above. Thus, the agency might ask the following questions: first, to what extent will the prospective investor use domestic funds to finance the proposed investment; second, what plan does the applicant have for the profits of his investment; third, to what extent will the proposed investment utilize imported goods; fourth, does the applicant aim to secure either scarce natural resources or innovative United States technology; and fifth, will the proposed investment involve the acquisition of an already established enterprise. Finally, the agency should use investment incentives to encourage investments in geographic areas or economic sectors that lack sufficient sources of investment capital.

CONCLUSION

The United States should adapt its policy on foreign direct investment to changes in the country's and the world's economic situation. The open door policy served the interests of the United

136. Most other industrialized nations currently offer investment incentives. 9 U.S. DEP'T OF COMMERCE, *supra* note 23, app. N, at N-2; *see, e.g., id.* at N-2, N-4 to -5, N-7, N-12 to -13, N-16 to -17, N-19 to -20, N-29, N-32 to -33, N-37, N-51 to -53, N-65.

137. An alternative to the creation of a new administrative agency is to endow the existing Committee on Foreign Investment in the United States with additional authority. *See supra* note 71. The Committee is a high level interagency committee run by the Treasury Department. H.R. REP. NO. 1216, *supra* note 19, at 22. It has three responsibilities: first, to set priorities on Federal data collection and research and analytical efforts concerning foreign direct investment; second, to formulate policy on foreign direct investment through reassessments and recommendations to the President; and, third, to examine actual investments that have major implications for United States national interests. *Id.* Currently, the Committee is nearly dormant. It has met only 10 times in the last five years and has reviewed only three actual cases of foreign direct investment. *Id.* With a change in leadership and a legislative mandate, however, Congress might employ the existing administrative structure of the Committee as a screening agency for foreign direct investment.

States well when Americans had no reason to concern themselves with the harmful effects of foreign direct investment. Today, however, the open door policy offers inadequate protection for the political and economic interests of the United States. The country needs a new policy that reduces the costs and augments the benefits of foreign direct investment.

Congress faces a range of policy options for foreign direct investment. Congress should reject House bill 7750 and similar proposals adopting the quid pro quo approach because they fail to distinguish among investments on the basis of individual merit. By contrast, a case by case screening procedure would serve that function. The case by case screening of foreign direct investment would permit the United States to participate in the international exchange of investment capital without unnecessarily exposing itself to the costs of such investment.

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