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AVIC International a Success: How Regulatory Changes to CFIUS Has Limited Political Interference and Empowered Chinese Investors to Obtain a Successful Review

*Amrietha Nellan**

Chinese businesses are wary of merging or acquiring United States companies due to a perceived hostile regulatory environment. The Committee on Foreign Investment in the United States (“CFIUS”) evaluates mergers and acquisitions of U.S. businesses by foreign companies for national security risks. It may deny the transaction or make recommendations to the President to divest a completed deal if a risk is found. After a string of highly public failed CFIUS reviews against Chinese acquirers, the process seemed insurmountable for Chinese investors. However, the recent success of a Chinese aviation firm, AVIC International, in acquiring a U.S. based aviation company, Teledyne Continental, indicates that the United States is not an impenetrable market for Chinese investors. In particular, AVIC International’s use of the informal prenotice review and mitigation agreement with CFIUS minimized political interference during the formal review and helped ensure a favorable outcome. This note suggests that Chinese investors should follow AVIC International’s strategy rather than being dissuaded from acquiring U.S. companies.

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I. INTRODUCTION

The Great Recession is widely seen as the worst economic crisis since the Great Depression, and has left deep wounds in the American economy.¹ Despite the official end to the recession in 2009, the United States is still recuperating from the millions of jobs lost in the process.² The United States has reported positive economic growth since 2010,³ however, unemployment at the end of 2011 was 8.5 percent, which is over 3 percent the pre-recession unemployment rate.⁴ In order to create more jobs in the United States, the country must stimulate greater economic growth.⁵ One key method of increasing growth is by attracting foreign direct investment (“FDI”) into the United States.⁶

The Obama administration has identified foreign investment as an important element to the country’s road to recovery.⁷ The administration has actively welcomed FDI and has committed itself to making the United States the most attractive place for investment.⁸ In particular, FDI will help accelerate current growth rates while also being the foundation for long-term economic growth.⁹ The administration has been successful at attracting foreign investment, which declined during the recession from 2007 to 2009.¹⁰ However, the key to attracting significant amounts of FDI is attracting China to invest in the United States.

China has the largest foreign exchange reserves of any country,¹¹

1. David B. Grusky, Bruce Western, & Christopher Wimer, *The Great Recession*, RUSSELL SAGE FOUNDATION, <https://www.russellsage.org/publications/great-recession> (last visited Mar. 2, 2012).

2. *Id.*

3. *Data: GDP growth (annual)*, THE WORLD BANK, <http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG> (last visited Mar. 10, 2012).

4. *Database, Tables & Calculators by Subject*, BUREAU OF LABOR STATISTICS, <http://data.bls.gov/timeseries/LNS14000000> (last visited Mar. 2, 2012).

5. See U.S. Department of Commerce, *Assessing Trends and Policies of Foreign Direct Investment in the United States*, INTERNATIONAL TRADE ADMINISTRATION (July 2008), <http://trade.gov/publications/pdfs/fdi2008.pdf>.

6. *Id.*

7. Mary Bruce, *White House Touts Growing Foreign Direct Investment in the U.S.*, ABC NEWS BLOGS (Jun. 20, 2011), <http://abcnews.go.com/blogs/politics/2011/06/white-house-touts-growing-foreign-direct-investment-in-the-us/>.

8. Bruce, *supra* note 7.

9. *Id.*

10. See *Foreign Direct Investment, Net Inflows*, THE WORLD BANK, <http://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD> (last visited Mar. 2, 2012).

11. *China’s Foreign-Exchange Reserves Surge Exceeding \$2 Trillion*, BLOOMBERG (Jul. 15, 2009), <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aZg14B1lt3s>.

a large trade surplus,¹² and is currently the world's second largest economy.¹³ However, China currently spends much less in outward FDI compared to major developed countries. In 2010 China's FDI was 0.67 percent¹⁴ of its GDP, while the major developed countries¹⁵ on average spend over 2 percent¹⁶ of their GDP on FDI. Moreover, China's FDI to the United States is significantly less than major developed countries. In 2010 only 1.9 percent¹⁷ of China's FDI went to the United States, while major developed countries directed more than 10 percent¹⁸ of its total FDI to the United States. This suggests that not only will there be a significant increase in overall Chinese foreign investment as China continues to develop, but that even more so may be directed to the United States if China's investment profile becomes more like developed countries. This huge source of potential investment could very well accelerate growth in the U.S. to the level necessary to bring down unemployment,¹⁹ but this investment is not guaranteed.²⁰

Obviously, the investment from China is not guaranteed for many reasons but one major reason is the belief among Chinese investors that the United States is a difficult place to invest due to political hostility.²¹ In particular Chinese investors point to CFIUS on Foreign Investment in the United States' ("CFIUS") history of thwarting Chinese acquisition of domestic firms.²² Moreover, the

12. *China Balance of Trade*, TRADING ECONOMICS, <http://www.tradingeconomics.com/china/balance-of-trade> (last visited Mar. 2, 2012).

13. *China Overtakes Japan as World's Second-Biggest Economy*, BBC (Feb. 14, 2011), <http://www.bbc.co.uk/news/business-12427321>.

14. *The World Factbook: China*, CENTRAL INTELLIGENCE AGENCY, <https://www.cia.gov/library/publications/the-world-factbook/geos/ch.html> (last visited Mar. 2, 2012); *2010 Statistical Bulletin of China's Outward Foreign Direct Investment*, MINISTRY OF COMMERCE PEOPLE'S REPUBLIC OF CHINA (2010), hzs.mofcom.gov.cn/accessory/2011109/1316069658609.pdf.

15. *A Guide to Committees, Groups, and Clubs, About the IMF*, INTERNATIONAL MONETARY FUND (Sept. 28, 2012), <http://www.imf.org/external/np/exr/facts/groups.htm#G7>.

16. UNCTADSTAT, United Nations Conference on Trade and Development *available at* <http://unctadstat.unctad.org/TableViewer/tableView.aspx> (last visited Mar. 11, 2013). Refer to Appendix I for calculations.

17. *Id.*; See also *2010 Statistical Bulletin of China's Outward Foreign Direct Investment*, MINISTRY OF COMMERCE PEOPLE'S REPUBLIC OF CHINA, Table 1, (2010), hzs.mofcom.gov.cn/accessory/2011109/1316069658609.pdf.

18. UNCTADSTAT, *supra* note 16; OECD.StatExtracts, Organisation of Economic Co-operation and Development *available at* http://stats.oecd.org/Index.aspx?DatasetCode=FDI_FLOW_PAR_TNER# (last visited Mar. 11, 2013). Refer to Appendix II for calculations.

19. David Barboza, *As China Invests, U.S. Could Lose*, N.Y. TIMES, May 4, 2011, www.nytimes.com/2011/05/04/business/global/04yuan.html.

20. *Id.*

21. Barboza, *supra* note 19.

22. Derek Scissors, *A Better committee on Foreign Investment in the United States*, THE HERITAGE FOUNDATION (Jan. 28, 2013), <http://www.heritage.org/research/reports/2013/01/enhancing-the-committee-on-foreign-investment-in-the-united-states-cfius>.

recent divestiture of private Chinese software company Huawei's acquisition of California-based company 3Leaf Systems is seen as proof that politics still sway CFIUS's review and creates an unfair investment environment for Chinese firms despite modern regulatory changes to the process.²³

Despite the contrary example above, Chinese aviation firm AVIC International's successful acquisition of the Alabama-based aviation manufacturing firm Teledyne Continental in 2011 tells a different story.²⁴ The fact that this acquisition was deemed to not implicate national security, in spite of AVIC International being a state-owned enterprise with ties to the Chinese government and in a politically sensitive industry, suggests that the CFIUS review is not politically hostile against all Chinese investors.²⁵ In particular, the complete lack of Congressional interference with the proposed deal indicates a departure from past political pressure on the CFIUS process. Moreover, AVIC International's success in contrast to Huawei's failure indicates that the Chinese party acquirer strategy is a vital factor in minimizing potential political opposition and influencing CFIUS's stance.

The first part of this note will layout the legal framework of CFIUS and the changes made to it by the Foreign Investment and National Security Act, the implementing Executive Order, and the relevant Treasury Regulation. Next, a case study of AVIC International will highlight how these regulatory changes have reduced the level of political intervention in the CFIUS process. This discussion will identify particular changes in CFIUS and its procedures that disincentivize early response by Congress on such transactions and opportunities for foreign investors to limit political scrutiny. Additionally, this note will compare AVIC International with Huawei and identify key strategic differences between the two companies that greatly impacted their interaction with CFIUS and the kind of political reaction to their investment. Finally, solutions to remedy the poor perception of Chinese investors of the United States' CFIUS review will be offered, including the adoption of AVIC International's strategy by future Chinese investors and changes to

23. Chen Weihua, *Pay the Lobbyists to Beat Double Standards*, CHINA DAILY (Mar. 14, 2011), http://www.chinadaily.com.cn/opinion/2011-03/14/content_12164992.htm.

24. *China's AVIC International Completes US Acquisition Deal*, CHINA DAILY USA (Apr. 21, 2011), usa.chinadaily.com.cn/us/2011-04/21/content_12368667.htm; *Teledyne Technologies Agrees to Sell Teledyne Continental Motors to AVIC International*, AVIATIONPROS.COM (Dec. 14, 2010), http://www.aviationpros.com/press_release/10392512/teledyne-technologies-agrees-to-sell-teledyne-continental-motors-to-avic-international.

25. See Edward Sun, *Milbank Advises on First US Acquisition by Chinese Aviation Company*, MILBANK (May 16, 2011), <http://www.milbank.com/news/milbank-advises-on-first-u-s-acquisition-by-chinese-aviation.html>.

the data in CFIUS' annual report to Congress to include individual country information in general and industry breakdowns.

II. THE ORIGINAL CFIUS: EXECUTIVE ORDERS, EXON-FLORIO, AND THE CHINESE EXPERIENCE

CFIUS was established in 1975 by President Ford to help the presidency determine national security risks associated with foreign investment directed to the United States.²⁶ Executive Order 11858²⁷ set up the basic framework of CFIUS, establishing it as an inter-agency²⁸ Committee chaired by the Secretary of the Treasury.²⁹ Executive Order 12661³⁰ provided general guidelines of CFIUS's responsibilities. Executive Order 12661 tasked CFIUS with determining whether particular transactions warranted investigation, and if so, required CFIUS to conduct a 45-day investigation and advise the President of its findings.³¹

Under these Orders, the scope and authority of CFIUS was extremely limited. Firstly, they lacked clear guidelines of what constituted a national security interest that warranted investigation, resulting in minimal voluntary reporting by foreign firms. Therefore, CFIUS relied heavily on recommendations by the Department of Defense as to what transactions to investigate.³² Secondly, the limited investigation timeframe of 45-days greatly limited the capability of CFIUS in conducting thorough investigations.³³ Finally, the limited power of the President to directly alter these foreign transactions, through his power to declare a state of national emergency, similarly limited the power of CFIUS because their investigative findings and advice to the President had minimal actual consequences that could affect such foreign transactions.³⁴

These shortcomings and increasing levels of foreign investment that Congress believed to concern national security resulted in

26. JAMES K. JACKSON, CONG. RESEARCH SERV., RL33388, THE COMM. ON FOREIGN INV. IN THE U.S. 1 (2010), <http://fpc.state.gov/documents/organization/138611.pdf>.

27. Exec. Order No. 11858, 40 Fed. Reg. 20263 (May 7, 1975).

28. Exec. Order No. 11858, at §1.

29. *Id.*

30. Exec. Order No. 12661, 54 Fed. Reg. 779 (Dec. 27, 1988).

31. Exec. Order No. 12661, at §3-201(1)(A).

32. JACKSON, *supra* note 26, at 3.

33. Exec. Order No. 11858, 40 Fed. Reg. 20263 (May 7, 1975).

34. JACKSON, *supra* note 26, at 4.

Congress passing the Exon-Florio amendment in 1988.³⁵ Exon-Florio authorizes the President to investigate any merger or acquisition of United States companies by foreign persons that may result in shifting control over to these foreign entities.³⁶ Additionally, it empowers the President to block or divest any transaction where there is “credible evidence”³⁷ that the transaction could “impair national security,”³⁸ but only if all other presidential authority to remedy such risk of impairment would not be feasible.³⁹ Moreover, the Treasury Department’s final regulation implementing the amendment stipulates that the President can request an investigation of a transaction that has not already been investigated at any time and divest the transaction if warranted.⁴⁰ Though the President is given this power, CFIUS implements the amendment as the designated entity conducting the investigation into the national security implications of the foreign transaction.⁴¹

As a result, the CFIUS process was bolstered by the additional direction contained within the amendment. The amendment directed CFIUS to determine the effects of the transaction on the national security of the United States by considering eleven specific areas of concern regarding national security.⁴² This focused CFIUS’s investigation by providing a more concrete definition of national security. Moreover, CFIUS is now instructed to conduct an initial 30-day review, and if national security concerns are not addressed in that time, may initiate an additional 45-day investigation.⁴³ This additional time expanded CFIUS’s ability to conduct thorough investigations. Most importantly, the President’s power to block or divest a transaction greatly increased the power of CFIUS’s national security determination. Thus, Exon-Florio transformed CFIUS into an administrative body “with a broad mandate and significant authority to advise the President” and determine the outcome of foreign investment in the United States.⁴⁴

In 1991, Congress provided even more direction to CFIUS

35. Leon G. Greenfield & Peter Lange, *The CFIUS Process: A Primer*, 6 THE THRESHOLD 10, 10 (Winter 2005/2006), available at <http://www.wilmerhale.com>.

36. *Id.*

37. 50 U.S.C.A. app. § 2170 (West 2007).

38. *Id.*

39. *Id.*

40. JACKSON, *supra* note 26, at 5.

41. 50 U.S.C.A. app. § 2170; Exec. Order No. 12,661, 54 F.R. 779 (1988).

42. 50 U.S.C.A. app. § 2170.

43. DAVID N. FAGAN, DELOITTE, THE U.S. REGULATORY AND INSTITUTIONAL FRAMEWORK FOR FDI 15 (2010), available at [http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/us_csg_ColumbiaFaganPaper_Chinese031809\(3\).pdf](http://www.deloitte.com/assets/Dcom-UnitedStates/Local%20Assets/Documents/us_csg_ColumbiaFaganPaper_Chinese031809(3).pdf).

44. JACKSON, *supra* note 26, at 5.

through the “Byrd Amendment” to Exon-Florio.⁴⁵ The Byrd Amendment requires CFIUS to investigate proposed mergers, acquisitions, or takeovers when the acquirer is controlled by or acting on behalf of a foreign government and the acquisition may result in control of a person engaged in interstate commerce in the United States that could affect the national security of the country.⁴⁶ This amendment added to the list of characteristics of what may constitute a national security risk, and for the first time, it created a situation where an investigation was mandatory.

This framework for the CFIUS review disproportionately impacted Chinese investors. First, almost all of the Chinese investors were state-owned enterprises often triggering a mandatory investigation under the Byrd Amendment. Secondly, Chinese foreign investment has typically focused on acquiring know-how and technology, which implicates national security concerns under Exon-Florio.⁴⁷ Thus, Chinese investors looking to acquire U.S. firms would almost certainly be subject to the CFIUS review. Chinese investors felt this was unfair, because the regulations seemed to target their investments and subject them to heightened CFIUS review. This concern was further buttressed when, for the first and only time, the Presidential divestiture power was exercised under Exon-Florio against China Aero-Technology Import and Export Corporation’s acquisition of MAMCO Manufacturing Company.⁴⁸

Despite CFIUS’s increased ability to regulate foreign acquisitions, Congress was still not satisfied with the process. First, Congress was unhappy with the secrecy of CFIUS’s operations, because the secrecy hampered Congress’s ability to assess the thoroughness and accuracy of CFIUS’s investigations.⁴⁹ Moreover, Congress believed that the current scope of CFIUS’s national security analysis was too limited for modern day concerns.⁵⁰ This resulted in significant changes to CFIUS and their investigation.

45. JACKSON, *supra* note 26, at 6.

46. 50 U.S.C.A. app. § 2170.

47. Nargiza Salidjanova, GOING OUT: AN OVERVIEW OF CHINA’S OUTWARD FOREIGN DIRECT INVESTMENT, U.S.-CHINA ECONOMIC AND SECURITY REVIEW COMMISSION, 17 (Mar. 30, 2011), *available at* <http://www.uscc.gov/Research/going-out-overview-china-outward-foreign-direct-investment>.

48. Lawrence R. Fullerton, et al., *Review of Foreign Acquisitions Under the Exon-Florio Provision* 151–52 (Am. Bar Ass’n Section of Antitrust Law, Working Papers, Nov. 25, 1992), *available at* <http://books.google.com>.

49. JACKSON, *supra* note 26, at 2.

50. *Id.*

III. THE NEW AND IMPROVED CFIUS: FINSA, EXECUTIVE ORDER, AND TREASURY REGULATION

The Foreign Investment and National Security Act (FINSA) was passed in 2007 to amend Exon-Florio and in January 2008 President Bush issued Executive Order 13456 implementing the law.⁵¹ Later that year, the Treasury Department published regulatory guidelines on FINSA and the amended CFIUS review.⁵² Together, FINSA and the Treasury regulations formalized CFIUS's practice of informal pre-notice review and mitigation agreements with foreign investors, expanded the scope of national security issues, changed the composition of CFIUS, and heightened CFIUS's accountability to Congress.⁵³

Prior to the passage of FINSA, CFIUS would entertain informal reviews of proposed transactions.⁵⁴ These informal reviews gave CFIUS more time to conduct their investigations by easing compliance with the strict 30-day timeframe that commenced once official notice is filed.⁵⁵ Though FINSA does not specifically allow this practice, the Treasury Regulation encourages voluntary notice and CFIUS, more specifically, expresses its preference for informal review.⁵⁶ Thus, the lack of mention in FINSA for a specifically required practice for review has helped establish the informal review as a formalized step in the review process.

On the other hand, FINSA explicitly codifies CFIUS's practice of negotiating mitigation agreements with parties when there are initial national security concerns.⁵⁷ Under the Act, CFIUS can "enter into, or impose, and enforce" any condition in order to "mitigate any threat to the national security of the United States that arise as a result of the covered transaction."⁵⁸ The act further requires CFIUS to conduct a "risk-based analysis" before imposing any mitigating conditions on the parties to the transaction.⁵⁹ This practice has worked for the benefit of the parties, because it allows CFIUS to approve of more transactions despite initial security concerns. Moreover, in combination with the pre-notice informal review, many

51. JACKSON, *supra* note 26, at 2.

52. Guidance Concerning the National Security Review Conducted by CFIUS on Foreign Investment in the United States, 73 Fed. Reg. 74567 (Dec. 8, 2008).

53. JACKSON, *supra* note 26, at 14.

54. *Id.* at 18.

55. *Id.*

56. Guidance Concerning the National Security Review Conducted by CFIUS on Foreign Investment in the United States, 73 Fed. Reg. 74567 (Dec. 8, 2008).

57. Foreign Investment and National Security Act, 50 U.S.C. § 2061 (2007).

58. *Id.*

59. *Id.*

parties can implement these changes prior to the formal notice ensuring an expeditious and successful outcome from the CFIUS review process.

Besides retaining the key practices of CFIUS, FINSA was also a response to perceived weaknesses in CFIUS's analysis of national security issues.⁶⁰ To address this concern, FINSA and the Executive Order made various changes to the composition of CFIUS. The Act officially added the Secretary of Homeland Security onto CFIUS as a voting member, resulting in CFIUS having seven voting members, including the Secretary of State, the Secretary of the Treasury, the Secretary of Defense, the Secretary of Homeland Security, the Secretary of Energy and Commerce, and the Attorney General.⁶¹ The implementing Executive Order added five observing members—the Director of the Office of Management and Budget, the Chairman of the Council of Economic Advisors, the Assistant to the President for National Security Affairs, the Assistant to the President for Economic Policy, and the Assistant to the President for Homeland Security and Counterterrorism—who have a duty to report to the President under certain situations.⁶² Additionally, the Order reserves for the President the right to appoint any temporary member. These changes to CFIUS provide a more comprehensive perspective as to the economic and security consequences of the transactions.

Finally, FINSA requires extensive reporting requirements by CFIUS to Congress in order to overcome the secrecy of its investigations. Under FINSA CFIUS must provide an annual report to Congress that includes information on “investment trends with respect to types of investments, investors’ nationality, targeted sectors of the United States industry, and practices adopted by foreign acquirers.”⁶³ Moreover, CFIUS must notify Congress of each transaction they investigate after CFIUS has concluded its review.

All these changes to CFIUS aimed to improve CFIUS's functioning to adequately protect Congress's national security concerns regarding foreign transaction. Ultimately, this increased mandate on CFIUS to consider Congress's concerns changed the relationship between Congress and CFIUS by alleviating the need of Congress to intervene in particular transactions. This essentially has

60. Edward L. Rubinoff & Tatman Ryder Savio, *CFIUS Implements FINSA to Exon-Florio Foreign Investment Law*, THE METROPOLITAN CORPORATE COUNSEL 33, 33 (May 2008).

61. JACKSON, *supra* note 26, at 8.

62. *Id.* at 8–9.

63. Ronald A. Oleynik & Antonia I. Tzinova, *CFIUS Reform Brings More Transparency to the Foreign Investment Review Process*, THE METROPOLITAN CORPORATE COUNSEL, Oct. 1, 2007, at 5.

given CFIUS more autonomy in their investigations, and has reduced the political intervention in foreign transactions as evidenced by the AVIC International deal.

IV. THE AVIC INTERNATIONAL CASE STUDY

A. Regulatory Changes Limiting Political Interference

In April of 2011, AVIC International completed its acquisition of Teledyne Continental Motors' general aviation piston engine manufacturing business for \$186 million.⁶⁴ AVIC International is the international branch of China Aviation Industry Corporation ("AVIC").⁶⁵ AVIC is the modern incarnate of the China National Aero-Technology Import and Export Corporation ("CATIC"), which is associated with China's Ministry of Aerospace Industry and is one of China's largest state-owned enterprises.⁶⁶ AVIC International engaged in pre-notice review, filed a voluntary notice with CFIUS, agreed to specific mitigating conditions, and was approved within the 30-day review period.⁶⁷

AVIC International's experience with CFIUS was largely void of direct political interference by Congress. This is a marked departure from past Chinese acquisitions in sensitive industries, where it was typical for Congress to directly intervene in the CFIUS review and pressure foreign parties to withdraw their bid before a decision can be rendered. For example, in 2005, China's National Offshore Oil Corporation ("CNOOC") bid to acquire United States oil company Unocal.⁶⁸ Within days of the offer, members of Congress expressed their fears that CFIUS would approve a CNOOC-Unocal deal because their narrow mandate would not be capable of a full assessment of the risks.⁶⁹ This resulted in the House of

64. *Teledyne Completes Sale of its Piston Engine Business*, BUSINESSWIRE (Apr. 19, 2011), <http://www.businesswire.com/news/home/20110419007015/en/Teledyne-Completes-Sale-Piston-Engine-Business>.

65. AVIC INTERNATIONAL, www.avic-intl.cn/avicIntl/home/index.do?cmd=goToChannel&cid=328, (last visited Mar. 2, 2012).

66. *Id.*

67. Sun, *supra* note 25; Charles A. Hunnicutt, *\$2 Million deal = Big CFIUS Mistake*, TROUTMAN SANDERS (Mar. 7, 2011), <http://www.troutmansanders.com/2-million-deal--big-cfius-mistake-03-07-2011/>.

68. GARY CLYDE HUFBAUER, YEE WONG & KETKI SHETH, *US-CHINA TRADE DISPUTES: RISING TIDES, RISING STAKES* 47 (2006), available at http://www.piie.com/publications/chapters_preview/3942/05iie3942.pdf.

69. Hufbauer, *supra* note 68, at 47.

Representative passing various bills to delay the CFIUS review process.⁷⁰ Since there was no guarantee CFIUS would approve the acquisition, the delay made the acquisition too risky and expensive for CNOOC causing CNOOC to withdraw its bid.⁷¹ The next year, a study by the Department of Energy found that China's national oil companies were not a threat to the United States economy and suggested that if CFIUS completed an investigation, the Department of Energy may have approved the deal.⁷² Thus, Congress's political concerns broke up a potentially valid foreign acquisition.

AVIC International's experience indicates a departure from this kind of meddling relationship between Congress and CFIUS considering the fact that the deal was approved without petitioning by Congress members. This change can be traced to the regulatory changes to CFIUS through FINSA and the implementing Executive Order. These changes effectively safeguarded against Congress's concerns with CFIUS's process, thus reducing the need for direct intervention into CFIUS's review.

One of FINSA's main accomplishments was formalizing CFIUS's practice of informal prenotice review and mitigation agreements.⁷³ Formalizing these two practices gave foreign investors a way to begin the process without attracting the attention of Congress and disincentivized Congressional interference during CFIUS's review. Investors can use the prenotice informal review prior to even a formal bid for acquisition or merger.⁷⁴ This is extremely beneficial for all investors because it allows the investor to get a review and feedback from CFIUS prior to any media or political backlash to the potential deal. Investors such as AVIC International are increasingly using this option to better situate their company and the details of the acquisition before formal notice.⁷⁵ Thus, this prenotice review allows foreign investors to escape early political opposition that may undermine a deal that may not have real security implications upon further investigation.

Additionally, formalizing the mitigation capabilities of CFIUS greatly reduces Congress's incentive to intervene prior to a complete CFIUS review. FINSA established a broad power of CFIUS to not

70. Hufbauer, *supra* note 68, at 48.

71. *Id.*

72. *Id.* at 50.

73. Guidance Concerning the National Security Review Conducted by CFIUS on Foreign Investment in the United States, 73 Fed. Reg. at 74,572 (Dec. 8, 2008).

74. Amy E. Worlton, John Reynolds & Cari Stinebower, *New CFIUS Rules Largely Codify Existing Practice, Including Increased Scrutiny*, WILEY REIN (Apr. 2008), www.wileyrein.com/PUBLICATIONS.CFM?SP=ARTICLES&ID=707.

75. Leon G. Greenfield & Peter Lange, *The CFIUS Process: A Primer*, The Threshold – The Newsletter of the Mergers & Acquisitions Comm., Vol. VI Issue 1 at 13.

only suggest but also force certain conditions onto a foreign investor in order to mitigate national security concerns.⁷⁶ This process essentially obviates the need for Congress to intervene during the investigation because the mitigation agreement may completely eliminate the concern. AVIC International agreed to a long list of mitigating conditions including promises to retain manufacturing in Alabama, expand the manufacturing facility, and retain local employees.⁷⁷ This effectively addressed the key political concern of a foreign takeover of a major employer in Alabama, eliminating the need for Congressional interference.⁷⁸ Thus, formalizing mitigation agreements delays political intervention into the CFIUS investigation, and allows CFIUS to complete their initial review independently.

FINSA and the Executive Order's changes to the composition of CFIUS has expanded the perspectives represented in CFIUS. In particular, adding members whose focus is national security rather than economic has instilled greater Congressional trust in CFIUS's investigation and recommendations.⁷⁹ Prior to FINSA, members of Congress had expressed concerns for the motivations of the Treasury and Commerce Secretaries.⁸⁰ Though the Secretaries were tasked to consider national security concerns as members of CFIUS, the departments they represent are generally pro-investment.⁸¹ Thus, Congress often was not confident that reviews primarily conducted by either Secretary would give enough weight to security issues.⁸² Congress's confidence in the review was improved by adding the Secretary of Homeland Security as well as five observing members to balance the pool of perspectives in CFIUS; this reduced Congress's motivation to interfere.

Moreover, the required reporting requirements have relaxed the extent of direct Congressional intervention in CFIUS's practices and investigations.⁸³ The requirement that CFIUS must inform Congress of every transaction after it conducts its investigation ensures that Congress is aware of every potential deal.⁸⁴ This essentially reduces Congress's scrutiny of proposed mergers and acquisitions it comes

76. 50 U.S.C.A § 2170 (West 2012).

77. *Teledyne Technologies Agrees to Sell Teledyne Continental Motors to AVIC International*, *supra* note 24.

78. *Id.*

79. Alan P. Larson & David M. Marchick, *Foreign Investment and National Security: Getting the Right Balance*, COUNCIL OF FOREIGN RELATIONS 13 (July 18, 2006), i.cfr.org/content/publications/attachments/CFIUSreport.pdf.

80. *Id.*

81. *Id.*

82. *Id.*

83. 50 U.S.C. § 2061 (West 2007).

84. 50 U.S.C. § 2061.

across in the media, because Congress can rely on CFIUS notifying them with sufficient time to act if Congress sees fit. As in the case of AVIC International, the company had already begun discussions with CFIUS prior to any media publication of the proposed deal, allowing for an objective review by CFIUS.⁸⁵ This is especially beneficial for Chinese investors with initial security issues, because they have time to work out those issues before Congress examines the deal, unlike the CNOOC incident where Congress intervened beforehand.

However, Huawei critics argue that CFIUS's review is still subject to political interference as evidenced by the petitioning by Congressional members for CFIUS to review Huawei's acquisition and their accusations that Huawei was connected to the People's Liberation Army (PLA).⁸⁶ Huawei does present a more politically active situation than AVIC International. However, Congress's petitioning only resulted in CFIUS requiring Huawei to file a notice for investigation.⁸⁷ CFIUS was able to complete their investigation without being delayed or otherwise obstructed by Congress and individually determined there was a national security issue.⁸⁸ Thus, even Huawei's experience indicates that FINSA and the Executive Order has successfully minimized political intervention into CFIUS's review.

However, one might argue that the political intervention by Congress has merely changed form, from directly interfering with CFIUS, to covertly interfering by influencing CFIUS's decision itself. This argument is supported if Huawei's contention that it does not have any connection with the PLA is true, since CFIUS's national security analysis seems to rest on this issue.⁸⁹ However, many sources confirm that Huawei's ownership structure is very opaque making it difficult to definitively dispel its purported connection with the PLA.⁹⁰ Thus, CFIUS's decision was ultimately based on existing national security concerns rather than Congressional pressure for a particular outcome.

Huawei does have an argument that the accusation by Congress

85. *Teledyne Technologies Agrees to Sell Teledyne Continental Motors to AVIC International*, *supra* note 24.

86. Dan Ikenson, *Despite Huawei's Experience America is Increasingly Open to Chinese Investment*, FORBES (Feb. 23, 2011), <http://www.forbes.com/sites/beltway/2011/02/23/despite-huaweis-experience-america-is-increasingly-open-to-chinese-investment/>.

87. *Id.*

88. Ikenson, *supra* note 86.

89. Paul Weiss, *Huawei Resists CFIUS Demand to Divest U.S. Technology Firm*, CURRENT TELECOM DEVELOPMENTS (Feb. 18, 2011), <http://www.paulweiss.com/files/Publication/727b4a08-a98c-4610-a01f-7f8fb2af2f29/Presentation/PublicationAttachment/1f71cd47-3459-47f6-bd74-80492f937953/CTD2-18-11.pdf>.

90. Ikenson, *supra* note 86.

tainted the overall CFIUS review and subjected Huawei to heightened scrutiny by CFIUS. Essentially, if Congress never said that it believed that Huawei was connected to the PLA, when CFIUS reviewed Huawei's ownership structure the fact there was no clear indication of a connection would have been enough. Instead, CFIUS had to disprove the connection. This may be true, and the regulatory changes are not equipped to deter this kind of interference by Congress. However, this kind of bias from statements by political leaders on the CFIUS review is not inherent in the process as evident by the AVIC International deal. In fact, AVIC International suggests that even this form of subtle political influence on CFIUS can be avoided by key strategic choices by the Chinese investor.

B. Chinese Investor Strategy

AVIC International's success in contrast to Huawei's failure is extremely significant. Both companies have ties to the Chinese government⁹¹ and both tried to acquire businesses in key industries of importance to national security,⁹² suggesting that the reason for a particular CFIUS decision under such conditions does not rest on a general bias against Chinese government affiliated companies. Instead, a close examination of AVIC International's approach to the investment compared to Huawei indicates that the Chinese investor's strategy is a vital factor in the CFIUS review.

A key difference between AVIC International's and Huawei's strategies was the fact that AVIC International voluntarily filed with CFIUS while Huawei only filed after it was asked by CFIUS to do so.⁹³ This was a major misstep for Huawei because it raised suspicion within CFIUS before the review even began. CFIUS not only inferred from the lack of notice that Huawei was trying to avoid review,⁹⁴ but also looked at the small dollar amount of the deal (\$20 million) as another deliberate action by Huawei to complete the acquisition under CFIUS's radar.⁹⁵ Thus, not voluntarily filing with CFIUS is looked at as a red flag to scrutinize the transaction more closely to determine whether the investor was trying to avoid

91. Ikenson, *supra* note 86; AVIC INTERNATIONAL, *supra* note 65.

92. AVIC INTERNATIONAL, *supra* note 65.

93. Ikenson, *supra* note 86; *Teledyne Technologies Agrees to Sell Teledyne Continental Motors to AVIC International*, *supra* note 24.

94. Scott M. Flicker & Dana M. Parsons, *Huawei-CFIUS Redux: Now It Gets Interesting*, PAUL HASTINGS STAY CURRENT (Mar. 2011), www.paulhastings.com/assets/publications/1868.pdf.

95. Ikenson, *supra* note 86.

CFIUS's review because of an existing national security issue.

Huawei advisors stated that they avoided filing notice, because Huawei had been implicated by the United States government in previous transactions as having a connection with the Chinese military. In 2010, Huawei's attempted joint deal to buy out United States telecommunications company SprintNextel was heavily opposed by members of Congress due to the belief that Huawei had ties to the PLA and access to SprintNextel's network would leave U.S. airwaves vulnerable to military interceptions.⁹⁶ Huawei adamantly denied such association. However, the opposition from Congress pressured Huawei to withdraw its bid prior to a complete CFIUS review.⁹⁷ Huawei stated that it believed it would be unfairly treated if it notified CFIUS as in the SprintNextel deal and structured the deal merely to avoid that bias.⁹⁸ However, AVIC International also has had a troubled history with CFIUS. Thus its current success indicates that past behavior does not necessarily prejudice the present analysis by CFIUS.

AVIC's old alias CATIC, tried to acquire MAMCO in 1990.⁹⁹ The transaction was subject to CFIUS review because the technology purchased may have had military applications.¹⁰⁰ CFIUS ultimately recommended to the President to divest the company, due to CATIC's prior violations of United States export regulations for purchasing prohibited materials for the Chinese military and CATIC's association with the Chinese Ministry of Aerospace Industry.¹⁰¹ CATIC's past history with CFIUS is very similar to the issues Huawei faced in the SprintNextel deal, but AVIC International's voluntary notice did not suffer due to this. Rather, the voluntary notice led to a thorough investigation, which found a very different organization that did not implicate national security concerns.¹⁰² Thus, Huawei's strategy of non-notice to avoid bias does not seem necessary because AVIC International shows that CFIUS is able to move on from past indiscretions provided that the investigation warrants such a result.

Huawei's argument may have more force if one considers the

96. Weiss, *supra* note 89.

97. *Id.*

98. Flicker & Parsons, *supra* note 94.

99. Lawrence R. Fullerton et al., *Review of Foreign Acquisitions Under the Exon-Florio Provision* 151 (Am. Bar Ass'n Section of Antitrust Law, Working Papers, Nov. 25, 1992), available at <http://books.google.com>.

100. *Id.* at 151.

101. *Id.* at 151–52.

102. Dara A. Panahy & Li Chen, *CFIUS Challenges for China Companies Investing in the U.S.*, MILBANK, <http://transasialawyers.com/publicfiles/N2-Milbank-E.pdf> (last visited Mar. 2, 2012).

timeframe between each company's prior unsuccessful interaction with CFIUS and the current transaction. More than twenty years passed between AVIC International's transactions, while only about one year passed between Huawei's transactions. This suggests that the length of time between transactions allowed for the bias to subside against AVIC International while the short time between transactions means that even if Huawei voluntarily notified CFIUS the bias would have still impacted the decision. This argument definitely has support, because the press surrounding AVIC International's acquisition did not mention the company's past as CATIC. Also, the mitigating conditions to the deal focused on domestic labor issues rather than technology or privacy, indicating that CFIUS was not concerned that AVIC International would repeat those practices.¹⁰³ Despite the strength of this argument, Huawei's strategy still failed, because the lack of notice ultimately exacerbated the bias. Huawei's action of completing an acquisition in an industry with similar national security concerns as the SprintNextel deal so soon after without notice was a signal to CFIUS that those concerns still exist warranting an investigation.¹⁰⁴ Thus, the potential existence of bias is a reason to voluntarily notify CFIUS in order to challenge that preconceived belief against the foreign investor.

Another key difference between AVIC International's and Huawei's strategy is that AVIC International took substantial steps to change its image between the CATIC-MAMCO divestiture and the Teledyne acquisition. CATIC was criticized for purportedly buying engines for business purposes but in fact giving it to the Chinese military to reverse engineer.¹⁰⁵ Thus, the main security concern with CATIC at the time of the MAMCO deal was that it was connected with the Chinese military and its business dealings were not purely economically motivated. Since then, AVIC International changed its business structure, established itself as an internationally competitive company, and has worked on its reputation within the aviation industry. These changes shifted the dynamics of this company's interaction with the United States government, undermining the government's ability to lodge its old opposition to the current investment.

In 2008, after the CATIC-MAMCO incident, CATIC changed its corporate structure.¹⁰⁶ AVIC and AVIC International were created

103. *Teledyne Technologies Agrees to Sell Teledyne Continental Motors to AVIC International*, *supra* note 24.

104. Ikenson, *supra* note 86.

105. LAWRENCE R. FULLERTON & CHRISTOPHER G. GRINER, REVIEW OF FOREIGN ACQUISITIONS UNDER THE EXON-FLORIO PROVISION 150-51 (1992).

106. AVIC INTERNATIONAL, *supra* note 65.

as equal shareholders of CATIC.¹⁰⁷ The military arms trade business was separated out from AVIC and AVIC International as CATIC's sole practice.¹⁰⁸ This structural change created a degree of separation between AVIC International's business practice from its past military dealing, essentially diluting the potential government influence on the company's foreign business activities. AVIC International still holds a 50 percent stake in CATIC and its military arms business,¹⁰⁹ so it is not void of a connection to the Chinese military; however, this restructuring goes a long way to clarify the relationship and create transparency in AVIC International's business dealings.

Additionally, AVIC International became an international player in the aviation industry by aggressively expanding its presence and network of trade partners across the world. AVIC International company motto is to "build up a multinational corporation with international competitiveness."¹¹⁰ Since 2008, AVIC International has established over 60 overseas branches in over 30 countries and has clients in over 180 countries.¹¹¹ Moreover, AVIC International has been on the Fortune 500 list since 2009.¹¹² All these factors indicate the company's commitment to the international economy and the furtherance of their business, thus shifting the presumption that the company has ulterior motives to one that is market-driven.

Finally, AVIC International has established a solid reputation within the aviation industry as a company with quality aviation products and as a successful exporter. This is reinforced by the fact that Teledyne completed the deal with AVIC International because they were confident AVIC International would help Teledyne expand internationally and make it competitive in the modern market.¹¹³ Additionally, AVIC International has contracts with the leading firms in the business, including a long-standing supply relationship with Boeing and technological and manufacturing partnerships with Hamilton Sundstrand and Safran.¹¹⁴ By establishing itself as a key player within the aviation industry, AVIC International repositions itself from being a major Chinese state-owned aviation company to

107. AVIC INTERNATIONAL, *supra* note 65.

108. *Id.*

109. *Id.*

110. *Id.*

111. *Id.*

112. Xin Dingding, *Aerospace Firm AVIC in Fortune Rank List*, CHINA DAILY (July 10, 2009), http://www.chinadaily.com.cn/bizchina/2009-07/10/content_8406574.htm.

113. *Teledyne Technologies Agrees to Sell Teledyne Continental Motors to AVIC International*, *supra* note 24.

114. Jon Grevatt, *Paris Air Show 2011: AVIC Expands International Partnerships*, IHS (June 21, 2011), <http://www.janes.com/products/janes/defence-securityreport.aspx?id=1065929845>.

being a major aviation company, period. Together, these changes to AVIC International's business structure and practices undermines Congress's ability to influence CFIUS's review with past security concerns, further insulating the deal from political intervention.

Huawei by contrast, did not take any remedial steps to address the concerns Congress lodged against its earlier deal with SprintNextel before acquiring 3Leaf Systems. This allowed Congress to reassert its previous concerns regarding Huawei, inciting CFIUS to review the transaction. Congress's concerns ultimately were the basis of CFIUS's recommendation to divest. Huawei could have limited the influence of past security concerns by taking bona fide measures to weaken Congress ability to use the same argument against their future investments. In particular, AVIC International's structural change is instructive for Huawei as a viable option to dispel fears of its connection with the PLA.

However, Huawei might argue that the changes AVIC International undertook were not the reasons for the lack of political opposition, since Huawei is also a multinational corporation, on the Fortune 500 list, the second largest telecommunications company in the world, and in fact is a private business as opposed to a state-owned enterprise, and yet was still not successful under CFIUS's review.¹¹⁵ These similarities between AVIC International and Huawei are poignant and do indicate these characteristics alone are not enough to change political perception of a Chinese investor. However, Huawei assumed all these characteristics by the time of the SprintNextel acquisition and not between the SprintNextel deal and 3Leaf Systems deal.¹¹⁶ This reinforces AVIC International's strategy that the key tactic in limiting past political opposition is to engage in substantive changes between the negative review and the present deal.

Overall, AVIC International's success indicates that CFIUS is to Chinese investors. More importantly, AVIC International has laid a roadmap of how Chinese investors can steer their interaction with CFIUS in a positive direction. Through strategic choices such as using the pre-notice informal review and taking steps to challenge the ability of Congress to pose political opposition, Chinese investors have the power to set themselves up for a speedy and successful CFIUS review despite past problems with CFIUS.

115. Sheridan Prasso, *What Makes China Telecom Huawei so Scary?*, CNNMONEY (July 28, 2011), <http://tech.fortune.cnn.com/2011/07/28/what-makes-china-telecom-huawei-so-scary/>.

116. *Id.*

VI. RECOMMENDATIONS

AVIC International's successful acquisition of Teledyne indicates that the CFIUS process is not necessarily hostile to Chinese investors. AVIC International's overall approach to the CFIUS review, specifically using FINSA's pre-notice review and mitigation agreement and voluntarily filing with CFIUS was vital to its success. Other Chinese investors looking to merge with or acquire United States' companies should adopt this approach. The pre-notice review and implementation of suggested mitigation prepares the deal substantively for a successful formal CFIUS review, while voluntary notification insulates the deal from political interference. This overall strategy changes the dynamics of the CFIUS process to one where the Chinese party has more control over the outcome of the deal. Therefore, Chinese investors are advised to follow AVIC International's strategy in order to ensure a hospitable investment environment in the United States.

However, AVIC International also highlights the disparity between the perception and reality of Chinese foreign investment in the United States. AVIC International depicts a much friendlier environment for Chinese investors than the popular examples of Chinese experiences in the United States such as CNOOC and Huawei. Unfortunately, the success of AVIC International and its strategy may not be enough to change the perception of Chinese investors, since it is only one instance of success against many instances of failed CFIUS review. This is a problem for the future growth of Chinese FDI because the negative perception is enough to deter investment.¹¹⁷

There are many options to change this negative perception. For one, CFIUS itself can be a powerful agent for change. In particular, CFIUS can release information regarding the number of notifications, withdrawals, approvals, and divestitures of Chinese investors each year. This could easily be done as part of CFIUS's annual report to Congress, which is made publically available. Currently the report already provides statistics in each of these categories based on region, China being in the East Asia category.¹¹⁸ However, it is difficult to extrapolate from those numbers, since multiple countries are grouped together, and it is difficult to find comprehensive information of those

117. Sheridan Prasso, *Chinese Investors Still Searching for U.S. Welcome Mat*, CNNMONEY (May 4, 2011, 12:20 PM), http://money.cnn.com/2011/05/04/news/international/chinese_investors_america.fortune/index.htm.

118. COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES, ANNUAL REPORT TO CONGRESS 29 (Dec. 2011), <http://www.treasury.gov/resource-center/international/foreign-investment/Documents/2011%20CFIUS%20Annual%20Report%20FINAL%20PUBLIC.pdf>.

countries investment histories. Therefore, it is near impossible to discern what proportion of each category represents Chinese investors. By breaking down the numbers by country, CFIUS will give an accurate picture of CFIUS's treatment of Chinese investors. Releasing this information could possibly change Chinese investors' perception of, and ultimately encourage greater, investing in the United States.

Moreover, by releasing the information, CFIUS could also implicitly impact its own behavior in favor of Chinese investors. CFIUS has an interest in being seen as a legitimate authority in determining national security issues with foreign transactions. Thus, publishing the numbers by country may provide an incentive in CFIUS to be more discerning when they recommend divestiture so that they can defend those numbers with authority. Thus, releasing country data, can initiate self-policing within CFIUS to limit political influence on their decisions.

CFIUS can also break down individual country information into industries. Chinese investors have expressed their hesitancy to invest after the Huawei incident despite not being in the technology industry.¹¹⁹ This is because there is an overall perception of hostility towards Chinese investors. Currently the report aggregates regional data in nine industries.¹²⁰ However, if the report broke down the information on an industry-by-industry level, Chinese investors can determine whether they are in an industry that may have better results with CFIUS, rather than being discouraged by failed deals of companies in different industries.

Information is the key to changing perception. Not only does the information itself present objective data for Chinese investors to accurately ascertain the investment environment in the United States, but it is also a step towards greater transparency. This gesture of goodwill on the part of CFIUS, to allow itself to be accountable to individual country investors, could encourage Chinese investors regardless of what the data indicates.

VII. CONCLUSION

AVIC International's successful CFIUS review is a clear example of how key regulatory changes to CFIUS's power has created a process that minimizes political interference and maximizes a Chinese

119. COMMITTEE ON FOREIGN INVESTMENT IN THE UNITED STATES, ANNUAL REPORT TO CONGRESS, *supra* note 118.

120. *Id.*

investor's chance for a successful CFIUS review. Moreover, AVIC International's strategy of voluntarily notifying CFIUS allayed political backlash to the deal. Therefore, Chinese investors should not be deterred from investing in the United States, but should follow the AVIC International model other Chinese to navigate the CFIUS process successfully. However, as the United States continues to encourage foreign investment to stimulate growth, it will also be important for CFIUS to dispel the perception among Chinese investors that it is difficult to invest in the United States. CFIUS should include country-by-country data in their annual report on general investment categories so that Chinese investors can objectively evaluate CFIUS's treatment of Chinese investors. Moreover, CFIUS should include an industry breakdown for each country, and indicate the approval rates for each industry. This will help create a more nuanced appreciation for CFIUS's decisions and help avoid broad deterrence in industries CFIUS is not particularly concerned with.

Appendix I

Country	2010 Total FDI Outflow (Billions U.S. Dollar)	FDI Output % of GDP
G7 Nations		
Canada	38.585	2.45%
France	76.867	3.00%
Germany	109.321	3.33%
Italy	32.655	1.59%
Japan	56.263	1.03%
United Kingdom	39.502	1.75%
United States	304.399	2.09%
G7 Nations Average		2.18%
China	68.811	1.20%

Appendix II

Country	2010 FDI Outflow to U.S. (Billions U.S. Dollar)	2010 Total FDI Outflow (Billions U.S. Dollar)	U.S. FDI % of Total FDI Outflow
Canada	5.522	38.585	13.534%
France	9.336	76.867	12.146%
Germany	17.362	109.321	15.882%
Italy	1.326	32.655	4.061%
Japan	17.612	56.263	31.308%
United Kingdom	23.931	39.502	60.582%