NOTES

From Fretting Takeovers to Vetting CFIUS: Finding a Balance in U.S. Policy Regarding Foreign Acquisitions of Domestic Assets

ABSTRACT

Merger law in the United States has historically relied on a system of private ordering with as little intervention from the federal government as possible. This scheme lies in stark contrast to the merger law of many other developed nations and, as such, has become a trademark of U.S. corporate law. Recent events, however, have brought into question the system's desirability in cross-border transactions where foreign entities are investing in U.S. assets. Proponents of reform argue that the federal government should become more involved in the approval process for these transactions given increased concerns of national security, while opponents argue that welcoming foreign investment is a hallmark of U.S. foreign policy not to be changed. This Note suggests a reform addressing both of these concerns in the hope that, when the next such transaction is called into question by U.S. politicians, the concerned parties will have a well-established legal doctrine to guide them.

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I. INTRODUCTION

On April 4, 2005, California-based oil and natural gas powerhouse Chevron Corporation (Chevron) announced its intention to acquire another California-based industry leader, Unocal Corporation (Unocal).[1] The deal obtained antitrust approval from the U.S. Federal Trade Commission, and negotiations were proceeding according to schedule until June 23, 2005, when China National Offshore Oil Corp. (CNOOC) announced an unsolicited $18.5 billion bid for Unocal, topping Chevron's bid by $2 billion.[2] At the time of the bid, China was experiencing an increased need for a secure energy supply as a result of its growing economy.[3] Moreover, as a result of China's trade surplus with the United States, foreign investment seemed to make good economic sense as a way for the Chinese to satiate this heightened need for energy supplies.[4]

1. Dick K. Nanto et al., *China and the CNOOC Bid for Unocal: Issues for Congress* (Feb. 2006), at CRS-1, *available at* https://www.hsdl.org/homesec/docs/crs/nps21-060806-12.pdf#search=%22china%20and%20the%20cnooc% 20bid%20%22.
2. *Id.*
3. *See id.* at CRS-3 to -6.
4. *See* Stan Crock, *Keeping America Safe – From Foreign Buyouts*, BUS. WK., Oct. 24, 2005, at 53.

Within hours of the announcement of the bid, however, concerned rumblings could be heard in Congress regarding national security issues arising from the possibility of a foreign company taking control of a U.S. company in the already tight energy market.[5] This apprehension was exacerbated by the fact that the CNOOC Ltd. entity was a subsidiary of a large, state-owned Chinese petroleum company, thereby adding fuel to the political fire.[6] The opposition in Congress took the form of several bills and resolutions that were introduced over the course of the summer.[7] The first such Congressional missive came in the form of a House Resolution, drafted by Representative Richard Pombo of California, voicing the concerns that had been discussed in Congress and calling for President Bush to conduct a thorough review of the proposed acquisition—if indeed Unocal and CNOOC were to enter into an agreement.[8] On the same day, June 30, 2005, the House also passed an amendment to an appropriations bill, which prohibited the use of Treasury funds for the purpose of gaining approval for the proposed transaction.[9]

In an effort to make assurances to stockholders and to quell the minor political uproar that followed CNOOC's bid, the directors of the Chinese company subsequently volunteered to undergo review by the Committee on Foreign Investments in the United States (CFIUS). CFIUS is a multi-agency panel comprised of twelve members, including representatives from the Department of Homeland Security and the Commerce Department, which assesses a deal's viability in terms of national security before making a recommendation to the President.[10] CNOOC's June 27, 2005 letter to the U.S. Congress aimed to "stress the key commitments that are an integral part" of the "friendly and open offer for Unocal."[11] After establishing CNOOC's willingness to participate in a CFIUS review, the letter went on to assure Congress that "substantially all of the oil and gas produced by Unocal in the U.S. will continue to be sold in the U.S. should a merger occur" and reiterated CNOOC's commitment to "retain[ing] the jobs of substantially all of Unocal's employees, including those in the U.S."[12] Because the foundation of political

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5. *See* Nanto, *supra* note 1, at CRS-1, -3, -14 to -15.
6. *Id.* at CRS-1.
7. *Id.* at CRS-14 to -16.
8. H.R. Res. 344, 109th Cong. (2005) (enacted); Nanto, *supra* note 1, at CRS-15.
9. 151 CONG. REC. 90, 5515–16, 5537–38 (2005) (amending H.R. Res. 3058, 109th Cong. (2005) by way of floor amendment).
10. Nelson D. Schwartz, *Why China Scares Big Oil*, FORTUNE, July 25, 2005, at 89, 89–93.
11. Letter from CNOOC to the U.S. Congress (June 27, 2005), *available at* http://www.ft.com/home/us [hereinafter *CNOOC Letter*].
12. *Id.*

opposition to mergers is generally the risk of job loss, this move was aimed directly at alleviating the fears pervading the U.S. political scene.[13]

In the meantime, Chevron sweetened its offer to $17 billion on July 20, 2005.[14] Political pressure and regulatory risk continued to mount regarding CNOOC's offer, despite the company's assurances in the June 27 letter to Congress that indicated CNOOC's readiness to undergo CFIUS review.[15] At this juncture, CNOOC chief executive Fu Chengyu began to publicly consider a pledge to sell the entirety of Unocal's U.S. assets to assuage the political concern.[16] This proposed restructuring of the transaction would appear to please both sides—CNOOC was primarily interested in Unocal's "extensive Asian assets," and Congressional concern centered on the control of Unocal's U.S. assets.[17]

Days later, however, the CNOOC board determined that the regulatory risk surrounding the proposed transaction had reached insurmountable levels, and citing "unprecedented political oppression," the CNOOC board withdrew its offer for Unocal.[18] CNOOC's August 2, 2005 press release went on to assert that the events of the summer were "regrettable and unjustified" and had "created a level of uncertainty that presents an unacceptable risk" to CNOOC's ability to secure the transaction.[19] Further, the CNOOC board acknowledged its efforts (volunteering to undergo CFIUS review, pondering the immediate sale of all of Unocal's U.S. assets, etc.) to make the deal work in the face of adversity: "CNOOC has given active consideration to further improving the terms of its offer, and would have done so but for the political environment in the U.S."[20] Perhaps most significantly, CNOOC felt that it was no longer in the "fundamental best interests" of its shareholders to continue to pursue the bid.[21]

On August 10, 2005, the Unocal shareholders voted to accept Chevron's bid, and the transaction has since proceeded relatively uneventfully.[22] In the aftermath, the "losers" appear to be Unocal shareholders, who perhaps lost the opportunity for a more lucrative

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13. *See* Antony Page, Editorial, *Trust the Market in the Sale of Unocal*, BALTIMORE SUN, June 27, 2005, at 13A.
14. Nanto, *supra* note 1, at CRS-1.
15. Stephanie Kirchgaessner et al., *CNOOC in Unocal Sale Pledge*, FIN. TIMES (London), July 27, 2005, at 15.
16. *Id.*
17. *Id.*
18. Press Release, CNOOC, Ltd., CNOOC Limited to Withdraw Unocal Bid (Aug. 2, 2005) (on file with author).
19. *Id.*
20. *Id.*
21. *Id.*
22. Nanto, *supra* note 1, at CRS-1.

transaction, and CNOOC, which lost the opportunity to obtain valuable assets that it was financially capable of procuring. The "winner" appears to have been Chevron, which, although it had to sweeten its original offer slightly in response to CNOOC's offer, nonetheless came away from the acquisition without having to match or exceed the CNOOC offer. Since these events unfolded in the summer of 2005, CNOOC itself has shown signs that it has recovered from any ill effects the failed transaction may have caused. In fact, on January 10, 2006, CNOOC announced a $2.27 billion purchase of a 45% stake in a Nigerian offshore oil and gas field, the company's largest acquisition to date.[23] Further, this is the company's first acquisition outside of Asia, indicating its unyielding desire to expand, regardless of whether or not U.S. merger law allows it to do so on U.S. soil.[24] This relentless movement to expand abroad has been termed by the Chinese as their "go out strategy," and as CNOOC's determination to grow abroad demonstrates, this policy is unquestionably established and quickly becoming a reality of Chinese diplomacy.[25]

Though this scenario—a foreign company seeking to gain assets in a U.S. entity—is hardly a new one, the failed Unocal/CNOOC transaction is eyebrow-raising for a variety of reasons. First, the stakes of the transaction were certainly high, with Unocal finally being sold to Chevron for over $17 billion.[26] Moreover, the fact that the transaction was in an increasingly crucial sector of the market is undoubtedly noteworthy. The impact of this failed transaction on U.S-Sino relations is yet to be seen, but as China's economic prowess continues to grow, it is clear that diplomacy in this regard has benefits.[27] In fact, there appear to be many players potentially interested in U.S. energy properties, as both state-owned and privately owned companies in Russia, France, Venezuela, and Saudi Arabia have all been purchasers of U.S. energy interests in recent years.[28] Also, China-based Lenovo Group Ltd. acquired IBM's PC division in early 2005, and China's largest home-appliance maker, Haier Group Co., was in the midst of a bidding war for U.S.-based

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23. Kate Linebaugh & Shai Oster, *CNOOC Pays $2.27 Billion for Nigerian Oil, Gas Stake*, WALL ST. J. (H.K.), Jan. 10, 2006, at 1.

24. *See id.*

25. *See* Peter S. Goodman & Ben White, *Haier Withdraws Maytag Bid: Move is a Sign of Caution in China's Pursuit of Foreign Films*, WASH. POST, July 20, 2005, at D02.

26. *See Chinese Company Drops Bid to Buy U.S. Oil Concern*, N.Y. TIMES ABSTRACTS, Aug. 3, 2005, 2005 WLNR 12231596, at A1.

27. *See* James A. Dorn, *U.S.-China Relations After CNOOC*, 55 FREEMAN 10, Dec. 2005, at 30, 30–32.

28. Page, *supra* note 13, at 13A.

Maytag Corp. until it dropped out during the summer of 2005.[29] Even more recently, Congressman Ralph Hall, a Republican from New York, expressed concern in Congress over the proposed sale of U.S.-based Westinghouse Electric Company, whose potential buyers included a Japanese company.[30] Though the level of Congressional opposition thus far has paled in comparison to that incited by the Unocal/CNOOC proposed transaction, the nuclear energy sector raises many of the same national security concerns that would result in calls for a revamping of the merger process in the United States.[31]

Most recently, in a news item that has dominated the headlines, perhaps even more so than the CNOOC affair, the Bush administration—somewhat surprisingly given its attitude towards the CNOOC/Unocal proposed transaction—approved a business deal involving the sale of six major U.S. ports to Dubai Ports World, a company substantially owned by the United Arab Emirates.[32] After CFIUS found no reason not to go forward with the proposed transaction and President Bush approved it, the U.S. Congress expressed serious concerns regarding the transaction, primarily for reasons of national security.[33] In fact, the shareholders of Peninsular and Oriental Steam Navigation Company (P&O), the UK-based holding company currently in possession of the ports in question, went so far as to vote on and approve the transaction.[34] To the extent that the uproar over CFIUS reform had subsided since it was on the forefront of Congress's agenda last summer, this deal has promptly and forcefully thrown the issue of CFIUS reform back on the table.[35] Furthermore, as this situation unfolds, perhaps its most noteworthy aspects are the fundamental disagreement between the executive and legislative branches of the U.S. government and the legislative branch's vulnerability in the currently existing CFIUS review process.[36] Again, there are tensions between the U.S. need for foreign investment, given a trade deficit that amounted to hundreds of billions of dollars last year, and the need for increased national security, with particular attention paid to emerging markets such as

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29. Pavel Molchanov, *U.S. Revives Japan Inc. Fears Over China's Buying Spree: Americans Are Uncomfortable About Just How Powerful China is Becoming*, NAT'L BUS. REV., Aug. 12, 2005, *available at* 2005 WLNR 13373895.

30. Carola Hoyos & Stephanie Kirchgaessner, *Concern Over Likely Sale of Westinghouse Nuclear Power*, FIN. TIMES (London), Dec. 13, 2005, at 22.

31. *Id.*

32. Greg Hitt, *Lawmakers Push for New Review Of Port Deal Amid Security Fears*, WALL ST. J., Feb. 17, 2006, at A4.

33. Dennis K. Berman et al., *Bush, Congress Head For Clash Over Ports Deal*, WALL ST. J., Feb. 22, 2006, at A1.

34. Andreas Paleit, *How the DP World Deal Unraveled*, FIN. TIMES (London), Mar. 11, 2006, at 8.

35. *Id.*

36. *Id.*

the United Arab Emirates.[37] This scenario stands as further proof that CNOOC was certainly not the last foreign corporation to seek U.S. assets in an economically and politically crucial industry sector.[38]

In a development similar to what occurred in the CNOOC/Unocal transaction just a few months prior, on March 9, 2006, Dubai Ports World bowed to "extreme public and political pressure" and gave up its management stake in the U.S. seaports.[39] Thus, the management of Dubai Ports World made a decision like that made by CNOOC management that the backlash that had arisen was too strong to overcome.[40] This situation gave renewed relevance to the CFIUS question and resulted in numerous pledges to reform the takeover review process in the United States.[41]

It is clear that this is an issue that will not subside, but rather will swell in the coming years, as the effects of globalization continue to spread and cause an increasing number of economies around the world to seek overseas expansion in a variety of vital industry sectors.[42] Regarding China in particular, the comments of William Reinsch, president of the National Foreign Trade Council and a member of the congressionally appointed China Economic Security and Review Commission, will likely prove prescient: "China is piling up dollars, it's only a matter of time before they start going into the acquisition of U.S. companies. People shouldn't be surprised."[43]

This Note ultimately aims to suggest a solution for like scenarios, which will inevitably arise in the near economic future, given that heavy-growth economies, such as those in China, India, and the United Arab Emirates, will have both the resources and the need to expand beyond their borders. Accordingly, Part II of this Note examines the process of completing a merger pursuant to the current body of U.S. corporate law and compares this statutory framework to that which presently exists in several foreign jurisdictions. Part III examines the role of CFIUS and the recent movement to expand the scope of this agency, thereby proposing

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37. Michael M. Phillips et al., *Port Debate Exposes Conflicts Between Security Needs And Foreign Investment*, WALL ST. J., Feb. 23, 2006, at A1.

38. *Id.*

39. Gwyneth K. Shaw & Julie Hirschfeld Davis, *Dubai Firm to Shed Stake in U.S. Ports*, BALTIMORE. Sun, Mar. 10, 2006, at 1A.

40. *Id.*

41. Edward Alden & Stephanie Kirchgaessner, *The Americas: Pledge to Reform Takeover Vetting*, FIN. TIMES (London), Mar. 10, 2006, at 8.

42. *See* Harry L. Clark & Sanchitha Jayaram, *Intensified Trade and Security Policies Can Present Challenges for Corporate Transactions*, 38 CORNELL INT'L L.J. 391, 391–95 (2005) (presenting a fairly exhaustive listing of cross-border transactions involving U.S. targets which have been subject to enhanced scrutiny in recent years).

43. Martin Vaughan, *Observers Brace For Foreign Acquisitions of Key Firms*, CONGRESS DAILY, Feb. 10, 2006, *available at* 2006 WLNR 2417020.

dramatic changes to the U.S. merger statutory framework described in Part II. Lastly, Part IV offers a solution to this scenario, with the hope that its implementation will allow for a smoother, less controversial process when the next foreign entity attempts to acquire a U.S. conglomerate.

II. COMPARATIVE LOOK AT THE STATUTORY FRAMEWORK FOR MERGERS AND ACQUISITIONS TRANSACTIONS IN THE UNITED STATES AND ABROAD

A. *Statutory Framework of Delaware General Corporate Law Concerning Mergers*

Corporate law in the United States is based primarily on state law regimes, with Delaware leading the way; more than half of the largest corporations in the United States, including Unocal Corporation, are incorporated in Delaware.[44] Since other states have generally followed Delaware's lead on many fundamentals of corporate law, including merger law, it is sensible to examine the relevant Delaware statutory language as a means of extrapolating the overriding norms of U.S. merger law.[45] Of course, this statutory structure only applies to entities incorporated under the laws of Delaware, which may not be the case in cross-border transactions. However, using the Delaware statute as a base nonetheless is insightful because it reflects the fundamental principles of U.S. merger law.

Delaware General Corporate Law § 251 sets forth the requirements for corporations incorporated in Delaware to enact a merger.[46] The statute first requires that the corporations adopt "an agreement of merger or consolidation."[47] Section 251(b) sets forth the various provisions that must appear in this merger agreement and further specifies that it is the directors of the involved corporations who are responsible for approving the agreement and "declaring its advisability."[48] The statute also requires that any agreement adopted pursuant to § 251(b) be submitted to the "stockholders of each constituent corporation at an annual or special meeting for the purpose of acting on the agreement."[49] The remainder of this

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44. CHARLES R.T. O'KELLEY & ROBERT B. THOMPSON, CORPORATIONS AND OTHER BUSINESS ASSOCIATIONS 141 (2003); Troy A. Paredes, *A Systems Approach to Corporate Governance Reform: Why Importing U.S. Corporate Law Isn't the Answer*, 45 WM. & MARY L. REV. 1055, 1097 (2004).

45. *See* O'KELLEY & THOMPSON, *supra* note 44, at 141.

46. DEL. CODE ANN. tit. 8, § 251 (2005).

47. *Id.* § 251(b).

48. *Id.*

49. *Id.* § 251(c).

provision delineates certain exceptions to the stockholder vote requirement, including the *de minimis* change exception and the short-form merger exception, but does not impose any additional requirements on the parties seeking to effect a merger.[50]

Notably absent from the basic statutory corporate law governing mergers in Delaware is any requirement of government approval of a particular merger agreement. Indeed, in the cross-border merger context, there is a "general absence of government regulation of foreign investment . . . and exchange controls in the United States."[51] By simply adhering to the requirements of § 251, the parties can complete a merger without government involvement, while fulfilling all requirements of state corporate law.[52] Unlike the regimes in place in many other nations, the United States "exercises few controls over foreign exchange transactions by U.S. citizens or foreign exchange transactions," as "no approval of the Treasury Department or other finance authorities is required to make an investment."[53] In fact, foreign exchange transactions of substantial size are monitored by the U.S. government only for informational purposes.[54]

There are, however, several instances in which the federal government does become involved in the merger process in the United States. The most significant occasion for government involvement in the merger process arises in the antitrust arena.[55] Title II of the Hart-Scott-Rodino Antitrust Improvements Act delineates the premerger notification process that is necessary under federal law to effect a merger.[56] Likewise, federal law becomes involved when the state statutory structure is combined with the mandatory disclosure regime of federal securities laws, a combination which reflects the "market-based corporate governance system of the United States."[57] Both of these instances in which federal law—and hence the federal government—becomes involved in the merger process, however, exist outside of the corporate law with which this Note is concerned. The last (and at present, least significant) instance in which federal law becomes intertwined with state corporate law arises in the context of cross-border transactions and is described in further detail in subsequent parts of this Note.

In U.S. corporate law there exists an inherent trust of private ordering, which in turn leads to a trust of the markets at large to

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50. *Id.* § 251(d)–(g).

51. DAVID J. BENDANIEL & ARTHUR H. ROSENBLOOM, THE HANDBOOK OF INTERNATIONAL MERGERS & ACQUISITIONS 26 (1990).

52. DEL. CODE ANN. tit. 8, § 251 (2005).

53. BENDANIEL & ROSENBLOOM, *supra* note 51, at 27.

54. *Id.*

55. 54 AM. JR. 2D *Monopolies and Restraints of Trade* § 310 (2005).

56. *Id.*

57. Paredes, *supra* note 44, at 1097.

ensure equitable transactions in this area of the law.[58] Moreover, private ordering increases efficiency, in that corporate mergers are often time-sensitive and government involvement would inevitably cause delay.[59] It is sensible that these efficiency-diminishing governmental constraints would not exist, considering that Delaware courts "frequently note that mergers . . . are 'encouraged and favored.'"[60] There appears to be a general consensus that private ordering is more efficient than government regulation. This provides a compelling reason to preserve at least a vestige of this trademark of U.S. corporate law which, as is demonstrated in the following section, is not necessarily a feature of many foreign corporate governance systems.[61]

B. *Statutory Framework of Foreign Law Concerning Mergers*

In comparing foreign statutory frameworks to the Delaware formulation generally followed in the United States, the presence of a government entity responsible for enforcing all aspects of takeover law is the most readily visible difference.[62] Though the United States has such entities in the securities and antitrust areas (the Securities and Exchange Commission and the Federal Trade Commission, respectively) there is no entity charged with enforcing other mergers in the United States.[63]

The United Kingdom has established a Panel on Takeovers and Mergers, which acts pursuant to the City Code on Takeovers and Mergers.[64] "Public companies adhere to the Code and the rulings by the Panel are respected."[65] Germany and Austria, other EU economic powers, have developed a similar system of takeover regulation, whereby entities exist both in and out of the government to ensure that companies are complying with statutory laws and more significantly, that those companies meet investment approval standards.[66] Likewise, in France, the acquisition of more than 20% of a particular company requires prior authorization from the Treasury

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58. *See* O'KELLEY & THOMPSON, *supra* note 44, at 146.

59. Mark E. Van Der Weide, *Against Fiduciary Duties to Corporate Stakeholders*, 21 DEL. J. CORP. L. 27, 75–76 (1996).

60. 2 RODMAN WARD JR. ET AL, FOLD ON THE DELAWARE GENERAL CORPORATION LAW 39 (4th ed.2001).

61. Michael P. Vandenbergh, *The Private Life of Public Law*, 105 COLUM. L. REV. 2029, 2079 (2005).

62. CHRISTIN M. FORSTINGER, TAKEOVER LAW IN THE EU AND THE USA: A COMPARATIVE ANALYSIS 118–37 (2002).

63. *Id.*

64. *Id.* at 118.

65. *Id.*

66. *Id.* at 124, 132.

Department of the French Ministry of Economy and Finance.[67] Similarly, China's takeover law, though still in an early stage of development, appears to be moving in the same direction, with a great deal of involvement on the part of the state.[68] However, it is worth noting that because China's law and policy on this issue are still in a somewhat formative stage, there is a well-placed concern that U.S. policy could "prevent China from following the free-market way."[69]

With an eye towards foreign investment in domestic companies, where no mandatory process is in place in the Delaware General Corporation Law or the U.S. law in general, "many countries restrict foreign ownership of commercial ventures."[70] This list includes India and numerous countries throughout Latin America, the Middle East, and Asia.[71] This type of protectionism, which is apparently prevalent in many other foreign statutory constructions, is non-existent in the United States at the present.

In Japan, though foreign takeovers and mergers are relatively rare, a nonresident tender offeror must file its offer with the securities company or bank it has appointed to manage the transaction.[72] Moreover, the Foreign Investment and Trade Control Law (FITCL) requires notice to be given to the Minister of Finance when a foreign corporation is attempting to transact with a Japanese corporation.[73] At this point, the Minister of Finance may require a license for the transaction "if the transaction might disturb the equilibrium of Japan's balance of international payments; might result in a drastic fluctuation of Japanese foreign exchange rates; or might result in transfers of funds between Japan and foreign countries in a large volume, thereby adversely affecting the Japanese money or capital market."[74] Further, the Minister may refer the matter to the Committee on Foreign Exchange and Other Transactions for recommendations on various matters, including whether the transaction "could imperil the national security of Japan."[75] Thus, there is a decided concern for the protection of Japanese assets evident in Japanese merger law. Although this has relaxed in recent years given the effects of globalization, it is

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67. BENDANIEL & ROSENBLOOM, *supra* note 51, at 64.
68. Hui Huang, *China's Takeover Law: A Comparative Analysis and Proposals for Reform*, 30 DEL. J. CORP. L. 145, 147–57 (2005).
69. Page, *supra* note 13, at 13A.
70. BENDANIEL & ROSENBLOOM, *supra* note 51, at 65.
71. *Id.*
72. H. LEIGH FRENCH, INTERNATIONAL LAW OF TAKE-OVERS AND MERGERS 16 (1986).
73. *Id.* at 17.
74. *Id.*
75. *Id.*

nonetheless rare for parties entering a merger to be able to "contract freely, without government influence or guidance."[76]

Similarly, the Reserve Bank of India, which also falls under the Ministry of Finance, is the central administrative agency charged with regulating foreign investment in India.[77] The Industrial Policy Statement of 1977 lays out the terms under which foreign investment and acquisition of technology are allowed, stating that such transactions will only be permitted when they are deemed to be "in the national interest."[78] The document goes on to state that "majority interest in the ownership of companies, and effective control of companies, should be in the hands of Indian nations."[79] In addition, the Foreign Exchange Regulation Act regulates foreign financial participation in Indian business, stating that all proposals must be cleared by the Foreign Investment Board of the Indian government and delineating an elaborate process for approval of a merger proposal.[80] The regulatory infrastructure in place, even in a developing economy like India's, is far more elaborate and demanding than that which is found in U.S. corporate law.

It is evident that there are more, and better developed, statutory restrictions on foreign investment in place in foreign jurisdictions than in the United States. Indeed, economists, politicians, and lawyers would likely agree that the open investment policy of the United States has been one of the hallmarks of U.S. diplomatic posturing throughout its history. The ability of this open investment policy to coexist with a new infrastructure for vetting foreign investment in the United States. is uncertain—both in terms of its feasibility and its desirability. As the following section of this Note will demonstrate, however, there is, in fact, a mechanism within the mire known as "alphabet soup" in Washington, D.C., that at least ostensibly was designed to perform a function similar to that of the various panels and agencies existing in the European and Asian countries described above: the Committee for Foreign Investment in the United States (CFIUS).[81] Its power and role in cross-border transactions involving U.S. entities has, however, been almost negligible up to this point.[82] Whether this will continue to hold true given new found national security concerns in the United States is a

76. *Id.* at 18.
77. *Id.* at 223.
78. *Id.*
79. *Id.*
80. *Id.* at 224.
81. *See* James Rosen, *The Little Agency that Created a Great Big Stink*, CAPITOL HILL BLUE, Feb. 24, 2006, http://www.capitolhillblue.com/content/2006/02/the_little_agency_that _created.html.
82. *Id.*

question that will be answered only in the context of future situations that mirror the proposed Unocal/CNOOC transaction.

III. CFIUS EXPANSION AND IMPLICATIONS FOR DIRECTORS AND SHAREHOLDERS OF U.S. CORPORATIONS

A. *What is CFIUS? A Brief History and Examination of the Mechanics Behind the CFIUS Review Process*

The naissance of CFIUS came with Former President Ford's passing of Executive Order 11858 in 1975.[83] President Ford created CFIUS and charged it with "continuing responsibility within the Executive Branch for monitoring the impact of foreign investment in the United States, both direct and portfolio, and for coordinating the implementation of United States policy in such investment."[84] The original motivation for this Executive Order and the ensuing birth of CFIUS was likely the establishment of the Organization of Petroleum Exporting Countries (OPEC), which left several oil-producing nations with surplus cash that they could potentially use to purchase U.S. assets.[85]

Allowing such acquisitions to go forward without government monitoring has raised concerns within the Executive Branch of the U.S. government in the past. One of the most prominent such instances, mentioned by U.S.-China Economic and Security Review Commission (USCC) member Patrick Mulloy in his congressional testimony regarding CFIUS, was the post-OPEC proposed transaction between Kuwait Petroleum Company and Santa Fe International Company, a U.S. entity.[86] The Executive Branch objected to the transaction, but was essentially helpless to do anything about it because of the liberal U.S. statutory framework regarding merger activity.[87] The transaction had to be stalled on antitrust grounds, the only way in which the government could reasonably get involved, until a merger agreement more suitable to the Executive Branch was reached.[88]

This helplessness of the Executive Branch in the face of an undesirable merger was brought to an end with the passage of the

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83. *Foreign Investment on U.S.: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs* (Oct. 20, 2005) (statement of Patrick A. Mulloy, Member, U.S.-China Economic and Security Review Commision), *available at* 2005 WLNR 16994551.

84. *Id.*

85. *Id.*

86. *Id.*

87. *Id.*

88. *Id.*

Exon-Florio Amendments in 1988.[89] This legislation empowered the President to "investigate and, if necessary, block foreign takeovers of American businesses on national security grounds."[90] Though the Exon-Florio Amendments acknowledge the open investment policy of the United States, they nonetheless authorize the President to "suspend or prohibit foreign acquisitions, mergers, or takeovers of U.S. companies if a foreign controlling interest might take action that threatens national security."[91]

In 1975, the President delegated the investigative authority he was given via the Exon-Florio Amendments to CFIUS.[92]

> Exon-Florio establishes a four-step process for examining a foreign acquisition of a U.S. company: (1) *voluntary* notice by the companies, (2) a 30-day review to identify whether there are any *national security* concerns, (3) a 45-day investigation to determine whether those concerns require a recommendation to the President for possible action, and (4) a Presidential decision to permit, suspend, or prohibit the acquisition.[93]

Because notification is completely voluntary, parties who are certain that their transaction does not implicate national security issues can elect not to notify CFIUS, but with full understanding that a failure to do so leaves their transaction "subject to Presidential action indefinitely."[94]

In terms of precisely what CFIUS is supposed to address in its inquiry, the statute provides some guidance, but seems to allow for differing interpretations:

> For the purposes of this section, the President or the President's designee may, taking into account the requirements of national security, consider among other factors –
>
> (1) domestic production needed for *projected national defense requirements*,
>
> (2) the capability and capacity of domestic industries to meet *national defense requirements*, including the availability of human resources, products, technology, materials, and other supplies or services,

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89. Anthony Michael Sabino, *Transactions That Imperil National Security: A Look at the Government's Power to Say "No",* 77 N.Y. ST. B.J. 20 (2005).

90. *Id.*

91. U.S. GOV'T ACCOUNTABILITY OFFICE, ENHANCEMENTS TO THE IMPLEMENTATION OF EXON-FLORIO COULD STRENGTHEN THE LAW'S EFFECTIVENESS 1 (Sept. 2005) [hereinafter GAO REPORT].

92. *Id.*

93. *Id.* at 2 (emphasis added).

94. DEPARTMENT OF THE TREASURY, DEPUTY SECRETARY ROBERT M. KIMMITT TESTIMONY BEFORE THE UNITED STATES SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS (Oct. 20, 2005), *available at* 2005 WL 2673050 [hereinafter KIMMITT TESTIMONY].

> (3) the control of domestic industries and commercial activity by foreign citizens as it affects the capability and capacity of the United States *to meet the requirements of national security* . . .
>
> (5) the potential effects of the proposed or pending transaction on United States international technological leadership in areas *affecting United States national security*.[95]

The third clause of this provision seems to be especially susceptible to multiple interpretations.[96] In any case, with or without concrete guidelines, CFIUS is to complete its inquiry and deliver a report to the President upon completion of its investigation, which begins the next step in the process, Presidential review.[97]

The President is given fifteen days in which to conduct his review and decide whether it is necessary to prohibit the transaction or appropriate to allow the transaction to go forward.[98] If the President finds that "(1) there is credible evidence . . . to believe that a foreign controlling interest might take action that threatens to impair national security and (2) laws other than Exon-Florio and the International Emergency Economic Powers Act are inadequate or inappropriate to protect national security," a Presidential prohibition may be appropriate.[99] The President's authority to prohibit a transaction cannot be exercised, however, if "(1) the Committee has informed the companies in writing that their acquisition was not subject to Exon-Florio or had previously decided to forego investigation, or (2) the President has previously decided not to act on that specific acquisition under Exon-Florio."[100] The President has prohibited only one transaction from going forward, when Former President George H.W. Bush determined that a Chinese aerospace company should not be allowed to invest and gain part ownership in a U.S. aircraft parts manufacturer in 1990.[101] Thus, this provision for Presidential review has been, like much of CFIUS, more of a formality than an actual bar to cross-border transactions.

It is worth noting that the Exon-Florio Amendments do not explicitly define "national security," thereby evincing perhaps one of the most problematic features of the legislation, which will be dealt with later in this Note.[102] The only guidelines provided indicate that

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95. 50 U.S.C.S. app § 2170(d) (LexisNexis 2005) (emphasis added).

96. *See* Sabino, *supra* note 89, at 22 (citing H.R. Rep. No. 100-576 at 926 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 1547, 1959 (stating that legislative history declares "[t]he term 'national security' is intended to be interpreted broadly without limitation to particular industries")).

97. *Id.*

98. GAO REPORT, *supra* note 91, at 9.

99. *Id.* at 9–10.

100. *Id.* at 10.

101. *Id.*

102. Eric Simonson, *Specialized Areas of Concern in Acquisition Transactions*, *in* A GUIDE TO MERGERS & ACQUISITIONS 243, 262 (2006).

"companies providing technology to the military or to the defense industrial base may implicate national security concerns" and that "acquisitions of businesses in industries having 'no special relation to national security' would not ordinarily give rise to national security concerns."[103] The regulations go on to cite various examples of items that would not give rise to national security concerns (i.e., toys, games, hotels, food products, legal services, etc.) and also to state that certain transactions, including "purchases solely for purposes of investment by investors acting in the ordinary course of business and amounting to 10% or less of the stock of an entity," are exempted from CFIUS review.[104]

A few procedural aspects of the current CFIUS review process are also worth highlighting because of their relevance to the changes proposed in this Note. Section 721(a) of the Exon-Florio Amendments permits any transaction within the ambit of the Amendments to be subject to investigation that must commence within thirty days after notice of the transaction has been made.[105] This notice provision does not require that the parties provide notice of the transaction, and historically many parties have chosen not to do so. By failing to do so, however, the parties implicitly allow CFIUS to commence an investigation at any time.[106] Technically, CFIUS also has the power to begin an investigation and seek divestiture of a transaction after the acquisition has closed and to unilaterally decide to review a particular transaction after providing the parties with written notice.[107] Interestingly, "[c]ompetitors, shareholders and governmental agencies" have no authority to trigger CFIUS review, though they can contact CFIUS to raise questions or express concern about a transaction.[108] Although they have rarely come into play in the past, these procedural provisions do provide the basis for some significant opportunities for reform.

The Exon-Florio Amendments also state that if there are national security concerns—however that term may be construed—then the Chief Executive is required to make specific findings that "there is credible evidence . . . to believe that the foreign interest exercising control might take action that threatens to impair the national security," and that other legal avenues do not provide "adequate and appropriate authority for the President to protect the national security" with respect to the proposed transaction.[109] The statute also explicitly states that the President's findings are not

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103. *Id.*
104. *Id.*
105. *Id.* at 261.
106. *Id.*
107. *Id.*
108. *Id.*
109. 50 U.S.C.S. app § 2170 (LexisNexis 2005).

subject to judicial review, indicating the tremendous amount of deference given to the President in evaluating the results of the CFIUS investigation.[110] In short, the President "enjoys the power to completely prohibit a contemplated transaction."[111] That is not to say, however, that there are no checks on the President's power in this regard. The statute requires him to provide a written report of his determination, including a "detailed explanation" of his findings and the factors considered.[112]

Responding to concerns about the "lack of transparency" in the CFIUS review process, Congress passed the Byrd Amendment to the Exon-Florio Amendments in 1992.[113] This provision requires the President to deliver a report to Congress if the President makes any decision regarding a proposed foreign acquisition.[114] Further, it makes clear that an investigation is required in cases where "the acquirer is controlled by or acting on behalf of a foreign government; and the acquisition could result in control of a person engaged in interstate commerce in the U.S. that could affect the national security of the U.S."[115] Until the past year, this marks the only concerted attempt to reform the CFIUS process, and the Byrd Amendment did not address the most problematic aspects of the regulations in question.

Though the inner workings of CFIUS have remained out of the spotlight for nearly its entire existence, it has recently been thrust into the spotlight as efforts to expand its power have arisen in the wake of the failed Unocal/CNOOC transaction.[116] Part of the secrecy is intentional, of course, because the "highly sensitive nature of the national security issues with which the Committee grapples" demands a certain degree of secrecy.[117] But part of the secrecy is also simply a function of the fact that the CFIUS process has not been extensively used—at least not to the fullest of its potential—so there has not been sufficient opportunity or occasion to illuminate many of the subtleties of the legislation.[118] Regardless, the fog surrounding the CFIUS process will likely be lifted in the near future, given the determination with which some members of Congress are pushing for an enhancement in the wake of the Unocal/CNOOC and Dubai Ports World confusion. When that fog is lifted, it is likely that Washington policymakers on both sides of the matter will take issue with the

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110. § 2170(e).
111. Sabino, *supra* note 89, at 22.
112. § 2170(g).
113. GAO REPORT, *supra* note 91, at 10.
114. *Id.*
115. Pub. L. No. 102-484, 106 Stat. 2315, 2464 (1992).
116. Crock, *supra* note 4, at 53.
117. Sabino, *supra* note 89, at 24.
118. *Id.*

CFIUS process, and changes will inevitably be proposed—not only by those in favor of expanding the scope of CFIUS, but also by those simply hoping the agency will be in a position to make efficient and equitable decisions as it is used with increasing frequency in the future.[119]

Before addressing proposed changes to the CFIUS process and the reasons behind them, it should be stressed that there are positive aspects to the way in which the current CFIUS process operates.[120] The "highly sensitive" nature of these matters requires secrecy, and the CFIUS process addresses this concern by vesting a great deal of power in the Executive Branch of government.[121] This results in "minimized risk of disclosure" which is, in turn, of great value to parties engaging in these types of transactions.[122] Further, the Committee consists largely of Presidential appointees, and as such, its composition changes from administration to administration, as the "prevailing winds of politics, diplomacy, and policy, both foreign and domestic" change as well.[123] However, the CFIUS review process as it currently stands is also sufficiently protected from fleeting political movements because it intentionally lies out of the reach of Congress.[124]

B. *The Recent Movement for Expansion of the Scope of CFIUS Power*

If CFIUS is amended, the face of U.S. corporate law could undergo a dramatic transformation that would presumably come into play quite frequently given the increasing number of cross-border transactions involving U.S. corporations in recent years.[125] The "protectionist howls" heard in Washington following the narrowly-averted CFIUS review of CNOOC's proposal have been followed by proposals to revamp CFIUS, thereby altering the Delaware statutory structure, so that it is more powerful and better equipped to handle the next foreign player to make a bid for a domestic company in a vital sector.[126] This movement has been countered by a faction arguing that foreign trade provides an "immeasurable boost to U.S. economic prosperity."[127]

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119. *Id.*
120. *Id.*
121. *Id.*
122. *Id.*
123. *Id.*
124. Jonathan Weisman, *Legislation To Keep Ports Issue Boiling*, SEATTLE TIMES, Mar. 11, 2006, at A6.
125. Crock, *supra* note 4, at 53.
126. Editorial, *Unocal Won't Be the Last, So Set the Rules Now*, BUS. WK., July 11, 2005, at 96.
127. *Id.*

The members of Congress who spearheaded the movement to prevent the proposed Unocal/CNOOC transaction now argue that the process is nothing more than a "doormat operation" that is in need of expansion.[128] Indeed, out of the more than 1,500 transactions CFIUS has reviewed since its inception, it has only blocked one.[129] The process itself remains "excessively murky," and thus, the "extent to which changes are warranted . . . is unclear."[130] As previously stated in this Note, the only transaction ever prevented at the stage which CFIUS review reaches the Executive Branch occurred when President George H.W. Bush did not allow a Chinese aviation company (which was state-owned, much like CNOOC) from acquiring a domestic maker of parts used in Boeing aircraft.[131] However, in two of the largest cross-border transactions in recent history, British Petroleum's acquisition of Amoco and Daimler's purchase of Chrysler, both of which occurred in 1998, there was little opposition within the ranks of the U.S. government.[132] Whether the lack of opposition to these large-scale transactions was due to the industries in which they occurred or to the fact that the two foreign acquirers were headquartered in countries that are U.S. allies, or perhaps both, is unclear.[133] Nonetheless, this demonstrates the remarkable inconsistency that has plagued CFIUS and adds to the confusion concerning its present role.[134]

To shed some light on the rather secretive process, a Government Accountability Office (GAO) report was issued on September 28, 2005, at the request of concerned congressmen, which assessed the operation of CFIUS. The report suggested, among other things, an expansion of the window of time the agency is given to analyze deals raising national security concerns.[135] Further, the members of Congress who backed the GAO investigation are pushing for an expanded scope of review to cover national security issues that may not be readily apparent, such as in the Unocal/CNOOC situation.[136] The GAO report concluded that "increased insight and oversight could strengthen the law's effectiveness."[137] The report did, however, express some limits to its findings. For instance, it stated that

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128. Crock, *supra* note 4, at 53.

129. Page, *supra* note 13, at 13A.

130. *Role of the Committee on Foreign Investment in the United States: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, 109th Cong. (2005) (statement of Sen. Shelby).

131. Molchanov, *supra* note 29.

132. *Id.*

133. *Id.*

134. *Id.*

135. GAO REPORT, *supra* note 91, at 15.

136. *China Update*, INSIDE U.S. TRADE, Oct. 7, 2005, *available at* 2005 WLNR 16272492.

137. GAO REPORT, *supra* note 91, at i.

CFIUS should probably not initiate these investigations because that would result in discouragement of foreign investment, which it acknowledges as undesirable.[138]

The GAO report spurred a series of Congressional hearings in September and October of 2005 to discuss the alleged problems with CFIUS.[139] The legislative proposals to strengthen the Exon-Florio Amendments now under consideration include the following: providing Congress with veto power regarding CFIUS's clearance of a deal; broadening the definition of "national security" to include critical infrastructure, economic security, and energy needs; requiring CFIUS to report to Congress on each deal for which notification is provided; mandating more time for CFIUS review; ranking U.S. companies based on perceived importance to national security; and reassigning the Chair of CFIUS to a more "security-minded" department of the federal government infrastructure.[140]

Opponents of these changes would likely argue that they would increase the amount of time spent on a number of routine cases and detract from the controversial proposed transactions, such as Unocal-CNOOC.[141] Moreover, opponents of change to CFIUS contend that prolonging the review process would be economically harmful because it would delay transactions where time is of the essence.[142] Indeed, it seems clear that if these proposals to expand CFIUS were passed into law, the due diligence landscape for foreign acquisitions would change considerably, "adding regulatory delay and political risk and diminishing the accessibility of the United States to foreign direct investment."[143] Many express the sentiment that engaging Congress in CFIUS reviews will, in the words of U.S.-China Economic and Security Review Commission (USCC) member Stephen Bryen, "so confound the process that foreign investment in the United States will be chilled."[144] Underlying all of these concerns is the notion that "a strong economy is part of national security," and that "openness to global trade in goods, services and capital" has historically been a "key ingredient" in the success of U.S. capital markets.[145]

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138. *Id.* at 3.

139. Christopher Corr, *Pressures to Stiffen Exon-Florio: The Chinese Bid for Unocal Sparks a Firefight Over Inbound Deals*, MERGERS & ACQUISITIONS: THE DEAL MAKER'S J., Jan. 1, 2006, *available at* 2006 WLNR 105447.

140. *Id.*

141. *See* GAO REPORT, *supra* note 91, at 15.

142. Ron Orol, *Senate Panel Slams CFIUS*, DAILY DEAL, Oct. 7, 2005, *available at* 2005 WLNR 16256877.

143. Corr, *supra* note 139.

144. Bill McConnell, *China Watchdog Warns of M&A Tide*, DAILY DEAL, Nov. 11, 2005, *available at* 2005 WLNR 18233536.

145. Douglas Holtz-Eakin, *You Can't Be CFIUS*, WALL ST. J., July 13, 2006, at A8.

The most recent and substantive plans for change have come on the heels of the Dubai Ports World affair. House Majority Whip Roy Blunt, a Republican from Missouri, has announced that the Republican party is in the process of drafting a bill that will require Congressional oversight, though additional details are unclear at this point.[146] A separate measure, being drafted by Congressman Richard Shelby, a Republican from Alabama and the Chairman of the Senate Banking, Housing, and Urban Affairs Committee, goes one step further and would empower Congress with the ability to "pass a resolution of disapproval, even after the administration gives a deal the green light."[147]

Congressional hearings in the summer of 2006 yielded "rival" bills in the House and the Senate, both of which were "inspired by the Dubai Ports controversy."[148] The House bill requires "giving more information to Congress," increasing disclosure, removing some of the secrecy, but also sacrificing the confidentiality that is valuable to investors.[149] The Senate bill, meanwhile, takes a much firmer stance, proposing to put in place regulations if a deal will cause "any possible impairment to national security . . . or have a debilitating impact on national economic security."[150] Exactly how the implementation of these pieces of legislation will eventually play out is yet to be seen, but the concern that the United States' status as "the biggest net winner from the free flow of global capital" is in jeopardy is certainly being questioned by entities in the upper echelons of the U.S. business and legal communities.[151]

C. *The Implications of the Seemingly Imminent Expansion of CFIUS for Directors and Shareholders*

Both those who fear business interests taking precedence over national security and those who extol the continuing virtues of foreign investment in the United States appear to be in accord that certain changes—if not a complete overhaul—need to be made to the CFIUS process.[152] Thus, a higher level of CFIUS involvement in

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146. Jonathan Weisman, *GOP Leadership to Seek Congressional Oversight In Foreign Business Acquisitions*, WASH. POST, Mar. 11, 2006, at A7, *available at* 2006 WLNR 4067547.

147. *Id.*

148. Greg Hitt, *House, Senate Vote to Tighten Rules on Foreign Investments*, WALL ST. J., July 26, 2006, at A11.

149. *Id. See also* H.R. 5337, 109th Cong. (2006); *Hearing of the Commerce, Trade, and Consumer Protection Subcommittee of the House Energy and Commerce Committee*, FED. NEWS SERVICE, July 11, 2006.

150. Editorial, *The Don't Invest in America Act*, WALL ST. J., July 19, 2006, A12 (quoting S. 3549, 109th Cong. (2006)).

151. *Id.*

152. KIMMITT TESTIMONY, *supra* note 94.

cross-border transactions involving U.S. targets seems likely, if not inevitable.[153] The question naturally arises then as to what this will entail for directors and shareholders of U.S. corporations—those who, until now, held substantially all of the influence in allowing or blocking these transactions.

Supposing CFIUS review was to become a mandatory part of Delaware corporate law, shareholders would essentially lose some of the value in their voting power. The Delaware merger statute is unique in that it gives shareholders the opportunity to vote on (to approve or disapprove) an action of the board of directors.[154] Ordinarily, shareholders have the ability to vote for the directors serving the corporation, but do not have the power to override directors' decisions.[155] If CFIUS were able to determine whether or not it is appropriate for a U.S. corporation to enter into a transaction, it would essentially be assuming the role of the corporation's directors.[156] Far-reaching changes in the CFIUS process would undoubtedly find their way into state corporation codes, or at least require courts to determine, in yet another instance, how state law and federal law are to interact with one another. Since Delaware courts have traditionally shown a great deal of deference toward directors via doctrines such as the business judgment rule (deferring to the decisions of directors in business matters), this change would mark a radical departure from much of the well-settled Delaware case law.[157] Again, the shareholders would be shortchanged in that their primary power, the ability to vote for those who make the company's business decisions (ordinarily the directors) would be taken away. From the vantage point of potential investors in a company, the decision to invest in the company is necessarily an uninformed one, for they arguably do not know who will be making the company's business decisions—an incredibly significant piece of information that would surely factor into any rational investor's decision.

Depending on the rigor with which a revamped CFIUS would examine proposed transactions, the implications for potential investors could plausibly render them increasingly wary of investing in the firms in the first place—an indisputably deleterious outcome in terms of the domestic economy. Indeed, returning momentarily to the Unocal/CNOOC paradigm, the Unocal shareholders were arguably the ultimate losers because they were deprived of the opportunity to

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153. *Id.*

154. *See* DEL. CODE ANN. tit. 8, § 251 (2005).

155. MODEL BUS. CORP. ACT §§ 7.01, 7.28 (2005).

156. *See id.*

157. *See* Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985); Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1985).

accept the highest bid offered.[158] Significantly, if the CNOOC bid were not withdrawn, and the Unocal directors had nonetheless selected the Chevron bid, there would likely have arisen the issue of whether the Unocal directors had fulfilled their fiduciary duty.[159] Because the company was for sale, the directors had a duty to maximize shareholder value and they would probably not have done so had they opted for the Chevron bid in the face of the CNOOC bid, which was more lucrative for their shareholders.[160] In a world where this well-established doctrine were not in place (as a result of a potential acquirer backing away from an otherwise sound transaction due to protectionist concerns), shareholders would end up shortchanged and arguably less likely to put themselves in such a position (that of the passive investor) in the future.

If we place any value on our unique system of corporate governance in regard to merger activity—whereby private ordering is favored and a trust of market forces is preached to generate the most economically sound outcome—it would be in our best interest to ensure that the CFIUS reforms which are effected strike a balance between national security interests and economic/financial interests. National security has become increasingly important since U.S. vulnerability to foreign attack was exposed on September 11, 2001. At the same time, the flow of capital in response to market demand that our corporate law allows produces well-documented benefits to employment and productivity.[161] Arguably, we would not want to allow either of these concerns to slip away in the quest to overhaul the process by which the government becomes involved in foreign acquisitions of domestic assets.

Given the U.S. position as the "cornerstone of the global investment atmosphere" and the fact that U.S. policy has "influenced the course and defined the shape of laws and policies governing the acceptance of foreign capital worldwide," the importance of these decisions cannot be stressed enough.[162] Indeed, the policy adopted in Washington will likely have an effect, not only on foreign investment in the United States, but also on the ability of U.S. companies to invest abroad—assuming that similar regulations will subsequently be adopted by major U.S. trade and business partners.[163]

Perhaps William Reinsch's comments best sum up the point of view that this type of regulation is inappropriate: "A year from now

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158. *CNOOC Letter, supra* note 11.

159. *See Van Gorkom*, 488 A.2d at 879; *Revlon*, 506 A.2d at 182.

160. *Revlon*, 506 A.2d at 182.

161. KIMMITT TESTIMONY, *supra* note 94.

162. Note, *U.S. Policy Towards Foreign Direct Investment Post-September 11: Exon-Florio in the Age of Transnational Security*, 41 COLUM. J. TRANSNAT'L L. 195, 197 (2002).

163. *Id.* at 248–49.

we will all be embarrassed by this."[164] Those subscribing to this school of thought wish to preserve the openness to foreign investment in the United States.[165] On the other hand, the "protectionist bandwagon" in Congress is countering that desperate times call for desperate measures and sees no harm in addressing newly relevant concerns about the existing process.[166] The remainder of this Note aims to propose a formulation of the CFIUS process that will strike a balance between the twin aims articulated in the congressional hearings subsequent to the failed Unocal/CNOOC transaction.

IV. A PROPOSED REFORM TO U.S. MERGER LAW IN THE CONTEXT OF CROSS-BORDER TRANSACTIONS

A. *Various Economic, Political, and Social Goals Should Not Be Compromised*

It should be reiterated that the CFIUS process only requires additional scrutiny for 10% of the transactions that are submitted for review.[167] The other 90% of cross-border transactions submitted to CFIUS undergo a routine review that is completed in less than thirty days, either because "they do not raise significant national security issues" or "the parties have worked with the government to mitigate national security concerns."[168] Therefore, proposals for reform can focus on this subset of transactions, which implicate the types of national security issues about which U.S. politicians and businessmen have become concerned.

Further, any reform to the process for this subset of cases must continue to cater to both sides of the current debate by continuing to promote the open investment policy on home soil—historically a defining feature of the U.S. economy—but also ensuring that national security considerations do not take a back seat to the maintenance of this policy.[169] In reforming the current system, a continued trust of private ordering in U.S. corporate law would undoubtedly prove beneficial to the health of the economy. At the same time, this reliance on private ordering should not go so far as to compromise the irrefutable need for enhanced national security in the post-9/11 era. With these goals in mind, one can begin to construct a revised process

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164. *Ports Deal Collapse Could Lead to More Restrictions on Investments*, GRAND RAPIDS PRESS, Mar. 11, 2006, at B1.

165. *Id.*

166. *Id.*

167. Robert Kimmitt, *America Seeks to Balance Investment and Security*, FT.COM (London), Jan. 30, 2006, *available at* 2006 WLNR 1697831.

168. *Id.*

169. *Id.*

for evaluating the viability of cross-border transactions involving foreign entities acquiring U.S. assets.

B. *Revising CFIUS*

The focus of the actual CFIUS review process has probably been the subject of debate the most among Washington policymakers in the months since the failed Unocal/CNOOC transaction.[170] Indeed, regardless of which side of the issue a particular individual is on, all interested parties would agree that a clarification of the actual review process would be beneficial.

Firstly, the voluntary aspect of the CFIUS process must be abolished if the agency is to make any steps toward becoming a more legitimate and effectual force in U.S. merger law. With this abolishment of the voluntary nature of CFIUS review comes an inevitable loss in efficiency, but the revamped process, as described below, will be as streamlined as possible, so as to avoid unnecessary inefficiencies in administration of the review.

The two categories subject to CFIUS analysis should be as follows: 1) issues of national security and 2) issues of economic prosperity. At the outset, it should be noted that the line between these two is not clear-cut, and there will inevitably be overlap between the categories. However, creating the categories will nonetheless add structure to the CFIUS review process, forcing the Committee to address both components in every case.

As to national security, CFIUS has apparently been using a relatively narrow definition, as evidenced by the lack of transactions actually prevented by the Committee.[171] A broadening of this definition is undoubtedly necessary in the wake of increased security concerns in recent years. Questions of economic security have traditionally been dealt with by CFIUS in a typically murky fashion, and it is frankly unclear what criteria are presently being used by the Committee.[172]

A first step would be the formulation of statutory definitions of both "national security" and "economic prosperity," neither of which exists in the current version of the Exon-Florio Amendments.[173] Ideally, these definitions should be formulated with the assistance of

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170. *See generally supra* note 91 (delineating the major issues with the Exon-Florio Amendments, and the very existence of which serves as evidence of the focus on the CFIUS review process in the months immediately following CNOOC's withdrawal of its bid).

171. Press Release, Government Press Releases, Bayh to Introduce Comprehensive Legislation to Ensure U.S. Control of Security Concerns (Feb. 22, 2006), *available at* 2006 WLNR 3068243.

172. Crock, *supra* note 4, at 53.

173. GAO REPORT, *supra* note 91, at 11.

the Department of Homeland Security and the Department of the Treasury. A concrete, carefully worded definition would undoubtedly be more effective than the list of factors to be considered currently in the statute. The following proposed definitions would perhaps best serve as a starting point for the individuals and entities that will eventually be responsible for drafting the text of the revised statute:

> "National Security" – pertaining to matters of production needed for national defense requirements, including human resources, products, technology, materials, and other supplies or services.
>
> "Economic Prosperity" – relating to matters that the Department of the Treasury [or other appropriate federal governmental body] would deem appropriate and beneficial to the national trade deficit.

It should be noted that both of these definitions have the propensity to either become overly broad or overly narrow, and there are certainly factions in favor of both extremes. In providing these very basic starting points, the definitions above attempt to tread a middle ground. Inevitably, however, the definitions that ultimately find their way into the actual statute will have a much stronger and more evident tendency to sway toward either a broad or narrow rendering.

Once these definitions are in place, the next step in revising the statute will be to decide precisely who will sit on the Committee and, further, who will have involvement regardless of whether they sit on the Committee. However the definition that eventually appears in the revised statute may be worded, the individuals (and the various agencies and groups behind them) who will be interpreting the language of the statute are just as important, if not more so, than the language itself. It has already been noted that the Treasury, in its current role as Chair of the Committee, has taken a narrow view of what constitutes a threat to national security.[174] Therefore, it is of utmost importance that each representative from a group with incentives to construe the statute in a particular fashion be counter-balanced by a representative that has an incentive or propensity to construe the statute in the countervailing fashion. This precept must be kept in mind when it comes time to reconstruct the makeup of CFIUS.

C. *Revamping the CFIUS Process*

When a transaction is reviewed under CFIUS, there are obviously two immediate options: either the transaction will be approved, or not. If it is approved, of course, the parties are free to carry on negotiating the terms of the transaction and go forward with the deal. If the CFIUS review results in less than satisfactory findings, however, this reform proposal suggests that the parties be

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174. *Id.* at 11–12.

given an opportunity to amend the terms of the transaction before the issue goes to Congress.

Allowing the parties to step in and renegotiate key terms at this point will maintain the trust of private ordering aspect of U.S. merger law.[175] The parties will have a chance to make adjustments to the terms of their transaction in the hope that they can alleviate the national security or economic concerns raised during the CFIUS review process.

Returning to the Unocal/CNOOC paradigm scenario, a need for this type of mechanism is evidenced by the letter transmitted from CNOOC CEO Fu Chengyu to the U.S. Congress amidst the opposition to CNOOC's bid.[176] As previously referenced, Mr. Chengyu made several assurances to the U.S. Congress in that letter that Congress's concerns regarding national security and a loss of employment for U.S. workers were unfounded and went on to list several reasons supporting these assurances.[177] Had the parties been given the opportunity to discuss the specifics of the terms themselves, and put the results of their negotiations into the proposed merger agreement, it is likely that members of Congress who opposed the transaction going forward would have been left with a considerably diminished platform on which to stand. Again, the parties would have been able to rely on private ordering to come to an agreement that suited both parties. Further, involvement by Congress would not have been a factor because the parties themselves would have been given a chance to address the concerns raised in the CFIUS process. Although it is nearly impossible in this era to separate matters of business and matters of politics, this system would prevent a business transaction from becoming an explicitly political matter—which the world witnessed during the failed Unocal/CNOOC transaction.

In the interest of efficiency, the time that the parties are given to renegotiate the terms of their transaction should be limited to either a thirty-day or sixty-day window. This would prevent the interested parties from dragging their feet and keep the process moving smoothly towards resolution. The determination of the precise window of time should be made based on the level and severity of the CFIUS issues that arise. Perhaps a thirty-day window, with the possibility that the parties can apply for a thirty-day extension pending CFIUS approval, would be the most sensible approach. CFIUS approval of the extension would be based on the Committee's own assessment of the severity and complexity of its objections to the proposed transaction.

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175. *See* O'KELLEY & THOMPSON, *supra* note 44, at 148.
176. *See CNOOC Letter, supra* note 11.
177. *Id.*

Once the opportunity to amend the terms of the transaction has been given to the parties, then they could resubmit the revised plan of merger to CFIUS for a secondary review. Again, if CFIUS approves the terms of the transaction (arguably the ideal outcome if this system is to function as intended), the transaction can go forward as the parties have delineated in the merger agreement. If, however, CFIUS still has objections to the transaction on any substantive grounds, the review process should continue at this point in the same fashion as it has historically. Though this process is lengthy and thus may contravene the efficiency goal to some extent, it would be used only after the parties had been given the opportunity to avoid it within a relatively controlled time frame.

Admittedly, this type of process would result in companies being required to give at least as much attention to international trade and security policies in structuring transactions as they do to more traditional areas of concern such as tax, pension, and environmental policies.[178] Among the variables that can and should be considered are: "expected participation in the transaction by non-U.S. parties; connections between parties and compliance-sensitive activities, such as whether a party is a defense contractor, technology company, oil company, or financial company; connections between parties and compliance-sensitive areas of the world, such as the Middle East, Central or Southeast Asia, or Africa; and a party's heavy reliance on export markets."[179] It is most efficient to shift much of this burden onto the parties themselves, rather than allowing them to become overly reliant on the government's newly-implemented mechanisms for resolving these issues.[180] If the parties take the time to negotiate the merger terms, even where they did not find that necessary in the past, and conduct "particularly intensive due diligence," the burden on the government will be less, and the cross-border merger process will sacrifice as little as possible in terms of efficiency.[181]

D. *Proposed Change to Delaware Merger Statute*

A final, and relatively minor, change that should be made is creating some statutory record at the state level of the new process described above. Even though the changes to CFIUS are exclusively federal in nature, it is sensible to include a provision in the Delaware General Corporate Law (and, of course, a corresponding provision in the body of corporate law governing other states as well) making clear

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178. Clark & Jayaram, *supra* note 42 at 408.
179. *Id.* at 408–09.
180. *Id.* at 409.
181. *Id.*

to the appropriate entities that additional procedures are required when the Delaware company is the target of a foreign acquisition.

The addition of this provision would be as simple as adding a subsection (h) to § 251 of the Delaware General Corporate Law. The provision could be worded as follows:

> (h) In the event that an entity incorporated in this jurisdiction is being acquired by an entity incorporated under laws other than those of the United States, the parties must comply with the Committee on Foreign Investment in the United States' review process as delineated in [insert citation to relevant federal statute].

Such a provision would make it abundantly clear that the CFIUS process is mandatory when a Delaware entity finds itself in this situation, with the hope that this compulsory provision would relay the significance of the provision to foreign entities as well. In this fashion, the notion that CFIUS is merely a "doormat" for foreign acquirers will quickly be corrected.[182]

It should be noted that a more detailed provision is certainly a viable option, but other references to foreign issuers, for instance, in the Delaware General Corporate Law are generally brief and provide cross-references to the relevant bodies of law.[183] As such, it seems most sensible to treat this new provision in the same fashion, rather than launching into a detailed description of the CFIUS process within the Delaware statute itself.

V. CONCLUSION

As the nation's attention turns, with increased frequency and intensity, towards reforming merger law in the United States regarding cross-border transactions, an understanding of the problems facing the current mechanism in place is essential. As such, this Note has first and foremost attempted to lay out the current problem and the most prominent situations in which the issue has arisen in recent years. Secondly, the guidelines for overhaul of the CFIUS process are informed by a thorough understanding of the needs of the areas in which the current process is lacking—namely that it has not been created with an appreciation for heightened security risks and changing standards of economic prosperity given the U.S. trade deficit.

One critique that will undoubtedly be leveled at the factors mentioned above as guidelines for revising the CFIUS process—and thereby substantially changing the face of U.S. merger law with respect to cross-border acquisitions of U.S. assets by foreign entities—

182. Crock, *supra* note 4, at 53.
183. DEL. CODE ANN. tit. 8, § 251 (2005).

is that such change of longstanding principles of U.S. merger law and, indeed, U.S. foreign policy as it relates to corporate law (respect for private ordering, openness to foreign investment, etc.) will not be easy to effect. Concededly, this type of change would require cooperation and endorsement from a number of parties in different sectors of our business and political communities—from politicians in Washington, to corporate executives at home and abroad. Indeed, these are individuals who operate in very different spheres of society, but efforts must begin soon to inform these parties of the need to intensify scrutiny of these transactions for national security reasons, while still eschewing protectionism and maintaining the openness to foreign investment that has played an integral role in U.S. economic and social growth since its founding. There is no doubt that this is a fine line to walk, but the appropriate foresight at this relatively early juncture, combined with the cooperation and understanding of all necessary parties, a compromise can surely be reached that will reflect these new needs but not stray too far in the direction of either extreme.

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