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Before the U.S. House Energy & Commerce
Subcommittee on Digital Commerce and Consumer Protection
April 26, 2018

Chairman Latta, Ranking Member Schakowsky, Vice Chairman Kinzinger, and distinguished Members of the Subcommittee, thank you for the opportunity to testify in support of the Foreign Investment Risk Review Modernization Act (FIRRMA), H.R. 4311, 115th Cong. (2017). I would also like to thank those members of the subcommittee who have joined FIRRMA as co-sponsors, including Representative Mullin.

My top priority as Assistant Secretary is ensuring that the Committee on Foreign Investment in the United States (CFIUS) has the tools and resources it needs to perform the critical national security functions that Congress intended it to.[1] I believe FIRRMA—a bill introduced with broad, bipartisan support—is designed to provide CFIUS with the tools it needs to meet the challenges of today and those likely to arise in the future. Of particular importance to this subcommittee is the challenge of protecting against the harm that could result from the acquisition of companies that collect or store large pools of sensitive data about individual Americans. Malicious actors could exploit sensitive healthcare, financial, and other personally identifiable information to the detriment of U.S. national security. The Administration believes that FIRRMA will protect our national security from these and other kinds of risks while strengthening America's longstanding open investment policy that fosters innovation and economic growth.

Importance of Foreign Investment in the United States

From the early days of our Republic, the United States has been a leading destination for investors, entrepreneurs, and innovators. In his famous *Report on the Subject of Manufactures*, Alexander Hamilton argued that foreign capital was not something to be feared or viewed as a rival to domestic investment, but was instead a "precious acquisition" in fostering our economic growth.[2] Throughout the nineteenth and twentieth centuries, capital from abroad funded the construction of America from our railways to our city skylines, while at the same time helping make such innovations as the automobile a reality.[3] Foreign investment has also brought significant benefits to American workers and their families in the form of economic growth and well-paid jobs.

The same is true today, with a total stock of foreign direct investment in the United States standing at a staggering $7.6 trillion (at market value) in 2016.[4] Numerous studies have

[1] *See Nomination Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 115th Cong. (May 16, 2017) (testimony of Dr. Heath P. Tarbert).
[2] Alexander Hamilton, *Report on the Subject of Manufactures* (Dec. 5, 1791), *available at* https://founders.archives.gov/documents/Hamilton/01-10-02-0001-0007.
[3] *See* Mira Wilkins, *The History of Foreign Investment in the United States to 1914* (Harvard Univ. Press 1999).
[4] U.S. Bureau of Economic Analysis, *U.S. Net International Investment Position at the End of the Period*, Table 1.1. (Dec. 28, 2017), *available at* https://bea.gov/scb/pdf/2018/01-January/0118-international-investment-position-tables.pdf.

demonstrated that the benefits from foreign investment in the United States are substantial. Majority-owned U.S. affiliates of foreign entities accounted for over 23 percent of total U.S. goods exports in 2015.[5] They also accounted for 15.8 percent of the U.S. total expenditure on research and development by businesses.[6] They employed 6.8 million U.S. workers in 2015, and provided compensation of nearly $80,000 per U.S. employee, as compared to the U.S. average of $64,000.[7] One study estimated that spillovers from foreign direct investment in the United States accounted for between 8 percent and 19 percent of *all* U.S. manufacturing productivity growth between 1987 and 1996.[8] As Secretary Mnuchin—echoing his predecessor, Secretary Hamilton—has observed, "we recognize the profound economic benefits of foreign investment" today and place the utmost value on having "industrious and entrepreneurial foreign investors" continue to invest, grow, and innovate in the United States.[9]

Evolution of CFIUS

Despite its many benefits, we are equally cognizant that foreign investment is not always benign. On the eve of America's entry into World War I, concerned by German acquisitions in our chemical sector and other war-related industries,[10] Congress passed the Trading with the Enemy Act, giving the President broad power to block investments during times of war and national emergency.[11]

During the Great Depression and World War II, international investment flows dropped dramatically.[12] And in the boom years of the 1950s and 1960s—as many countries devastated by World War II were rebuilding their economies—investment in the United States from abroad was modest compared to outflows. Indeed, for the first time ever, America became a net source

[5] U.S. Dep't of Commerce, Economics & Statistics Admin., *Foreign Direct Investment in the United States,* ESA Issue Brief 06-17, Oct. 3, 2017, at 2.
[6] *Id.*
[7] *Id.*
[8] Wolfgang Keller & Stephen R. Yeaple, *Multinational Enterprises, Int'l Trade, and Productivity Growth: Firm Level Evidence from the United States*, 91 Review of Economics & Statistics, November 2009, at 821, 828.
[9] Steven T. Mnuchin, Secretary, Dep't of the Treasury, SelectUSA Investment Summit Welcome Address (June 20, 2017).
[10] Edward M. Graham & David M. Marchick, Institute for Int'l Economics, *U.S. Nat'l Security & Foreign Direct Investment* 4-8 (2006). Prior to America's entry into World War I, it was revealed that the German government made a number of concealed investments into the United States, including establishment of the Bridgeport Projectile Company which "was in business merely to keep America's leading munitions producers too busy to fill genuine orders for the weapons the French and British so desperately needed." Ernest Wittenberg, *The Thrifty Spy on the Sixth Avenue El*, American Heritage (Dec. 1965), *available at* http://www.americanheritage.com/content/thrifty-spy-sixth-avenue-el. The company placed an order for five million pounds of gunpowder and two million shell cases "with the intention of simply storing them." *Id.* The plot was revealed when a German spy inadvertently left his briefcase containing the incriminating documents on a New York City train, with the documents being returned to the custody of the Treasury Department. *Id.*
[11] 50 U.S.C. § 4305. TWEA, originally passed in 1917, empowered the President to "investigate, regulate, direct and compel, nullify, void, prevent or prohibit, any acquisition holding, withholding, use, transfer, withdrawal, transportation, importation or exportation of, or dealing in, or exercising any right, power, or privilege with respect to, or transactions involving, any property in which any foreign country or a national thereof has any interest." *Id.* § 4305(b)(1)(B).
[12] Graham & Marchick, *supra* note 10, at xvi, 14, 18.

of investment capital instead of its destination.[13] And what foreign investment did exist posed little risk since our main strategic adversaries—the Soviet Union and its satellites—were communist countries whose economic systems were largely isolated from our own.

When the post-war trend changed in the 1970s, however, CFIUS was born. The oil shock that made OPEC countries wealthy led to concern that petrodollars might be used to purchase key U.S. assets. In 1975, President Ford issued an Executive Order creating CFIUS to monitor and report on foreign investments, but with no power to stop those posing national security threats.[14] Then in the 1980s, a growing number of Japanese acquisitions motivated Congress to pass the Exon-Florio Amendment in 1988.[15] For the first time, the President could block the foreign acquisition of a U.S. company or order divestment where the transaction posed a threat to national security without first declaring an emergency. That law created Section 721 of the Defense Production Act of 1950, which remains the statutory cornerstone of CFIUS today.

Subsequently, in 1992, Congress passed the Byrd Amendment which requires CFIUS to undertake an investigation where two criteria are met: (1) the acquirer is controlled by or acting on behalf of a foreign government; and (2) the acquisition results in control of a person engaged in interstate commerce in the United States that could threaten our national security.[16] In the years that followed, it became evident that CFIUS and Congress did not share the same view on when a 45-day investigation period was discretionary rather than mandatory, a rift that was more clearly exposed in the wake of the Dubai Ports World controversy. In order to instill greater procedural rigor and accountability into CFIUS's process, Congress enacted the Foreign Investment and National Security Act of 2007 (FINSA), which formally established CFIUS by statute and codified its current structure and processes.[17]

Critical Need for CFIUS Modernization

Now, more than a decade after FINSA and three decades after Exon-Florio, we find ourselves at another historic inflection point. Within the last few years, the national security landscape as it relates to foreign investment began shifting in ways that have eclipsed the magnitude of any other shift in CFIUS's 40-year history. Nowhere is that shift more evident than in the caseload CFIUS now faces. The resources of CFIUS are challenged by increased case volume and complexity. The average volume of CFIUS cases has been growing steadily from fewer than 100 in 2009 and 2010 (the two years following the financial crisis) to nearly 240 last year. While it is difficult to measure case complexity in real terms, one indicator is the rate at which cases have proceeded to CFIUS's investigation stage, which is more resource intensive. In 2007, approximately 4 percent of cases went to investigation; in 2017, approximately 70 percent did. Another potential measure of complexity is the number of cases in which CFIUS determines that mitigation or prohibition is necessary to address national security concerns, which require significantly more time and resources. From roughly 2008 through 2015, such cases represented fewer than 10 percent of the total covered transactions CFIUS reviewed; this

[13] *Id.* at 9.
[14] Exec. Order 11,858, 40 F.R. 20,263 (May 7, 1975).
[15] Pub. L. 100-418, Title V, § 5021, 102 Stat. 1107 (1988).
[16] Pub. L. 102-484, 106 Stat. 2315 (1992).
[17] Pub. L. 110-49, 121 Stat. 246 (2007).

figure has risen to approximately 20 percent of total covered transactions CFIUS reviewed in 2017.

The added complexity CFIUS is confronting arises from a number of different factors, including: the way foreign governments are using investments to meet strategic objectives, more complex transaction structures, and increasingly globalized supply chains. Complexity also results from continued evolution in the relationship between national security and commercial activity. Military capabilities are rapidly building on top of commercial innovations. Additionally, the digital, data-driven economy has created national security vulnerabilities never before seen.

The gravity of the last point regarding the vulnerabilities arising from the digital, data-driven economy must not be lost on this subcommittee given your critical role on digital commerce and consumer protection issues. In several cases we have seen even within the last 12 months, the company being acquired—which may, for example, be in the technology hardware, technology services, or financial services industry—has access to significant amounts of sensitive information on Americans that can be exploited by state actors. The sensitivity could arise because a given company has concentrations of data regarding American military servicemen and women, deeply private information such as medical records, or simply personally identifiable information on such a vast scale that the national security concerns are just too large to ignore. Thus today, the acquisition of a Silicon Valley start-up or even a healthcare provider may raise just as serious concerns from a national security perspective as the acquisition of some defense or aerospace companies, CFIUS's traditional area of focus.

CFIUS's exposure to such cases has allowed it to play a critical role in protecting against threats to national security, but has at the same time highlighted gaps in our jurisdictional authorities. We continue to be made aware of transactions we lack the jurisdiction to review but which pose similar national security concerns to those already before CFIUS. These gaps are widening as more threat actors seek to exploit them. The problem lies in the fact that CFIUS's jurisdictional grant is now 30 years old, originating with the Exon-Florio Amendment and maintained in FINSA. Under current law, CFIUS has authority only to review those mergers, acquisitions, and takeovers that result in foreign "control" of a "U.S. business." That made sense in the 1980s and even in the first decade of this century, but the foreign investment landscape has changed significantly, with non-controlling investments and joint ventures becoming ever more prolific.

Consequently, certain transactions—such as investments that are not passive, but simultaneously do not convey "control" in a U.S. business—that the Committee has identified as presenting a national security risk nonetheless remain outside its purview. Similarly, CFIUS is also aware that some parties may be deliberately structuring their transactions to come just below the control threshold to avoid CFIUS review, while others are moving critical technology and associated expertise from a U.S. business to offshore joint ventures. While we recognize that parties can choose among a variety of transaction structures, purposeful attempts to evade CFIUS review put this country's national security at risk. Finally, we regularly contend with gaps that likely never should have existed at all. For example, the purchase of a U.S. business in close proximity to a sensitive military installation is subject to CFIUS review, but the purchase of real

estate at the same location (on which one could place a business) is not. These gaps can lead to disparate outcomes in transactions presenting identical national security threats.

Support for FIRRMA

The Administration has endorsed FIRRMA because it embraces four pillars critical for CFIUS modernization. First, FIRRMA expands the scope of transactions potentially reviewable by CFIUS, including certain non-passive, non-controlling investments, technology transfers through arrangements such as joint ventures, real estate purchases near sensitive military installations, and transactions structured to evade CFIUS review. The reasons for these changes are twofold: (1) they will close gaps in CFIUS's authorities by expanding the types of transactions subject to CFIUS review; and (2) they will give CFIUS greater ability to prevent parties from restructuring their transactions to avoid or evade CFIUS review when the aspects of the transaction that pose critical national security concerns remain.

Second, FIRRMA empowers CFIUS to refine its procedures to ensure the process is tailored, efficient, and effective. Under FIRRMA, CFIUS is authorized to exclude certain non-controlling transactions that would otherwise be covered by the expanded authority. Such exclusions could be based on whether other provisions of law—like export controls—are determined to be adequate to address any national security concerns. Only where existing authorities cannot resolve the risk will CFIUS step in to act. FIRRMA also allows CFIUS to identify specific types of contributions by technology, sector, subsector, transaction type, or other transaction characteristics that warrant review—effectively excluding those that do not.

Third, FIRRMA recognizes that our own national security is linked to the security of our closest allies, who face similar threats. In light of increasingly globalized supply chains, it is essential to our national security that our allies maintain robust and effective national security review processes to vet foreign investments into their countries. FIRRMA gives CFIUS the discretion to exempt certain transactions from review involving parties from certain countries based on such factors as the nature of the U.S. strategic relationship with the country and the other country's process to review the national security implications of foreign investment. FIRRMA will also enhance collaboration with our allies and partners by allowing information-sharing for national security purposes with domestic or foreign governments.

Fourth, FIRRMA requires an assessment of the resources necessary for CFIUS to perform its critical mission so that Congress has a full understanding of the needs required to fulfill CFIUS's expanded scope. FIRRMA would also establish a "CFIUS Fund," which would be authorized to receive appropriations. Under FIRRMA, these monies are intended to cover work on reviews, investigations, and other CFIUS activities. FIRRMA further authorizes CFIUS to assess and collect fees, which would be set by regulation at a level anticipated not to affect the economics of any given transaction. Once appropriated, these funds could also be used by CFIUS. Finally, FIRRMA grants the Secretary of the Treasury, as CFIUS chairperson, the authority to transfer funding from the CFIUS Fund to any member agencies to address emerging needs in executing requirements of the bill. This approach would enhance the ability of agencies to work together on national security issues.

Since my earlier testimony before the Senate Committee on Banking, Housing, and Urban Affairs on January 25, 2018 and the House Financial Services Subcommittee on Monetary Policy and Trade on March 15, 2018, my colleagues and I have been meeting regularly with members of Congress and the business community to hear their views on CFIUS-related legislation. Notably, while some have suggested technical amendments aimed at improving the core proposal, all agree on one essential point: CFIUS must be modernized through a comprehensive piece of legislation. Based on the feedback we received, we have been working on proposed amendments to ensure that FIRRMA is even better tailored to remedy existing gaps in CFIUS's authority without harming—but rather, encouraging—the foreign direct investment that has benefitted our country so greatly.

In sum, CFIUS must be modernized. In doing so, we must preserve our longstanding open investment policy. At the same time, we must protect our national security from current, emerging, and future threats. The twin aims of maintaining an open investment climate and safeguarding national security are the exclusive concern of neither Republicans nor Democrats. Rather, they are truly American aims that transcend party lines and regional interests. But they demand urgent action if we are to achieve them. I look forward to working with this subcommittee on improving and advancing FIRRMA, and I am hopeful the bill will continue to move forward on a bipartisan, bicameral basis.