Statement of the Honorable Clay Lowery
Managing Director
Rock Creek Global Advisors LLC

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Examining CFIUS
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Chairman Crapo, Ranking Member Brown, and Members of the Committee, I would like thank you for the opportunity to testify on Examining the Committee on Foreign Investment in the United States (CFIUS). My name is Clay Lowery and I am currently Managing Director of Rock Creek Global Advisors, a consulting firm that advises clients on international economic and financial policy matters. My testimony should be considered my own views alone.

I served in the U.S. Government from 1994 to 2009, principally with the Treasury Department, although I also had a stint at the National Security Council. From 2005 to 2009, I served as the Assistant Secretary of International Affairs for the Treasury Department, and one of my primary responsibilities was overseeing CFIUS during the last time substantial CFIUS reform occurred.

I am pleased to be testifying alongside Kevin Wolf and Jim Lewis, both of whom I respect and of whose views and expertise I think highly.

In my testimony, I will discuss briefly (i) the nature of CFIUS and its process, (ii) its performance, and (iii) some thoughts on CFIUS reform.

CFIUS plays a critical role in protecting US national security. I recognize there are gaps in the current system that must be addressed, but I would also counsel that CFIUS's objective is to protect legitimate national security interests while promoting foreign investment, and thus CFIUS should not be used as an economic, protectionist or overly-broad tool.

The most important aspect of CFIUS is to understand what it is trying to achieve: ensure national security while promoting foreign investment. These words come directly from the legislation that created CFIUS and has guided it for the last 30 years. When experts raise concerns about national security issues that may have recently become more prominent and recommend that the best – and sometimes only – tool to address those concerns is CFIUS, my view is to evaluate those recommendations against what CFIUS was designed to achieve.

Roughly 7 million American workers, or about 6 percent of total U.S. private-sector workers, are employed directly through foreign direct investment (FDI). These jobs are higher paying: providing average compensation per worker 24 percent higher than U.S. private-sector wages.

These jobs are disproportionally in the manufacturing sector: 20 percent of all manufacturing employment is due to FDI. And, according to a recent Reuters analysis – two-thirds of the manufacturing jobs created from 2010 to 2014 can be attributed to foreign direct investment.

In short, FDI is in the national interest of the United States. However, we should not be complacent. While the U.S. remains the largest destination for FDI, our share of attracting such investment has fallen about 40 percent in the past 16 years.[1]

Last, I want to note how this could be used against US companies overseas. The United States has always been the leader in defining "national security" in a reasonable and fair way. I would remind the Committee that any actions we take are likely to be copied and used by other countries, potentially to the detriment of US interests abroad.

CFIUS Evolution

CFIUS is an interagency committee established by Executive Order in 1975 with the Secretary of the Treasury as its chair. Its central purpose at that time was to monitor foreign direct investment in the United States. In 1988, driven by concerns regarding growing Japanese investment in the United States, Congress enacted the Exon-Florio amendment that expanded these powers significantly, including (i) giving CFIUS the responsibility to investigate foreign acquisitions of companies engaged in business in the United States, and (ii) providing the President the ability to suspend or prohibit a covered transaction that, in the President's judgment, threatens the national security and existing laws are not adequate or appropriate to address the threat.[2] In 2007, following concerns that had been raised over a Middle Eastern investment in U.S. port facilities, Congress amended and further strengthened CFIUS through the Foreign Investment and National Security Act (FINSA).

A new Executive Order directing CFIUS followed in early 2008 and new regulations implementing FINSA were issued later that year. The key reforms resulting from those efforts include:

- Increasing accountability in the executive branch as Senate-confirmed officials now must certify that CFIUS has completed its work on each transaction;
- Broadening the factors that CFIUS may consider in terms of investigating cross-border M&A transactions, particularly in areas such as critical technology, energy, and critical infrastructure;
- Raising the certification bar for cases in which the acquirer is a state-controlled entity;
- Increasing CFIUS interaction with Congress;

[1] United Nations Conference on Trade and Development (UNCTAD) World Investment Report 2017.
[2] To be precise, the President delegated the investigative functions to CFIUS by Executive Order.

- Providing for a more formal role for the intelligence community; and
- Clarifying CFIUS criteria for evaluating whether an acquirer is obtaining control of a U.S. business.

CFIUS Process

CFIUS is chaired by Treasury and is comprised of the Departments of Commerce, Defense, Energy, Homeland Security, Justice, and State as well as the Office of the U.S. Trade Representative and the Office of Science and Technology Policy. In addition, the Intelligence Community under the leadership of the DNI and the Department of Labor serve as non-voting members of CFIUS.[3]

Parties submit their transactions to CFIUS for review on a voluntary basis, although CFIUS has the authority to compel a filing if necessary. The statute prescribes strict timelines for CFIUS's review, but parties are encouraged to pre-file with CFIUS to provide the government with an opportunity to begin its analysis before the "clock starts ticking."

CFIUS officials are obligated by law, and subject to the possibility of criminal or civil penalties, not to disclose information regarding transactions. The rationale behind this rule is to protect both proprietary and intelligence information.

Once a transaction has been filed, CFIUS first determines whether it has jurisdiction to review the transaction – that is, does it involve foreign control of a U.S. business in interstate commerce – and, if it does, CFIUS then undertakes a three-part evaluation:

1. Does the acquirer pose a threat to national security? This analysis is led by the Intelligence Community.
2. Is national security made more vulnerable by virtue of the acquisition of the U.S. assets? This analysis tends to be driven by the CFIUS agency with applicable subject-matter expertise.
3. Do the consequences of permitting the threat and vulnerabilities to be combined through a specific transaction risk impairing national security?

CFIUS investigates these questions in the first 30 days after it accepts the filing. If at the end of those 30 days, CFIUS is not satisfied or in most transactions where the acquirer is state-controlled, then CFIUS will undertake a second stage investigation that lasts up to an additional 45 days.

[3] Several offices in the executive office of the president also serve as observers of CFIUS.

The process, the timelines, the composition of CFIUS, the protection of information, and the reforms of 2007/08 have all been designed by Congress and respective Administrations to protect national security and to do so in the context of maintaining the United States' long-standing policy openness to investment. In addition, knowing that some transactions may raise national security issues, Congress has expressly authorized CFIUS to enter into mitigation agreements with the transaction parties to address those concerns. There are many different types of methods of mitigating a transaction. Examples include establishing special security procedures at facilities that can be verified by the government, implementing certain passivity mechanisms, or even forcing a company to divest specific assets. In short, these mitigation agreements impose measures on the parties that address national security risks.

These mitigation agreements are the pressure valve that enables CFIUS to find solutions to more difficult transactions – to welcome foreign investment and protect national security.

If at the end of that 75-day period, CFIUS cannot make a decision or recommends that a transaction should be prohibited – then the matter is referred to the President who has 15 days to make a decision. Only the President has the ability to block a transaction.

In the past 27 years, the President has prohibited or unwound only three transactions. The primary reason that such activity by the President is so rare is that most transactions do not pose a national security risk or risks can be mitigated through diligent work by CFIUS. The other reason is corporate concern about reputational risk. When the President makes a formal decision on a transaction, that decision is made public. Companies that believe the President could prohibit their transaction are understandably reluctant to be subject to a public rejection. Accordingly, most companies will withdraw from the CFIUS process and abandon their transaction.

How CFIUS has performed

Since FINSA was enacted ten years ago, CFIUS – in my opinion – has performed in an exceptionally professional and thoughtful manner. Congress and the American people should be proud of how well the group of individuals across the government have carried out their duties. Their scrutiny of cases is thorough; they have protected national security; they have protected information as well as anyone in the U.S. Government; and they have preserved the reputation of the United States as open to investment from around the world. CFIUS in many respects has been a model not only within our government but also for other countries; various nations are now considering how they can emulate the U.S. process.

That said, there is little question that the investment landscape has changed substantially in those ten years. By far, the most important change has been the rise of China as a direct investor in the

United States. Ten years ago, CFIUS would review just one or two transactions a year that had involved a Chinese acquirer – today, it is literally dozens and dozens of transactions every year. While I believe we should welcome Chinese investment and that each transaction should be judged on its own merits, these transactions have more complex financial structures, sometimes are more opaque, and come from a country where the state plays a much larger role in the economy. Often, these factors and others, raise the threats to national security. I know that fellow panelist Jim Lewis is focusing his remarks on Chinese investment and the threats it raises so I will not elaborate further.

The other development is the concern that technology is being transferred that could make our national security more vulnerable. I know that Kevin Wolf is an expert on export control laws so I'll let him elaborate on the importance of these developments.

CFIUS Reform

As for me, these changes in the investment landscape as well as the fact that it has been ten years since CFIUS was reformed suggest that a close, sober evaluation by Congress, by the GAO, and by the Administration is in order. As with any analysis, it is best to think of any potential reforms in terms of benefits and costs, including intended and unintended consequences.

I would have three starting points beyond a cost/benefit analysis:

First, I want to note the importance of providing appropriate resources to both Treasury and other agencies for CFIUS cases. The CFIUS process is currently under stress because of a significant increase in cases, without a commensurate increase in resources. While I strongly believe that we should set good policy on the merits, we also need to provide adequate resources to effectively carry out those policies.

CFIUS reviewed over 170 transactions last year, which is the highest number since CFIUS was strengthened ten years ago. As mentioned earlier, there is a much larger proportion of cases originating from China and that are structurally more complex. In 2017, my understanding is that CFIUS is on pace to investigate a much higher number than in 2016. There is little question in my mind that the individuals doing their jobs are under too much strain – they need more resources before we consider how to increase their work load.

I am very concerned that a significant expansion of CFIUS will overwhelm the system and significantly impact its effectiveness and ability to function. So while resources are not the issue on the table today, I do not think you can separate them from the policy if you want the system to function efficiently and effectively.

Second, as part of the new FINSA law of 2007, this committee added an Assistant Secretary of Treasury to oversee CFIUS. The Trump Administration has nominated a highly qualified individual in Heath Tarbert. This committee approved him with near unanimous support roughly four months ago. Why he has not been confirmed is a mystery to me, but at a time when CFIUS is under as much strain as it has ever been and when Congress is considering reforms that would expand CFIUS – it is past time to confirm the individual with the most direct responsibility for overseeing the system.

Third, as we consider reforming CFIUS, we should adopt a set of guiding principles to ensure that the United States both safeguards its national security and remains the destination of choice for investment:

- Minimize the opportunity for politicizing transactions.
- Keep CFIUS narrowly focused on national security and resist the impulse to use it for broader economic policy goals.
- Ensure accountability of the executive branch for protecting national security while welcoming foreign investment.
    - This means that the executive branch should find solutions by "working a problem" and use its authority to craft appropriate mitigation measures, which may mean additional resources – maybe paid by fees from the filing parties – for monitoring and verification.
    - It also means providing filing parties an opportunity to "make their case" directly to Senate-confirmed individuals so that parties to transactions are not faced with the situation where staff-level officials are deadlocked or uncommunicative and the next step is a decision by the President.
- Maintain CFIUS's focus on – and review should be triggered only by -- foreign mergers and acquisitions of US businesses, and not broaden the scope to sweep in thousands of commercial or licensing transactions.
- Increase scrutiny over state-controlled acquirers, including the possibility of making the filing of such transactions mandatory.

Thank you and I'm happy to field any questions.