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**BEFORE THE HOUSE SUBCOMMITTEE
ON DIGITAL COMMERCE AND CONSUMER PROTECTION**

**TESTIMONY FOR THE HEARING:
"PERSPECTIVES ON REFORM OF THE CFIUS REVIEW PROCESS"**

CELESTE DRAKE
**THE AMERICAN FEDERATION OF LABOR &
CONGRESS OF INDUSTRIAL ORGANIZATIONS (AFL-CIO)**

APRIL 26, 2018

Contents

Introduction..... 2

The Foreign Investment Risk Review Modernization Act (FIRRMA) 4

 Figure 1: China’s Foreign Direct Investment Transactions in the United States, 2005-2016
 (Source: The Rhodium Group)..... 4

Beyond FIRRMA..... 8

 Why Additional Greenfield Investment Review is Important: The Case of Tainjin Pipe 10

Conclusion 12

Introduction

The AFL-CIO is the umbrella federation for America's unions, with 55 unions representing more than 12 million working men and women in every sector and industry of the American economy. We aim to ensure that all people who work receive the rewards of that work—decent paychecks and benefits, safe jobs, respect, and fair treatment. We work to make the voices of working people heard in the White House, on Capitol Hill, and in state capitals, city councils, and corporate boardrooms across the country.

The AFL-CIO and its affiliate unions support investment that creates good jobs, whether that investment is foreign or domestic. We believe that the value of an investment in the U.S. should be determined not primarily by the nationality of the investor, but by whether the investment will create good job opportunities and provide employees with a voice at work. In determining whether any particular foreign investment would be beneficial for the security of United States, we believe the determination must recognize that our economic and national security are inextricably intertwined. Our economy is the source and foundation of our national security.

While foreign direct investment (FDI) *can* contribute to the creation and maintenance of high-skill, high-paying jobs, such an outcome is not inevitable. The potential failure of some FDI to create and sustain high-wage jobs is a real concern. The goal of some foreign investors may not be to make a long-term or even medium-term investment in the U.S., but rather to drive existing U.S. competitors out of the market or to transfer valuable technology, equipment, intellectual property, and other assets to the home country or other points abroad. Either goal is likely to ultimately cause job loss in the U.S. and injury to national security interests.

Because of these risks, we have long supported updates and improvements to the foreign direct investment reviews performed by the Committee on Foreign Investment in United States

(CFIUS). CFIUS's current charge is quite limited: it reviews mergers and acquisitions (as opposed to "brand new" investments, known as "greenfield" investments), and it very narrowly assesses threats to national security (as opposed to economic security). Even more importantly, CFIUS provides no systematic review process. Parties to a proposed or pending transaction may, but are not required to, jointly file a voluntary notice with CFIUS. Otherwise, the President or the Committee may initiate a review, but first a transaction must come to their attention. There are reportedly thousands of transactions that have never been submitted to CFIUS, but which are potentially subject to later review.

This Subcommittee's attention to CFIUS comes at an important and opportune moment. During the past year, the administration has engaged in a number of studies and enforcement actions aimed at reforming U.S. trade and investment policy. These actions are nominally intended to address the enormous, job-killing U.S. trade deficit, protect our national security, and combat trade cheating by China and others. If these studies and actions represent part of a coordinated, thoughtful strategy, they could help recalibrate trade policy to grow jobs in the cutting-edge manufacturing sector, reduce incentives to outsource, and provide greater benefits of trade to ordinary working families. It remains to be seen if Congress and the administration can work together to reset trade and investment policy in this manner. In the meantime, a focus on FDI is an area ripe for bipartisan cooperation.

We appreciate the opportunity to raise issues important to working people in the context of CFIUS reform. The next section will provide a brief summary of the ways in which the Foreign Investment Risk Review Modernization Act (FIRRMA) will benefit America's working people while enhancing our national security. The final section of this testimony will highlight

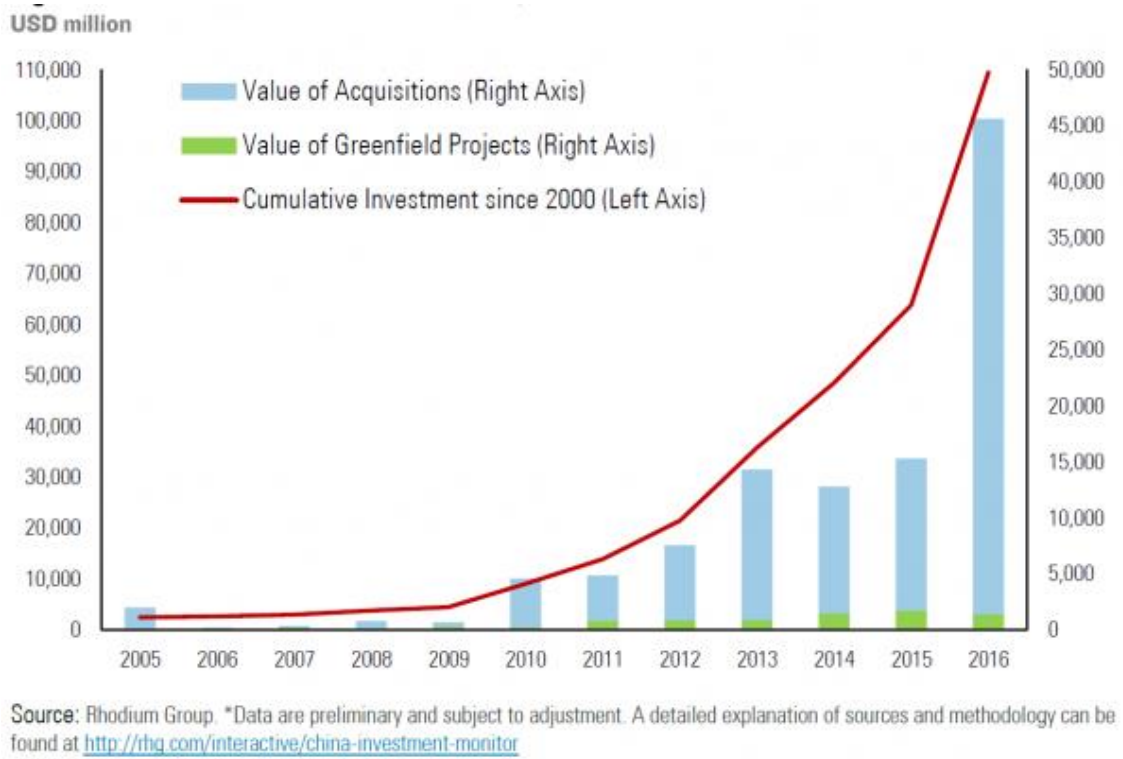
additional issues of special concern to working families in the review of foreign investments in the U.S.

The Foreign Investment Risk Review Modernization Act (FIRRMA)

The Foreign Investment Risk Review Modernization Act (FIRRMA) is reasoned legislation that balances the desire to maintain an open investment climate with important national security interests. We oppose efforts to diminish the scope of the legislation. Indeed, the AFL-CIO would recommend expanding it in a variety of ways.

The United States has witnessed unprecedented foreign investments from strategic competitors including China, which invested a record \$45.6 billion in the U.S. in 2016. (See *Figure 1 for trends in China's investment.*)

Figure 1: China's Foreign Direct Investment Transactions in the United States, 2005-2016 (Source: The Rhodium Group)



In response to this long-term trend, the bipartisan U.S. China Economic and Security Review Commission (USCC) has repeatedly recommended that Congress consider strengthening CFIUS, including by offering these critical recommendations in 2012:

- (1) requiring a mandatory review of all controlling transactions by China's state-owned and state-controlled companies investing in the United States;
- (2) adding a net economic benefit test to the existing national security test that CFIUS uses; and
- (3) prohibiting investment in a U.S. industry by a foreign company whose government prohibits foreign investment in that same industry.¹

Since the 2012 Report, the USCC has reiterated and expanded its recommendations even while the threat has grown. CFIUS has been criticized in the intervening years for not acting to block or mitigate a number of transactions, including with respect to the Chicago Stock Exchange, the Vertex Joint Venture with the China Railroad Rolling Stock Company, and the Ingram Micro acquisition.

FIRRMA represents a critical opportunity to address some of the USCC's long-standing concerns in a bipartisan manner. FIRRMA will provide CFIUS with increased support and flexibility, enabling it to respond more effectively to efforts by China and other nations² to buy the technological and military competencies of the United States. While we had hoped that FIRRMA would recognize the common-sense conclusion that economic security is an inherent component of national security (as does Section 232 of the Trade Expansion Act of 1962 (*see* 19

¹ These recommendations, still unaddressed, come from the 2012 Report to Congress of the U.S.-China Economic and Security Review Commission, Executive Summary and Recommendations, available at https://www.uscc.gov/sites/default/files/annual_reports/2012-Report-to-Congress-Key%20Recs.pdf.

² It is important to note that, while the examples used in this testimony focus on China-based enterprises, the AFL-CIO is concerned with the question of how particular investments will help support or harm national security, broadly construed—not with the country from which investments originate. The discussion focuses primarily on China because of the magnitude of China's investment and the level of participation in such investment by the Government of China, as well as the fact that the USCC is an excellent source of reasoned policy advice with respect to how to appropriately address increased investment that may pose threats to America's long term interests. The AFL-CIO urges the Subcommittee to consider the USCC's recommendations to expand FIRRMA and CFIUS with respect to foreign investors *of any national origin*.

U.S.C. §1862)) and adopt a net economic benefit consideration when reviewing transactions, we believe the bill, as introduced, is an important and necessary step forward.

The United States cannot allow its economic and technological advantages to fall into the hands of foreign companies that engage in efforts to undermine our nation's strength and security, as happened in the Magnequench acquisition.³ As such, the U.S. must strengthen its opportunities, in the words of Ericsson Vice President and General Counsel John Moore, "to properly vet and scrutinize the efforts by foreign entities to gain access to our markets and our technology."⁴

China, though not the only threat to the United States, is of particular concern given its ongoing use of illegal and unfair strategies to deprive the American people of their economic and national security. Such strategies include, but are not limited to: denial of national treatment and refusal to open market access to U.S. firms; the use of prohibited subsidies, forced technology transfer, and improper export controls; preferential debt and equity financing for state-owned and state-controlled enterprises; overcapacity in strategic industries including steel and aluminum that drives U.S. firms out of business; dumping; hacking, cyber espionage, and intellectual property theft; the denial of internationally recognized workers' rights that drives down China's labor costs and retards consumer demand; and predatory lending to developing countries that undermines their opportunities for growth and expansion.

³ For more information on this acquisition of a U.S. firm that made products used in magnets integral to the guidance system of cruise missiles, by a China state-owned enterprise please see Jeffrey St. Clair, "The Saga of Magnequench," in *Counterpunch*, April 7, 2006, available at <https://www.counterpunch.org/2006/04/07/the-saga-of-magnequench/>. A little over a decade after the original 1995 acquisition, Magnequench shuttered operations in the U.S. for good, transferring its remaining machinery to China. See also John Tkacik, *Magnequench: CFIUS and China's Thirst for U.S. Defense Technology*, May 2, 2008, The Heritage Foundation, <https://www.heritage.org/asia/report/magnequench-cfius-and-chinas-thirst-us-defense-technology>.

⁴ Letter from John Moore to the Honorable Robert Pittenger, dated January 16, 2018.

FIRRMA's reforms, focused on national security concerns, represent a measured approach to troubling trends in FDI that CFIUS is currently ill-equipped to address. As drafted, FIRRMA would:

- Expand CFIUS jurisdiction to include certain joint ventures, minority-position investments, and real estate transactions near sensitive national security facilities;
- Update the definition of "critical technologies" to include emerging technologies that could be essential for maintaining a U.S. technological advantage;
- Authorize CFIUS to exempt certain transactions if all foreign investors are from an allied country;
- Create shorter "light filings" with reduced paperwork burdens, as well as mandatory filings for certain higher risk transactions; and
- Expand the national security factors for CFIUS to consider in its analyses, but not create a net economic benefit test.

Simply put, the time has come to mandate reporting of significant, high-risk FDI transactions. Among the other important changes FIRRMA would make are ensuring that new investment strategies and structures can be addressed by CFIUS, that critical technologies can be identified and protected, and that joint venture and cooperative investments by U.S. companies will be subject to review when they potentially jeopardize U.S. security. Globalization has changed the way business is done. CFIUS must rise to these new challenges.

Some may wonder why the AFL-CIO has an interest in strengthening the ability of CFIUS to review investments on national security grounds—our interest is two-fold. First, as the representative of America's working families, we have an interest in CFIUS because CFIUS is a jobs issue. Second, foreign investments to acquire U.S. assets that undermine our national

security both weaken our country and weaken our defense industrial base, affecting manufacturing jobs and wages even in the absence of a net economic benefits test. Simply put, we want CFIUS to work because that is what is right for America's working families.

Accordingly, we support FIRRMA as a step toward helping ensure that America's competitors cannot take advantage of our openness in an attempt to strip the United States of its global economic and security leadership.

Beyond FIRRMA

FIRRMA does not address all of CFIUS's shortcomings. America's working people have a number of additional concerns.

The United States has benefitted from open markets, but that benefit is not absolute, nor guaranteed. It must be safeguarded and preserved with smart policies. Congress has a responsibility to monitor developments in the U.S. economy and act to protect U.S. residents when market failures injure America's hardworking families. One such market failure is occurring now: unrestrained, unreviewed foreign investments that have the potential to rob us and our children of our economic future.

That is why the AFL-CIO recommends following the USCC's advice to add a net economic benefits test to CFIUS. Already, trading partners including Australia⁵ and Canada⁶

⁵ In Australia, the Foreign Investment Review Board typically considers national security; competition; the impact on other Government policies (including taxation); the impact on the economy and the community; and the character of the investor in determining whether any particular investment is in the national interest. "Australia's Foreign Investment Policy," (January 1, 2018) available at <https://cdn.tspace.gov.au/uploads/sites/82/2017/06/Australias-Foreign-Investment-Policy.pdf>.

⁶ In Canada, investments made to directly acquire ownership and control of certain Canadian businesses with assets above a minimum threshold are approved only if the Minister of Industry determines the transaction is likely to be of "net benefit" to Canada. Factors considered in the determination are: 1) the effect of the investment on economic activity in Canada; 2) the degree of participation by Canadians; 3) the effect of the investment on productivity, efficiency, technological development, innovation and product variety in Canada; 4) the effect on competition; 4) the compatibility of the investment with national industrial, economic and cultural policies; and 6) the contribution to Canada's ability to compete globally. Mathieu Frigon, "Foreign Investment in Canada: The Net Benefit Test," (Library of Parliament), available at <https://lop.parl.ca/content/lop/ResearchPublications/cei-22-e.htm>.

require foreign investments to undergo a similar review. Such a review would consider not just strategic acquisitions that could turn advanced technologies against us, but also strategic acquisitions designed to strip high value-added production jobs from the U.S. Adding an economic benefits test could change an intended “acquire and run” acquisition into a longer-term investment and induce the investor to continue operating the U.S., creating more jobs opportunities for U.S. workers. Limiting CFIUS review to a narrow and outdated definition of national security leaves open the prospect of predatory acquisitions designed to weaken our economy—not just acquire strategic technology and know-how. A weakened economy has fewer jobs and lower wages and creates impediments to making the security investments necessary to keep working families safe.

The AFL-CIO also recommends expanding CFIUS’s ability to review greenfield investments beyond those proximate to a military base or other strategic facility. Given the demonstrated ability of the Government of China to guide and manage foreign investments to achieve long-term goals, it would seem prudent to expand the scope of investments subject to CFIUS review, so that we do not, as a nation, face challenges that could have been prevented or mitigated with appropriate and timely action.

Finally, we encourage the Subcommittee to consider whether remaining unaddressed recommendations from the 2017 USCC report could be adapted in ways that would boost U.S. security, including both national and economic security.⁷

⁷ Those additional recommendations include prohibiting the sale of U.S. assets to China’s state-owned or state-controlled entities, including sovereign wealth funds and prohibiting a transaction that would confer control of critical technologies or infrastructure to a foreign entity. See the 2017 Report to Congress by the U.S.-China Economic and Security Review Commission for a complete list, available at https://www.uscc.gov/sites/default/files/annual_reports/2017%20Executive%20Summary%20and%20Recommendations_1.pdf.

Why Additional Greenfield Investment Review is Important: The Case of Tainjin Pipe

The AFL-CIO has previously raised risks posed by CFIUS's lack of a broad review process for greenfield investments because such investments have the potential to negatively affect both traditional national security-related concerns as well as economic concerns. In the traditional area, intelligence and law enforcement experts have identified issues relating to the proximity of investments to sensitive installations. For example, a greenfield investment near a military base would not fall under the jurisdiction of CFIUS as currently authorized⁸ even though the ability to engage in intelligence activities is extensive given technologies like laser microphones, which are readily available on the Internet. FIRRMA would rectify this omission.

However, greenfield investments raise national security concerns beyond the issue of proximity. On these issues, FIRRMA is silent, but could be improved with added greenfield review responsibilities.

Tainjin Pipe provides a case study that emphasizes how FIRRMA might be improved by including a broader greenfield review. Relevant to this analysis is the President's March 2018 announcement of action under Section 232 of the Trade Expansion Act of 1962 to address the impact of imports of steel and aluminum on our national security. In response to a detailed report by the Department of Commerce, and in consultation with the Department of Defense, the President decided to take action on imports of steel and aluminum. Both products are vital to national defense (e.g., submarines and aircraft) and critical infrastructure (e.g., roads, railroads, airports, and military installations).

⁸ In 2012, citing national security risks, President Obama blocked Ralls, a company owned by Chinese nationals, from taking ownership of a wind farm *near* a Navy base. However, in that case, the key factor was not "proximity," but rather "restricted airspace." FIRRMA would enable the review of real estate transactions "in close proximity to a U.S. military installation or another facility or property of the U.S. Government that is sensitive for reasons related to national security," providing assurance that a greenfield acquisition near a military installation could be reviewed, and, if necessary, modified or blocked, an assurance not available under current law. Other greenfield investments, such as Tainjin Pipe, would not be covered by FIRRMA.

Tainjin Pipe, a state-owned entity that bills itself as “China’s largest seamless steel pipe maker,”⁹ is in the final stages of opening a greenfield investment in a pipe production operation in the Texas Coastal Bend region. This new facility represents a \$1 billion investment with substantial productive capacity that has the benefit of state-supported funding, which may be low cost, or, as is the case with many of China’s state-supported investments, with no capital costs at all, and potentially no repayment obligation. Substantial overseas investments such as this are cleared by the Government of China to make sure they advance the interests of the Chinese Communist Party.

In contrast, U.S. companies must respond to market forces and lack the access to low- or no-cost capital available to Tainjin. Additionally, the inputs that will be utilized by Tainjin could very well be what is known as “green pipe”—pipe that is shipped here needing only minor transformations to be utilized in the U.S. market. If that is the case, Tainjin will profit from having the bulk of its production in China (which may be made contrary to World Trade Organization and International Labor Organization standards) while avoiding the scrutiny of U.S. trade remedy law, including Section 232—as well as the more familiar anti-dumping and countervailing duty laws.

U.S. producers—and by extension their employees—simply cannot compete fairly against such subsidized production, which is one of the principal causes of the broader crisis in the U.S. steel industry and a recognized threat to national security.¹⁰ Following numerous trade cases filed by U.S. industry in the past two decades to respond to predatory and protectionist

⁹ <http://tianjinpipe.com/>.

¹⁰ For more information about the threat to U.S. security from the global overcapacity in steel production, see U.S. Department of Commerce, *The Effect of Imports of Steel on the National Security* (2018), available at https://www.commerce.gov/sites/commerce.gov/files/the_effect_of_imports_of_steel_on_the_national_security_-_with_redactions_-_20180111.pdf.

practices by China, state-owned enterprise Tainjin sidestepped trade remedy rules by buying land on which to build a new U.S. production facility.

While it is easy to see why the Tainjin's investment may be in China's national interest, many question whether the investment is in the U.S. national interest. "What will the long-term impact on the U.S. steel industry be?" is a question that remains unanswered. FIRRMA would not empower CFIUS to review this transaction to determine what the facts are, and whether the U.S. should act to mitigate the transaction and ensure that working families benefit. In our view, FIRRMA should do so.

Conclusion

The AFL-CIO strongly supports FIRRMA. We also encourage the Subcommittee to expand the reach of FIRRMA to address greenfield reviews and net economic benefits and to consider the remaining USCC recommendations. We appreciate the opportunity to present our views and look forward to further dialogue on these important issues.