

Testimony
of
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Policy, Trade, and Technology

Foreign Investment, Jobs and National Security: The
CFIUS Process

Good morning Madam Chairman, Congresswoman Maloney and members of the Committee, my name is Todd Malan and I am President and CEO of the Organization for International Investment or OFII.

OFII is an association representing the interests of U.S. subsidiaries of companies based abroad or “insourcing” companies. OFII has 140 member companies, which range from mid-sized businesses to some of the largest employers in the United States, such as Honda, HSBC, Sony, AEGON Insurance, Nestlé, Unilever and L’Oreal.

Collectively, insourcing companies employ 5.3 million Americans, pay 34% higher compensation than at all U.S. firms, support 21% of all U.S exports and in 2004 reinvested \$45 billion in profits back into the U.S. economy.

As the representative of the largest collection of companies that regularly seek review of acquisitions by the Committee on Foreign Investment in the United States (CFIUS) under the Exon-Florio Amendment to the Defense Production Act, we very much appreciate the opportunity to participate in this important hearing.

I am pleased to share my organization’s views on each of the topics that are enumerated in the hearing title: national security, foreign investment and the jobs it provides, and the CFIUS process that Congress created to balance the benefits of the one against the absolute necessity of the other.

At the outset, let me make clear that neither DP World nor P&O are member companies. I cannot comment about the particulars of that transaction, as I am not aware of its details, its review by CFIUS, or any agreements made as part of the CFIUS process.

National Security is the Priority

Some people view the business community skeptically when it comes to national security discussions. Unfortunately, this perspective ignores that the terrorists are aiming at our

economic system, not just our political system. From the tragic events of September 11th, to last week's foiled attack in Saudi Arabia -- economic and business interests are prime targets. Companies and the people that run them understand this fact of life. The business community works hard to cooperate with governments on all aspects of national security. My member companies take this national security mandate very seriously.

The statute that is the focus of today's hearing is ultimately about national security. Our respect for the law, the CFIUS process, the government officials who participate in it and the debate about possible changes to the process are all grounded in the recognition that national security is the first priority. We also respect Congress's role in providing meaningful oversight.

The Benefits of Foreign Investment In The U.S.

In carefully crafting the Exon-Florio Amendment, and the narrow changes to it since then, Congress recognized that foreign investment in the United States makes a positive contribution to the economy. This law is a scalpel, not a meat cleaver. Congress could have chosen to create a more rigid, restrictive system that would have resulted in steeper barriers to foreign direct investment. It did not. This flexibility is testament that the United States has long welcomed and benefited from foreign investment. According to the most recent government figures, the benefits of insourcing's contribution to the economy are clear:

- U.S. subsidiaries employ 5.3 million Americans and operate in all 50 states.
- U.S. subsidiaries support an annual payroll of \$317.9 billion.
- Average compensation per employee is \$60,527 – 34% more than compensation at all U.S. firms.
- U.S. subsidiaries heavily invest in the American manufacturing sector. Thirty-four percent of the jobs at U.S. subsidiaries are in manufacturing.
- Contrary to many people's assumptions, these companies don't just invest here to access our market. U.S. subsidiaries account for over 21% of all U.S. exports.

- New foreign direct investment (FDI) in the U.S. totals \$79.8 billion, an increase of \$16.2 billion or 26 percent over the previous year.
- U.S. subsidiaries reinvested \$45 billion in their U.S. operations. In other words, profits earned here, stay here.
- U.S. subsidiaries spent \$29.5 billion on U.S. research and development activities, up \$2 billion from the previous year.
- Ninety-four percent of total assets owned by foreign companies are from OECD countries.
- Ninety-eight percent of U.S. FDI is from private sector firms -- only two percent of total direct investment (*assets*) is owned by companies that are controlled by foreign governments.

In today's global economy, labels such as "foreign" or "domestic" are less and less relevant. In my 11 year experience working with insourcing companies at OFII, I have seen a number of changes in business practices and trends that in my mind blur the clear demarcation between foreign and domestic firms. I think some of this experience is useful for Members to keep in mind as they contemplate the benefits of our open investment policy and possible changes to the national security screening regime.

Many foreign multinationals have moved U.S. personnel into very senior global positions. For instance, many CEOs of U.S. subsidiaries, most of whom are American citizens, have recently gone on to become the CEO of the global company.

Also, I see a trend in which many foreign companies are moving key functions and senior personnel *into* the U.S. These functions often have world wide responsibility for a business unit or function.

This type of global leadership activity for U.S. personnel or operations is highly beneficial to the U.S. economy and should also be taken into account when thinking about the behavior of "foreign" companies vis-à-vis national interests.

In addition, more and more Americans are shareholders in “foreign” companies. In an effort to diversify their investments, Americans now hold over \$2.9 trillion in foreign equities. Millions of Americans, either directly or through their mutual funds and pension funds are “owners” of these firms. Within my membership, there are numerous examples where American shareholders hold a majority of shares in a “foreign” company.

Exon-Florio Strikes A Balance: National Security & Foreign Investment

While national security is any nation’s first priority, it must be managed alongside other important national priorities. Maintaining national security and economic strength are interdependent.

When Congress enacted the Exon-Florio statute in 1989, it struck a balance between two interrelated priorities: national security protection and the economic benefits of an open investment policy.

I believe that Members of the Committee have been briefed extensively on the workings of CFIUS and the previous panel testified at some length about its function. As such, I will not repeat what others have already outlined.

However, I would like to focus on those aspects of the law and current CFIUS practice that OFII believes demonstrate a positive balance between national security protection and the economic benefits of foreign direct investment:

- Each transaction is reviewed on a case-by-case basis;
- The 12 members of CFIUS bring a diversity of experience and perspective to the review of a transaction;
- CFIUS members can initiate requests for reviews;

- The full resources of the U.S. government intelligence capabilities are used in the review;
- The ability of CFIUS to invite other agencies with particular expertise to participate in a review;
- The authority that CFIUS has to require parties to adopt measures that CFIUS members believe are necessary to protect national security;
- The ability of CFIUS, in most instances, to work without political intervention, preventing a competitor with a financial motive, not a national security motive, to seek to influence a less resolute process;
- The recognition by CFIUS agencies that, as a general matter, foreign investment in the United States is a positive contribution to our economic health;

Finally, I would point out that CFIUS has blocked or deterred certain transactions. While we can never know exact figures, we do know that the CFIUS process has led to one transaction being denied by the President, resulted in the withdrawal of 13 transactions, and no doubt dissuaded some parties from attempting to make certain US acquisitions.

Does CFIUS Need To Be Changed?

In many respects, CFIUS has changed over time. For instance, the President altered the CFIUS membership to reflect new capabilities and structures by adding the Department of Homeland Security in 2003. As technology and our interfaces with it have changed, CFIUS has adjusted its scope to heighten its review of transactions in critical infrastructure areas such as telecommunications.

However, in OFII's view, CFIUS is not broken and does not need wholesale reform.

Admittedly, there needs to be better mechanisms in place for consultation between the Congress and CFIUS. This process needs to be focused (perhaps to committees of jurisdiction) as it is in other oversight responsibilities and it needs to ensure that confidential, business proprietary information is protected. There are numerous examples of other such procedures in monetary policy, trade policy or anti-trust reviews.

On the other hand, some of the proposals for amending CFIUS would have profound negative impacts on vital economic interests. I would like to share a few brief thoughts on some of those proposed changes:

Increasing the Time Periods for Reviews and Investigations: The GAO study that was conducted in September of last year suggested that the CFIUS process may need more time for its reviews. OFII believes that the current structure of 30 days for review and 45 days for the investigation phase is adequate. Expanding the time frame would mean that CFIUS could be viewed as a major impediment to closing cross-border transactions and could require insourcing companies to pay premium prices or be excluded from some potential transactions. I would note that the addendum to the GAO study, which was a consensus view of CFIUS members, supported the view that timeframes for review and investigation are adequate.

Mechanisms for Congressional Disapproval of President's Decision: Members of Congress have a strong interest in the CFIUS process and its decisions. The process relates to national security and Members are accountable to their constituents in that regard. But this is also an administrative process based in law. There is no other instance in commercial administrative procedures where a formal mechanism exists for Congress to change or disapprove of a specific outcome. In other contexts, Congress has realized that it is not best equipped for making sensitive fact-based, case-by-case decisions. In all other contexts, Congress creates the law, creates an administrative procedure, and conducts oversight to ensure the law is being appropriately implemented and enforced. Congress does not second guess the process in regard to specific anti-trust reviews, International Trade Commission decisions or patent and trademark awards. It shouldn't start here.

Expanding the Scope of CFIUS to Include Economic Security: Some have suggested that the scope of CFIUS should include the concept of “economic security.” This would be a huge mistake that emulates the very worst of other nation’s restrictive policies regarding foreign investment – policies that we have long encouraged those nations to change.

Theoretically, economic security is a concept that can be used as a rationale to prevent any and all foreign investment. It has been used many times to justify blocking U.S. based firms’ investments in other countries where the competitiveness of a domestic industry is linked to “economic security.”

Expanding the scope of CFIUS reviews will significantly overload the CFIUS review process with transactions that have nothing to do with true national security. If CFIUS members have to examine the extent to which a European consumer food products company’s acquisition of a major U.S. ice cream maker impacts the “economic security” of the U.S. dairy industry, then they have less time and resource to focus on true national security related transactions. We should not take CFIUS’s focus off national security.

Also, one of OFII’s major concerns in the past has been the extent to which a domestic competitor, who loses out in mergers and acquisitions competition, can use the CFIUS process to lobby to block the deal and achieve in the legislative process what they couldn’t achieve in the marketplace. I do not perceive that to be the case in this most recent transaction, but we have seen it in plenty of other cases. If economic security were an aspect of CFIUS review, domestic firms will try to use the process to block new entrants to the market, to the detriment of U.S. consumers and our economy generally.

And finally, one of the key benefits of the current law is that it is flexible. If an agency within CFIUS is concerned about a transaction, CFIUS can initiate a request for a review. Adding economic security to the scope of CFIUS will significantly distract from the core national security function.

Moving the Chair of CFIUS from Treasury: Some have suggested that the Chair of CFIUS should be moved from Treasury to another agency such as the Departments of

Defense or Commerce. This issue is a diversion. In a “first among equals” Committee structure, the chair does not enjoy extraordinary power. At the end of the day, each member has one vote. All of the agencies that participate in CFIUS are experienced in the interagency process and are generally adept at representing their perspective. If DOD, DHS or Commerce opposes a transaction, I doubt very seriously that they are cowed by an opposing view from Treasury.

National Security and Capital Ownership

As the Committee considers this important topic, I wanted to offer a more general observation about the relationship between national security and economic activity.

When it comes to national security concerns arising from commercial operations of critical infrastructure, why should the nationality of the owners of the capital stock be the principal or sole concern? Certainly, there may be instances of foreign ownership that do raise special concerns as in the case of government ownership of the acquirer -- a situation where CFIUS already pays special attention. But the national security risks arising from certain activities -- such as infrastructure operations -- are present whoever owns the capital stock and should be addressed on their merits, not only in the context of an acquisition. If we agree that there are vulnerabilities in a particular area, the solution is to address the risk comprehensively and not take the view that the risk lies only with ownership.

U.S. ownership of such facilities does not mean the risks have been mitigated. A disproportionate focus on nationality may in fact distract from accomplishing the real national security objectives. U.S. ownership is not an inoculation from bad actors or bad events.

On the other hand, just because a firm is headquartered abroad doesn't mean it shouldn't be a partner in national security. OFII encountered an odd example in the period after September 11th. The FBI started a program with the business community to create a task force on critical infrastructure. The idea was to compile a list of key personnel at business sites that could be terrorist targets and create a network to share developments in

the event of suspicious activity. While a useful idea, the task force had one major shortcoming: the FBI excluded the U.S. operations of foreign-owned companies from the task force, apparently deeming them less trustworthy than U.S. companies. Yet one of America's largest petroleum refineries is a California facility owned by a European-based firm – a plant that employs hundreds and serves the entire nation. A security risk at one of these facilities is certainly as important to American safety as any other U.S. business. This glaring omission has since been rectified but it is an example of how linear, “us vs. them” thinking can yield results that are not in our national interest.

While the Committee is focused on this area, it is constructive to step back and consider some of our fundamental assumptions about national security, and how best to address the risks in commercial activities. It may be time to modernize our perspective in today's global economy and with today's cunning enemy, to come up with approaches that turn less on nationality and more on comprehensive risk assessment.

Conclusion

The enormous public focus that the DP World transaction has brought to this area will have both positive and negative effects. We welcome the focus on the CFIUS review process and the role that foreign investment plays in the U.S. economy. We believe that if both are better understood, they will be more appreciated.

Madam Chairman, thank you again for calling this hearing. We look forward to working with you, your colleagues and the Administration to enhance America's national security because a more secure nation is one that will attract investment, encourage capital accumulation, and realize long-term economic growth.