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Trump's protection plan to keep 'competitor' China at bay

The US wants more scrutiny of deals with Chinese companies but critics fear the System will hurt innovation

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Its deliberations are opaque and its decisions have the power to kill multibillion-dollar international business deals. Its acronym strikes fear into companies and investment bankers. Its day-to-day staff is an earnest and elite band of 16 Ivy League-educated lawyers who labour deep inside the US Treasury, ostensibly to protect America's economic future. And it is poised to gain a lot more power.

The Committee on Foreign Investment in the United States (Cfius) is one of the most powerful — and enigmatic — regulators in the world. An inter-agency committee that brings together defence and intelligence staff with economic policymakers, it was created to vet inbound foreign investment for potential national security threats. Yet reforms being pushed by President Donald Trump and contained in a bill now working its way through Congress would, if enacted, expand its workload from a few hundred transactions a year to potentially thousands. And like so much of economic policymaking in Washington these days, it has one target in mind: China and its appetite for US intellectual property.

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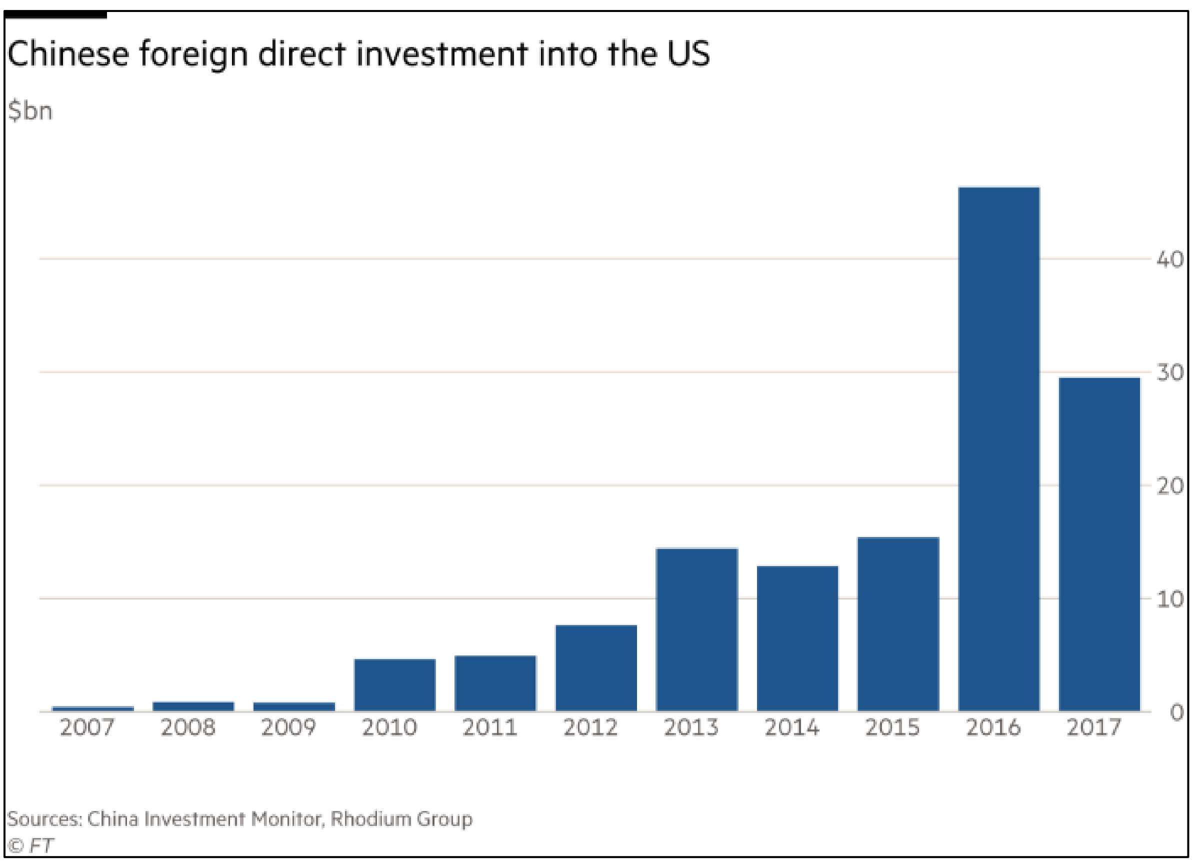
The planned reforms fit with an international pattern. From Australia to the EU, jurisdictions are tightening their scrutiny of inbound investment largely in reaction to what many governments suspect has been a strategically driven Chinese buying spree that in the US alone has been worth $116.6bn in the past five years according to the Rhodium Group, a consultancy.

However, the US proposals go further. For the first time, the bill now under consideration would give Cfius broad jurisdiction over major outbound investment by US companies, that since 1990 has been worth some $250bn, and the overseas ventures of US-based multinationals. And for that reason it has provoked a growing revolt from blue-chip American companies such as General Electric and IBM and a debate in Congress over how best to curtail Chinese pressure on US companies.

The plans for Cfius strike to the heart of the Trump administration's dilemma over how to deal with China, which it has called a strategic "competitor". White House officials and their allies in Congress are struggling to respond to what they see as an existential economic threat from a China that aims to be the leader in artificial intelligence, autonomous vehicles and other new industries.



However, many of those plans are causing anxiety or are actively opposed by some leading US companies which see their growth prospects as closely tied to China, the second-largest economy in the world. Many fear the new rules would effectively become a murky system of technology controls and place a major regulatory damper on one of the most dynamic parts of the US economy. "This is a radical change," says Rod Hunter, who oversaw Cfius while on President George W Bush's National Security Council and is now a partner at law firm Baker McKenzie. "You would basically turn the US technology industry into a regulated industry. If there was ever a way to turn the US technology industry into [failed carmaker] British Leyland this is how you do it."

One reason why the Cfius bill is attracting a lot of attention is that it is one of the few ideas that has won support from both Republicans and Democrats in an otherwise divided Congress this year.

"China has weaponised investment in an attempt to vacuum up our advanced technologies and simultaneously undermine our defence industrial base," John Cornyn, the Texas Republican who is the legislation's chief backer, told Congress this month.

Over the past few years, scrutiny of Chinese purchases of US and European semiconductor and other technology companies has increased. But the proposed legislation would require Cfius to monitor overseas joint ventures in places like China that US officials fear often involve the forced transfer of vital and potentially sensitive technologies in exchange for doing business."

We're all for [overseas investment]," says Robert Pittenger, the North Carolina Republican sponsoring the legislation in the House of Representatives.

"We just don't want our businesses in a position where they are coerced or they are exploited by a foreign government. . . to obtain critical data and security-related [technologies]."Critics say export control rules provide a way to monitor the relatively small number of transactions involving sensitive technologies. They fear the legislation would vastly expand the mandate of the overstretched Cfius and harm the ability of US businesses to compete by subjecting any overseas deals they made to the rigorous scrutiny of Cfius.

The committee reviewed around 240 transactions but that could expand to thousands or even tens of thousands of business deals around the world, experts say.

Some companies have backed the legislation, with software company Oracle declaring in a November letter that the changes were needed to close loopholes that now were "putting at

risk critical innovations that bolster and ensure our national security". But tech rivals such as IBM have mounted a public fight against the bill.

"A system of technology controls that unilaterally stops American firms from doing business abroad will not advance national security interests if it simply hands markets to foreign competitors," Chris Padilla, IBM's vice-president of government and regulatory affairs, told the Senate Banking Committee during a January hearing. The current version of the bill would capture all manner of innocuous business done overseas by IBM such as the sale of servers or the licensing of trademarks "that could not be less threatening to national security".

The pushback from business has forced congressional aides to promise the release of a finessed version soon. Treasury officials have also said that they would make sure that any Cfius interest in outbound investment remains narrowly focused on national security. "From Cfius' perspective we don't want to be looking at lots of transactions that are unlikely ever to raise national security concerns," says a senior US Treasury official.

There are also signs that some in Congress see the business concerns as valid and would like to see the outbound measures put into separate legislation updating the export control regime, a much more transparent process managed by the US commerce department.

Mr Pittenger says he and his colleagues are eager to address business concerns. "We're listening. We're listening very hard. We want to be responsive," he says. But he and Mr Cornyn also say they remain committed to monitoring transactions involving overseas joint ventures, with a particular eye on China. They have accused opponents of being alarmist and even unpatriotic."

I would call this a patriotism deficit on their part," Mr Cornyn said in a speech last month that raised eyebrows in a business community that he accused of trying to "perpetuate the status quo". Mr Pittenger, meanwhile, likens abandoning the proposal about overseas deals to removing airport security checks because of complaints that the queues have become too long. "Would that be a smart thing to do? No. And it would not be smart to allow people to bypass a security review by Cfius," he says.

The debate over Cfius reform in Congress comes as the committee and its staff are stretched by a rising caseload that is more complex than it used to be.

Lawyers who work on transactions reviewed by Cfius say even simple cases have in recent years begun to face procedural delays and complain that the Trump administration was too slow to nominate many of the appointees who sit on its panel. Things have become better in recent months and especially since Heath Tarbert, the assistant treasury secretary who oversees Cfius, began work at the end of September.

But Cfius experts also detect signs that the balance between economic and defence interests on the committee has shifted under the Trump administration. The Pentagon and

the wider intelligence community appear to have more power on the committee, lawyers say, and that has affected cases, particularly when China is involved.

Cfius' rejection in January of a $1.2bn bid by Jack Ma's Ant Financial to buy MoneyGram was understandable given the US payment company's access to sensitive personal data of millions of Americans, including government employees and US soldiers, experts say. But when Cfius intervened in November to force Germany's Biotest to sell its US operations before it would approve the takeover of the blood plasma products maker by a Chinese investor, it caused a perplexed reaction from some.

"It's not clear what the national security angle is there," says a Cfius lawyer. "We're talking about blood plasma!"

Other high-profile transactions have run into trouble. HNA's takeover of SkyBridge Capital, whose founder Anthony Scaramucci was Mr Trump's White House communications director, has stalled before Cfius on questions over the conglomerate's murky ownership structure and rumours of possible links to Beijing. China's Hubei Xinyan Equity Investment Partnership last week was also forced to abandon its $580m bid to buy Xcerra, a US semiconductor testing equipment maker, after Cfius made its opposition clear to the companies. Some of the proposed reforms are meant to streamline the process.

An initial 30-day review would be extended to 45 days under Mr Cornyn's bill. That, people close to Cfius say, would give intelligence agencies more time to review cases. It also would help discharge more cases before triggering a secondary 45-day investigation stage that Cfius has often employed.

Opponents of the bill are also concerned it would turn a voluntary process into one mandating notification of Cfius. The move is meant to give the committee wider power including over many smaller transactions that involve minority stakes in tiny start-ups. That would mean potentially thousands more cases on its docket. It could also put a chill on the angel investments that fuel innovation in hubs such as Silicon Valley, they argue. "Capital is mobile. Talent is mobile. If the regulatory burdens are too much people will take their talents and their capital elsewhere," says Mr Hunter.

Critics argue that the Trump administration, which has put deregulation at the centre of its agenda, and the bill's backers in Congress are underestimating the bureaucratic monster they are creating. Treasury officials insist they do not want to do that, but former officials are sceptical. "The current system can barely handle the 240 cases that it has now and we are looking at an expansion of scope of hundreds or thousands of additional cases," says Kevin Wolf, who represented the commerce department on Cfius during the Obama administration. "That's going to need a very large organisation of people and new people at agencies that don't yet exist," he adds. "It's going to create an extraordinary bureaucracy.

"US takes aim at China over IP Beijing's alleged manipulation of the renminbi once drew the greatest ire from Washington, these days the dominant obsession is control of technology. In a world where the biggest geopolitical question has become how to manage a developing

clash between a rising China and a divided America, the market for "foundational" technologies such as artificial intelligence is becoming a key battleground. Call it the innovation war.

In its recently released National Security Strategy the Trump administration labelled protecting the "national security innovation base" a priority. "The genius of creative Americans, and the free system that enables them, is critical to American security and prosperity," it said.

The administration wants to crack down on what it sees as a plethora of legal ways that make it too easy for China and other strategic rivals to acquire important technologies.

Backing a strengthening of Committee on Foreign Investment in the US is one way the administration is doing that. In a report last year, a venture capital arm of the Pentagon, which invests in tech start-ups doing work with potential military uses, recommended that the US use Cfius to cut off the flow of foreign investment into early-stage tech companies and look at outbound investments as well.

The White House has made an attack on Beijing's intellectual property regime the centrepiece of its approach towards China. It launched an investigation last summer into intellectual property theft and Chinese policies that pressure companies to transfer technology in return for market access. That probe could prepare the ground for new tariffs and measures to curtail Chinese investment in US sectors in which Beijing will not allow reciprocal investments.