

PolicyWatch #1240

Middle Eastern Investment in the United States: Avoiding Another Dubai Ports World Controversy

By [Michael Jacobson](#) and David Jacobson
June 5, 2007

On May 10, 2007, President Bush and U.S. Treasury secretary Henry Paulson launched an "open investment" initiative to encourage foreign investment in the U.S. economy. In a statement, the president emphasized that his administration "is committed to ensuring that the United States continues to be the most attractive place in the world to invest." Washington's focus on this issue is at least partly a reflection of the ongoing fallout from last year's Dubai Ports World (DPW) controversy. Although it is still premature to gauge the long-term economic impact of the DPW case, the process for reviewing foreign investments has already changed significantly.

Background

In early 2006, the Committee on Foreign Investment in the United States (CFIUS), the interagency body charged with reviewing requests by foreign companies to purchase U.S. entities, approved DPW's bid to purchase the Peninsular & Oriental Steam Navigation Company (P&O). The deal would have given DPW -- a company owned by the government of Dubai, part of the United Arab Emirates (UAE) -- ownership of a firm with terminal operations at six U.S. ports.

The decision thrust CFIUS into the limelight, setting off a congressional and media firestorm. Members of Congress argued that the deal posed a serious national security threat, pointing to the UAE's historical ties to the Taliban (it had recognized the regime before September 2001), and to the fact that two of the September 11 hijackers were citizens and, with other hijackers, used Dubai as a transit point. The thoroughness of the CFIUS review was also questioned, and there were threats of legislation to block the sale. Once it became clear that the controversy was not subsiding, DPW backed down and sold its newly acquired U.S. port operations to an American buyer.

Expanding CFIUS Role

CFIUS was established in 1975 by executive order. The committee was initially responsible only for "monitoring" and "evaluating" the impact of foreign investment. Its mandate was expanded in 1988 in the Omnibus Trade and Competitiveness Act, with the passage of the Exon-Florio Amendment. This amendment gave the president new authority to prevent foreign entities from acquiring U.S. companies for national security reasons. In Executive Order 12661, President Reagan delegated this authority to CFIUS.

Twelve U.S. government agencies are members of CFIUS, including the Departments of State, Defense, Justice, and Homeland Security. The Treasury Department chairs the committee, and additional agencies are invited to participate in specific cases as needed. Although foreign companies are not required to submit to CFIUS review, they run the risk of being involuntarily subjected to scrutiny, since the president has the unilateral authority to suspend or prohibit any transaction. Under the statute, CFIUS has thirty days to review a transaction to determine whether it "threatens national security." If any of the agencies still have unresolved

concerns at the end of this period, CFIUS can trigger an additional forty-five-day review.

A Renewed Push for Foreign Investment

In announcing the open investment initiative, President Bush explained that "as both the world's largest investor and the world's largest recipient of investment, the United States has a key stake in promoting an open investment regime," adding that "a free and open international investment regime is vital for a stable and growing economy, both here at home and throughout the world."

The initiative comes at a time when Washington has reason to be concerned about trends relating to foreign investment. According to the U.S. Bureau of Economic Analysis, foreign direct investment in the United States was \$183 billion in 2006, representing a 43 percent drop from 2000. While Secretary Paulson cautioned that it is too early to tell whether this is a long-term decline or merely a short-term trend, he noted that bipartisan support for open investment in the United States, which has existed for many years, is eroding.

The drop-off can be at least partly attributed to the DPW scandal. As Paulson remarked, "In the wake of the Dubai Ports confusion and publicity, [foreign companies] are questioning whether we'll really welcome investment." Middle Eastern companies in particular seem to be placing more of their investments in regions such as Asia, presumably out of concern that transactions with U.S. firms could be subjected to harsh scrutiny.

Reformed Process

Although a number of bills are pending in Congress to overhaul CFIUS, it is clear that the process has already been changed considerably since the DPW incident. CFIUS now holds weekly policy discussions instead of the ad hoc meeting schedules of the past. Senior policy officials are now briefed on all CFIUS cases, primarily in response to concerns that the DPW decision was made without adequate senior-level input. The director of national intelligence has been granted a more formal role in the process, and the intelligence community provides reports and briefings for every transaction.

Perhaps most important, both CFIUS and foreign investors now recognize that they can no longer conduct this process in relative secrecy. Greater transparency and effective public relations are key not only to the success of individual CFIUS transactions, but also to the goal of attracting broader foreign investment, particularly from the Middle East. The Bush administration has addressed this issue head-on in the open investment initiative, contending that there are increased "misconceptions" about the CFIUS process and its impact on foreign investment. The process has not, according to Washington, restricted America's openness to foreign investment. In fact, CFIUS reviewed less than 10 percent of foreign direct investment in the United States in 2006.

In addition, CFIUS has made changes to the process itself that are designed to improve transparency and communication. For example, the Treasury Department now notifies Congress at the completion of every CFIUS transaction. Although this measure is not required by law, it helps avoid situations -- such as DPW -- in which the administration and Congress end up at public loggerheads. In addition, the Treasury Department encourages parties to consult with CFIUS before formally filing and triggering the start of the thirty-day review period. This gives the committee more time to consider and resolve any issues before the period expires, which might help prevent the need for a higher profile forty-five-day investigation.

Foreign companies have also made changes to how they approach investing in the United States. The number of voluntary CFIUS filings has increased dramatically -- including by Middle Eastern firms -- presumably indicating that companies want to avoid any perception that they are circumventing the process. In 2006, CFIUS reviewed 113 transactions -- a 74 percent increase over 2005. According to the Treasury Department, this upward trend has continued in 2007.

Companies are also incorporating more traditional Washington strategies into their efforts, such as retaining

lobbyists to promote acquisition and conducting outreach to Congress and the media at all stages of the process. For example, after the DPW scandal, the UAE created "the Emirates Alliance," devoting \$15 million to improve its image in the United States. Richard Mintz, a principal at the Harbour Group public relations firm that manages this alliance, noted that, until DPW, "the Emirates did not feel that they needed to make an investment in public diplomacy because they felt their relationship with America was understood."

Difficult Balancing Act

Washington continues to face a difficult balancing act in the foreign investment arena. It has to persuade investors that the United States welcomes them while at the same time convincing domestic audiences that it is conducting rigorous national security reviews. So far, the administration appears to have successfully navigated the latter obstacle -- since the DPW case, no other proposed transaction has ignited the same level of domestic controversy. Successfully courting foreign investment may be more difficult, though the open investment initiative appears to be a promising start. Greater transparency regarding this once-secretive process is a good step toward building confidence and working to achieve both important objectives.

Michael Jacobson, a senior fellow in The Washington Institute's Stein Program on Terrorism, Intelligence, and Policy, previously served as a senior advisor in the Treasury Department's Office of Terrorism and Financial Intelligence. David Jacobson is a research assistant in the Stein Program.

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