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An Evaluation of the Need for Further Statutory Controls on Foreign Direct Investment in the United States

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NOTES

AN EVALUATION OF THE NEED FOR FURTHER STATUTORY CONTROLS ON FOREIGN DIRECT INVESTMENT IN THE UNITED STATES

I. INTRODUCTION

The level of foreign direct investment in the United States[1] has risen dramatically in the past year. Unofficially, the Department of Commerce estimates that more than two billion dollars of such direct investment entered the United States in 1973, an amount that is roughly triple the 708 million dollars invested in the United States in 1972, and more than five times the 1971 figure.[2] The book value of all foreign direct investment in the United States stood at sixteen billion dollars at the end of 1973, an increase of 50 per

1. "Foreign direct investment in the United States" occurs when a foreign investor gains control of the operation of an American company, either through the acquisition of a controlling share of corporate stock, through the creation of an American subsidiary or through the formation of a joint venture in the United States. An investment in which the foreign investor lacks such control, whether intentionally or not, is known as a "portfolio investment." The United States Commerce Department uses a 25% ownership as the criterion for "control" in these definitions. The Department, however, reportedly plans to change this test to require a 20% ownership in the future for its determinations of foreign direct investment. *Statement of Peter M. Flanigan at Hearings on Foreign Direct Investment in the United States Before the Subcomm. on Foreign Economic Policy of the House Comm. on Foreign Affairs,* 93d Cong., 2d Sess. (Feb. 5, 1974) (prepublication transcript) [hereinafter cited as *Flanigan Statement*]. *See also* F. ROOT, R. KRAMER, & M. D'ARLIN, INTERNATIONAL TRADE AND FINANCE 459 (1966).

2. Wall Street J., Jan. 22, 1974, at 1, col. 6. The accuracy of this figure is disputable because of the lack of procedures by which the entry of foreign direct investment may be measured. Two recent private analyses have suggested that this total for the year 1973 should be estimated conservatively at $3 billion. *See* N.Y. Times, Feb. 18, 1974, at 39, col. 7 (report by David Bauer, an international economist with the Conference Board, a non-profit research organization); *Statement of Jeffrey Arpan and David Ricks at Hearings on Foreign Direct Investment in the United States Before the Subcomm. on Foreign Economic Policy of the House Comm. on Foreign Affairs,* 93d Cong., 2d Sess. (Feb. 5, 1974) (prepublication transcript) [hereinafter cited as *Arpan Statement*].

cent in just five years.[3] This massive influx of foreign capital has taken many different forms in a variety of economic sectors. The bulk of this inward flow is invested in direct plant construction and expansion, and is concentrated most heavily in the fields of electrical and non-electrical machinery, chemicals and scientific equipment.[4] For example, the American subsidiary of Farbwerke Hoechst AG, the West German chemical producer, proposes to build a 100 million dollar petrochemical complex in Texas.[5] Foreign interests also have engaged in numerous successful stock acquisitions, such as the British takeover of Gimbels Bros. department stores.[6] Real estate, particularly resort properties, are yet another area of sizeable foreign investment. Japanese purchases of properties in Hawaii reportedly have surpassed 300 million dollars in value.[7] In addition, reports of existing or planned investments by the newly rich Arab nations now are circulating widely.[8]

A multitude of factors account for this surge of foreign investment in the United States. Realizing the desirability of access to the huge and rapidly expanding American market, foreign firms

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3. Wall Street J., Jan. 22, 1974, at 1, col. 6. Foreign direct investment in the United States stood at $10.8 billion at the end of 1968. *Flanigan Statement, supra* note 1, at Appendix, Table III-A.

4. In a recent survey, 86% of the responding firms from abroad entered the American market for capital investment by creating entirely new subsidiaries rather than by acquiring existing companies. In addition, 45% of all foreign direct investment in the United States was concentrated in four basic industries: electrical machinery (14%), non-electrical machinery (13%), chemicals (9%) and scientific equipment (9%). *Arpan Statement, supra* note 2, at 5; Wall Street J., Feb. 18, 1974, at 39, col. 7.

5. Wall Street J., March 22, 1974, at 3, col. 2.

6. Other well-known firms now under foreign control include Grand Union Co. (supermarkets) and TraveLodge International, Inc. (motels). Many companies, such as Thos. J. Lipton, Inc. (tea) and Lever Bros. (soaps) long have been owned by foreign interests. *Id.*, Jan. 22, 1974, at 1, col. 6; N.Y. Times, Feb. 18, 1974, at 39, col. 7.

7. Japanese governmental approval for investment in United States real estate totalled over 47 million dollars between July 1971 and March 1973, of which more than 40 million dollars went into resort and other commercial real estate. *Statement of Nelson A. Stitt at Hearings Before the Subcomm. on Foreign Economic Policy of the House Comm. on Foreign Affairs*, 93d Cong., 2d Sess. (Feb. 5, 1974) (pre-publication statement) [hereinafter cited as *Stitt Statement*].

8. *See, e.g.*, Wall Street J., March 5, 1974, at 1, col. 6 and Jan. 22, 1974, at 1, col. 6.

are beginning to recognize the growing economic benefits of production in the United States through direct capital investment—direct, tariff-free access to consumers; protection from any future trade barriers; and avoidance of competitive labor costs and rapidly escalating shipping costs, among others.[9] The two devaluations of the dollar by the United States Government since 1971[10] and the endemic inflation abroad[11] have recently heightened these benefits and contributed to a rise in direct investment in the United States. The continued depressed prices of American corporate stock, in turn, make foreign acquisition of United States stock and companies a much less expensive proposition than previously.[12] Active encouragement of foreign direct investment by state and federal governments, through such promotional devices as development seminars, overseas offices, and tax breaks, assuredly has contributed to foreign interest in American investment opportunities.[13] Lastly, since the 1930's and the debacle of the protectionist Hawley-Smoot Tariff,[14] the United States has pursued a liberal trade policy encouraging the free flow of goods and

9. N.Y. Times, Feb. 18, 1974, at 39, col. 7; Statement of *Thos. L. Farmer, at Hearings Before the Subcomm. on Foreign Economic Policy of the House Comm. on Foreign Affairs*, 93d Cong., 2d Sess. *Feb. 5, 1974* (pre-publication transcript) [hereinafter cited as *Farmer Statement*].

10. Largely in response to continued and worsening deficits in United States international balance of payments, the United States Government formally devalued the dollar in December 1971 and February 1973. Wall Street J., March 22, 1974, at 6, col. 3. As of April 19, 1974, furthermore, the effective value of the dollar dropped even lower to 1.59% below the last devaluation, and 7.16% below the rates of December 1971. Wall Street J., April 5, 1974, at 22, col. 2 and April 19, 1974, at 4, col. 2.

11. Most industrialized European nations in recent years have suffered inflation at rates exceeding 7%. In addition, during 1973 those levels generally rose to above 8%. Recently inflation in the United States, while usually below that of Europe, has soared to greater than 9%. Wall Street J., March 13, 1974, at 1, col. 6.

12. Between April 1972, and March 1974, the Dow Jones Industrial Average, a standard indicator of the health of the stock market, dropped 100 points. Wall Street J., April 4, 1972, at 1, col. 2, and March 29, 1974, at 1, col. 2.

13. *See* notes 151-54 *infra* and accompanying text.

14. The Tariff Act of 1930, ch. 497, 46 Stat. 590, *as amended* 19 U.S.C. §§1202-1654 (1964), raised the average tariff level to 51% *ad valorem*, the highest level since the 1828 Tariff of Abominations. Note, *The Trade Act of 1971*, 80 YALE L.J. 1418, 1425 (1971).

capital among the nations of the world.[15] A limited number of domestic statutory restrictions on foreign direct investment in the United States naturally has accompanied this policy. To protect essential national interest, federal statutes prohibit or severely restrict foreign direct investment in the areas of aviation, atomic energy, federal land mining, hydroelectric power development, public utilities, radio communication and coastal shipping.[16] Many states, however, similarly limit foreign control of realty, banks and insurance companies.[17] Except for these restrictions, foreign investors enjoy national treatment, having the same opportunities as American investors.

The most critical result flowing from this sudden surge of direct investment into the United States has been the adverse reaction, particularly among members of the press and of the United States Congress.[18] Negative opinions about the expansion of direct foreign participation in the American economy have ranged from xenophobic fears of a foreign economic takeover of the United States to more responsible concerns for the possible need to inhibit foreign penetration of certain critical industries and raw material sectors. These fears and negative reactions have been exacerbated by a paucity of available information to verify or rebut them. A number of congressional committees, therefore, have responded by scheduling investigatory hearings on foreign direct investment,[19] while

15. The President's Commission on International Trade and Investment Policy (the Williams Commission) in its July 1971, report endorsed the "traditional U.S. open door to direct investment in the United States. The U.S. has much to gain from an inflow of foreign resources . . . . [I]t is essential that we treat foreign investors in the same manner as we expect and press other host countries to treat U.S. investors." *Flanigan Statement, supra* note 1, at 4.

16. *See* notes 58-72 *infra* and accompanying text.

17. *See, e.g.,* CONN. GEN. STAT. ANN. §§33-395, 33-396 (1958) (banks and insurance companies); N.C. GEN. STAT. §64-3 (1965); N.D. CENT. CODE §§6-02-02, 6-08-27,10-23-01 (1959) (banks and foreign corporations), §§26-01-13 to 26-01-15 (1970) (insurance companies); and OKLA. STAT. ANN. tit. 60, §121 (1971) (alien ownership of land).

18. *See, e.g.,* Wall Street J., Jan. 22, 1974, at 1, col. 6; Nashville Banner, March 18, 1974, at 7, col. 3; and Tennessean, March 11, 1974, at 6, col. 1, which publicize the adverse reactions in Congress and in the press to growing foreign direct investment.

19. Wall Street J., Jan. 22, 1974, at 1, col. 6. Those congressional subcommittees that have conducted hearings on foreign direct investment are the Subcom-

several members of Congress recently have sponsored legislation in this area. Senator Daniel Inouye (D—Hawaii), has introduced legislation calling for a massive two-year study of foreign direct investment in the United States to gain the information necessary to formulate a "coherent national policy" toward the inflow of such capital.[20] More directly, however, Representatives John Dent (D—Pa.) and John Moss, (D—Calif.) have sponsored bills in Congress that would sharply limit future foreign direct investment by restricting foreign acquisition of existing American corporate stock.[21]

This sharp increase in foreign direct investment in the United States, together with the negative reactions among responsible men in the press and government, has posed the difficult and complex question whether it is in the best economic and political interests of the United States to maintain its present policy of allowing a largely unrestricted inflow of foreign direct investment. This Note examines this question in light of the three congressional bills previously mentioned and offers recommendations for a desirable course for United States policy. Part II treats United States trade and investment policy and the statutes regulating foreign direct investment. A comparison of American practice and policy with that of other comparably industrialized nations comprises the third part of this Note. Part IV examines in depth the reasons for

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mittee on International Finance of the Senate Committee on Banking, Housing and Urban Affairs. *See* 120 CONG. REC. D14, D21 (Jan. 23 and Feb. 21, 1974); the Subcommittee on Foreign Commerce and Tourism of the Senate Commerce Committee (unconfirmed reports in advance of hearings on Feb. 19 and March 7, 1974 in the Congressional Record); and, the Subcommittee on Foreign Economic Policy of the House Committee on Foreign Affairs. *See also* 120 CONG. REC. D34, D70, D124 (Jan. 29, Feb. 21 and March 5, 1974).

20. S. 2840, 93d Cong., 1st Sess. (1973).

21. H.R. 8951, 93d Cong., lst Sess. (1973) (a bill to amend the Securities Exchange Act of 1934 to restrict persons who are not citizens of the United States from acquiring more than 35 per centum of the nonvoting securities or more than 5 per centum of the voting securities of any issuer whose securities are registered under such Act, and for other purposes), proposed by Congressman Dent and his co-sponsor, Joseph M. Gaydos of Pennsylvania; H.R. 12040, 93d Cong., 1st Sess. (1973) (bill to amend the Securities Exchange Act of 1934 to prevent control by foreign persons of American companies engaged in vital industries), proposed by Congressman Moss. *See* 119 CONG. REC. E8188 (1973) for explanatory remarks by Mr. Moss.

the recent growth in foreign direct investment in the United States and its present and prospective nature and extent. Part V concludes with an analysis—built upon the observations in the earlier sections of the Note—of the political and economic repercussions in the United States caused by the entry of foreign direct investment, and suggests conclusions for appropriate United States policy.

II. United States Trade and Investment Policy in Theory and Practice

A. *An Historical Overview*

Until the first part of the twentieth century, the two distinct components of United States trade policy followed opposing economic philosophies—a protectionist tariff program against the importation of goods and products, and a policy favoring foreign direct investment in the American economy.[22] With few exceptions, the United States had always utilized high tariffs as a method to protect the nation's infant, but growing, industries from cheaper, and perhaps more efficiently produced, foreign products.[23] As early as 1791, however, Alexander Hamilton stated, "Instead of being viewed as a rival, [foreign direct investment] ought to be considered as a most valuable auxiliary, conducing to put into motion a greater quantity of productive labor, and a greater portion of useful enterprise than could exist without it."[24] This remark sets forth the historical, and still operative, liberal policy of American government toward foreign direct investment. From the very earliest times, foreign capital was an essential part of American economic development because of the inadequacy of

22. S. Metzger, *American Foreign Policy and American Foreign Trade,* 47 Texas L. Rev. 1075 (1969); Note, 80 Yale L. J. 1418 (1971); Weintraub, *Why the United States Welcomes Foreign Investments,* in Proceedings of the Conference on Foreign Direct Investment in the United States 8 (1970) (sponsored by the Institute for International and Foreign Trade Law, Georgetown University) [hereinafter cited as Proceedings].

23. 80 Yale L.J. 1424; E. Root, *supra* note 1, at 374-77.

24. Weintraub, *supra* note 22, at 8. *See also* Hamilton, *Report of the Secretary of the Treasury on the Subject of Manufactures,* in State Papers and Speeches on the Tariff 1 (F. Taussig ed. 1895), *as cited in* Note, *supra* note 14, at 1423 n.23.

domestic capital and resources to create a developed economy. Foreign investment in the United States totaled 1.5 billion dollars by 1869, and was crucial in many ways to the nation's economic development.[25] For example, the development of the transcontinental railroad system and the western lands during the latter half of the nineteenth century depended heavily on foreign capital participation. Indeed, it would not be incorrect to acknowledge that the American West was won with American sweat and European capital.[26] By 1914, the United States had grown sufficiently enough to invest 2.7 billion dollars abroad,[27] yet foreign investment in America had soared to 5.9 billion dollars in portfolio securities and real estate, and 7.2 billion dollars in direct investment.[28] The financial needs of the European belligerents during World War I caused such a substantial liquidation of foreign holdings in America that in 1919 the relative sizes of American investment abroad and foreign capital in the United States had reversed their 1914 figures.[29] Foreign direct investment in the United States since then has grown at a sporadic rate and has failed to match the extraordinary world-wide expansion of United States direct investment, which is now seven times greater than the total of all foreign direct investment in the United States.[30] Except in areas of essential national interest, governmental policy continues strongly to support nondiscrimination against foreign investors in the United States. The government consistently justifies this liberal position on grounds of the nation's commitment to free world trade and the economic benefits accruing to the United States in greater productivity, higher incomes, greater inflow of technology and a more favorable effect on the balance of payments.[31]

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25. *Flanigan Statement, supra* note 1, at Appendix Table XIV (United States Investments Abroad and Foreign Investments in the United States, 1869-1972).

26. Weintraub, *supra* note 22, at 8.

27. *Flanigan Statement, supra* note 1, at Appendix, Table XIV.

28. *Id.*

29. *Id.*

30. *Flanigan Statement, supra* note 1, at Appendix, Table XIV.

31. *Id.* at 13. In his April 10, 1973 message to Congress concerning the Trade Reform Act, President Nixon noted that "an open system for international investment, one which eliminates artificial incentives or impediments here and abroad, offers great promise for improved prosperity throughout the world." *Id.* at 3.

B. *Modern Economic Objectives of American Policy*

United States protectionist trade policy peaked disastrously in the controversial Tariff Act of 1930,[32] known as the Hawley-Smoot Tariff and labeled the "crowning achievement of protectionism."[33] This tariff's record—high protection against imports—provoked a flood of retaliatory tariff legislation among United States trading partners that reduced both the American share of international trade, and world trade itself, by almost one-third between 1929 and 1933.[34] This trade protectionism, contributing significantly to the subsequent world economic depression, thereafter caused an almost complete reversal of United States trade and investment policy. Consequently, the perceived domestic economic benefits flowing from the free and largely unrestricted flow of trade and investment have ever since comprised the chief justification for the contemporary "liberal" trade policy pursued by the United States Government. Moreover, since then, the unrestricted movement of goods in domestic and international trade is believed to engender the optimal allocation of resources among national economic units. A rationalization of resource allocation, in turn, produces the desirable economic benefits of greater and more efficient productivity through production specialization in which costs are lowest. In addition, technological advancements are more rapid because most efficient production is best able to bear such costs. Efficiency in allocation and production naturally should create real economic benefits to the populace in lower prices for goods and in higher incomes. Higher employment in the long-term should also follow from this economic chain. A liberal trade policy, moreover, if practiced on a world scale, creates greatly expanded markets for American goods and investment.[35]

The efficacy with which a liberal economic policy serves the goals of United States foreign policy has constituted another effective argument in favor of trade liberalization.[36] Since World War

32. *See* note 14 *supra*.
33. F. ROOT, *supra* note 1, at 377.
34. *Id.*; Note, *supra* note 14, at 1425.
35. B. BALASSA, TRADE LIBERALIZATION AMONG INDUSTRIAL COUNTRIES 94-148 (1967); F. ROOT, *supra* note 1, at 47-118.
36. S. Metzger, *supra* note 22, at 1078-84; *Flanigan Statement, supra* note 1, at 3, 7-9, 14, 17-19.

II, containment of Communism has been a vital factor in American foreign policy. The unrestricted flow of trade and investment that a liberal trade program encourages is a natural adjunct to American foreign policy because it promotes economic and political interdependence among the non-Communist world and reduces the threat of Russian influence. The United States, therefore, has sought to maximize the utility of free trade through such means as agreements to reduce tariffs,[37] free trade areas, expansion of United States trade and investment and the growth of American multinational corporations.[38]

C. *Federal Statutes Implementing Post-1930 United States Trade Policy*

The Reciprocal Trade Agreement Act[39] enacted by Congress in 1934 marked the adoption by the United States Government of a liberal trade program and was the precursor of a continuous series of American and world measures that have successively lowered trade barriers among the developed nations. The Reciprocal Trade Agreement Act granted the President extraordinary authority to conclude, without Senate approval, bilateral trade agreements to lower tariff rates in an amount up to 50 per cent of the Hawley-Smoot tariff barriers.[40] Amended during the 1950's to protect United States industries through the addition of several protectionist measures,[41] the Reciprocal Trade Agreement Act governed

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37. *See* notes 49-53 *infra* and accompanying text.

38. *See generally* Vagts, *The Multinational Enterprise: A New Challenge for Transnational Law*, 83 HARV. L. REV. 739 (1970).

39. Ch. 474, 48 Stat. 943 (1934).

40. Trade Agreements Act, ch. 474, §§350(a)(1)-(2), 48 Stat. 943 (1934), *amending* 46 Stat. 708 (1930). The President, however, was required to "seek information and advice" of the Tariff Commission with respect to these reductions, and consult the Departments of State, Agriculture and Commerce. Trade Agreements Act, ch. 474, §350(a)(2), 48 Stat. 943 (1934).

41. The most important of these amending provisions were the "peril-point provision," which required the Tariff Commission to set minimum tariff rates below which domestic industries might be harmed (Trade Agreements Extension Act of 1951, ch. 141, §3, 65 Stat. 72); the "escape clause provision," to be inserted in all agreements and which would permit the withdrawal of all concessions that should prove harmful to domestic industries (Trade Agreements Extension Act of 1951, ch. 141, §6(a), 65 Stat. 72); and, the "defense essentiality amendment,"

American bilateral trade relations until 1962 and reduced *ad valorem* American tariff rates from an average of 51.5 per cent for dutiable imports in 1934 to 11.1 per cent in 1962.[42] In the landmark Trade Expansion Act of 1962,[43] which supplanted the Reciprocal Trade Act and constituted another giant step in the liberalization of United States trade policies, Congress granted the Executive the following: (1) the power to reduce, by as much as 50 per cent, the customs duties existing as of July 1, 1962; (2) the power to eliminate all tariff barriers on the products of industries in which the United States and the European Economic Community (EEC) together controlled 80 per cent of the free world trade; and (3) the power to eliminate tariff duties that, as of July 1, 1962, were at levels of five per cent or less.[44] Of particular note is the limitation imposed by the Trade Expansion Act of 1962 on the presidential authority to issue emergency restrictive measures, such as higher duties or quantitative limitations, whenever foreign political or economic action might injure American interests. Instead, the Trade Expansion Act of 1962 provided various forms of governmental assistance to beleaguered industries in such situations.[45] Since the expiration of the Trade Expansion Act in 1967,[46] the United States has had no statutory trade policy despite numerous efforts to legislate one. The proposed Trade Act of 1971, which exhibited the then burgeoning protectionist sentiment, failed to gain congressional approval.[47] The Congress presently is considering a new trade bill that would prepare the United States for further world tariff reduction and reaffirm United States dedication to free trade.[48]

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a provision to protect the endangered national security by reducing imports of harmful foreign goods (F. Root, *supra* note 1, at 380). *See* Note, *supra* note 14, at 1427-30 for an elaboration and evaluation of these amendments.

42. F. Root, *supra* note 1, at 381-84, 388.

43. 19 U.S.C. §§1801-1991 (1970).

44. *See* 19 U.S.C. §§1821(b)(1), 1822, 1831(a) (1970); F. Root, *supra* note 1, at 391-92.

45. The government was empowered to provide technical and financial assistance to affected firms and to provide workers with allowances for retraining, relocation and adjustment. Note, *supra* note 14, at 1430-32.

46. F. Root, *supra* note 1, at 396.

47. *See* Note, *supra* note 14.

48. H.R. 10710, 93d Cong., 1st Sess. (1973), known as the Trade Reform Act of 1974.

D. *United States International Trade and Investment Policy: An Instrument of Foreign Policy*

The United States has employed a variety of devices and strategies to gain a freer flow of world trade and the concomitant foreign policy benefits of economic and political interdependence among the non-Communist nations. First, the United States has helped create a number of post-World War II economic agreements and institutions that promote greater trade and economic cooperation. The General Agreement on Tariffs and Trade (GATT),[49] perhaps the best known of these organizations, has emerged as the central international trade institution of the post-war period. The commitment of GATT's members to trade liberalization is exemplified by the GATT preamble that calls for "the substantial reduction of tariffs" and "the elimination of discriminatory treatment in international commerce" to gain the full economic benefits propounded therein.[50] In operation the GATT has sponsored five major trade conferences, the last being the so-called "Kennedy Round" in Geneva between 1964 and 1967. The Kennedy Round of trade negotiations, entered into by the United States under the authority of the Trade Expansion Act of 1962, produced the most significant trade liberalization in American history.[51] Other cooperative institutions that have served economic and political functions similar to GATT are the International Monetary Fund, the World Bank and the Organization for Economic Cooperation and Development.[52] Secondly, most bilateral treaties of friendship, commerce and navigation between the United States and its major world trading partners require each contracting party to grant full national treatment to investors from the other.[53] Thirdly, the United States has always

49. Oct. 30, 1947, 61 Stat. A11, T.I.A.S. No. 1700, 55 U.N.T.S. 187 [hereinafter cited as GATT].

50. *See* Note, note 14 *supra*, at 1428 n.53.

51. *See* GATT.

52. *See generally* F. ROOT, *supra* note 1, at 354-59 (International Monetary Fund), 365-66 (Organization for Economic Cooperation and Development), 449 (the World Bank).

53. Treaty of Friendship, Commerce and Navigation with the Federal Republic of Germany, Oct. 29, 1954, arts. V, VII, [1956] 2 U.S.T. 1839, T.I.A.S. No. 3593 (effective July 14, 1956). Article VIII does limit this right of national treatment in certain areas in which aliens may not carry on, establish or acquire

advocated the creation of economic free trade areas and customs unions such as the Common Market because such entities ideally increase the flow of intra-market and world trade, and consequently make the participants stronger economic and political allies of the United States.[54] Fourthly, the United States has sought to increase trade with and financial assistance to the less developed nations through such means as preferential treatment under the GATT.[55] Fifthly, the world expansion of American economic, and often political, influence through the growth of multinational corporations, incorporated in the United States, has received warm governmental support.[56] Lastly, the American Government occasionally has applied direct economic pressure, such as with Japan in 1971, to force the liberalization of foreign trade and investment regulations.[57]

E. *Domestic Federal Statutory Regulation of Foreign Direct Investment*

The limited number of federal statutes inhibiting foreign direct investment illustrates the continuing United States policy to accord foreign investors "national treatment" on an equal footing with domestic corporate entities and investors. Based solely on grounds of essential national security and international practice, statutory limitations protect coastal and internal shipping,[58] domestic radio communication,[59] atomic energy,[60] domestic air transportation,[61] minerals under federal lands[62] and hydroelectric

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enterprises: communications, air and water transport, taking and administering trusts, banking involving depositary functions, or the exploitation of land and natural resources.

54. *See* B. BALASSA, *supra* note 35, at 23-43; Metzger, *supra* note 22, at 1080-81.

55. GATT, *supra* note 49, at art. 24.

56. *See generally* B. BALASSA, *supra* note 35, at 23-43.

57. H. TANIKAWA, D. ALLAN, M. HISCOCK & D. ROEBUCK, CREDIT AND SECURITY IN JAPAN 10 (1973). The latest measures of liberalization in Japanese investment policy were introduced directly in response to United States withdrawal of tariff concessions. *Id.*

58. 46 U.S.C. §§289, 808, 865, 883 (1970).

59. 47 U.S.C. §310 (1970).

60. 42 U.S.C. §2133 (1970).

61. 49 U.S.C. §§1301(13), 1378(c), 1378(f), 1401, 1508(b) (1970).

62. 30 U.S.C. §§22, 24, 72, 181, 352 (1970); 43 U.S.C. §§3102-3300 (1970).

power.[63] The degree and complexity of restriction imposed in these statutes varies greatly. All of them require United States citizenship of the applicable person or entity. The most inhibitory regulation governs commercial licenses for the use of atomic energy; no license will be granted to "an alien, or any corporation or entity of whom the Commissioner knows, or has reason to believe is owned, controlled or dominated by an alien, a foreign corporation, or a foreign government."[64] Slightly less strict prohibitions govern the development of hydroelectric power on navigable streams and mining of federal lands.[65] Most of these statutes, however, allow a minority percentage of foreign stock ownership.[66] Registration for operation of aircraft between points within the United States, and of ships for transportation of merchandise in coastal or internal commerce requires that an applicant be a United States citizen, and if the applicant is an aviation or shipping corporation, both the chief executive officer and either two-thirds (for aviation corporations)[67] or a majority (for shipping corporations)[68] of the board of directors must be United States citizens, with 75 per cent of its stock owned or controlled by individual United States citizens.[69] To obtain a license to engage in radio communications, a corporate applicant must have no foreign officers or directors and no more than 20 per cent foreign ownership of stock, or the corporate applicant must not be directly or indirectly controlled by another corporation any of whose officers, or more than 25 per cent of whose directors, are aliens, or of which more than 25 per cent of the stock is owned by aliens.[70] The severity and breadth of these statutory limitations may yield, nevertheless, in certain instances to circumvention and available exceptions. The required United States citizenship may be satisfied by a foreign investor that engages in United States business activity through an American subsidiary incorporated for these purposes. Foreign corporations engaged in mining and manufacturing operations enjoy a special exception to

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63. 16 U.S.C. §797(e) (1970).
64. 42 U.S.C. §2133 (1970).
65. *See* notes 62, 63 *supra*.
66. *Id.*
67. 49 U.S.C. §1301 (1970) (aviation).
68. 46 U.S.C. §808 (1970) (shipping).
69. *See* notes 67, 68 *supra*.
70. 47 U.S.C. §310 (1970).

the restrictions on coastal and internal shipping.[71] Domestic United States air commerce, furthermore, is open to foreign civil aircraft, upon a grant of reciprocity by the other nation concerned, so long as such aircraft do not carry for compensation or hire any persons or property going aboard within and destined for another point within the United States.[72]

A host of domestic regulatory statutes of general applicability pose additional problems for foreign investors and lessen their desire and ability to locate or invest here. A fear uppermost in the minds of foreign corporate investors is potential injunctive action against them by the Federal Trade Commission for alleged anti-competitive practices. Foreign corporations seeking to acquire control of domestic entities are especially wary of this police power because it can be utilized both before and after a transaction, and, therefore, lends more uncertainty to an already risky venture.[73] The Federal Trade Commission (FTC) has shown itself ready to wield its anti-competitive stick, as in the now successful British Petroleum acquisition of a 25 per cent interest in Standard Oil Company of Ohio,[74] and its recent inquiry into the 1970 acquisition by Nestle Alimentana S.A., the giant Swiss food and beverage concern, of majority control in Libby, McNeil & Libby, and its purchase of Stouffer Corp. in March 1973.[75] Despite American claims that the FTC does not discriminate against foreign investors, FTC investigations have aroused considerable protest from abroad as well as threats of retaliation.[76]

Any apparent discrimination may be explained, moreover, by

71. 46 U.S.C. §883-1 (1970).

72. 49 U.S.C. §1508(b) (1970).

73. 15 U.S.C. §45 (1970). *See also* Remarks by J.J.A. Ellis, former Attorney General of the Netherlands, in PROCEEDINGS, *supra* note 22, at 12. In general, as the Commission of the European Economic Community noted recently, "It is often noted that the non-U.S. investors encounter numerous difficulties in setting up in the U.S.A. and that U.S. regulations are substantially more stringent with regard to European investment than are the European regulations with regard to U.S. investment." *Flanigan Statement, supra* note 1, at 17.

74. Remarks by Sir Eric Drake, Chairman of the Board of British Petroleum Co., Ltd., in PROCEEDINGS, *supra* note 22, at 6.

75. Wall Street J., March 19, 1974, at 18, col. 2. In addition, the Federal Trade Commission (FTC) recently has moved to revoke the acquisition by British Oxygen Co. of 35% of the stock of Airco, Inc. *Id.*, Feb. 27, 1974, at 10, col. 2.

76. PROCEEDINGS, *supra* note 22, at 6, 12. The FTC inquiry into the acquisi-

the perceived risks of foreign investment in the United States which have militated against acquisitions except by the largest, American-style foreign multinational—the entities naturally most susceptible to FTC inquiry. The practical necessity for registration of transactions in equity capital with the Securities and Exchange Commission (SEC) similarly arouses concern and perhaps leads to avoidance of American investment since the rigorous disclosure expected in SEC registration statements is a new and painful experience for most foreign investors.[77] Another obstruction is the requirement of governmental approval for mergers or acquisitions in most realms of industrial activity.[78] The public hearings customarily held by most American regulatory agencies may act as a touchstone for public rejection, as may the agency's required determination of whether the application is in the public interest.[79] Investment in domestic entities that seek government contracts also raises problems for foreign investors because contracts that involve access to or development of classified information require security clearance of all relevant corporate officers.[80] Further, the extensive

tions by Nestle prompted its chairman, Pierre Liotard-Vogt, to suggest that the FTC, contrary to Nixon Administration policy, is trying to create trouble for the establishment of foreign companies in the United States. Wall Street J., March 19, 1974, at 18, col. 2. Chairman Liotard-Vogt, furthermore, warned of possible foreign retaliation to American restrictions on inward foreign investment. Wall Street J., March 25, 1974, at 1, col. 5.

77. *See* PROCEEDINGS, *supra* note 22, at 7 (remarks by Sir Eric Drake).

78. *See, e.g.*, 16 U.S.C. §824 (1970) (utilities); 49 U.S.C. §5(a) (1970) (railroad companies and motor carriers); 46 U.S.C. §808 (1970) (shipping); 49 U.S.C. §1378(a)(4) (1970) (aviation controls).

79. *See, e.g.*, 49 U.S.C. §5 (1970) (the procedures for approval by the Interstate Commerce Commission).

80. Since security clearance for governmental contracts usually is granted by the government to United States citizens only, corporations having foreigners in key positions, therefore, may be unable to gain clearance for the contracts. *Farmer Statement, supra* note 9, at 11. Defense Department practice to treat private contractors as ineligible for security clearance if the contractor, or its parent corporation, is under foreign ownership, control of or influence may be circumvented by using voting trusts that insulate the contractor from such foreign ownership, influence or control. Liquifin Aktiengesellschaft AG, of Liechtenstein, used this method in its efforts to overcome possible objections to its acquisition, by stock tender offer, of a 51% interest in Ronson, Inc. Wall Street J., Jan. 21, 1974, at 19, col. 1.

state and federal power of taxation over corporate income must be evaluated by foreign investors for its effect on the viability of American investment. In addition, many states have restricted such investments in banking, insurance and realty transactions.[81] The methods by which the United States may control the entry of foreign direct investment, therefore, actually extend far beyond the direct statutory limitations in the enumerated "critical" areas.

III. FOREIGN STATUTORY CONTROL OF FOREIGN DIRECT INVESTMENT

A. *Introduction*

Statutes that directly regulate the entry of foreign capital for direct investment are common throughout the world. No international standard, or rule of international law, exists against which to measure these statutes, and their stringency varies greatly. Recent tides of nationalistic fervor have sparked increasingly strict controls on such foreign investment, particularly among, though not limited to, the less developed nations. The requirements that all future foreign direct investments be limited to minority interests, and that nationals acquire majority control within fifteen years in all such existing investment, as stated in the Investment Code of the Andean Common Market, are typical of such new measures.[82] The applicable statutes in force in the developed nations generally are much less inhibitory than those of the less developed countries and range from extensive discretionary restrictions to virtually no limitations whatsoever. Common to the methods of most of these nations is supervision of foreign direct investment in both existing companies and newly created entities or subsidiaries. Other typical features found more extensively in other industrialized nations are the absolute bar to entry of foreign capital in certain sectors and the existence of governmental monopolies or companies that severely reduce the opportunity for private competition. Utilities, communications and transit systems typify these governmentally controlled areas.[83] Foreign stat-

81. *See* note 17 *supra*.

82. Furnish, *The Andean Common Market's Common Regime for Foreign Investments,* 5 VAND. J. TRANSNAT'L L. 313,315 (1972).

83. 3 CCH COMM. MKT. REP. ¶¶ 23, 116 (Germany) 1973, 23, 615 (Britain) 1973, 22, 623 (France) (1974).

utes of general applicability that are not solely intended to govern foreign direct investment also act as potential barriers. This sort of legislation either applies to foreigners in general, as in tax, work permit, personnel hiring, equipment import and financing controls, or to both domestic and foreign entities. Antitrust and incorporation laws, as well as labor standards, fall under this latter category.[84]

B. *Statutory Controls in a Representative Group of Developed Nations*

Of particular relevance to an understanding of the controls exercised by the United States over foreign direct investment is an examination of foreign statutes of a similar nature currently in force in comparably industrialized nations. Canada, France, Japan, West Germany and the United Kindgom constitute a representative sample, which conveniently may be divided into two groups according to the severity of restrictions: Japan, France and Canada are less open to foreign direct investment than are West Germany and the United Kingdom. Following an elaboration of the statutory controls used by members of these two groups, this Note offers comments explaining the political and economic forces that appear responsible for these statutes.

1. *Japan.*—Foreign direct investors encounter in Japan a relatively comprehensive and complex system controlling the entry of foreign capital, notwithstanding a governmental program of liberalization in this area since 1967.[85] Under the Law Concerning Foreign Investment,[86] virtually all direct investments by foreigners[87]

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84. King, *Foreign Restrictions on U.S. Investment,* 11 SAN DIEGO L. REV. 27, 36-43 (1973).

85. *See generally* CURRENT LEGAL ASPECTS OF DOING BUSINESS IN THE FAR EAST (R. Allison, ed. 1972) [hereinafter cited as DOING BUSINESS]; INTERNATIONAL FINANCE BUREAU, JAPANESE MINISTRY OF FINANCE AND FOREIGN DEPARTMENT, BANK OF JAPAN, MANUAL OF FOREIGN INVESTMENT IN JAPAN (1974) [hereinafter cited as MANUAL]; TANIKAWA, *supra* note 57; King, *supra* note 84; Michida, *Capital Liberalization as a Treaty Question and Offensive and Defensive Strategies Concerning Foreign Capital,* 2 LAW IN JAPAN 1 (1968).

86. "Foreign investors" include nonresident non-juridical persons, juridical persons and other organizations established under the laws of foreign countries, and the following: (1) branch offices, branch factories, etc., in Japan of corporations established under the laws of foreign countries; (2) resident non-Japanese

require governmental sanction from the Ministry of Finance and other "competent ministries." "Direct investment" is defined as an acquisition made to obtain participation in the management of existing or newly created companies, or as a transaction involving the establishment in Japan of a branch of a foreign enterprise.[88] The discretion that these authorities may exercise under this statute is great, for the creation of a serious problem affecting the national economy may justify rejection of an investment. Reportedly, the Japanese Government uses this power liberally.[89] Additionally, foreign direct investment in a branch or directly operated factory requires the filing of a registration statement with the Bank of Japan.[90] Automatic validation of an incoming direct investment in an existing or newly created enterprise, is possible, however, depending on the industry involved, the percentage of stock ownership sought and compliance with certain conditions. These standards vary directly according to whether the investment concerns the creation of a new Japanese subsidiary or joint venture, or the acquisition of stock in an existing company, and they demonstrate an obvious governmental preference for maintaining national control of existing enterprises. Foreign investors automatically may hold complete ownership of a new company except in 22 protected industries, including data processing, real estate and drugs, to which the government has not yet extended full liberalization.[91]

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nationals, overseas residents with both Japanese and foreign nationality (dual nationality); and (3) Japanese corporations whose stocks or proprietary interests are wholly owned by nonresidents, corporations established under the laws of foreign countries, and residents not having Japanese nationality, or whose management is virtually controlled by such. MANUAL, *supra* note 85, at 1 n.1.

87. The Law Concerning Foreign Investment was enacted in 1950 to deal specifically with the entry of long-term foreign direct investment. It supplements the pre-existing Foreign Exchange and Foreign Trade Control Law that governs all foreign exchange and trade. MANUAL, *supra* note 85, at 1-2. Except in minor cases, the "competent ministers" must consult the Foreign Investment Council, a body of fifteen men of knowledge and experience that is appointed by the Minister of Finance. *Id.* at 4.

88. MANUAL, *supra* note 85, at 6, 8, 14.

89. *Id.* at 4. DOING BUSINESS, *supra* note 85, at 22-27.

90. This statement must be supplemented by a business prospectus and annual reports on the settlement of the branch's accounts. MANUAL, *supra* note 85, at 13.

91. *Id.* at 8. The complete list of protected industries may be found in MANUAL, *supra* note 85, apps. 1-2.

This "automatic" validation, nevertheless, hinges upon compliance with certain conditions, among which are the prohibition of any transfer of business from, or future combination with, an existing company.[92] In 16 of those 22 industries, foreign participation may reach 50 per cent if accompanied by satisfaction of a lengthier set of conditions.[93] In the remaining protected industries, a single foreign investor may acquire less than 10 per cent equity interest, as long as the total foreign investment in the industry is less than 25 per cent.[94] For existing Japanese corporations not in the 22 protected industries, foreign investors may acquire 100 per cent of a company's stock as long as the company consents to the acquisition. Absent this consent, a foreign direct investment in such a company receives automatic validation only if a foreign investor individually acquires less than 10 per cent of the stock and the aggregate number of shares so held is less than 25 per cent. In a wide range of certain restricted sectors, such as utilities and banking, the limit of total foreign stock ownership, however, is fifteen per cent.[95] In cases in which automatic approval may not occur, the investor is subjected to thorough screening, and consequently, government validation is less likely.[96]

2. *France.*—Like Japan, France mandates prior governmental approval for all foreign direct investments by "foreign investors," including French companies under foreign control and French branches of foreign corporate entities.[97] In France foreign direct investments consist of the purchase, creation or extension of any new or existing enterprise or branch, excluding initial acquisitions of less than twenty per cent stock interests in existing French companies.[98] Certain sizeable foreign borrowings also may fall

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92. *Id.* app. 3(B).

93. *Id.* app. 3(A).

94. *Id.* at 8-9.

95. MANUAL, *supra* note 85, at 9-10. A complete list of the "restricted industries" includes such typically protected areas as all forms of transportation, communications, fishing and mining. *Id.* at 7.

96. MANUAL, *supra* note 85, at 10.

97. *See* 3 CCH COMM. MKT. REP.; R. DICKIE, FOREIGN INVESTMENT: FRANCE (1970); Torem & Craig, *Developments in the Control of Foreign Investment in France,* 70 MICH. L. REV. 285 (1971).

98. A direct investment includes the "purchase, the creation or the extension of any business, branch or individual enterprise; [and] [a]ll other operations

within the category of foreign direct investment.[99] Prospective foreign investors must submit to the Ministry of Finance detailed information about themselves, the size and nature of the investment and its beneficial effects on the French economy. In reviewing applications, the Ministry approves only those of obvious economic merit to France, such as those which introduce new technology, increase employment and favorably influence the balance of trade.[100] The Ministry enjoys wide discretion and characteristically is very selective in its approval.

3. *Canada.*—Under the mechanism of its recently enacted Foreign Investment Review Act,[101] to insure that foreign investments are or likely will be of significant benefit to Canada[102] the Canadian Government[103] reviews the establishment of all new businesses, the expansion of established businesses, the expansion of established foreign-controlled entities into unrelated fields, and foreign acquisitions of 50 per cent or more of the voting stock of Canadian enterprises, which rebuttably constitutes control,[104] by "non-eligible persons."[105] Following required notice by a foreign investor of plans

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which alone or together with others, concurrently or consecutively, have the effect of permitting a person or persons to acquire or increase the control of a company . . . whatever may be its form, or to assure the expansion of such company already controlled by them." Torem & Craig, *supra* note 97, at 286 (emphasis omitted). Exempt from the authorization requirement is an initial acquisition of less than 20% of the stock of a French company that is quoted on the stock exchange *(La Bourse).* 3 CCH COMM. MKT. REP. ¶ 22, 655 (1974); R. DICKIE, *supra* note 97, at 27.

99. Torem & Craig, *supra* note 97, at 289-90.

100. The Ministry also favors those investments that help develop the nation's less industrialized or economically backward regions, and those that demonstrate the investor's willingness to cooperate closely with the government. The Ministry may consult other governmental departments while making its decision about the desirability of the investment, and then must act on the application no later than two months after its receipt. R. DICKIE, *supra* note 97, at 29, 72-92; Torem & Craig, *supra* note 97, at 318-22.

101. Foreign Investment Review Act of 1973, 2 Eliz., c. 46 (Can.) [hereinafter cited as FIRA].

102. FIRA §2(1).

103. The Review Act establishes a Foreign Investment Agency to supervise this regulatory process. FIRA §7(1).

104. FIRA §§2(1), 3(2)(a), 3(3), 5(1), 6. A 50% or more ownership or acquisition of stock in a Canadian corporation gives rise to a conclusive presumption of control. FIRA §3(3).

105. FIRA §3(1).

for such an investment, the Foreign Investment Review Agency determines whether the investment offers the benefits necessary for approval by weighing it against five judgmental criteria,[106] among which are the degree and significance of Canadian participation in the proposed investment, and its effect on Canadian productivity, technological development, and industrial competition. The Agency has wide investigative powers to accomplish its task.[107]

4. *Strict Statutory Control—A Summary.*—The stringent controls exercised by the governments of Japan, France and Canada are products of political and economic forces that are not duplicated in West Germany and the United Kingdom. In Japan and France, the governments long have used restrictions to inhibit the growth of foreign direct investment. The level of this investment in Japan, in particular, is markedly lower than in any other comparably industrialized society.[108] The Japanese perceived the necessity of protecting their economy from outside competition to insure reconstruction following World War II, and consequently adopted restrictions virtually prohibiting the entry of foreign capital and trade.[109] The remarkable resurgence of Japanese economic power almost without foreign investment only strengthened their justification for governmental protection, which continued in full force until 1967.[110] Mounting world, particularly United States, criticism demanding reciprocity for liberal trade policies and noting outright contradictions between Japanese investment statutes and its international commitments under the Treaty of Friend-

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106. FIRA §2(2).

107. FIRA §§14-17.

108. Japanese stocks held by foreigners, with participation in the management of the Japanese company in question, totalled $899,626,000 in March 1973. MANUAL, *supra* note 85, at 28 (App. (4)). In West Germany at the end of 1972, in contrast, 1700 foreign companies with German subsidiaries or branches had invested DM 26 million (approximately $10.6 million, according to the prevailing currency exchange rates on May 10, 1974. Wall Street J., May 13, 1974, at 22, col. 5). 3 CCH COMM. MKT. REP., *supra* note 97, at ¶¶ 23, 151 (1973). The book value of foreign direct investment in Canada in 1967, furthermore, stood at $20,699,000. THE GOVERNMENT OF CANADA, FOREIGN DIRECT INVESTMENT IN CANADA 15 (1972) [hereinafter cited as THE GRAY REPORT].

109. DOING BUSINESS, *supra* note 85, at 18.

110. *Id.* at 21-22; MANUAL, *supra* note 85, at 2.

ship, Commerce and Navigation with the United States[111] and under the Organization for Economic Cooperation and Development,[112] subsequently forced Japan to commence its current program of liberalization that will conclude in 1976.[113]

Several reasons, in turn, may be set forth for French policy toward foreign investment. First, governmental interference with and regulation of business is an historical phenomenon in France;[114] some form of foreign exchange controls have existed since 1939.[115] Secondly, post-World War II French receptivity to foreign direct investment in France yielded in the mid-1960's to nationalist desires to tame foreign influence and insure its subordination to French national interests in the future.[116] The publication

111. Treaty of Friendship, Commerce and Navigation with Japan, Sept. 15, 1953, [1953] 4 U.S.T. 2063, 2082, T.I.A.S. No. 2863. Criticism of Japanese policy toward inward foreign direct investment has come primarily from the United States because of the Treaty terms that mandate full liberalization of Japanese law and national treatment in Japan for American investments and management of companies. *Id.* at 1087; Michida, *supra* note 85, at 10, 21.

112. Convention of the Organization for Economic Cooperation and Development, Dec. 14, 1960, [1961] 2 U.S.T. 1728, T.I.A.S. No. 4891 [hereinafter cited as OECD]. In this regard, note particularly the OECD Code of Liberalization of Current Invisible Transactions and the Code of Liberalization of Capital Movements, which call upon member governments to abolish gradually all restrictions on international capital movements. DOING BUSINESS, *supra* note 85, at 19.

113. Liberalization measures were effected in July 1967, March 1969, September 1970, and in May 1973, to expand the scope of automatic validation of the acquisition of stocks by foreign investors for the purpose of participation in the management of corporations. The Japanese Government currently plans to terminate its liberalization program on May 1, 1976, with controls maintained on the extent of foreign participation in many industries. MANUAL, *supra* note 85, at 2, 22-24 (appendices that set forth the extent of present and future governmental control).

114. The inclination of the French Government to interfere in both domestic and foreign business dates back at least to the Physioeconomics of the eighteenth century, and continues today in the Five-Year Plans. R. DICKIE, *supra* note 97, at 28-30.

115. *Id.* at 22.

116. The lack of foreign exchange reserves and of investment following World War II forced France to seek inward foreign investment. From the early 1960's onward, however, French pride and fear of excessive foreign economic influence as well as foreign political influence, triggered particularly by sizable layoffs of employees in 1962 by Remington Rand and General Electric, gave rise to much stricter investment controls than before. R. DICKIE, *supra* note 97, at 67-72.

of Jean-Jacques Servan-Schrieber's *Le Dêfi Amèricain* in 1967, warning of the danger of an American takeover of the French economy, characterized and helped create a massive and peculiarly French reaction against foreign investment.[117] The French Government soon thereafter instituted the present regime of controls.[118] Fearing the economic benefits accruing to its neighbors due to their more liberal attitudes toward foreign capital, France not surprisingly has advocated a restrictive Common Market investment policy.[119]

Unlike Japan and France, Canada possessed virtually no direct restrictions of foreign investment until 1973, when the government acted to stop the growth of an existing level of foreign ownership and control of economic activity that is unmatched in any other similarly developed state.[120] Sixty per cent of Canadian manufacturing, for example, is controlled by foreigners, while in the petroleum and resource industries this level amazingly exceeds 90 per cent. Equally startling is that approximately one-third of all economic activity in Canada is under foreign domination, with the predominate share held by the United States.[121] These statistics, together with a recent governmental study that concluded an exhaustive examination of the effects of foreign direct investment on Canadian political and economic life with a recommendation for immediate statutory controls,[122] sparked latent Canadian nationalism and brought forth the Foreign Investment Review Act.

5. *The United Kingdom*.—Under the 1947 Exchange Control Act,[123] virtually all investment transactions between residents of

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117. J.-J. SERVAN-SCHREIBER, LE DEFI AMERICAIN (1967).

118. The principal statutory instruments of French policy toward inward foreign investment are the Law concerning Financial Relations with Foreign Countries, of Dec. 28, 1966, [1966] J.O. 11621; the Decree No. 67-78 of Jan. 27, 1967, [1967] J.O. 1073, and the Arrete of Jan. 27, 1967, [1967] J.O. 1074, both of which implement the earlier law. R. DICKIE, *supra* note 97, at 25-28.

119. *Id.* at 72-74.

120. *See* THE GRAY REPORT.

121. *Id.* at 5. In addition, 65% of Canadian mining and smelting is foreign controlled. United States interests control approximately 80% of the total foreign domination in Canadian manufacturing and natural resources. *Id.*

122. *See* THE GRAY REPORT.

123. The Exchange Control Act of 1947, 10 & 11 Geo. 6, c. 14. *See* M. STEUER, P. ABELL, J. GENNARD, M. PERLMAN, R. REES, B. SCOOT & K. WALLIS, THE IMPACT OF FOREIGN DIRECT INVESTMENT OF THE UNITED KINGDOM 9:2, 9:5, 9:6 (1973)

the United Kingdom and non-residents require prior approval from either the Bank of England or the Treasury. As in the aforementioned nations, the British Government weighs the effect of a proposed inward direct investment on foreign exchange reserves, its broader political and economic implications, and other non-statutory and discretionary considerations.[124] To insure a beneficial addition to foreign exchange reserves, the government ordinarily demands that the amount of foreign currency used to finance the investment be proportionate to the size of the interest acquired or created.[125] In addition, any acquired firm that supplies more than one-third of the total market for its commodity, or that holds more than five million pounds in assets is regulated under the 1965 Monopolies and Mergers Act.[126] The government may also condition approval of an investment upon the fulfillment of certain requirements. Few undertakings, however, have been thus conditioned, and in such cases the investors have complied readily to avoid undesirable conflicts with the British Government and public opinion.[127] An investment that offers particularly desirable ef-

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[hereinafter cited as THE STEUER REPORT]. The Exchange Control Act is the only British legislation that is directed specifically at foreign investors, who otherwise enjoy the same treatment that is given British firms. The Exchange Control Act, furthermore, governs investors in the establishment of a new firm or subsidiary, the acquisition of an existing company, and in the subsequent management of the investor's financial affairs in Britain. The Exchange Control Act §§1, 2, 5(c), 6, 8, 9 and 30(2).

124. The rationale for these criteria rests on a *quid pro quo* argument: in return for the right to invest in Britain, foreign investors should yield to the British Government benefits in the form of additions to the foreign exchange reserves. The discretionary criteria of acceptability generally also require that the purchase price of an investment be a "fair consideration" for the assets acquired by the foreign company, and that any further fixed assets financing should be supplied by capital imports in an amount proportionate to the foreign share of the company. Since joining the European Economic Community (EEC), the United Kingdom has allowed unlimited access to British loans for subsidiaries in Britain of companies directly owned by residents of EEC countries for direct investment in the United Kingdom. The STEUER REPORT 9:8-10, 9:12.

125. A major exception to this requirement occurs when the subsidiary's activities "promise special advantage" to the United Kingdom, as when the subsidiary plans to locate in a depressed area. *Id.* at 9:8(a).

126. Any such application may be referred by the Department of Trade and Industry to the Monopolies Commission. *Id.* at 9:16.

127. In the acquisition of majority control of British Rootes, Ltd. by Chrysler,

fects on the British economy, such as location in a rural or depressed region may even be granted special favorable consideration.[128] In fact, despite the available restrictions, the government has approved virtually all inward foreign direct investment.[129]

6. *West Germany.*—Germany exercises perhaps the least control on the inflow of foreign capital of any of the nations considered in this Note. Governmental approval is not required for any foreign direct investment, although foreign investors must report their activity to the government.[130] Of course, foreign investors, like German investors, must still comply with the 1973 Amendment Act, which greatly strengthened the merger and monopoly controls and which is applicable to all business entities, foreign and domestic, operating within Germany.[131]

7. *Liberal Statutory Regulations—A Summary.*—The German and British liberal policies toward foreign direct investment illustrate governmental attitudes that recognize the positive benefits to a host country from the entry of foreign capital. On the part of Germany, a post-World War II adherence to a free market economy, *freie Marktwirtschaft*, together with a desire to use foreign capital to advance post-war reconstruction, underlay the German

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the requested undertakings of Chrysler included the maintenance of a majority of British directors on the Rootes board, a progressive increase in exports, the nomination of a British Rootes director to each of the boards of Simca (French Chrysler) and Chrysler International, and the retention of 15% of the equity of Rootes by shareholders other than Chrysler. Though the British Government possesses no instruments with which to enforce these undertakings, it has enjoyed great success in obtaining cooperation from foreign investors. *Id.* at 9:18-19.

128. *Id.* at 9:8(a).

129. THE STEUER REPORT, at 9:12.

130. 3 CCH COMM. MKT. REP., *supra* note 97, at ¶ 23, 156 (1973).

131. Domestic or foreign parties to a German merger or acquisition must report the transaction to the Federal Cartel Office if 20% or more of the market in a certain sector thereby comes under the control of a single enterprise, or if the entities participating in the transaction together have sales of DM 500 or more, or a combined work force of 10,000 or more. *Id.* at ¶ 23, 510A. The acquisition of 25% or more of the stock of another entity similarly requires a report to the German Government. *Id.* A planned merger in which two or more of the participants enjoy annual sales of DM 1 billion or more necessitates advance reporting. *Id.* at ¶ 23, 510B. The Federal Cartel Office has special power to dissolve or prohibit any planned or completed merger that creates or strengthens a "market dominating position." *Id.* at ¶ 23, 510C.

receptivity to foreign direct investment.[132] This governmental policy has stimulated a massive influx of foreign investment, totalling DM 26 billion by the end of 1972 and representing the operations of 1700 foreign-controlled companies, of which approximately 1200 were American-owned.[133] A recurring and chronic balance of payments surplus forced the West German Government in 1972 to impose restrictions of further inward foreign direct investment to prevent the inflow of speculative capital;[134] however Germany rescinded these provisions in early 1974.[135]

The liberally applied British regulations governing foreign capital investment are a product of an historic national posture that encourages free trade and the creation of substantial British capital holdings in other nations, including the United States.[136] Understandably, then, foreign capital constitutes a large and accelerating position in the British economy.[137] At least 75 per cent of this investment originated in the United States, and all sectors of the American economy have established capital interests in the United Kingdom.[138] Of late, however, this sizeable foreign corporate presence in Britain has provoked a number of evaluative studies, which are of particular interest to Americans who fear the expansion of foreign direct investment in the United States. The most authoritative of these studies, the Steuer Report, was prepared under the auspices of the Department of Trade and Industry[139] and concentrated its evaluation of the effect of foreign direct investment in seven areas—balance of payments, technology, labor relations, monopoly and competitive power, regional economic growth, and

132. 3 CCH COMM. MKT. REP., *supra* note 97, at ¶ 23, 116 (1973).

133. *See* note 108 *supra*; 3 CCH COMM. MKT. REP., *supra* note 97, at ¶ 23, 151 (1973).

134. 3 CCH COMM. MKT. REP., at ¶¶ 23, 124 & 23, 151 (1973).

135. CCH EUROMARKET NEWS, Feb. 5, 1974, at 3.

136. At the end of 1972, British entities held approximately $4.581 billion in American direct investments, or 32% of all foreign direct investment in the United States. *Flanigan Statement*, *supra* note 1, at Table V. Total British direct foreign investments in other countries is greater than £10,720 million. BRITISH INFORMATION SERVICES, BRITAIN'S EXTERNAL TRADE AND PAYMENTS 18 (1973).

137. The book value of all direct foreign investment in the United Kingdom, excluding oil, banking and insurance investments, is £3980. *Id.* at 18.

138. *Id.*; THE STEUER REPORT at 5:10-16, 5:20.

139. *See* note 123 *supra*.

national sovereignty.[140] In brief, the Steuer Report found no present harm to Britain from foreign direct investment. Indeed, it concluded that overall the effect is favorable.[141] The Steuer Report observed in particular that notwithstanding the difficulty in measuring the impact of foreign direct investment on the nation's balance of payments, such investment nevertheless does contribute approximately a two per cent increase in real domestic income.[142] Noting the complex indicia involved in an assessment of technological impact, the authors of the Steuer Report concluded that none of the traditional arguments exactly identify the diverse and apparently neutral effect of foreign capital on the development of British technology.[143] In addition, the largely oligopolistic foreign firms that have invested in Britain have posed a strong deterrent to domestic monopolies and may have increased the level of competition.[144] Foreign direct investment, the Steuer Report noted, also raised employment and increased wages, particularly when the investment was applied in economically weak areas.[145] The authors found practical foreign control of British subsidiaries existed in fewer instances than was feared.[146] Lastly, the investigation not only produced little evidence to indicate a loss of national sovereignty from this investment, but it also suggested that such foreign capital actually increases host country options by raising domestic income and by introducing investment that is naturally more accountable than domestic capital to governmental and public influence.[147] Except for an overall limit on foreign direct investment in Britain, the Steuer Report suggested no further governmental regulation of foreign investment. Indeed, the only affirmative action in this regard counselled by the Steuer Report's authors was a much intensified monitoring of foreign capital activity in Britain to remedy the present lack of thorough data in this area.[148]

140. THE STEUER REPORT, at chs. 2 (balance of payments), 3 (technology), 4 (labor relations), 5 (monopoly power), 6 (regional aspects), 7 (control of subsidiaries), and 8 (national sovereignty).

141. *Id.* at 1:44-51.

142. *Id.* at 1:45, 2:1-33.

143. *Id.* at 1:26, 3:1-42.

144. THE STEUER REPORT, at 1:32-35, 5:1-49.

145. *Id.* at 1:36-38, 6:1-55.

146. *Id.* at 1:39.

147. *Id.* at 1:40-43, 8:1-37.

148. *Id.* at 1:50-51, 9:21-22.

IV. The Current Rise of Foreign Investment in the United States

A. *Causes*

The evident increase in direct foreign investment in the United States may be traced to five factors: (1) the increasingly obvious economic advantages of producing in the American market, especially for those abroad who have exported to the United States in the past; (2) the search for scarce raw materials, food and fuel; (3) the stimulus to foreign investors by both state and federal governments; (4) the devaluations of the dollar and other recent changes in the world economic equilibrium; and (5) the growing Arab and oil-producing nations' monetary reserves that need outlets for investment. First, the economic advantages and potential of the American market make it an obvious place for expansion and exploitation. The sheer size, growth, and unrestricted flow of goods possible in the United States are a lure to the increasing number of foreign entities and multinational corporations that have the ability and desire to expand.[149] In addition, the huge labor resources and technological expertise found in the United States, such as automation, instant communications and computers, provide opportunities for tremendous expansion and economic capabilities not duplicated elsewhere. For those exporters who manufacture abroad for sale in the United States, the advantages are especially apparent. A location nearer their market, as United States multinationals long ago found, may considerably reduce expenses, increase familiarity with the market and lessen the impact of any restrictions that the United States may impose on trade imports. Americans are also more likely to buy goods produced domestically, though in foreign-owned factories, than those produced abroad. The economic reasons alone, are great, then, for foreigners to seek American facilities for production. Secondly, in their efforts to compensate for scarce domestic resources, other nations have found the United States at least a partial source for their needs. Japan, in particular, has sought to assure its future

149. The sheer size and rate of growth of the United States economy were cited by virtually all firms that responded to the Arpan and Ricks survey as being the most important reasons for coming to the United States. *Arpan Statement*, *supra* note 2, at 4.

timber, food and fuel needs by purchasing interests in these commodities in the United States.[150] Thirdly, state and federal governments have actively encouraged direct inward capital investment through foreign advertising, trade seminars and fairs, and development offices in foreign capitals.[151] For example, state development agencies[152] participated in an "Invest in the U.S.A." seminar in Tokyo and Osaka in May 1973, which was co-sponsored by the American and Japanese Governments, and at least twelve states maintain foreign development offices to attract and assist foreign investors.[153] To supplement these efforts the states offer incentives such as low-cost industrial sites, tax breaks and labor training programs.[154] Fourthly, the two devaluations of the dollar in the past three years[155] have altered the United States economic position *vis-à-vis* its world trading partners and made America a much more attractive place in which to manufacture and sell. By reducing the value of the dollar 17.16 percent from its pre-December 1971 level, the American Government considerably lowered the comparative cost of production in the United States.[156] In

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150. Japanese interests have invested chiefly in seafood, timber and pulp in Alaska. *Stitt Statement, supra* note 7, at 5. The Japanese also are investing throughout the world in land and agricultural products because it depends so heavily on imports for its food supply. Since the United States is its major source of food, Japan naturally has great interest in insuring the stability and continuity of the source through direct investment in the United States. *Id.* at 10-11.

151. *See Stitt Statement, supra* note 7, at 7-8; Statement of Frank Alspaugh, Director of the Virginia Division of Industrial Development, and Chairman of the International Committee of the National Association of State Development Agencies (NASDA) at *Hearings on Foreign Direct Investment in the United States Before the Subcomm. on Foreign Economic Policy of the House Comm. on Foreign Affairs*, 93d Cong., 2d Sess., Feb. 5, 1974 (pre-publication transcript) [hereinafter cited as *Alspaugh Statement*], at 2-4.

152. *Stitt Statement, supra* note 7, at 7-8. In the past two years, approximately twenty individual state, city and county missions have visited Japan to encourage investment in the United States. *Id.* at 8.

153. Those states are Alabama, Alaska, Georgia, Illinois, Maryland, Michigan, New York, North Carolina, South Carolina, Texas, Virginia, Wisconsin and Puerto Rico. *Alspaugh Statement, supra* note 151, at 3.

154. *Stitt Statement, supra* note 7, at 8.

155. These devaluations occurred in December 1971, and in February 1973. Wall Street J., Apr. 5, 1974, at 18, col. 1.

156. N.Y. Times, Dec. 19, 1971, at 1, col. 8; *Id.* Feb. 13, 1973, at 45, col. 4; Wall Street J., Apr. 19, 1974, at 4, col. 2.

addition, skyrocketing world inflation and burgeoning labor costs outside the United States have contributed to this new advantage.[157] This trend is highlighted by the recently negotiated 30 per cent increase in Japanese wage rates following the annual "spring offensive" by Japanese labor.[158] American realty costs, especially as compared to those in Japan, are now especially competitive in the world market because of both the devaluation and the amount of available land.[159] Coupled with devaluation, the fall in American stock prices during the past two years has made United States securities even cheaper and foreign corporate purchases of American stock a much more viable proposition.[160] Fifthly, the 400 per cent increase in the world price of oil[161] during the past year has precipitated a huge and growing accumulation of monetary reserves by the major oil producing nations and much of this bounty has been invested in the United States.[162] The stabil-

157. *See* note 11 *supra*. While United States labor costs rose 1% in the first six months of 1973 above the comparable period in 1972, Japan's labor expenses jumped 11.6%, measured in United States dollars. According to the United States Bureau of Labor Statistics, between 1969 and 1972, United States labor costs rose an average of 1.8% annually, while those of Japan climbed at a much sharper rate of 4.1% per year. Wall Street J., Jan. 21, 1974, at 6, col. 2.

158. N.Y. Times, Apr. 14, 1974, at 15, col. 1.

159. Property in downtown Los Angeles, for example, sells at $50 per square foot, while similar land in Tokyo sells at $900 per square foot. Among the Japanese purchases that are concentrated on the West Coast are the Beverly Wiltshire Hotel in Beverly Hills, and numerous golf courses, apartment buildings and expensive homes. Wall Street J., Jan. 21, 1974, at 6, col. 2.

160. *See* note 12 *supra*.

161. The posted price of crude oil stood at approximately $11.63 per barrel on March 15, 1974, a 400% increase from a year earlier. N.Y. Times, Mar. 15, 1974, at 45, col. 7. The posted price is a mythical number on which government taxes and royalties are computed. N.Y. Times, Mar. 16, 1974, at 11, col. 1.

162. The oil revenues of the Arab oil producing nations should soar from a total of $22 billion in 1973 to between $85 billion and $110 billion in 1974, and will create a pool of approximately $50 billion for foreign investment. Chase Manhattan Bank estimates, furthermore, that by 1980 Arab foreign currency reserves should swell to more than $400 billion from a total of $5 billion in 1970. Wall Street J., Mar. 5, 1974, at 1, col. 6. The combined GNP of all the Arab producers should reach $74 billion in 1974, double the figure for 1973. N.Y. Times, Mar. 20, 1974, at 59, col. 2. Per capita income in the Sheikdom of Abu Dhabi, in addition, will rise to $45,000 in 1974, compared to $6,127 in the United States. *Id.* Changing their traditionally ultraconservative investment policy, the Arabs are evincing interest in United States real estate, banks and joint ventures, particularly in energy-related fields. Wall Street J., Mar. 5, 1974, at 1, col. 6.

ity and growth of the American economy have particularly attracted the attention of the Arabs, and they have reportedly decided to abandon their traditionally conservative investment goals in favor of more growth-oriented ventures, which abound in the United States.[163]

B. *The Current Extent of Foreign Direct Investment in the United States*

The Commerce Department's book value of direct foreign investment in the United States stood at approximately 14.363 billion dollars on January 1, 1973, compared to a 94.031 billion dollar book value for direct United States investments abroad.[164] The United Kingdom, Canada, the Netherlands and Switzerland are the chief sources of this inward investment.[165] Of this total book value, foreign capital invested in manufacturing counted for half, and petroleum, one-fourth.[166] Approximately 1200 foreign companies engage in American manufacturing, mining and petroleum production.[167] New foreign direct investment is concentrated chiefly in four areas: electrical machinery, non-electrical machinery, chemicals and scientific equipment.[168] Moreover, the vast majority of investments have taken the form of newly created subsidiaries or direct manufacturing operations of existing foreign companies, funded from abroad and created without any United States Government assistance.[169] United States citizens constitute virtually all of the employees of these firms, and sit as presidents or members of the boards of directors in roughly half of these ventures.[170] All of the investors previously had invested directly in at least one other

163. *Id.*

164. *Flanigan Statement, supra* note 1, at A Table 1. The accuracy of the calculation for foreign direct investment in the United States is subject to some dispute. Messrs. Arpan and Ricks estimate that this total should be $38 billion, and ascribe the Commerce Department's figure to certain weaknesses in its investigatory methods. *Arpan Statement, supra* note 2, at 7.

165. *Flanigan Statement, supra* note 1, at Table V.

166. *Id.* at Table VI.

167. *Arpan Statement, supra* note 2, at 2. Messrs. Arpan and Ricks estimate that nearly 1500 firms in the United States are foreign controlled. *Id.*

168. *Id.* at 5.

169. *Id.*

170. *Id.*

foreign country before making their American investment and had had prior experience in exporting to the United States.[171] During 1973, the level of foreign direct investment in the United States rose much more sharply than in 1972 and increased by more than three billion dollars.[172] The leading sources of foreign direct investment in the United States in this period were Japan, Canada, West Germany and Britain.[173] More than two-thirds of these investments involved the construction of entirely new facilities, most of which constituted an initial direct capital investment in the United States.[174] The chemical, electrical-equipment and textile industries paced this growth, which occurred most heavily in the Southeastern states and California.[175] Typical major new projects include a 175 million dollar South Carolina plant for the Michelin Tire Company of France, plans for a 100 million dollar Volvo automobile factory in Virginia[176] and the 100 million dollar petrochemical complex in Texas of the American subsidiary of Farbwerke Hoechst AG, the West German chemical concern.[177] Foreign direct stock acquisitions in American corporations accounted for a much smaller percentage of foreign direct investment, but has included the takeover of numerous well known entities such as Gimbels Brothers' department stores, Grand Union Company's supermarkets, TraveLodge International, Inc.'s motels and Standard Oil Company of Ohio.[178] Foreign investors have also demonstrated an increasingly strong interest in real estate. The Japanese have moved with particular force in this sphere in western United States, and purchased several major hotels and reportedly acquired more than 300 million dollars alone in realty and resort

171. *Id.*

172. The Conference Board, a private nonprofit research organization, reached this conclusion based on the analysis by David Bauer, an international economist on its staff. N.Y. Times, Feb. 18, 1974, at 39, col. 7. This figure is considerably larger than the $2 billion unofficially estimated by the Commerce Department, and demonstrates the uncertainty of present statistics and information. Wall Street J., Jan. 22, 1974, at 1, col. 6.

173. N.Y. Times, Feb. 18, 1974, at 39, col. 7.

174. *Id.* at 39, col. 7 and 41, col. 1.

175. *Id.* at 41, col. 1.

176. *Id.*

177. *See* note 5 *supra.*

178. *See* note 6 *supra.*

properties in Hawaii.[179] Increasingly evincing a similar inclination are the Arabs, who may invest at least one billion dollars in United States real estate during the next two years.[180] Direct Kuwaiti investments of this nature already total 100 million dollars. The Kuwaiti Investment Company, jointly owned by the Kuwait Government and private Kuwaiti investors, has purchased a half interest in the Atlanta Hilton Center and plans to turn its 17.3 million dollar investment in Kiaweh Island, South Carolina into a 100 million dollar resort modeled on its neighbor, Hilton Head Island.[181] Likewise, the Shah of Iran has recently purchased a New York office building.[182] The above examples are but a few of the many realty investments of this sort.

The prospects for continued growth in inward direct investment are mixed and necessarily dependent on the vagaries of the world economic equilibrium and its determinants. Continued instability of the United States dollar and trade balance and the greater stability of balance of payments in foreign economies, naturally will be a key factor in future growth in this regard. Germany is in an especially strong position in that respect while the recent weakness of the yen has caused Japan to restrict the purchase of foreign securities by her citizens.[183] The extraordinary wage increases recently won by Japanese workers, however, and the continued governmental policy favoring direct capital expenditures abroad, argue for the probable continuation of expanding Japanese investment in the United States. The changes in other basic economic considerations, such as productivity, unit labor cost and technological developments, which are all partly dependent on the balance of payments, are difficult to ascertain, but the size and growth of the United States economy, together with the relative natural resource security of the United States and the continued growth of foreign firms having the expertise and size necessary to

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179. *See* note 8 *supra*.

180. Wall Street J., Mar. 5, 1974, at 33, col. 6.

181. *Id.*, Mar. 5, 1974, at 1, col. 6; N.Y. Times, Mar. 3, 1974, at §F, at 15, col. 4.

182. Wall Street J., Mar. 5, 1974, at 1, col. 6.

183. *Stitt Statement*, *supra* note 7, at 6. Nevertheless, the Japanese Government will continue to give priority to projects involving the exploration of petroleum and other natural resources, as well as investment in manufacturing abroad in order to maintain or expand markets. *Id.*

expand into the United States, likely should contribute to a sizeable growth of foreign direct investment in the United States in the near term. The inability of the oil producing nations to absorb their wealth, despite intensive efforts to use their new found riches in rapid domestic economic development, necessitates foreign investment.[184]

V. THE PROPOSED LEGISLATION

The legislative proposals submitted separately by Representatives John Dent and John Moss would restrict only the acquisition by foreign persons or entities of securities in existing American corporations that are registered under the Securities and Exchange Act of 1934. These bills, therefore, would not affect in any way the creation by foreign investors of subsidiaries or wholly owned direct manufacturing operations. Representative Dent's proposal, the stricter of the two, is known as the "Foreign Investors Limitation Act."[185] The addition of section 12(A) to the 1934 Act would prohibit in the future any non-citizen, or United States entity that is owned or controlled by a non-citizen, from acquiring directly or indirectly more than five per cent of the voting securities of any issuer that is registered under section 12 of the Securities and Exchange Act of 1934.[186] Any such person who, at the time of the Foreign Investors Limitation Act's passage, controlled more than five per cent of the voting securities of such an issuer could thereafter acquire no more of those securities.[187] Moreover, any noncitizen or foreign-controlled United States entity would have to register with the Securities and Exchange Commission prior to its acquisition of the securities of any registered American issuer.[188] The purpose of the Dent bill is to counteract the dangers of foreign control of American industry and encourage the diversification of foreign investment in domestic industry.[189] The legislation drafted by Representative Moss, entitled the "Energy and Defense Indus-

184. *See* note 161 *supra*.
185. H.R. 8951, 93d Cong., 1st Sess. (1973), at preamble [hereinafter H.R. 8951].
186. H.R. 8951, at §3. This prohibition would also extend to the acquisition of more than 35% of the nonvoting securities of such a company. H.R. 8951.
187. H.R. 8951.
188. H.R. 8951.
189. H.R. 8951, at §2.

try Production Act,"[190] is less restrictive than the Dent bill. This bill would make it illegal for a non-citizen of the United States, or by an entity that is owned or controlled by a non-citizen, to control any American issuer, registered under section 12 of the 1934 Securities and Exchange Act, that is engaged in an energy or defense industry.[191] For purposes of the Moss bill, "control" would mean the direct or indirect ownership of ten per cent of the voting securities of the American issuer, although the Securities and Exchange Commission in its discretion could lower this figure in special cases.[192] An issuer engaged in the energy industry would be one whose principal business is the production or processing of crude oil, residual fuel oil, refined petroleum products, shale, natural gas, coal, geothermal steam, uranium and electricity.[193] A "defense industry" issuer would be one that derives twenty per cent or more of its gross revenues either directly or indirectly from contracts with the armed services or the United States Department of Defense or whose products the Department of Defense designates as vital to the national defense.[194] After appropriate notice and opportunity for hearing, however, either the Administrator of the Federal Energy Administration or the Secretary of Defense could exempt an issuer engaged in the energy or defense industries, respectively, from the prohibitions of this bill if the Administrator or Secretary should determine that such an exemption would not adversely affect either the production or supply of energy within the United States, or the national defense.[195]

VI. An Evaluation of the Desirability of Further United States Statutory Restrictions

The legislation restricting further foreign stock purchases in and control of United States businesses offered separately by Representatives John Dent and John Moss, are symptomatic of the apprehension in the United States about the rapidly expanding level

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190. H.R. 12040, 93d Cong., 1st Sess. (1973), at preamble [hereinafter H.R. 12040].
191. H.R. 12040, at §2.
192. H.R. 12040, at §2.
193. H.R. 12040, at §2.
194. H.R. 12040, at §2.
195. H.R. 12040, at §2.

of foreign direct investment. Since this phenomenon is of extremely recent origin comparatively little statistical or evaluative information exists with which to ascertain its desirability. Consequently, the angry and worried response of the public, the press and members of Congress, which has prompted these bills, has been free from either statistical verification or refutation. The urgency with which the public and Representatives Dent and Moss have reacted, nevertheless, demands an evaluation of foreign direct investment in the United States and of the merit of further statutory restrictions on its growth.

The domestic economic benefits that the United States derives from the inward flow of foreign direct capital are substantial. New jobs are created and new technology is introduced that raises workers' skill levels, wages and overall productivity.[196] Foreign investment such as the Sony plant in San Diego[197] also increases competition, lowers prices and causes at least short-term improvement in the balance of payments by increasing the flow of money into the United States. Tax revenues, in addition, rise as new factories contribute to local tax bases. Moreover, the interest shown by foreign manufacturers in locating in the Southeastern states hastens the development of this less advanced area.[198] Foreign funds supplement the existing scarce investment resources that are essential to the expansion of the United States economy.[199] The beneficial economic effects of inward foreign investment also extend indirectly to the multitude of domestic suppliers, transporters and distributors, among others, who are part of the commercial process. The opportunities, therefore, are great for foreign direct investment to have a constructive impact on the American economy.

196. *Farmer Statement, supra* note 9, at 3-5.

197. Sony's San Diego factory produces 25,000 color televisions and 5,000 record players monthly with a labor force of 350 workers that will increase to 600 following present plant expansion. *See, Stitt Statement, supra* note 7, at 3.

198. South Carolina, Georgia, Alabama, North Carolina and Virginia currently are very attractive to foreign investors. N.Y. Times, Feb. 18, 1974, at 41, col. 1.

199. Chauncey E. Schmidt, vice chairman of the First National Bank of Chicago recently stated: "There is hardly a crisis today . . . . where the wise allocation of the world's capital resources could not contribute greatly to a solution [to] . . . apparent global shortage of the financial underpinning that is the first prerequisite for a healthy world economy. N.Y. Times, Mar. 10, 1974, §3, at 2, col. 8.

That the effects of foreign direct investments would be beneficial is substantiated by the positive conclusions found in the British Steuer Report.

One may argue, on the other hand, that opportunity also exists for foreign investors to gain control of whole sectors of the nation's economic life, as United States multinational corporations have done elsewhere,[200] and that foreign investment will detrimentally affect the long-term United States balance of payments through the outflow of dividends and profits to foreign corporate parents. The inevitability of these suppositions must be questioned. Despite the obvious injury wrought to the balance of payments by dividend payments abroad, inward direct investment will substitute goods produced domestically and by American labor for those formerly imported, and may even create sources for exports. Either or both of these beneficial consequences might well overcome long-range deleterious effects. The net beneficial impact on the balance of payments,[201] resulting from foreign direct investment is affirmed by the Steuer Report, which found a two per cent increase in domestic per capita income in Britain. Moreover, the likelihood of future foreign dominance in American industrial sectors is extremely remote. Existing foreign direct investment in the United States controls merely one-fourth of one per cent of American corporate assets, and is scattered in many fields.[202] The entire 1973 inward foreign direct investment equalled only two per cent of American expenditure during the same period on business, plants and equipment.[203] The prospect, therefore, of any foreign economic takeover is virtually nil. Should such a threat arise, however, the existing restrictions and statutory powers that the government already possesses could be effective instruments to prevent entry into a number of fields, or to obstruct monopolization and undue influence in others, and if necessary, the federal government could resort to nationalization.

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200. United States companies control the following percentages of the auto market in selected European nations: 38% in Germany, 12% in Italy, 20% in Sweden and 45% in Great Britain. In comparison, Germany contributed only 5.5% of the cars registered in the United States in 1972.

201. THE STEUER REPORT, at 1:45.

202. In contrast, American multinationals in Europe own approximately 5% of total European corporate assets. *Flanigan Statement, supra* note 1, at 11.

203. *Id.*

Future growth in the United States of foreign direct investment depends on the product of many widely fluctuating factors that suggest an uncertain and uneven growth, consequently further reducing the threat of extreme foreign economic influence. The past sporadic growth of foreign investment in the United States[204] should alone temper these fears. The volatibility of the world economy, in addition, argues strongly for the same conclusion. The fluctuating strength of the dollar, together with the occurrence of unfavorable foreign economic indices, such as negative Japanese trade balances,[205] which have forced the Japanese Government to impose foreign investment restrictions,[206] may dampen the flow of foreign capital to America. The prospect of massive and unified United States investment of Arab oil money, in turn, must yield to certain qualifying evidence. First, notwithstanding the lure of the apparent stability and prospective growth of the American market, the fear of anti-Arab sentiment among the American people and the remote chance of United States expropriation of investments has affected Arab thinking, and should cause them to exercise circumspection and discretion in their United States investments.[207] Secondly, historical evidence also indicates that the multinational sources of Arab investment will fail to effectively coordinate their economic power. Thirdly, all of the oil-producing nations recognize the need to develop economically and diversify their economies to protect against the dilution of their oil resources.[208] This development will tie up a huge share of the oil

204. Between 1960 and 1972, net annual foreign direct investment in the United States peaked at $1.45 billion in 1970, and then approached its low point for that period the next year, when the nation experienced a net outflow of $385 million in foreign investment. *Flanigan Statement, supra* note 1, at Table II.

205. Japan experienced a January 1974 trade deficit of $784 million, followed by a $650 million deficit in February. These deficits were the first for Japan in three years. N.Y. Times, Mar. 16, 1974, at 42, col. 4-5.

206. *See* note 182 *supra* and accompanying text.

207. Aware of the controversy surrounding growing Japanese interest in direct investment in the United States, the Arabs fear a similar backlash and a possible freeze on Arab assets in United States banks. Wall Street J., Mar. 5, 1974, at 33, col. 6.

208. N.Y. Times, Mar. 20, 1974, at 53, col. 5. Leonard Silk of the New York Times suggests that the Arabs have developed a five point strategy for the future: (1) maximize oil profits; (2) keep the oil price high; (3) maintain world dependence on oil; (4) maximize domestic capital accumulation; and (5) achieve lasting diversified economic development. *Id.*

income, and is a process in which United States multinationals shall participate and, therefore, increase United States influence in the oil world.[209] Lastly, much Arab money will likely be distributed through aid programs to the underdeveloped world. Iran, Algeria and Libya, supported by the World Bank and the United States, already have moved cautiously toward creating an Arab fund for economic development.[210] Kuwait itself supports its own existing 600 million dollar assistance fund.[211] With such evidence, therefore, one must not yield to an *ad hominem* conclusion that foreign direct investment is about to take over the American economy.

The political arguments against new restrictions on inward foreign direct investment are equally cogent. In a number of ways, a program of further controls would weaken the nation's liberal foreign trade policy of encouraging economic and political interdependence in the Western world. Further statutory restrictions would contradict the goals of the GATT and the Organization for Economic Cooperation and Development to maximize the flow of world trade and investment. The United States would contravene its bilateral treaties of friendship, commerce and navigation in which each signatory guarantees, with only limited exceptions, national treatment for foreign investors. The bargaining position of the United States in the proposed new round of tariff reduction negotiations under the GATT naturally would be less forceful than otherwise, if the government should adopt contradictory investment controls. The reactions of United States world trading partners might be especially harmful; after tolerating the inflow of massive American capital since the last world war, these nations would likely find hypocritical any efforts now to restrict investment flowing from these nations to the United States. The United Kingdom, Germany, and Canada, the prime recipients of Ameri-

209. The Saudi Arabian Government has approached several United States companies with plans for joint construction there of energy and petrochemical projects. Wall Street J., Apr. 10, 1974, at 5, col. 1.

210. The strongest support for this proposal comes from Iran, which suggested in February 1974 that a $2-3 billion fund be jointly created by the oil exporting and Western industrialized nations. Additionally Iran has already offered $600 million to the International Monetary Fund for short-term loans and aid to developing nations. N.Y. Times, Apr. 7, 1974, at 7, col. 1.

211. Wall Street J., Apr. 8, 1974, at 8, col. 3.

can capital, particularly would be offended at legislation such as the Dent and Moss proposals, which would prohibit direct stock ownership at levels much more restrictive than their own regulations. The Japanese, who were forced by the United States to liberalize their investment regulations, would also react unfavorably. Retaliation to new restrictions, a not unlikely prospect, would severely damage the security and productivity of American investment abroad and possibly portend a destructive wave of trade protection that could cripple world trade. New statutory restrictions on foreign direct investment, therefore, could undermine United States credibility and sever the now tenuous ties of Western policital unity. On the contrary, at least one major dividend to American foreign policy from an unrestricted inflow of foreign capital would be greater cooperation between the United States and the Arab nations. American investment of Arab oil money naturally could foster a greater identity of economic interest between the United States and the Arabs through a mutual desire for a stable and healthy American economy. The most decisive result of this situation could be greater United States leverage in the Arab world.

One must conclude, then, that any discriminatory restrictions against foreign direct investment at this time, such as proposed by Representatives Dent and Moss, at best would be premature, and at worst dangerous to United States economic and political interests. The sudden growth of this influx of foreign capital, the adverse public reaction to it and the paucity of information with which to judge its effect on the United States, however, all suggest the need for some sort of response. The ramifications of any governmental action still are sufficiently unclear and potentially dangerous that extreme care must be taken in this regard. Senator Inouye's proposal for an exhaustive survey and evaluation of current foreign direct investment in the United States[212] is the wisest course at this time. The knowledge, which such a survey could produce, far outweighs any intervening harm that more foreign investment could produce. Another course, simultaneously would be a multilateral convention creating a world investment code to govern rights of host and investor nations and the rights of private

212. S. 2840, 93d Cong., 1st Sess. (1973).

investors as well. Though a recent phenomenon in the United States, foreign direct investment already has so greatly influenced the economies of most other nations that its impact demands a global response.

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