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Outbound Investment Review Mechanism:
A Potential Means of Countering Risks in the U.S.-China Investment Landscape

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Abstract

Foreign investment review mechanisms have taken more prominence as a tool of national security strategy and an overall framework for economic competitiveness. One of the most important innovations was the expansion of CFIUS jurisdiction and capacity in the United States. The EU is also bolstering investment screening capabilities. A notable area that foreign investment review has not covered is that of outbound investments. (hereinafter abbreviated as "OBI-RM"). A number of Bills have been proposed in Congress. Although discussions of implementing OBI-RM are still in their infancy, this paper proposes that such mechanisms can be leveraged as an important component of national security strategy if done correctly. Furthermore, their use can be expanded as a negotiation tool with countries like China so as to reduce non-tariff barriers (such as joint venture and domestic equity requirements) in key sectors as well as promote greater market openness in the long term. The "trade war" with China under the Trump Administration was initially proposed as a method for dealing with issues like forced technology transfer (FTT) and a lack of market access reciprocity. This paper will not review the merits or critiques of leveraging tariffs in this regard, but rather suggest that a more granular, targeted approach using OBI-RM is a more effective way at achieving the same ends.

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I. Introduction

Investment review mechanisms have been an important element of national security policy for many decades. Coupled with additional policies such as export controls, they serve as important arrow in the quiver for safeguarding security of critical infrastructure, sensitive technology and American competitiveness. This was recognized back in 1975 when President Gerald Ford issued Executive Order 11858, which created the Committee on Foreign Investment in the United States (CFIUS). The Order tasked the Committee with analyzing trends in foreign investment into the United States, reviewing investments that might have major implications for U.S. national interests and considering proposals for new legislation or regulations to respond to issues on this front.[1] Specifically, the order gave the Committee *"the primary 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 on such investment."*[2]

The foreign investment landscape has transformed considerably since the 1970's, both in terms of inbound and outward capital flows. Looking just before the confounding variable of the COVID-19 pandemic came about (wherein total global foreign direct investment dropped 42%)[3], global investment flows in 2019 totaled \$1.39 trillion.[4] Inward foreign direct investment (FDI) into the United States totaled \$4.46 trillion in 2019 whereas outgoing FDI during that same year totaled \$5.96 trillion.[5] While this financial activity is vital for the world economy, it is not without its risks. Of course, investment of any sort carries its own financial risk profile. However, many policymakers and analysts have been keen to notice the national security threat that also emanates from this domain. While CFIUS has undergone many changes since its 1975 inception, a major update to both U.S. foreign investment review and export control policy took place under the Trump Administration in 2018. That year saw the passing of both the Foreign Investment Risk Review Modernization Act (FIRRMA) and the Export Control Reform Act (ECRA). Taken together, these acts sought simultaneously to bolster CFIUS' jurisdiction and ability to review inbound FDI as well as to identify areas of key concern in the export control space. As the Washington law firm Akin Gump wrote of the legislative pair, *"as part of the larger effort to reform the authorities governing CFIUS, the law [ECRA] effectively requires BIS to lead an interagency, regular order process to identify and add to the EAR controls on "emerging" and "foundational" technologies that are "essential to the national security of the United States."*[6] Whereas the hazards that accompany strategic foreign investment and the export of sensitive technologies is global, much of the readiness to update these policy frameworks stemmed from the threat of the Chinese Communist Party (CCP). Security risks are easy to imagine when assessing investments in or near United States critical infrastructure (power plants, energy grids, water treatment facilities, etc.), military installations or companies with sensitive data or intellectual property.

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[1] Congressional Research Service, "The Committee on Foreign Investment in the United States (CFIUS)". July 3, 2018

[2] Executive Order 11858 (b), May 7, 1975, 40 F.R. 20263.

[3] UNCTAD, "Global foreign direct investment fell by 42% in 2020, outlook remains weak". Jan. 24, 2021

[4] UNCTAD, "Global FDI Flows Flat in 2019 Moderate Increase Expected In 2020". Jan. 20, 2020

[5] Bureau of Economic Analysis, "Direct Investment by Country and Industry, 2019". July 23, 2020

[6] Akin Gump, "The Export Control Reform Act and Possible New Controls on Emerging and Foundational Technologies". Sept. 12, 2018.

Nevertheless, there is one key element that FIRRMA did not cover: outbound investment from the United States. As the international landscape has continued to evolve – particularly with regard to the CCP – the threat profile has concurrently developed on two key fronts. First, outbound FDI can bring sensitive data, technology and know-how into jurisdictions under which the United States does not have control or visibility. Second, capital outflows can also provide funding, directly or indirectly, to entities that are antagonistic to American interests, such as corporations that provide tactical or operational support to a foreign military. As David R. Hanke of the National Security Institute (NSI) at George Mason University's Antonin Scalia Law School stated in a testimony before the U.S.-China Economic and Security Review Commission, *"Opponents of FIRRMA's original construct were much more comfortable with maintaining the locus of any outbound controls and critical technology definitions at the Commerce Department, which had been generally far less concerned about technology and know-how flows to China."*[7] While these 2018 expansions to the investment review and export control mechanisms of the United States took important steps in the right direction, many have stated that the continued escalation of tensions between the U.S. and China have made a review of current capital outflows all the more necessary. Nazak Nikakhtar, former Assistant Secretary for Industry and Analysis, stated the issue bluntly in a March 2021 Congressional testimony: *"To be frank, the United States' reluctance to adequately control the flow of technology to China, our collective decision to off-shore manufacturing in strategic sectors to avail ourselves of China's distorted nonmarket economy, and our decision to pour capital into the PRC has been, for decades, tilting the competitive advantage in favor of China and against the United States and our allies."*[8]

These concerns have prompted a number of policymakers to search for solutions to address the issues stemming from the gap in oversights related to U.S. outbound capital flows. In September 2020 Senator Sherrod Brown (D-OH), Senator Chuck Schumer and other Senate Democrats sponsored the America Labor, Economic competitiveness, Alliances, Democracy and Security (America LEADS) Act, which was created with the aim of devising a comprehensive, long-term strategy on China. In a press release from Senator Brown's office, the legislation was guided by four key pillars: *"(1) invest in American competitiveness; (2) support American alliances and partners; (3) restore and advance a values-centered foreign policy; and (4) ensure China pays a price for its predatory actions."*[9] Of particular note, Section 411 of the bill included specific reference to the authority to review both inbound and outbound U.S. investments by making appropriate updates to the Trade Act of 1974.[10]

While the bill died in the previous Congress, Senators Bob Casey (D-PA) and John Cornyn (R-TX) picked up the torch by introducing the National Critical Capabilities Defense Act as an amendment to the United States Innovation and Competition Act of 2021. Among other things, the bill hosts a provision for the establishment of a committee which would *"focus on outbound investment or offshoring of critical capacities, supply chains, domestic production and manufacturing to foreign adversaries."*[11] As these pieces of legislation work through the legislative process, the need for such an outbound investment review mechanism (OBI-RM) was echoed by the U.S.-China Economic & Security Review Commission in their November 2021

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[7] David R. Hanke, "Testimony before the U.S.-China Economic and Security Review Commission". Sept. 8, 2021

[8] U.S.-China Economic & Security Review Commission, "Hearing on U.S. Investment in China's Capital Markets and Military-Industrial Complex". Mar. 19, 2021

[9] Office of Sherrod Brown, "Senate Democrats Unveil the America Leads Act to Make Comprehensive Investments in American Workers, Competitiveness, Alliances, and Diplomacy to Confront the Rise of China". Sept. 17, 2020

[10] S. 4629 — 116th Congress: America LEADS Act. Sept. 17, 2020

[11] Office of Bob Casey, "Casey and Cornyn Release a Joint Statement on National Critical Capabilities Defense Act". May 24, 2021

report to Congress. For the first time, the Commission voiced an explicit recommendation for the creation of an OBI-RM in the United States. Specifically, one of their top 10 recommendations advises that, *"Congress consider legislation to create the authority to screen the offshoring of critical supply chains and production capabilities to the People's Republic of China (PRC) to protect U.S. national and economic security interests and to define the scope of such supply chains and production capabilities. This would include screening related outbound investment by U.S. entities."*[12]

It is clear that there is already a framework for an OBI-RM being developed in the United States and it is important that such regulatory scaffolding is constructed with the appropriate considerations in mind. These considerations are multitudinous, but at their core are composed of three basic elements: 1) balancing national security concerns with the maintenance of the principles of free trade; 2) use of such mechanisms as a means of achieving market access reciprocity and negotiation for the construction of a fair playing field in international trade; and 3) close coordination with allies.

II. Review of U.S.-China Investment Landscape

Investment between the United States and China has grown rapidly since the "opening of China" in the early 1970's.[13] Trade and capital flows between the two countries have formed a central pillar in the relationship over the last several decades. Two-way direct investment and venture capital flows has slowed since 2016, but investments in equity and debt have continued to grow. As the Rhodium Group reported on U.S.-China investment in early 2021, *"The United States is China's most important financial counterpart, save for Hong Kong. US markets have been critical to Chinese company fundraising, and America is where government and household savers seek to reinvest surpluses and savings."*[14] While the COVID-19 pandemic did cause some disruption in global capital flows generally, the group estimated U.S. FDI into China at $8.7 billion and Chinese FDI into the United States at $7.2 billion for 2020. In terms of aggregate bilateral equity and debt holdings, the Rhodium Group calculated a massive $3.3 trillion – with US holdings of Chinese securities nearing $1.2 trillion and Chinese holdings of U.S. securities approximating $2.1 trillion.[15] Figure 1 provides an overview of key trends in U.S.-Chinese investment over the last several years as presented by the Rhodium Group.[16]

Data specifying trends in the various sectors provide a more detailed picture of the investment landscape. Top sectors for annual flows of U.S. FDI into China for 2020 were Automotive ($2 billion), Agriculture and Food ($1.4 billion) and Entertainment ($1.2 billion). The top sectors for Chinese FDI in the United States were Entertainment ($3.3 billion), Consumer Products and Services ($1.4 billion) and Health and Biotech ($625 million). Notably, U.S. FDI in China dropped $1 billion and $2 billion in Internet Communication Technology (ICT) and Health and Biotech in 2020 from 2019 levels respectively. Figure 2 shows a major downtick in key emerging sectors in bilateral venture capital flows between the two nations. The Rhodium Group attributes these changes to a number of factors such as a renewed focus on the Chinese government to nurture domestic industries and the *"stepped-up CFIUS enforcement under the new FIRRMA*

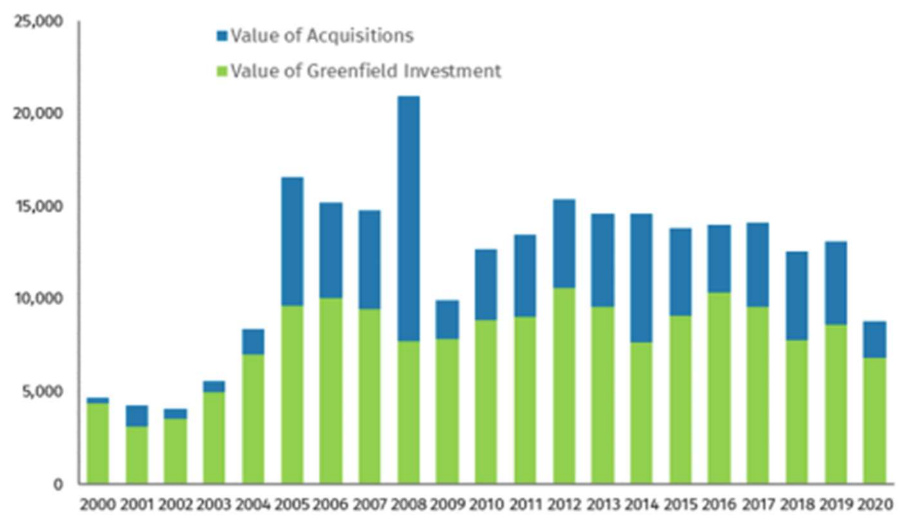
[12] U.S.-China Economic & Security Review Commission, "2021 Report to Congress". Nov. 2021
[13] Richard Nixon Foundation, "The Opening of China"
[14] Adam Lysenko, Mark Witzke, Thilo Hanemann, & Daniel H. Rosen, "US-China Financial Investment: Current Scope and Future Potential". Rhodium Group. Jan. 26, 2021
[15] Thilo Hanemann, Daniel H. Rosen, Mark Witzke, Steve Bennion, & Emma Smith, "Two-Way Street: 2021 Update US-China Investment Trends". Rhodium Group. May 2021
[16] Ibid.

statutes" in the United States. These trends can provide some insights into how emerging technologies are at a critical juncture with regard to U.S. and Chinese regulatory policy in light of increasing bilateral tensions.

Figure 1 – Selected Tables on Foreign Direct Investment from Rhodium Group 2021 Update on U.S.-China Investment Trends

Figure 1: Value of US FDI Transactions in China, 2000-2020

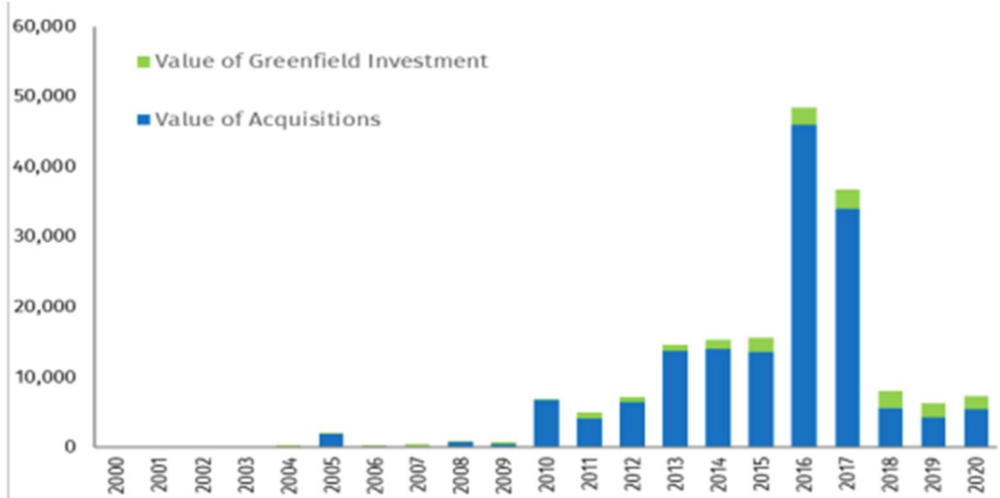
USD million



Source: Rhodium Group.

Figure 5: Value of Chinese FDI Transactions in the US, 2000-2020

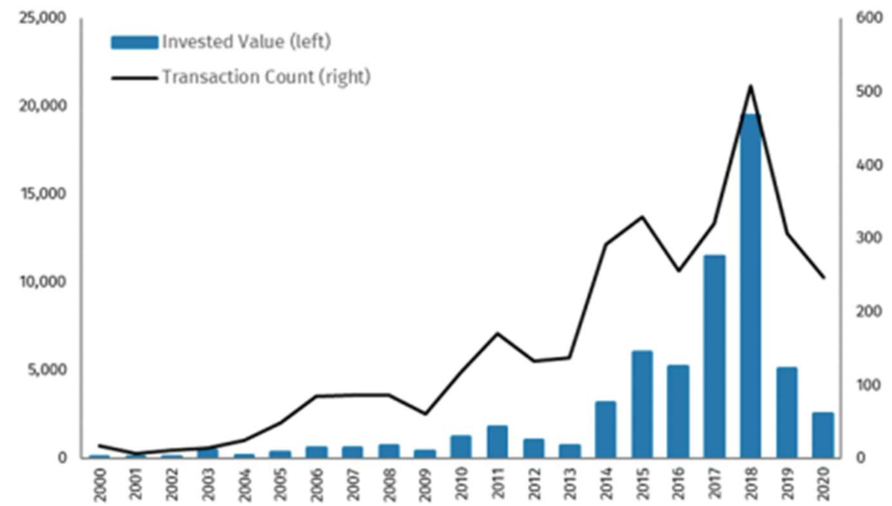
USD million



Source: Rhodium Group.

Figure 10: Annual US Venture Capital Investment in China, 2000 to 2020

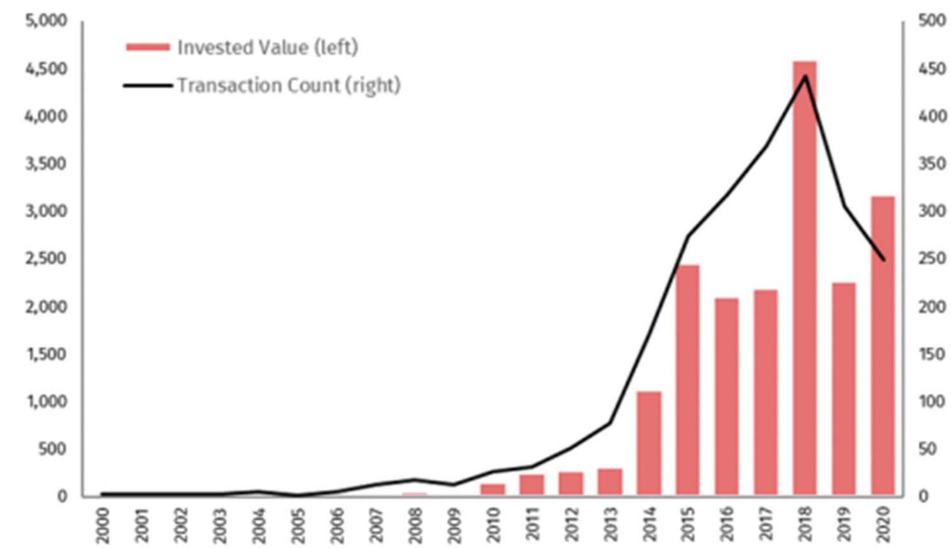
USD million, count



Source: Rhodium Group based on Bloomberg, Pitchbook and other databases. *Includes US-headquartered venture capital fundraising transactions involving at least one investor ultimately owned by a mainland Chinese entity.

Figure 13: Annual Chinese Venture Capital Investment in the United States, 2010-2020*

USD million, count

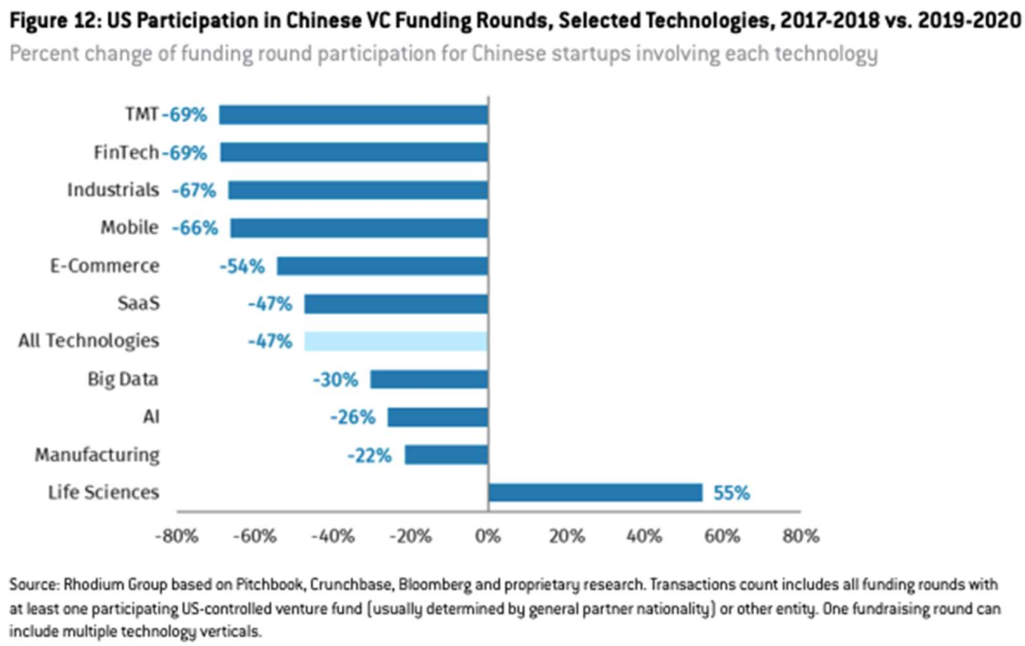


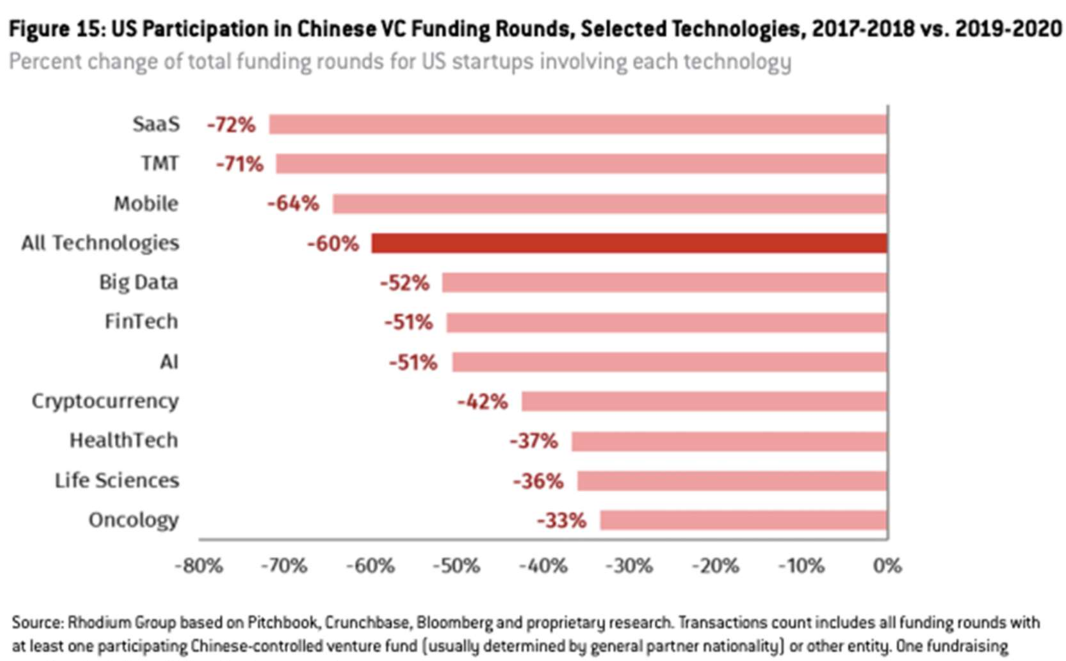
Source: Rhodium Group based on Pitchbook, Crunchbase, Bloomberg and proprietary research. Chinese transactions include all funding rounds with at least one participating Chinese-controlled venture fund (usually determined by general partner nationality) or other entity.

[17]

[17] Ibid.

Figure 2 – Selected Tables on Venture Capital Flow Changes from Rhodium Group 2021 Update on U.S.-China Investment Trends





[18]

[18] Ibid.

III. China's Foreign Investment Law (FIL) and Subversive Practices such as Forced Technology Transfer (FTT)

Review of the Problem

Forced technology transfer (FTT) and other practices that cause issue with securing sensitive and intellectual property have been a key sticking point in U.S.-China trade negotiations. Such practices have also been a key concern for policymakers with bilateral relations more generally. FTT can be implemented through a number of different avenues. In the context of the Chinese investment landscape, this often takes the form of targeted corporate structuring requirements (CSRs) in which foreign investors into certain key sectors must enter into a joint venture with a domestic partner. However, these processes can also be achieved through other methods such as data localization requirements, the requirement to have a domestic individual (often appointed by the government) to play a part in the firm's operations or general theft. As Alan O. Sykes notes on the broad nature of the term, *"the phrase ['forced technology transfer'] encompasses a number of different practices, but the most significant according to various commentators involve measures that require foreign investors in China to partner with domestic entities as a condition of making an investment, either by forming a joint venture or affording Chinese investors a controlling equity stake."*[19]

Forced technology transfer has been a concern for many years and eventually played a major part of the Phase One Trade Deal agreed to under the Trump Administration.[20] In 2011 the United States International Trade Commission (USITC) released the first report of its kind attempting to quantify the impact of Chinese intellectual property infringement and other indigenous innovation policies on the U.S. economy. The authors of the report noticed that despite finding great success in the Chinese market, *"many companies have reported that the infringement of their intellectual property rights (IPR) in China, as well as China's 'indigenous innovation' policies, have undermined their competitive positions."*[21] In order to understand some of the mechanisms that are used in conducting FTT and undermining U.S. competitiveness in the Chinese markets, the USITC examined data and testimonial from various sectors. Figure 3 provides a truncated version of Table 5.1 from the report, which highlights specific FTT mechanisms. The importance of safeguarding the central elements of technological innovation cannot be understated from both a national and economic security perspective. The USITC reports that, American IP-intensive firms claimed global losses of $48.2 billion from Chinese IPR infringement in 2009 and spent an additional $4.8 billion to protect themselves against it that same year.[22] On a larger scale, the report also points to the fact that the U.S. Department of Commerce has estimated that technological innovation has accounted for nearly three-quarters of the United States' annual economic growth since the mid-1940's[23] and is thus closely connected with broader U.S. strategy and interests. Hence, it is easy to understand why this became such a critical issue and scrutiny has only intensified in the subsequent decade after the release of the USITC's 2011 report.

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[19] Alan Sykes, "The Law and Economics of 'Forced' Technology Transfer and Its Implications for Trade and Investment Policy (and the U.S.–China Trade War)". Journal of Legal Analysis. Mar. 23, 2021

[20] Lauren Feiner, "China trade deal has new provisions to safeguard US tech secrets". CNBC. Jan. 15, 2020

[21] United States International Trade Commission, "China: Effects of Intellectual Property Infringement and Indigenous Innovation Policies on the U.S. Economy". USITC Publication 4226. May 2011

[22] Ibid.

[23] Ibid.

Figure 3 – Truncated Version of Table 5.1 from U.S. ITC 2011 Report on FTT Mechanisms in Key Industries	
Industry	**Key Indigenous Innovation and Industrial Policies Identified**
Wind energy equipment	• Government procurement preferences • Local-content requirements • R&D incentives and support
Telecommunications equipment (mobile handsets)	• Development of Time Division Synchronous Code Division Multiple Access (TDSCDMA) standard to reduce reliance on foreign technologies and royalty payments • Preferential lending and generous lines of credit to promote Chinese companies in third-country markets
Software	• Introduction of Multi-Level Protection Scheme (MLPS) and China Compulsory Certification (CCC) software security standards • Government procurement preferences
Automotive industry	• Mandatory joint-venture requirements Encouragement of technology transfer • R&D incentives and support for R&D limited to Chinese firms • Local-content requirements Government procurement preferences
Civil aircraft and parts	• Possible mandatory joint-venture requirements • Technology transfer requirements and incentives

[24]

Monitoring, assessing and debating solutions to Chinese forced technology transfer and similar policies has accelerated since 2011. In 2015 the U.S.-China Business Council (USCBC) released their annual member survey, which found that 59% of respondents were concerned about forced technology transfer and nearly a quarter (23%) had been asked to transfer technology in the prior three years. They also noted that 60% of requests came directly from the central government and/or the local government.[25] In 2017 the same question regarding requests of technology transfer over the prior three years garnered a 19% affirmative response and noted that joint venture (JV) and government approvals were a primary mechanism in carrying out FTT.[26] The following year, in 2018, the Office of the United States Trade Representative (USTR) initiated an investigation of China's technology transfer practices at the direction of the President and under Section 301 of the Trade Act of 1974. As noted in the report:

> *The evidence collected in this investigation from hearing witnesses, written submissions, public reports, journal articles, and other reliable sources indicates there are two key*

[24] Ibid.
[25] US-China Business Council, "2015 USCBC Member Survey Report"
[26] US-China Business Council, "2017 USCBC Member Survey Report"

aspects of China's technology transfer regime for inbound foreign investment. First, the Chinese government uses foreign ownership restrictions, such as formal and informal JV requirements, and other foreign investment restrictions to require or pressure technology transfer from U.S. companies to Chinese entities… Second, the Chinese government uses its administrative licensing and approvals processes to force technology transfer in exchange for the numerous administrative approvals needed to establish and operate a business in China.[27]

The USTR report played an integral part in the U.S.-China Trade War and many of the tariffs that were placed on Chinese goods. In the years following the report, U.S. business reported a slight relief in technology transfer pressures emanating from the Chinese public and private sectors. In 2019 only 5% of business reported being asked to transfer technology by Chinese actors.[28] This same metric ticked upward in 2020 to 13% before dropping back down to 5% again in 2021.[29] Yet as the USCBC noted in their 2021 report, *"While technology transfer has not been a widespread concern of respondents in recent years, it is an acute problem for affected companies. When companies are asked to transfer technology as part of joint venture requirements, administrative licensing requirements, or other regulatory processes as a condition for market entry, they are forced to weigh the value of their IP against access to the Chinese market."*[30] These businesses elaborated on the impact of IPR-related activities in China, with only 25% citing no impact, whereas 24% stated it limits R&D activities in China; that it limits products manufactured in China (18%); limits products co-manufactured or licensed in China (17%) and limits the products sold in China (16%).[31]

Similar concerns came from European businesses as well. A May 2019 report from the Wall Street Journal reported that, "*technology transfers have continued to take place despite official assurances that this practice would be stopped, according to an annual survey by the European Union Chamber of Commerce in China, with 20% of the survey's 585 participants saying they have felt compelled to transfer technology to maintain market access, up from 10% in 2017.*"[32] [33] Particular sectors were highlighted as having higher rates of FTT pressure, such as in petroleum (30%), medical device manufacturing (28%), pharmaceutical (27%) and automotive (21%).[34] Such concern from U.S. and European businesses is also borne out by data from the OECD FDI Regulatory Restrictiveness Index (FDI Index), which measures statutory restrictions against open foreign direct investment across four metrics: 1) foreign equity limitations; 2) screening or approval mechanisms; 3) restrictions on the employment of foreigners as key personnel; and 4) operational restrictions.[35] These types of restrictions are what Chinese entities are able to leverage for the purpose of conducting forced technology transfers. With a value of 1 being the most restrictive, China has an FDI Index of 0.214, which is over twice that of the average

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[27] Office of the United States Trade Representative, "Findings of the Investigation into China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation Under Section 301 of the Trade Act of 1974". Mar. 22, 2018
[28] US-China Business Council, "2020 USCBC Member Survey Report"
[29] US-China Business Council, "2021 USCBC Member Survey Report"
[30] Ibid.
[31] Ibid.
[32] Julie Wernau, "Forced Tech Transfers Are on the Rise in China, European Firms Say". Wall Street Journal. May 20, 2019
[33] European Union Chamber of Commerce in China, "Business Confidence Survey 2021". Jun. 8, 2021
[34] Ibid.
[35] OECD, "FDI Regulatory Restrictiveness Index"

of all countries measured (0.105) and 3.3 times greater than the average of the OECD average (0.063). Figure 4 compares the FDI Index of China vis-à-vis that of the United States overall and in key sectors.

Figure 4 – OECD Regulatory Restrictiveness Index (2020)		
	U.S.	**China**
Total FDI Index	0.089	0.214
Fixed Telecom	0.0020	0.750
Mobile Telecom	0.200	0.715
Communications	0.110	0.733
Business Services	0.000	0.225

[36]

Recent Legislative Improvements by the Chinese Government

Recent years have also shown some improvements in China's regulatory regime. For instance, the Economic and Trade Agreement Between the Government of the United States of America and the Government of the People's Republic of China (also known as the "Phase One Trade Deal") entered into force on February 14, 2020. Notably, this agreement contained specific provisions related to technology transfer and IPR concerns. Article 2.1 states that, *"Natural or legal persons ("persons") of a Party shall have effective access to and be able to operate openly and freely in the jurisdiction of the other Party without any force or pressure from the other Party to transfer their technology to persons of the other Party."*[37] Just a month prior, Foreign Investment Law of the People's Republic of China (FIL) entered into force on January 1, 2020. The FIL made explicit prohibitions on forced technology transfers and made additional reforms to protect the rights of foreign investors. This was the first time that Chinese law highlighted the issue of FTT, particularly embodied in Articles 22 and 23 of the FIL.[38] As the U.S. Department of State noted in their 2021 Investment Climate Statement on China, *"While Chinese pronouncements of greater market access and fair treatment of foreign investment are welcome, details and effective implementation are still needed to ensure foreign investors truly experience equitable treatment."*[39] Unfortunately, while these were positive steps in improving the overall regulatory regime in China, there remains a considerable gap between statute and implementation.

Jyh-An Lee, a law professor at the Chinese University of Hong Kong, notes the specifics of the FIL: *"Although Article 39 of the Foreign Investment Law mentions the administrative and criminal liability for government officials who violate the FTT provision and confidential obligation set forth in Articles 22 and 23, the exact administrative liability is not stipulated in the law. Consequently, the government has broad discretion in imposing such liability, which might constitute an action as light as giving the breaching official a warning."*[40] These concerns of lack of meaningful implementation are reflected in survey data regarding U.S. investors in China.

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[36] OECD.Stats, "OECD FDI Regulatory Restrictiveness Index"

[37] "Economic and Trade Agreement Between the Government of the United States of America and the Government of the People's Republic of China". Jan. 15, 2020

[38] National Development and Reform Commission, "Foreign Investment Law of the People's Republic of China". Order of the President of the PRC No. 26. Mar. 15, 2019

[39] U.S. Department of State, "2021 Investment Climate Statements: China"

[40] Jyh-An Lee, "Forced Technology Transfer in the Case of China". Aug. 22, 2020

Noting results collected by the American Chamber of Commerce in South China, the Rhodium Group writes that, *"survey data confirm that Beijing's latest efforts to modernize its FDI regime have been positive but not sufficient."*[41] The Chamber survey found that only 24% of members felt a "clear positive impact" from the FIL, with the remaining 65% stating they continue to feel treated unfairly in terms of market access.[42]

Beyond the business community, there are a number of other areas that have been highlighted as concerning by the United States government, including those related to national security considerations. In the abovementioned March 19, 2021 hearing before the U.S.-China Economic and Security Review Commission, Nazak Nikakhtar pointed to a number of additional laws that are aimed at exfiltrating sensitive information from U.S. investors as well as giving China a competitive edge in critical, defense-related sectors. Figure 5 provides a list of the key pieces of Chinese legislation that were highlighted. As Nikakhtar noted in her prepared statement before the Commission:

> *The objective of the CCP's data accumulation strategy is to hasten the demise of foreign competitors and to fast-track the PRC's technological dominance in key strategic sectors such as aerospace, artificial intelligence (AI) systems, cyber intelligence, biometrics, genomics, semiconductors, pharmaceutical medicines, and energy. In furtherance of these goals, the CCP has instituted a number of laws mandating that Chinese and foreign companies transfer sensitive IP, proprietary commercial secrets, and personal data to the central government and the PLA.* [43]

Figure 5 – Areas of Concern in China's Regulatory Framework Identified by Nazak Nikakhtar

Area	**Concern**
National Security/Intelligence Laws	Mandates the transfer of data, information, and technology to PRC authorities
Cybersecurity Law	Mandates that network operators cooperate with public security organs.
Cryptography Law	Any system with a CCP "approved" encryption must provide its encryption keys to the government
Data Security Law	Empowers CCP authorities to demand data from companies and requires companies to "favor economic and social development in line with the CCP's social morality and ethics."
Export Control Law	Prohibits exports of "important data," essentially any information (including R&D developed by foreign-owned companies) outside of China.

[44]

Hence, while the FIL and other measures taken by China in recent years provided nominal support for fair market access and the protection of investor rights, security and business concerns remain. This leaves the United States and other countries with business operations in China in the position of having to reassess the situation and develop a novel strategy. As Jyh-An Lee continues

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[41] Id. 15

[42] The American Chamber of Commerce in South China, "2021 White Paper on the Business Environment in China". Feb. 25, 2021

[43] Id. 8

[44] Ibid.

with regard to FTT apprehensions in China, *"Because FTT policies are usually implemented without formal written law or rules, it is difficult to detect, prove, or combat the practice. While FTT is not rare internationally, China in particular is known for this practice as part of its industrial policy... Therefore, the next step for the U.S. to address this issue is to build a sound monitoring mechanism to evaluate the actual enforcement of the law."*[45]

IV. Review Current Investment Review Mechanisms and Export Control Regulations

Inbound Investment Review via CFIUS

The "sound monitoring mechanism" described by Lee will be a key factor for addressing U.S. national security and economic interests. The prospect of such a mechanism will be discussed further at length below. However, it is important to note some of the tools that have already been implemented for inbound investments in U.S. territory as well as the export of sensitive technologies abroad. As mentioned above, the Committee on Foreign Investment in the United States (CFIUS) plays an integral role in assessing threats from inbound investment in the U.S. The Department of the Treasury characterizes CFIUS as an *"interagency committee authorized to review certain transactions involving foreign investment in the United States and certain real estate transactions by foreign persons, in order to determine the effect of such transactions on the national security of the United States."*[46]

CFIUS has undergone a number of important developments since its establishment in 1975. Figure 6 provides a legislative history of the body as provided by the Congressional Research Service (CRS), where detailed information on the Committee's history can be found. However, there are two key moments in CFIUS' history that marked important changes in the United States' use of such investment screening mechanisms. In 2006, major debate surrounded the national security implications of Dubai Ports World's proposed acquisition of six major U.S. ports, ultimately leading to the proposal's cancellation.[47] In December of that year and with the focus of national security concerns surrounding inbound FDI reignited, the Bush Administration placed conditions on the acquisition of Lucent Technologies, Inc. by the French-based Alcatel SA. The acquisition was conditioned upon the signing of a Special Security Arrangement (SSA), which restricted Alcatel's access to sensitive work done by the research arm of Lucent Technologies and provided for the ability for CFIUS to overturn the transaction at any time if there was a material failure of the SSA provisions. This was a significant administrative change to the CFIUS process in that it allowed the reviews of transactions involving foreign parties to be reopened and potentially overturned after initial approval. Writing on the matter the CRS notes, *"prior to this transaction, CFIUS reviews and investigations were portrayed and considered to be final."*[48] Following these developments, Senator Dodd introduced Foreign Investment and National Security Act of 2007 (FINSA) into Congress. Signed into law in late July of 2007, FINSA codified the statutory authority of CFIUS and, inter alia, expanded the criteria upon which transactions were scrutinized.

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[45] Id. 39
[46] U.S. Department of the Treasury, "The Committee on Foreign Investment in the United States (CFIUS)"
[47] David E. Sanger, "Under Pressure, Dubai Company Drops Port Deal". New York Times. Mar. 10, 2006
[48] Congressional Research Service, "The Committee on Foreign Investment in the United States (CFIUS)". Feb. 14, 2020

Figure 6 – Congressional Research Service Legislative History of CFIUS

CFIUS Legislative History

1975 CFIUS established by Executive Order.

1988 "Exon-Florio" amendment to Defense Production Act. Codified the process CFIUS used to review foreign investment transactions.

1992 "Byrd Amendment" to Defense Production Act. Required reviews in cases where foreign acquirer was acting on or in behalf of a foreign government.

2007 Foreign Investment and National Security Act of 2007 replaced Executive Order and codified CFIUS.

2018 Foreign Investment Risk Review Modernization Act of 2018 provided a comprehensive reform of the CFIUS process.

[49]

More recently, the 2018 Foreign Investment Risk Review Modernization Act (FIRRMA), coming in the wake of increased concern from Chinese investment in key technology sectors in the United States, provided CFIUS with greatly expanded jurisdiction. Along with important administrative updates (such as increased budgeting and staffing as well as shifting filing requirements for certain foreign investors from voluntary to mandatory), FIRRMA's main impact was greatly expanding the definition of "covered transaction," by amending the Defense Production Act of 1950. It also allows for additional scrutiny to be placed on "countries of special concern."[50] The expansion of the term "covered transaction" includes 1) real estate transactions in close proximity to military installations or U.S. government facilities; 2) non-passive investments in critical industries; 3) transactions where a foreign government has a substantial interest; 4) any other transaction deemed important to national security. Lawyers from the firm Holland & Knight summarize the key changes to CFIUS thusly:

> *"Under FIRRMA, CFIUS jurisdiction now also includes any foreign, non-passive investment in U.S. critical infrastructure or critical technology, or a U.S. business that maintains or collects sensitive personal data of U.S. citizens that may be exploited in a manner that threatens national security. Removing the control test will greatly expand the*

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[49] Ibid.

[50] "H.R. 5841 — 115th Congress "Foreign Investment Risk Review Modernization Act of 2018". May 16, 2018

number of reviewed and reviewable transactions, particularly in the high-tech startup sector, and will likely be used to try to protect new U.S. technologies from the perceived threat of Chinese acquisition under a parallel export controls regime."[51]

U.S. Export Control Regime

The above remarks from Holland & Knight make reference to the parallel export control regime that was simultaneously established during 2018. While export controls have a long history in international trade and U.S. national security legislation, that year saw the passing of the Export Control Reform Act (ECRA). As Gibson Dunn noted in October 2020 on the legislation, *"In addition to placing the U.S. export controls regime on firmer statutory footing for the first time in decades, ECRA significantly expanded the President's authority to regulate and enforce export controls by requiring the Secretary of Commerce to establish controls on the export, re-export, or in-country transfer of 'emerging or foundational technologies.'"*[52] This focus on "emerging and foundational technologies" was a key aspect of the legislation as well as one of the most difficult. Section 1758 of the ECRA tasked the Department of Commerce, Bureau of Industry and Security (BIS) with the identification of such technologies by taking into account: 1) the development of foundational technologies in foreign countries; 2) the effect export controls may have on the development of such technologies in the United States; and 3) the effectiveness of export controls imposed pursuant to ECRA on limiting the proliferation of foundational technologies to foreign countries.[53]

While BIS opened several of public comment periods as well as defined a number of emerging technology controls (such as semiconductor manufacturing and development equipment, surveillance equipment and certain spacecraft), many have been displeased with the slow pace of progress. The first advanced notice of proposed rulemaking (ANPRM), issued by BIS in November 2018, considered an expansive list of 14 technologies including artificial intelligence, 3D printing, quantum computing.[54] Yet these critically strategic technologies have still to be adequately addressed under the ECRA regime. Gibson Dunn noted a palpable *"feeling among some Congressional Republicans that BIS is taking too long to identify foundational and emerging technologies."*[55] Emma Rafaelof of the U.S.-China Economic and Security Review Commission provided an even starker critique of the slow pace of identification under ECRA Section 1758:

> *"The Department of Commerce has, to date, failed to carry out its responsibilities. Lack of clarity from the Department of Commerce on what constitutes emerging and foundational technologies impedes the ability of the Committee on Foreign Investment in the United States (CFIUS) to fulfill its responsibilities… In the absence of the complete list, CFIUS*

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[51] Ronald A. Oleynik, Antonia I. Tzinova & Libby Bloxom, "FIRRMA Expands CFIUS Jurisdiction in 2 Major Ways". Holland & Knight. Aug. 16, 2018

[52] Gibson Dunn, "New Controls on Emerging Technologies Released, While U.S. Commerce Department Comes Under Fire for Delay". Oct. 27, 2020

[53] Bureau of Industry and Security, "Identification and Review of Controls for Certain Foundational Technologies". 85 FR 52934. Aug. 27, 2020

[54] Bureau of Industry and Security, "Review of Controls for Certain Emerging Technologies". 83 FR 58201. Nov. 19, 2018

[55] Id. 51

continues to operate without this additional guidance and may be constrained in its ability to screen transactions."[56]

U.S. Regulatory Action related to Portfolio Investment

There have also been recent important developments with regard to portfolio investments into the Chinese market. As Adam Lysenko of Strider Technologies noted to the March 2021 panel, *"both foreign private equity and foreign passive securities investments provide Chinese firms with capital that may be used in ways that are detrimental to US interests or values…China is an ideological and strategic competitor with the United States, and no other nation has ever engineered such a massive state-led, whole-of-society approach to pursuing dominance in strategic technology areas like China has."*[57] On November 12, 2020 then President Trump signed Executive Order (EO) 13959, titled "Addressing the Threat from Securities Investments that Finance Communist Chinese Military Companies." This order leveraged presidential powers under the International Emergency Economic Powers Act (IEEPA) to stem the flow of U.S. capital to those companies that were linked to Chinese military, intelligence and security services. Specifically, it prohibited *"any transaction in publicly traded securities, or any securities that are derivative of, or are designed to provide investment exposure to such securities of any 'Communist Chinese military company'"*[58] It also contained provisions that scrutinized the ownership of such shares in exchange-traded funds (ETFs) and index funds. The Executive Order relied on a list-based approach, wherein the Department of Defense identifies "Communist Chinese military companies" under Section 1237 of the Strom Thurmond National Defense Authorization Act of 1999.[59]

While there was significant confusion and some pushback surrounding the November 2020 order, many were surprised when President Biden continued the trend in June 2021 with the signing of Executive Order 14032, titled "Addressing the Threat From Securities Investments That Finance Certain Companies of the People's Republic of China." As per the White House fact sheet on the order, EO 14032 sought to "*solidify and strengthen [EO 13959] to prohibit U.S. investments in the military industrial complex of the People's Republic of China…by creating a sustainable and strengthened framework for imposing prohibitions on investments in Chinese defense and surveillance technology firms."*[60] The Fact Sheet continues, making explicit that *"the Administration will not hesitate to prevent U.S. capital from flowing into the PRC's defense and related materiel sector."*[61] The order created the "Non-SDN Chinese Military-Industrial Complex Companies List (CMIC) List" and Biden simultaneously listed 59 entities subject to the provisions of the order therein. Notably, the EO also revised the scope of review by expanding to include not merely Chinese companies linked to military or intelligence services, but also those *"that undermine the security or democratic values of the United States and [its] allies."*[62]

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[56] Emma Rafaelof, "Unfinished Business: Export Control and Foreign Investment Reforms". US-China Economic and Security Review Commission. June 1, 2021
[57] Id. 8
[58] Dorsey & Whitney LLP, "Trump Administration Bars U.S. Investments in Certain Chinese Companies Linked to Chinese Military". Nov. 20, 2020
[59] S. 2057 — 105th Congress: Strom Thurmond National Defense Authorization Act for Fiscal Year 1999. May 11, 1998
[60] The White House, "FACT SHEET: Executive Order Addressing the Threat from Securities Investments that Finance Certain Companies of the People's Republic of China". Jun. 3, 2021
[61] Ibid.
[62] Ibid.

Both Executive Orders were a step in the right direction with regard to concerns from portfolio investments. However, the U.S.-China Economic & Security Review Commission makes it clear that, since these were exclusively done through executive action, there is no statutory authority to deter U.S. investment in foreign companies of concern. Furthermore, the Commission notes the potential struggle to keep pace with Chinese civil-military fusion as well as the challenge faced by U.S. companies in conducting due diligence to this end. Some risk intelligence companies have provided recommendations for identifying companies that have a military nexus, but have also noted the difficulty of this process.[63] As the Commission elaborates in their November 2021 Report to Congress:

> *"There is no template for outbound investment restrictions, and those that narrowly target only the most overtly threatening Chinese companies may miss the broader ecosystem of actors participating in China's military-industrial complex. Structural features of global financial markets also create multiple pathways for U.S. capital to flow toward Chinese companies of concern. Against this backdrop, the U.S. government's initial attempts to craft outbound investment restrictions reflect only a preliminary step toward safeguarding U.S. national security."*[64]

V. Current Proposals for a U.S. Outbound Investment Review Mechanism (OBI-RM)

Though the U.S.-China Economic & Security Review Commission is correct in their assessment that there exist no fully-developed and implemented outbound investment restrictions, there are several attempts at making this a more concretized piece of U.S. national security infrastructure. In September 2020, a number of Senate Democrats introduced the America Labor, Economic competitiveness, Alliances, Democracy and Security (America LEADS) Act. The Act was a sweeping proposal, which provided *"over $350 billion in new funding to synchronize and mobilize all aspects of U.S. national power."*[65] Among other things, the Act focused on building up critical capacities in the United States, improving the American education system and reviewing supply chain vulnerabilities. However, a very interesting aspect of the legislation was its proposal to amend the Trade Act of 1974 to create the Committee on Production Integrity in the United States. The proposed Committee would be composed of representatives from the following areas: 1) The United States Trade Representative (to serve as the chairperson of the Committee; 2) The Secretary of Commerce; 3) The Secretary of Defense; 4) The Secretary of the Treasury; 5) The Secretary of Homeland Security; 6) The Secretary of State; 7) The Attorney General; 8) The Secretary of Energy; 9) The Secretary of Labor; 10) The Secretary of Health and Human Services; 11) The Secretary of Agriculture; 12) The Administrator of the Federal Emergency Management Agency; 13) The Administrator of the Environmental Protection Agency; 14) the heads of such other agencies as deemed appropriate by the USTR.[66] The broad composition of the proposed Committee indicate the broad nature of the risk profile identified by policymakers with respect to "nonmarket economies" and China in particular. Pursuant to the language of the Act, the Committee would be tasked with carrying out the following via amending the Trade Act of 1974 and adding Section 1002 of a new title (Title X) therein:

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[63] Sayari, "How to Use Public Data to Identify Potential Chinese Military End Users". Nov. 10, 2021
[64] Id. 12
[65] Id. 9
[66] Id. 10

(1) conduct a review and issue a regular report on domestic manufacturing and supply chain resilience in accordance with section 1003;
(2) review annual reports submitted by covered businesses under section 1004;
(3) review outbound investments related to nonmarket economy countries or involving state-owned enterprises under section 1005; and
(4) review inbound investments for economic 16 effect and certain supply chain concerns under section 1006 [67]

Further amendments to Section 1005 focus specifically on a review of outbound investments that may pose a risk *"with respect to the national security and crisis preparedness",* consider *"the history of distortive trade practices"* in the country receiving outbound investment as well as any other concerns identified by the abovementioned Committee. As per the changes proposed in the Act, the Committee would focus on a number of particular transactions, specifically one that:

(1) is a merger with, acquisition or takeover of, joint venture with, or investment in, an entity in a nonmarket economy country;
(2) results in the establishment of a new entity in such a country;
(3) in the case of a transaction involving a 16 state-owned enterprise, is valued at $50,000,000 or more; or
(4) in the case of any other transaction, is valued at $1,000,000,000 or more.[68]

Interestingly, the Act specifies "nonmarket economy countries," making it clear that there are certain conditions in foreign markets that any investment review mechanisms are attempting to address, all of which have been considerable sticking points in U.S.-China relations. These include subsidies, state-owned enterprises, lack of market openness and a number of other factors as laid out in Section 771(18) of the Tariff Act of 1930.[69]

While the bill died in the 116th Congress due to inaction, it did spur a considerable discussion in the following months regarding the potential establishment of an outbound investment review mechanism. In May 2021, Senator Marco Rubio echoed the need for such a mechanism in light of the challenges posed by China. During his statement, Rubio indicated that the Congress *"should establish a system of outbound investment screening. Even if [the U.S. is] successful in preventing adversarial actors from acquiring federal research dollars or intellectual property developed by it, there is nothing to stop nationless corporations from simply buying the IP and using it to develop capacities to benefit China and hurt our interests."*[70] Shortly thereafter, National Security Advisor Jake Sullivan indicated the Biden Administration's attention to the issue. Speaking at the National Security Commission on Artificial Intelligence in July, Sullivan stated that, "*We have to work closely…with our partners on our export control and investment screening regimes to make sure they're postured for intense technology competition… In this regard, we're also looking at the impact of outbound U.S. investment flows that could circumvent*

[67] Ibid.
[68] Ibid.
[69] United States Code: Tariff Act of 1930, 19 U.S.C. §§ 1201-1641 (Suppl. 2 1934).
[70] Office of Marco Rubio, "Rubio Argues for American Industrial Policy in Legislative Efforts to Combat China". May 18, 2021

the spirit of export controls or otherwise enhance the technological capacity of our competitors in ways that harm America's national security."[71]

However, the biggest development on this front was the introduction of the National Critical Capabilities Defense Act (NCCDA) by Senators Bob Casey (D-PA) and John Cornyn (R-TX) on May 26, 2021. In an April press release preceding the introduction of the bill, Senator Casey noted that the United States must gain more visibility into potential threats coming from supply chain vulnerabilities and "*establish an outbound investment review mechanism to ensure we are not losing critical capacities to foreign adversaries."*[72] A very recent development was the introduction of a companion bill of the same title in the House by Representatives Bill Pascrell (D-NJ), Rosa DeLauro (D-CT), Victoria Spartz (R-IN) and Brian Fitzpatrick (R-PA). While the bill is identical to Senate version of the NCCDA, the discussion surrounding it is much more explicit for the need of an outbound investment review mechanism. A December 21, 2021 press release from the office of Congresswoman Victoria Spartz states the following regarding the sister bill:

> *This legislation would create a whole-of-government screening process for outbound investments and the offshoring of critical capacities and supply chains to ensure that the United States can quickly detect supply chain vulnerabilities…The COVID-19 pandemic and semiconductor shortages exposed that critical U.S. supply chains were not up to the task in robustly responding to the America's needs. We have to learn from our mistakes and cannot allow outbound investments from the United States to take critical supply chains overseas and into the hands of our adversaries such as China or Russia.*[73]

Again proposing amendments to the Trade Act of 1974, the NCCDA calls for the creation of the Committee on National Critical Capabilities. The composition of this Committee is similar to that proposed in the America LEADS Act. However, an amended Section 1002(b)(2) provides for Ex Officio Members that would serve in a nonvoting role on the Committee. The NCCDA appears to make greater emphasis on the financial side of the equation by also including, among others, the Chairperson of the Securities and Exchange Commission and the Chairperson of the Commodity Futures Trading Commission.[74] The NCCDA covers the same factors of consideration as the America LEADS Act. The most notable difference lies in the definition of a "covered transaction," wherein a *"United States business that engages in a covered transaction shall submit a written notification of the transaction to the Committee."*[75] A proposed Section 1001(5) of the Trade Act of 1974 simply defines this as any transaction by a United States business that:

> *(1) shifts or relocates to a country of concern, or transfers to an entity of concern, the design, development, production, manufacture, fabrication, supply, servicing, testing, management, operation, investment, ownership, or any other essential elements involving one or more national critical capabilities identified under subparagraph (B)(ii);*
> *(2) could result in an unacceptable risk to a national critical capability;*

[71] Brett Fortnam, "Sullivan: White House eyeing outbound investments that undermine export controls". Inside Trade. July 16, 2021
[72] Office of Bob Casey, "Senator Casey Outlines China Policy that Begins with Investments in American Workers and Children". Apr. 30, 2021
[73] Office of Victoria Spartz, "Spartz Introduces the National Critical Capabilities Defense Act". Dec. 21, 2021
[74] S. 1854 — 117th Congress: National Critical Capabilities Defense Act of 2021. May 26, 2021
[75] Ibid.

(3) is designed or intended to evade or circumvent the application of this title, subject to regulations prescribed by the Committee.[76]

Given that the Committee would have authority to define what constitutes a "national critical capability," the NCCDA appears to give much more discretion to the regulating body in determining just what falls under its jurisdiction. Since there are not distinct monetary figures or reference to previously-established statures as in the definition of "covered transaction" in the America LEADS Act, this may cause some initial confusion. However, it may also provide important leeway for the Committee to address the fast-changing and often nebulous risks in this domain.

Another important distinction lies in the definition of "country of concern". Whereas the America LEADS Act focused primarily on the "nonmarket economy" characteristic pursuant to Section 771(18) of the Tariff Act of 1930, the NCCDA additionally draws from the Secure and Trusted Communications Networks Act of 2019's by adding a provision on a "foreign adversary." Specifically, Section 8(c)(2) of the Secure and Trusted Communications Networks Act defines a foreign adversary as *"any foreign government or foreign nongovernment person engaged in a long-term pattern or serious instances of conduct significantly adverse to the national security of the United States or security and safety of United States persons."*[77] Figure 7 summarizes the key sections of the America LEADS Act (2020) with regard to potential outbound investment review whereas Figure 8 does the same for the National Critical Capabilities Defense Act (2021).

Figure 7 – Outbound Investment Review-Related Provisions in America LEADS Act (2020)	
Section	**Title/Description**
Sec. 411. Authority to review inbound and outbound investment	Proposes amendments to the Trade Act of 1974 by inserting "TITLE X — AUTHORITY TO REVIEW INBOUND AND OUTBOUND INVESTMENT"
Title X – Sec. 1001	Definitions
Title X – Sec. 1002	Committee on Production Integrity in the United States
Title X – Sec. 1003	Report on domestic manufacturing and supply chain resilience for critical supplies
Title X – Sec. 1004	Responsible investment reporting requirement
Title X – Sec. 1005	Review of outbound investment
Title X – Sec. 1006	Review of inbound investment
Sec. 412. Establishment of Special Investigations Unit in Office of the United States Trade Representative	Establishes a Special Unit responsible for investigating: a) potential violations of trade agreements to which the United States is a party; and b) other acts, policies, or practices of a foreign government that are unjustifiable, unreasonable, or discriminatory and burden or restrict United States commerce

[76] Ibid.
[77] H.R. 4998 — 116th Congress: Secure and Trusted Communications Networks Act of 2019. Nov. 8, 2019

Figure 8 – Outbound Investment Review-Related Provisions in the National Critical Capabilities Defense Act (2021)	
Section	**Title/Description**
Sec. 2 National Critical Capabilities Reviews	Proposes amendments to the Trade Act of 1974 by inserting "TITLE X — NATIONAL CRITICAL CAPABILITIES REVIEWS"
Title X – Sec. 1001	Definitions
Title X – Sec. 1002	Committee on National Critical Capabilities
Title X – Sec. 1003	Review of covered transactions
Title X – Sec. 1004	Action by the President
Title X – Sec. 1005	Factors to be considered
Title X – Sec. 1006	Supply chain sensitivities
Title X – Sec. 1007	Identification of additional national critical capabilities
Title X – Sec. 1008	Reporting requirements
Title X – Sec. 1009	Requirement for regulations
Title X – Sec. 1010	Requirements related to government procurement
Title X – Sec. 1011	Multilateral engagement and coordination
Title X – Sec. 1012	Authorization of appropriations
Title X – Sec. 1013	Rule of construction with respect to free and fair commerce

VI. Possible Path Forward – A Proposal to Expanded the Use of an OBI-RM

Given the proposals that have been and currently are underway in Congress, it is worthwhile for the United States to seriously consider the establishment of an OBI-RM. As Derek Scissors noted in a July 2020 report titled "Partial Decoupling from China: A Brief Guide", *"Where inbound Chinese investment does not call for new policy tools, outbound US investment in China lacks even basic oversight."*[78] The proposals developed in the time since July 2020 should provide some preliminary guidance in filling that gap. Scissors continued, writing that, *"An outbound version of CFIUS should be established… The new body should act cautiously, but it should also be created quickly because it is overdue."*[79] It is here noted that Scissors' assessment of the situation regarding outbound investment review seems correct. Furthermore, it is advised that the potential establishment of an OBI-RM be considered with three key elements in mind: 1)

78 Derek Scissors, "Partial Decoupling from China: A Brief Guide". American Enterprise Institute. July 7, 2020
79 Ibid.

how such a mechanism could be used as protection against coercive trade practices and for national security purposes; 2) how to leverage an OBI-RM as a negotiating tool for greater trade reciprocity; and 3) that coordination with U.S. allies should be a top priority.

VI(a). Potential Use as a Protection Against FTT and for National Security Purposes

The first and most obvious case for an OBI-RM is toward the aim of countering forced technology transfer practices and addressing other national security considerations. Perhaps the most important development is the growing understanding amongst U.S. policymakers regarding the security threat from China's Military-Civil Fusion (MCF) strategy.[80] This has made clear that a rethinking of how he United States approaches trade and capital flows with China and is certainly an important element to consider with respect to forced technology transfers. As Christopher A. Ford wrote in a June 2020 edition of the Arms Control and International Security Papers, *"Given the centrality of foreign technology acquisition to the PRC's 'Military-Civil Fusion' strategy…this challenge is particularly acuter in arenas of national security, export control implementation and visa screening."*[81] Due to the everchanging nature of MCF strategy and the countless ways it can be implemented, this has made visibility into the problem all the more difficult and has made it apparent that more data is needed. Although Lee Branstetter ultimately argued against granting CFIUS the authority to review outbound investments when such proposals were floated in 2017 and 2018, he does make a very important point with regard to lack of data in the space. As he writes, *"the principal reason forced technology transfer persists is that the US government has never been able to obtain the detailed data necessary to combat it."*[82]

Having a better idea of the threat landscape will be a first and important step to further these objectives, protect U.S. business from FTT and address broader security concerns. Section 1008 of the proposed Title X insertion to the Trade Act of 1974 covers reporting requirements for the Committee on National Critical Capabilities. Section 1008(a)(1)(C) provides for a reporting requirement for the Committee on the covered transactions under Section 1003 over the previous year. In the America LEADS Act, Section 1004 of the proposed Title X insertion also places a reporting requirement on "covered businesses" to submit annual reports to the Committee that identifies:

> *(1) patented technology and processes and any other proprietary information of the business that was sold or disclosed, during the year preceding submission of the report, to another entity in the course of business activities in a nonmarket economy country or with a state-owned enterprise;*
> *(2) any instances of the forced transfer of technology or related processes or information or intellectual property theft or suspected intellectual property theft, during the year preceding submission of the report, in the course of business activities in a nonmarket economy country or related to a state-owned enterprise; and*

[80] U.S. Department of State, "Military-Civil Fusion and the People's Republic of China"
[81] Christopher A. Ford, "Technology Transfers to the PRC Military and U.S. Countermeasures: Responding to Security Threats with New Presidential Proclamation". Arms Cntrol and International Security Papers, Volume 1: Number 9. June 5, 2020
[82] Lee G. Branstetter, "China's Forced Technology Transfer Problem – And What to Do About It". Peterson Institute for International Economics. June 2018

(3) corporate policies of and measures taken by the business to avoid inadvertent disclosure or theft of intellectual property or the forced transfer of technology or related processes or information.[83]

Furthermore, stipulations in the definitions section of the America LEADS Act provide clear criteria for what businesses would be covered by these reporting requirements. 1001(3) defines a "covered business" as:

(1) a publicly traded United States business conducting business activities in nonmarket economy countries or with state-owned enterprises through direct investments, joint ventures, partnerships, or substantial purchase or service contracts valued at more than 10 $100,000,000 per year in the aggregate
(2) any other United States business that produces or imports into the United States more than 5 percent of the total quantity of covered products sold in the United States in a year.[84]

Such a definition would be important so that action regarding outbound investment review is not overly broad and had a clear focus area. This will also help to assuage much of the consternation that came from the business community when a potential OBI-RM was discussed in connection to the FIRRMA in 2017 – 2018.[85] Unfortunately, this ultimately led to a slow-adapting and ineffective substitute in the export control regime under the ECRA. This will also help to curb one of William Reinsch's concerns of *"a wave of filings of benign investments in an excess of caution by nervous investors, which will overload the system"* as elaborated in his August 2021 critique of outbound investment review mechanisms.[86]

While updates may be required to this definition and legislation such as the NCCDA needs to include it moving forward, this can provide a roadmap for future national security policy on outbound investment review. An approach that brings these two reporting requirements together in an efficient way could provide a great deal of well-needed visibility into the problem landscape for the U.S. government. Leveraging more focused data and reports from specific U.S. business entities, a clearer picture can be painted of how Chinese MCF strategy operates and what the U.S. counterstrategy should look like. In addition to the list-based approach of Executive Orders 13959 and 14032, it will give additional insights into local governments of concern, networks of entities and specifics to the nature of attempted FTT.

In a rebuke of the original idea of giving CFIUS jurisdiction over outbound investments during the leadup to the passage of the FIRRMA, Branstetter continues noting that, *"The decision by a multinational to shift production or operations abroad through greenfield investment or acquisition may raise the risks of an accidental transfer or industrial espionage, but firms are in a better position than the government to judge these risks and balance them against potential returns."*[87] While it is certainly the case that firms are in much a better position to conduct a financial cost-benefit analysis and have better visibility into their respective sectors, it does not mean they have the same capacity to review prospective transactions in light of broader national security concerns. Of course, care would need to be taken to ensure that reporting requirements

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[83] Id. 10
[84] Ibid.
[85] Shearman & Sterling, "New CFIUS Law Moves to Protect Emerging Technologies and Personal Information, Takes Aim at Chinese Investment". Aug. 13, 2018
[86] William Alan Reinsch, "Controlling Investment: It Ain't Broke; Why Are We Fixing It?". Center for Strategic & International Studies. Aug. 9, 2021
[87] Id. 81

are not overly burdensome for public and private sector alike and that there are adequate resources and priority are given to the findings of such analyses. Nevertheless, this sort of intelligence collection in the foreign investment landscape appears to be a prerequisite for fully grasping the risk profile faced by individual companies and the U.S. government more broadly. As Derek Scissors writes bluntly, *"It seems obvious that all firms trying to develop technology covered by US export controls should not receive even indirect financial support."*[88]

VI(b). Potential Use as a Negotiating Mechanism

An additional use of an OBI-RM is that can be used strategically as a negotiating tool. Somewhat akin to the process through which tariffs levied on certain Chinese imports were used during the U.S.-China Trade War to get initial commitments to IPR protection on the national level, this can likewise be done through outbound investment review. It can also be a key tool in negotiating reciprocity in market access and perhaps even serve as an enforcement mechanism for the commitments made under the Phase One agreement. Writing in a Council on Foreign Relations Discussion Paper in 2017, Jennifer Harris made it clear that the United States *"should aim for a version of reciprocity that allows it the flexibility to maximize pressure on the broad range of Chinese industrial policy concerns while leaving a clear route to negotiations"* and that *"imposing reciprocity sooner than later is necessary to keep U.S. domestic political economy from warping under Chinese pressure in ways that constrain Washington's ability to enact tougher policies in the future."* [89] Of course, there are multiple routes toward negotiating reciprocity but leveraging an OBI-RM would add an important element to a much-needed multipronged approach. As Harris noted in 2017, *"the most effective tool to administer this form of reciprocity could be section 301(b) of the 1974 Trade Act."*[90] Since there have been important updates to the toolkit since 2017, simultaneous implementation of Section 301 investigatory powers and outbound investment review could serve as a potent combination.

On a more microlevel, an OBI-RM can also give the U.S. a novel tool in addressing transaction-specific concerns and forcing behavior change of Chinese companies or subnational governments. Section 1003(b) of the proposed Title X in the NCCDA provides for the ability to review and make suggestions for mitigating risk connected to a covered transaction. Similar to the Special Security Arrangement that played such a pivotal role in CFIUS' history during the 2006 Lucent Technologies, Inc. acquisition, a review by the appropriate Committee on outbound investment risk could provide businesses that find themselves in such situations a detailed roadmap for reconciling the issues found. The U.S. business in the proposed transaction could then bring this to the table in discussions with the prospective Chinese-based business. So long as there are clear recommendations for addressing concerns provided by the Committee (or other reviewing body), this could serve as an important avenue for promoting behavior change among Chinese entities. It can additionally weed out those entities that did not have benign intentions or were specifically established as part of MCF strategy, while maintaining those that are willing to make appropriate accommodations pursuant to relevant law and U.S. security concerns.

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[88] Id. 77

[89] Jennifer M. Harris, "Writing New Rules for the U.S.-China Investment Relationship". Council on Foreign Relations. Dec. 1, 2017

[90] Ibid.

VI(c). Potential Coordination with U.S. Allies

Of essential import is collaboration with U.S. allies. Such coordination has been a central to the development of export control policy since the end of World War II.[91] While the multilateral nature of export control regimes has faced *"significant challenges that affect their ability to fulfill their key functions,"*[92] a multilateral approach is still the best – and perhaps only – way forward. In a joint report by the U.S. Chamber of Commerce and the Rhodium Group on "Understanding U.S.-China Decoupling," the authors note that *"an approach to decoupling that is targeted and fact-based will be more appealing for U.S. allies and therefore have a better chance of success in the long run."*[93] Zachary Arnold of the Center for Security and Emerging Technology at Georgetown echoed this sentiment in testimony before the U.S.-China Economic and Security Review Commission, stating that, *"any U.S. restrictions on investment in China should be multilateral, better informed, and part of a broader strategy to maintain the technological advantage of the United States and its democratic allies."*[94] With the targeted and fact-based approach that can be achieved by executing the OBI-RM functions listed above, discussions on collaborative outbound investment review policies regarding China can bring forth a new chapter in multilateral security engagement.

On a global scale, investment screening mechanisms have become increasingly central to states' national and economic security policies over the last several years. As the OECD found in a June 2020 report, *"only since 2018 have more than half of the 37 OECD countries had a cross- or multi-sectoral investment screening mechanism in place, compared to less than a third a decade earlier"* and noted developments in France, Japan, Germany, Italy, Korea, Lithuania and many others.[95] The report also noted that the COVID-19 pandemic prompted even further investment review policymaking to address crisis preparedness and the heightened sensitivity to supply chain disruptions. Figure 9 shows the rapid increase of security-related and general investment screening mechanisms amongst OECD members since 1990. While these trends do include screening mechanisms for both inbound and outbound investments, inbound FDI has taken a much larger role in the arena and some key allies do not have any restrictions on nor review of outbound investments. For instance, the State Department 2021 Investment Climate Statement for Japan notes that the nation has no restrictions for outbound investment [96] although it did recently bolster its inbound investment review process under the Foreign Exchange and Foreign Trade Act (FEFTA) in June 2020.[97]

For its part, the European Union has made considerable moves related to investment review in recent years. An investment review framework was established in the EU in 2019 with Regulation 2019/452, which made it *"possible for the Union and the Members States to adopt restrictive measures relating to foreign direct investment on the grounds of security or public order, subject to certain requirements."* However, the policy also stated explicitly that *"outward*

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[91] John H. Henshaw, "The Origins of COCOM: Lessons for Contemporary Proliferation Control Regimes". The Henry L. Stimson Center. May 1993

[92] Kolja Brockmann, "Challenges to Multilateral Export Controls: The Case for Inter-regime Dialogue and Coordination". SIPRI. Dec. 2019

[93] U.S. Chamber of Commerce, "Understanding U.S.-China Decoupling: Macro Trends and Industry Impacts". Feb. 17, 2021

[94] Id. 8

[95] OECD, "Investment screening in times of COVID – and beyond". Jun. 23, 2020

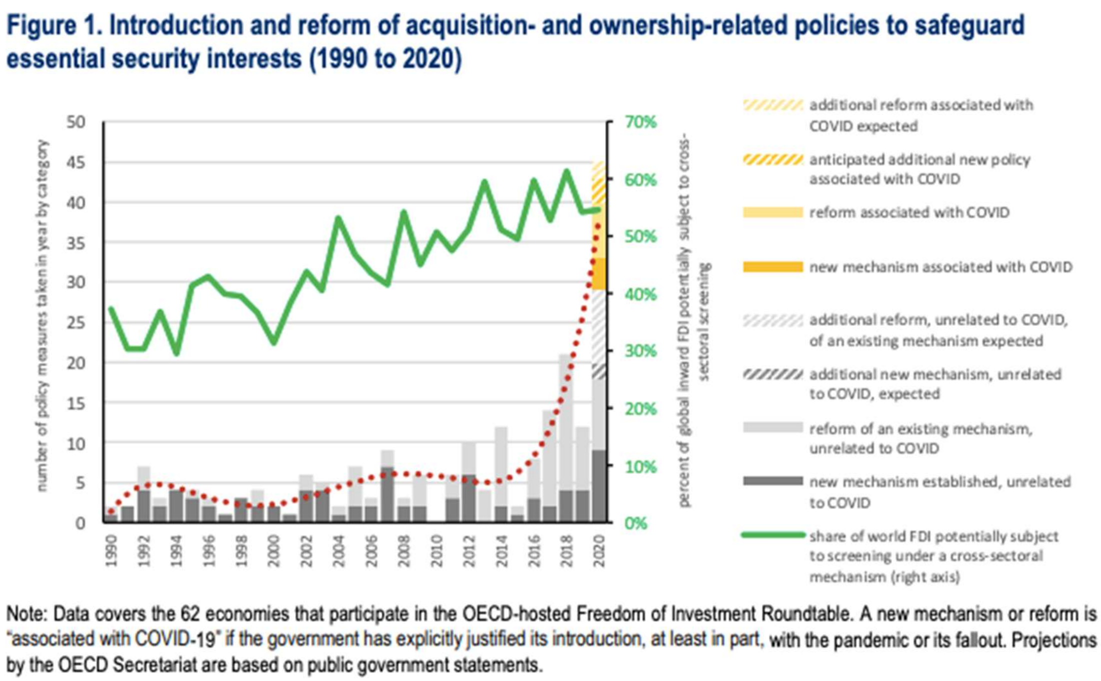
[96] U.S. Department of State, "2021 Investment Climate Statements: Japan"

[97] White & Case, "Foreign direct investment reviews 2020: Japan". Oct. 30, 2020

investment and access to third country markets are dealt with under other trade and investment policy instruments."[98] This framework became fully operational on October 11, 2020 wherein it was stated that the investment screening policies were established in order to *"respond to today's economic challenges, safeguard key European assets and protect collective security"*[99] Mathieu Duchâtel of the European Union Institute for Security Studies characterizes the current happenings in European Union technology and investment controls vis-à-vis China thusly:

> *The coming years will see a restructuring of EU-China relations in the area of investment and technology transfers. On the one hand, the discussion on the adoption of an EU-level investment screening system shows that the EU is creating a more restrictive environment to protect its sensitive technologies from intangible acquisition practices. On the other hand, EU-China interactions will continue to intensify, including in the form of Chinese foreign direct investment (FDI). A new balance will need to be achieved, one that is more beneficial for European interests.*[100]

Figure 9– OECD Figures on Investment Screening Policymaking in Member Countries (1990 – 2020) [101]



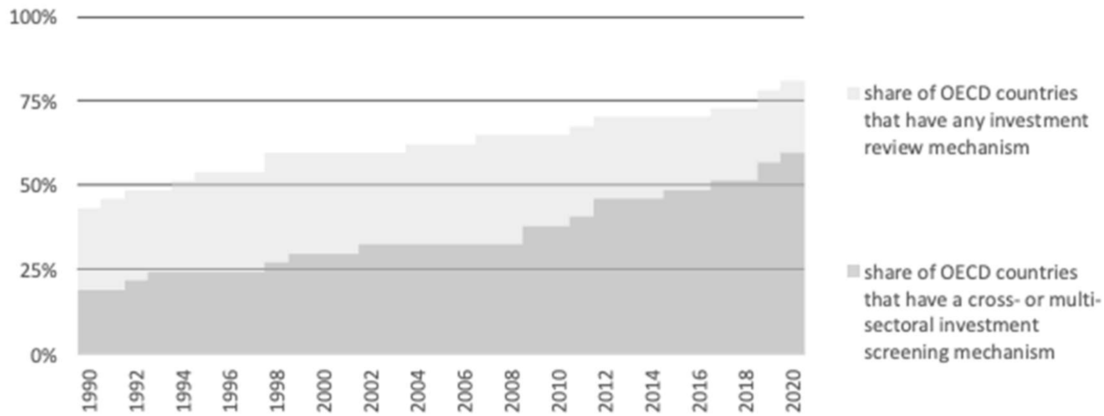
[98] Office Journal of the European Union, "Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union". Mar. 21, 2019

[99] European Commission, "EU foreign investment screening mechanism becomes fully operational". Oct. 9, 2020

[100] Mathieu Duchâtel, "Intangible technology transfers in EU-China relations". Guns, Engines and Turbines: The EU's Hard Power in Asia. Nov. 1, 2018

[101] Id. 94

Figure 2. Evolution over time of the presence of investment screening mechanisms in OECD countries, 1990-2020



Note: Cross- or multi-sectoral screening mechanisms include arrangements that cover all sectors of the economy or a significant number of individually listed sectors.

In a May 2021 paper Zenobia T. Chan and Sophie Meunier conducted an analysis on determinants of EU Member State preferences for an investment screening mechanism (ISM). As they observed, each Member State had unique reasons for their initial support or opposition for a pan-European ISM but found conclusively that, *"the technological level of the country is the most important determinant of national preferences for FDI screening."*[102] Between survey and quantitative analysis, Chan and Meunier ranked the initial preference of EU Member States for a multinational investment review mechanism. The results can be found in Figure 10 and show that Austria, France, Germany, Italy and Poland were all key initial supporters of the EU investment review regime. Such analyses provide important insights in that the United States should have a keen understanding of those allies it seeks to work with in multilateral investment screening practices. Not only will the U.S. be able to identify national champions for its policies, it will also be able to address concerns with those states that remain reluctant. This nuanced dialogue will be especially important if the U.S. is to develop joint investment screening capabilities in both direct and portfolio investment. As Tamar Groswald Ozery of Harvard Law School notes on the danger of going it alone, *"broader restrictions on portfolio investing, especially taken without similar restrictions by other global financial markets, will impose a burden on U.S. asset managers and investors. The industry might be pushed to find creative, costly ways to circumvent the restrictions through 3rd party countries and entities."* [103]

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[102] Zenobia T. Chan & Sophie Meunier, "Behind the screen: Understanding national support for a foreign investment screening mechanism in the European Union". The Review of International Organizations. July 13, 2021
[103] Id. 8

Figure 10 – EU Member State Preferences on Initial Investment Screening Mechanism Development within the European Union [104]

Table 1 Initial National Preferences for the EU-wide Investment Screening Mechanism

Oppose	Somewhat Oppose	Neutral	Somewhat Support	Support
Cyprus	Belgium	Bulgaria	Denmark	Austria
Estonia	Czechia	Croatia	Lithuania	France
Greece	Finland	Slovakia	Spain	Germany
Hungary	Latvia	Slovenia		Italy
Ireland	Luxembourg			Poland
Malta	Netherlands			
Portugal	Romania			
United Kingdom	Sweden			

Highlighting in particular a trilateral approach, Rod Hunter notes that the United States should work in tandem with the EU and Japan with respect to investment screening policy, with the G7 providing a possible platform for such coordination.[105] Importantly, multilateral coordination on investment review is already underway to some degree. On September 29, 2021 the U.S.-EU Trade and Technology Council (TTC) met for the first time in Pittsburgh, Pennsylvania to discuss various issues related to emerging economic and technological trends. In the inaugural joint statement, Annex 1 covered collaboration on investment screening. The TTC outlined the Investment Screening Working Group, which is intended to meet periodically and explore the following areas:

> *1) Exchanges on investment trends impacting security, including strategic trends with respect to industries concerned, origin of investments, and types of transactions;*
> *2) Exchanges on best practices, i.e. risk analysis and the systems for risk mitigation measures, with a focus on sensitive technologies, issues related to access to sensitive data, which may include personal data;*
> *3) Holistic view of the policy tools addressing risks related to specific sensitive technologies;*[106]

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[104] Id. 101
[105] Rod Hunter, "An Allied Response to Chinese Investment". German Marshall Fund of the United States. Apr. 1, 2017
[106] Carisa Nietsche, Emily Kilcrease, & Laura G. Brent, "U.S.-EU Trade and Technology Council Inaugural Joint Statement with Comments from CNAS Experts". Center for a New American Security. Oct. 1, 2021

The establishment of the above working group is an excellent start, although Emily Kilcrease of the Center for a New American Security pointed out that discussions of outbound investment review were "notably missing" from the annex.[107] Hence, there is certainly work to do on this front and it is clear that the United States will not be able to do it alone.

Even though the calls by the Trump administration for revisiting and rethinking the issues with China spurred a new interest among allies, the unilateralism which got the ball rolling is not sustainable. Specifically speaking to portfolio investment restrictions, Teresa Kong of investment firm Matthews Asia noted in prepared remarks for testimony before the U.S.-China Economic and Security Review Commission, *"unilateralism, absent coordination with our allies, could be counterproductive to our policy goals. It might end up putting U.S. investors at a disadvantage by limiting our opportunities in the global capital markets or even lead to losses to investor portfolios."*[108] To this end, Matthew P. Goodman and Dylan Gerstel of the Center for Strategic and International Studies provided some specifics on recommendations for allied coordination in investment review. They propose the establishment of an Allied Technology Control (ATC) group with like-minded countries that could better coordinate technology control regimes. Goodman and Gerstel propose an "Investment Screening Working Group" within the ATC that would develop a "multilateral investment review body" and fulfill the following obligations:

> *1) Facilitate sharing of business confidential information between different governments for foreign inbound investments;*
> *2) Issue opinions to ATC members on the strategic implications of potential investments in and acquisitions of critical technology companies headquartered in allied countries, which would inform national approval decisions;*
> *3) Provide technical assistance to members seeking to establish and strengthen investment screening regimes; and*
> *4) Expedite transactions between companies from ATC members with adequate screening regimes, including by classifying ATC countries as "excepted foreign states" in U.S. regulations.*[109]

With respect to broader trends in investment review (foreign direct investment, venture capital flows, passive portfolio investments, etc.), this will be an even bigger lift than focusing solely on sensitive technology flows when coordinating with allies. Nevertheless, a shared goal of national security and fair market access in certain countries can be the impetus. The NCCDA can again be turned to for the beginnings of a framework. Section 1011 of the proposed Title X to the Trade Act of 1974 within the NCCDA reads in full:

> *The United States Trade Representative—*
> *(1) should, in coordination and consultation with relevant Federal agencies, conduct multilateral engagement with the governments of countries that are allies of the United States to secure coordination of protocols and procedures with respect to covered transactions with countries of concern; and*

[107] Id. 105
[108] Id. 8
[109] Matthew P. Goodman & Dylan Gerstel, "Sharpening America's Innovative Edge". Center for Strategic and International Studies. Oct. 1, 2020

> *(2) upon adoption of protocols and procedures described in paragraph (1), shall work with those governments to establish information sharing regimes*[110]

In tandem with the current workings of the TCC Investment Screening Working Group and proposals such as those by Goodman and Gerstel, these directives to the USTR could provide fertile ground for the development of multilateral coordination in outbound investment review.

Finally, it should be noted that this does not have to be done all at once. In fact, it might be more beneficial to carry out multilateral coordination in a series of tranches, with data and information sharing capacity buildout as the first step. Jason Arterburn, Program Director of the Center for Advanced Defense Studies (C4ADS) sees *"tremendous opportunity for us to work with allies in developing a strategy about how we better leverage cheap, publicly available data sources to make sure that we're directing our expensive assets in the collection and analysis process towards only the most intractable problems, such that that public data can help answer the lowest-hanging fruit, and inform more tailored policy and enforcement responses."*[111] As mentioned previously, the "low-hanging fruit" of data collection is extremely important for the U.S. to gain visibility into the problem space and may prove ultimately to be the primary *raison d' être* for an OBI-RM. Perth Tolle, the founder of Life + Liberty Indexes, makes it clear that this should be a key action step for the U.S. government's response to China:

> *The United States should institute a system that better tracks capital flows in a manner that is accurate, timely, and transparent, and we should encourage our allies to do the same. Indeed, whenever capital from Americans and allied nations are transferred to dangerous actors in any country, we must have a better understanding of the nature, scope, and scale of the problem in order to appropriately address it. We are not quite there yet.*[112]

At the very least, this step of coordination in data and intelligence collection regarding investment flows could be an important initiation to the process. Even if restrictions are not placed immediately, building out these types of partnerships with allies beforehand may prove to be even more fruitful in the long run and the U.S. may be able to get to the place Ms. Tolle envisions in due course.

VII. Conclusion

In summary, the task of building out an outbound investment review mechanism in the United States will be a tall, although necessary, order. Issues such as lack of reciprocity in market access, Military-Civil Fusion strategy and forced technology transfer all compose a constellation of risks that the United States will have to contend with. Derek Scissors gives some important insights in stating that, *"American wealth plus voluntary and involuntary IP transfer have helped advance the PLA. Putting less money into Beijing's hands has the broadest set of benefits. Monitoring and limiting US portfolio investment in China could have denied Chinese entities tens of billions of dollars from 2017 through 2019."* He continues that slowing the flow of money and technology to China will *"reduce the odds of a destructive military conflict."*[113] Though it is unclear just how serious the odds of such a conflict are, it is apparent that the outbound flow of

[110] Id. 73
[111] Id. 8
[112] Ibid.
[113] Id. 77

U.S. technology and capital has provided both benefit and costs. Much of the advantage is reflected in economic data and in the quarterly reports of the businesses that operate in or with China and these benefits should not be overlooked. Nevertheless, the risks are more difficult to quantify and occur at a scale that is much larger and much longer-term. Hence, the creation of an OBI-RM could help in both better understanding the nature of the problem as well as address it in a meaningful way.

By assessing the 2020 America LEADS Act as well as the 2021 National Critical Capabilities Defense Act, the beginnings of an OBI-RM framework are emerging. It remains to be seen precisely how the Biden and future administrations will implement this, but it is one that should be done with a targeted approach. As Adam Lysenko notes, *"effecting capital starvation within our deeply interconnected and globalized financial system is extremely difficult, even if the United States is able to coordinate with like-minded allies on investment restrictions."*[114] Though full capital starvation in and of itself may be too lofty and unnecessary of a goal, targeted application of outbound investment review and monitoring seems like it will be a critical piece of the burgeoning national security policy framework. In order to do this, however, the United States must seriously consider three key aspects in potential construction of an OBI-RM: 1) It should carefully consider its use in curbing technology transfers and security threats by providing statutory authority to a specified entity. Clear guidelines can be found in both previously and currently proposed congressional legislation but may also require updates to account for present risks and resourcing; 2) It should additionally explore areas to use investment review mechanisms for negotiations and support the capacity of covered businesses to do so as well; 3) There is currently a growing trend for countries to develop investment screening mechanisms and this provides a key opportunity for the United States to work with its allies to address issues in global investment flows. Such mechanisms will not work without coordination from international partners and by considering individual states' concerns and combining a number of already extant proposals, the U.S. can get ahead of the curve with regard to multilateral action. With these aspects in mind, the United States is in a solid position to begin such policy development, for outbound investment controls seem like they will surely be an increasingly important tool in the "New Great Game." [115]

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[114] Id. 8

[115] Susan A. Thornton, "China in Central Asia: Is China winning the 'new great game'?". The Brookings Institution. June 2020