REKINDLING THE FLAME: HOW THE COMING FUNDAMENTAL CHANGES IN U.S. FINANCIAL MARKETS DUE TO THE GLOBAL FINANCIAL CRISIS COULD IMPROVE FOREIGN DIRECT INVESTMENT IN THE UNITED STATES

*Cyril V. Jones**

* *B.A. in Plan II and History, University of Texas; JD/MBA Candidate, University of Houston Law Center and the Bauer College of Business.* *He is grateful to Professor William Alexander of the Bauer College of Business for his comments and encouragement during the writing process. He would also like to extend a special thanks to Heidi Lewis and Josh Farkas at Dynegy, Inc.. Not only did they provide the inspiration for this paper and tremendous support during the editing process, they have become close friends and mentors. Finally, he would like to thank his parents for their support in writing this Comment and beyond.*

"If you owe the bank $100, that's your problem. If you owe the bank $100 million, that's the bank's problem."[1]

The global financial markets have plunged into a period of tremendous volatility and uncertainty over the past years[2] due to, among other things, the failure of numerous storied financial institutions and the resulting freezing of credit markets.[3] The result of this dramatic financial crisis in the United States will likely be a heavy-handed response from the federal government

1. *See* Justin Fox, *18 Tough Questions (and Answers) About the Bailout*, TIME, Sept. 30, 2008, http://www.time.com/time/business/article/0,8599,1845816,00.htm (attributing the quote to J. Paul Getty).

2. *See* James Surowiecki, *That Uncertain Feeling*, NEW YORKER, Sept. 1, 2008, at 60, *available at* http://www.newyorker.com/talk/financial/2008/09/01/080901ta_talk _ surowiecki (discussing the tremendous increase in market volatility over the past year and how it is fueled by rising investor uncertainty).

3. *See On Life Support*, ECONOMIST, Oct. 4, 2008, at 77 (discussing the worldwide freeze in credit markets and the unprecedented steps taken by various governments to rescue many of the financial institutions caught in the crossfire); *A Spent Force*, ECONOMIST, Oct. 18, 2008, at 84–85 (discussing how the failures of storied institutions such as Lehman Brothers will likely put a disastrous burden on the already weakened availability of credit).

in the form of regulations that could potentially reshape the financial industry into something entirely different and never before seen in the United States.[4] Particularly interested parties in this restructuring will be the numerous foreign entities controlling large pools of foreign capital.[5] Many of these entities take the form of sovereign wealth funds ("SWFs") as well as other forms of government controlled entities.[6] Government controlled capital, especially SWFs, have been viewed with a wary eye in the United States,[7] and as a result, these entities have alleged unfair treatment at the hands of the U.S. government because they believe their money is being treated as less valuable than money coming from domestic sources.[8]

This Comment attempts to show that the upheaval in the U.S. financial system, and the regulations that are likely to result, could have the counter-intuitive impact of actually

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4. Kim Dixon & Karey Wutkowski, *Bank Rules Reform Seen But Paulson Blueprint Doubted*, REUTERS, Aug. 25, 2008, http://www.reuters.com/article/ousivMolt/ idUS N2337728820080825.

5. *See Sovereign Wealth Funds and Recipient Country Policies*, OECD Investment Committee, Spring 2008, at 2 (discussing the benefits of recent injections of capital by sovereign wealth funds ("SWFs") into floundering financial institutions, as well as the desire of many SWFs to invest in an open and understandable regulatory framework); *Marauding Maharajahs*, ECONOMIST, Mar. 31, 2007, at 71 (examining the rapid expansion of Indian companies into the international investment arena and the increased acceleration with which these companies are seeking more investment opportunities); Peter Heyward, *Sovereign Wealth Fund Investments in U.S. Financial Institutions: Too Much or Not Enough?*, 27 BANKING & FIN. SERVS. POL'Y REP. 19 (2008).

6. *See* David Marchick & Matthew Slaughter, *Global FDI Policy: Correcting a Protectionist Drift*, COUNCIL ON FOREIGN RELATIONS, CSR No. 34, June 2008, at 2, http://www.cfr.org/publication/16503/global_fdi_policy.html.

7. *See id.* at 5 (describing the history of oversight of Foreign Direct Investment ("FDI") in the United States starting with the creation of the Committee for Foreign Investments in the United States ("CFIUS") in 1975 through the passage of the Foreign Investment and National Security Act of 2007 ("FINSA") in 2007).

8. *See id.* at 6 (discussing the Dubai Ports World transaction that became a political lightning rod in Congress in 2006 due to connections to the Middle East and concerns of dubious intent by the investors); JUSTIN O'BRIEN, ENGINEERING A FINANCIAL BLOODBATH (2009) (explaining that the China Investment Corporation has expressed "irritation" with its treatment by the U.S. government, calling it "unfair" and "groundless"). *But see* Jonathan Stagg, *Scrutinizing Foreign Investment: How Much Congressional Involvement is Too Much?*, 93 IOWA L. REV. 325, 330 (2007) (concluding the increased efforts of U.S. and state governments to promote democratic and capitalist ideologies have enticed foreign investors).

increasing SWFs' interest in investing in the United States. The most relevant legislation concerning the limitations on Foreign Direct Investment ("FDI") in the United States is House Resolution 556: Foreign Investment and National Security Act of 2007 ("FINSA").[9] Part I of this Comment provides an overview of FINSA and the Exon-Florio provision of 1975, which FINSA amends.[10] Following a discussion of the current status of FDI regulation in the United States as governed by FINSA, Part II briefly describes the variety of actors regulated by FINSA, including several SWFs, as well as a handful of multinational corporations and other foreign state actors. Part III discusses the likely regulatory responses and fundamental changes set to reshape the U.S. financial system in the wake of the recent financial crisis. Part IV analyzes why the financial system that is likely to rise from the ashes of the current crisis could be one more favorable to large foreign investors. Part V concludes with a series of suggestions that seek to create a sufficient compromise between often cited competing interests of state security and the need to allow valuable foreign investment into the United States.[11]

I. THE CURRENT STATUS OF FOREIGN DIRECT INVESTMENT LAW IN THE UNITED STATES

House Resolution 556's stated purpose is "[t]o ensure national security while promoting foreign investment and the creation and maintenance of jobs, to reform the process by which such investments are examined for any effect they may have on national security, to establish the Committee on Foreign Investment in the United States, and for other purposes."[12] FINSA's function is to amend the Exon-Florio provision, which provides for the creation of the Committee for Foreign Investment in the United States ("CFIUS").[13] Before a

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9. Foreign Investment and National Security Act of 2007, Pub. L. No. 110–49, 121 Stat. 246.

10. *Id.*; Exec. Order No. 11,858, 3A C.F.R. 159 (1975).

11. Stagg, *supra* note 8, at 327.

12. 121 Stat. at 246.

13. 3A C.F.R. at 159.

transaction may be completed, foreign investors seeking to invest in certain U.S. assets must gain approval from CFIUS.[14]

The CFIUS process had not garnered much attention until early 2006 when Dubai Ports World, a company run by the government of Dubai,[15] received approval from CFIUS and President Bush to purchase an operational stake in several major United States port facilities.[16] The transaction generated considerable press coverage,[17] and then quickly made its way into the halls of Congress where impassioned debates raged over national security and freedom of investment.[18] The various arguments centered on the need for a more transparent investment review process, a better definition of the types of investments that are prohibited, and whose investments should be denied.[19] The end result of the debates in Congress was the passage of FINSA.[20]

The major changes flowing from the FINSA amendment to the Exon-Florio provision include:

1) a clearer layout of the review process, in particular the timing requirements for filing a review and receiving a determination from CFIUS;[21]
2) a refined definition of the types of investments likely to receive the strongest scrutiny or outright

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14. Cecil Hunt, Review of Foreign Acquisitions of U.S. Business: The CFIUS Process Under FINSA, Presentation at the American Law Institute-American Bar Association Program, Fundamentals of International Business Transactions (May 8, 2008).

15. Lauren Etter, *Hot Topic: Dubai: Business Partner or Terrorist Hotbed?*, WALL ST. J., Feb. 25, 2006, at A9.

16. *Id.*

17. *Id.*

18. *See id.*; Editorial, *The Don't Invest in America Act*, WALL ST. J., July 19, 2006, at A12 (arguing that the Dubai Ports transaction eventually led to the passage of an amendment to the Exon-Florio provision).

19. ALAN P. LARSON & DAVID M. MARCHICK, FOREIGN INVESTMENT AND NATIONAL SECURITY: GETTING THE BALANCE RIGHT 15–16 (2006), *available at* http://www.cfr.org/publication/11146/foreign_investment_and_national_security.html.

20. Foreign Investment and National Security Act of 2007, Pub. L. No. 110–49, 121 Stat. 246; *The Don't Invest in America Act*, *supra* note 18.

21. *See* Hunt, *supra* note 14.

denial from CFIUS;[22]

3) a list of new factors to be included in the review process;[23] and
4) the power of CFIUS to require the parties to submit to various control conditions in order to mitigate any threat to national security.[24]

For three principal reasons, FINSA has caused considerable confusion and consternation for many practitioners involved with international asset purchase and sale transactions. First, FINSA's measures and conditions for mitigating any threat to national security result in the wary eye of government regulators continually watching a deal as it progresses.[25] These added layers of bureaucracy and cost in a highly competitive deal-making environment create the potential to hinder or mortally wound a transaction, especially if a CFIUS review is not dealt with early on.[26] Second, the Exon-Florio amendment lacked the clarity practitioners desired.[27] Most practitioners desired guidance from CFIUS concerning what it meant for a foreign entity to "control" a United States company, what constituted "critical infrastructure," and what actually rose to the level of a "foreign government-controlled transaction."[28] Finally, many foreign investors are concerned because congressmen and their aides are able to access CFIUS review

22. *Id.*

23. *Id.*

24. Stagg, *supra* note 8, at 345.

25. *See* Hunt, *supra* note 14.

26. Neal Stoll & Shepard Goldfein, *Post-FINSA Coordination of Antitrust, CFIUS Practitioners*, N.Y.L.J., Sept. 18, 2007, *available at* http://www.law.com/jsp/cc/PubArticleCC.jsp?id=1190106174477 (discussing the detrimental effects a CFIUS review can have on a transaction when it occurs in the middle to late stages of the transaction).

27. Edward Rubinoff & Tatman Savio, *CFIUS Implements FINSA Amendments to Exon-Florio Foreign Investment Law*, THE METRO. CORP. COUNSEL, May 2008, at 33, *available at* http://www.metrocorpcounsel.com/pdf/2008/May/33.pdf (discussing the three major definitions FINSA does not fully define and the fact CFIUS is delaying the implementation of the FINSA regulations because these definitions need to be properly explained for FINSA to be administered to meet the requirements of national security and investment freedom).

28. *Id.*

documents.[29] Leaks from these sources could result in political fallout surrounding the transaction or the companies involved with it due to the revelation of previously confidential and politically sensitive information, as well as the potential loss of proprietary information or trade secrets.[30]

The current state of U.S. FDI law is one of fairly aggressive oversight.[31] This is due to an atmosphere of heightened national security concerns exemplified by the loose language of FINSA, which allows CFIUS wide latitude to decide what constitutes a foreign government taking a controlling stake in an asset deemed critical to the national security of the United States.[32]

II. SOVEREIGN WEALTH FUNDS AND OTHER SOURCES OF FDI IMPACTED BY FINSA

Prior to 2006, the concept of a SWF was not one well-known or understood by the average American.[33] This changed quickly with the firestorm that erupted in Washington over the approval of the purchase of P&O North America—a company operating several large port facilities in the United States—by Dubai Ports World.[34]

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29. *See* Stagg, *supra* note 8, at 353 (discussing the potential problems with politicization and confidentiality of FINSA relating to the openness of the CFIUS review process, which allows certain members of Congress, their staff with appropriate security clearances, and even state senators in some situations to access CFIUS review documents).

30. *Id.*

31. *See* Rubinoff & Savio, *supra* note 27 (calling it an "elevated level"); Hunt, *supra* note 14, at 310–12 (discussing CFIUS's expanded authority under FINSA as well as the need to voluntarily file for a CFIUS review in order to avoid being dragged into a review once a deal is already underway).

32. Rubinoff & Savio, *supra* note 27.

33. *See* Heyward, *supra* note 5, at 19 (asserting that the rise in public interest in SWFs is tied not only to the increased media coverage from recent investments in United States assets, but also to both the staggering growth in the size of assets controlled by SWFs and the belief that this growth is likely to continue unabated for the foreseeable future).

34. *See* Thomas Crocker, *What Banks Need to Know About the Coming Debate Over CFIUS, Foreign Direct Investment, and Sovereign Wealth Funds*, 125 BANKING L.J. 457, 459–60 (2008) (discussing the Dubai Ports World transaction and the ensuing political conflict that arose over said transaction).

The controversy concerning the Dubai Ports World transaction arose over the portrayal of SWFs as an economic tool of foreign governments dedicated to doing economic harm, or worse, to the United States.[35] However, why did this controversy take hold so suddenly? From reading the headlines casual observers might think SWFs were new weapons created by terrorists determined to assault the American way of life.[36] SWFs have been defined as "separate pools of international assets owned and managed by governments to achieve a variety of economic and financial objectives."[37] For the most part, these state-run investment vehicles have sought the same thing that most other large institutional investors seek: a better return on their investment.[38]

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35. *See The Rise of State Capitalism: Coming to Grips with Sovereign-Wealth Funds*, ECONOMIST, Sept. 18, 2008, at 11 (discussing the meteoric growth of SWFs and the resulting wariness with which they are being treated, both in the countries receiving their investments, and in their home countries because of dissent as to whether SWFs are an efficient use of their resources).

36. "Do Sovereign Wealth Funds Make the U.S. Economy Stronger or Pose National Security Risks?": Hearing Before the Joint Economic Comm., 110th Cong. 2 (2008) (statement by Sen. Charles Schumer, Chairman); *see also* Irwin Stelzer, *Commentary — Irwin Stelzer: Sovereign Wealth Funds Pose Threat to U.S.*, http://www.examiner.com/a903184~Irwin_Stelzer_Sovereign_wealth_funds_pose_threat_to_U_S_.html (explaining that SWFs can make the recent financial crisis "look like a walk in the park").

37. Sovereign Wealth Fund Acquisitions and Other Foreign Government Investments in the United States: Assessing the Economic and National Security Implications: Hearing Before the Comm. on Banking, Housing and Urban Dev., 110th Cong. 2 (2007) [hereinafter "Truman Statement"] (statement of Edwin Truman, Senior Fellow, Peterson Institute).

38. *See The Rise of State Capitalism*, *supra* note 35, at 11 (quoting government officials of Abu Dhabi, which runs the world's largest SWF, the Abu Dhabi Investment Authority, as saying " 'it is important to be absolutely clear that the Abu Dhabi government has never and will never use its investment organizations or individual investments as a foreign policy tool . . . no one can point to a reported incident of such behavior' "); Robert M. Kimmit, Deputy Sec'y, U.S. Dep't of Treasury, Remarks to the U.S.-GCC Investment Forum in Bahrain (Dec. 4, 2007), *available at* http://www.treas.gov/press/releases/hp710.htm. *But see* Marchick & Slaughter, *supra* note 6, at 25 (discussing European concerns over investments made by Russian SWFs in the energy sector due to the dependence of European countries on Russian natural gas, as these investments could be used to further Russian political agendas under the cover of Gazprom's business objectives).

These investment vehicles cannot properly be characterized as wholly good or bad without gross oversimplification, if for no other reason than the vast diversity of the players in the field.[39] SWFs began appearing in the late 1950s and early 1960s.[40] In an attempt to create a more balanced economic portfolio, some countries use SWFs to raise money through the sales of commodities, such as oil (as in the case of the Gulf States),[41] or through large trade surpluses.[42] This allows the countries with SWFs to mitigate the potential negative economic consequences of both downswings in commodity prices and large, burdensome trade surpluses.[43]

The range in size and the unprecedented recent growth of SWFs makes categorizing them all together as a single type of investment entity impractical.[44] SWFs range in size from assets worth $2 billion, to the world's largest SWF in Abu Dhabi, worth between $500 and $875 billion.[45] The seven largest funds make up more than two-thirds of the world's SWF assets and are controlled by countries that run the U.S. foreign-relations gamut from friendly to frosty.[46]

The big numbers garnering the most attention recently have been those relating to the rapid growth of both the size of SWFs, as well as the amount of money these funds have invested into the United States.[47] As mentioned, the growth of SWFs is often

39. *See infra* Part II.

40. Heyward, *supra* note 5, at 19.

41. *Id.*

42. *Id.*

43. *Id.*

44. *Id.*

45. *Id.*

46. *Id.* (explaining that the seven largest SWFs are held in Abu Dhabi, Singapore, Norway, Kuwait, China, and Russia); *see* Daniel W. Drezner, *Sovereign Wealth Funds and the (In)Security of Global Finance*, J. INT'L AFFS., Oct. 1, 2008, http://www.allbusiness.com/government/public-policy/1170679-1.html (explaining that some Americans are concerned about the "lack of transparency, oversight, and accountability" in Russia and China).

47. *See generally* Marchick & Slaughter, *supra* note 6, at 23 (charting the increase in FDI from 2005 to 2006 into the United States and from which countries the money came); *The Rise of State Capitalism*, *supra* note 35 (discussing criticism of SWF investments from the funds' host countries as well as the recipient countries); Crocker, *supra* note 34, at 457 (discussing the "sudden growth of sovereign wealth funds");

tied to either trade imbalances or a spike in commodity prices.[48] As a result, from 2000 to 2006 FDI outflows from China (trade surplus) have increased by 6.9 times, Russia (commodities) by 5.9 times, and in some Gulf States (commodities) outflows have increased by thirty-five times.[49]

These tremendous recent investments in the United States have brought the stark reality of the power of SWFs onto the front page of the news,[50] but SWFs are not the only entities with a vested interest in the outcome of the debate over U.S. FDI policy.[51] Other major players drawn into the debate are the rapidly rising multi-national corporations based outside the United States.[52]

Under FINSA there are two non-mutually exclusive ways in which a transaction can fall under the review of CFIUS.[53] One way pertains to acquiring "critical infrastructure,"[54] while the other category of review is triggered by "foreign government-controlled transactions."[55] Due to the lack of a clear definition as

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Heyward, *supra* note 5, at 19–20 (discussing the sizes of some of the largest SWFs and some of the most highly publicized transactions with which they have been involved).

48. Heyward, *supra* note 5, at 19.

49. Marchick & Slaughter, *supra* note 6, at 24.

50. *See* Heyward, *supra* note 5, at 20 (explaining that between August 2007 and April 2008 over $30 billion was invested by SWFs to U.S. financial firms alone and that 90% of that money came from the UAE, Kuwait, Singapore, and China).

51. *See infra* notes 53–72 and accompanying text.

52. *See* Marchick & Slaughter, *supra* note 6, at 16–24 (discussing the benefits several countries have received from involvement of foreign multi-national companies in their countries, as well as the rapid expansion of multi-national companies based in rising economies like India and China).

53. *See* 50 U.S.C.A. app. § 2170(b)(2)(B)(II) (2007) (requiring the CFIUS to conduct an investigation and take any necessary actions to protect the national security of the United States in each case in which "the transaction would result in control of any critical infrastructure of or within the United States by or on behalf of any foreign person . . ."); Rubinoff & Savio, *supra* note 27.

54. 50 U.S.C. app. § 2152(3) (2009) (defining "critical infrastructure" as "any systems or assets, whether physical or cyber-based, so vital to the United States that the degradation or destruction of such systems and assets would have a deliberating impact on national security, including but not limited to, national security and national public health or safety").

55. 50 U.S.C.A. app. § 2170(a)(4) (2007) (defining a "foreign government-controlled transaction" as "any covered transaction that could result in the control of any person engaged in interstate commerce in the United States by a foreign government or an

to what specifically falls into either of these categories,[56] transactions involving large foreign multinational corporations can fall into either or both categories.[57] SWFs are more likely to receive scrutiny under the "foreign government-controlled transactions" prong of FINSA due to their inherent nature as a government investment entity.[58] But as a result of the vague definition of "foreign government control" and "critical infrastructure," many foreign multi-national corporations are drawn into the CFIUS review process as well.[59]

Multi-national firms have long been criticized as pillaging, destructive forces born of the first world.[60] However, these multi-national firms are rising with the same acceleration as SWFs from places like China, India, Singapore, and Brazil, instead of from the United States, France, Russia, and Germany.[61]

The major problem multi-nationals have with FINSA, as mentioned previously,[62] is FINSA does not explain exactly what constitutes "government control."[63] The paradigmatic example is a company under the direct control of its government, such as the Russian oil company Gazprom, in which the Russian

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entity controlled by or acting on behalf of a foreign government").

56. *Id*; *see also* § 2152(3).

57. *See* Christopher M. Weimer, *Foreign Direct Investment and National Security Post-FINSA 2007*, 87 TEX. L. REV. 663, 676–77 (2008) (describing FINSA as "bring[ing] arguably too broad a swath of potential FDI under the scrutiny of CFIUS," which "threaten[s] to inject uncertainty and delay into a number of transactions that pose few, if any, risks to the United States").

58. *See* Rubinoff & Savio, *supra* note 27 (describing how "in a post-FINSA world, CFIUS review of 'foreign government-controlled transactions' appears to be more robust").

59. *See* Weimer, *supra* note 57 (describing over-inclusive regulation as it applied to the entire FDI sector, not distinguishing between multi-national firms and government-controlled entities).

60. *Multinationals: Globalisation's Offspring*, ECONOMIST, Apr. 4, 2007, at 11 (tracing multi-nationals back to the 12th century and explaining how they have been used by the rich world to exploit the poor world).

61. *Id*; *See* Heyward, *supra* note 5, at 20 (explaining that Singapore is one of three countries that invested 90% of the $30 billion to U.S. financial firms between August 2007 and April 2008).

62. *See supra* notes 55–60 and accompanying text.

63. Rubinoff & Savio, *supra* note 27.

government purchased a controlling stake in 2005.[64] This is not always the case, though, as many other foreign multi-national companies are only partially owned by their home countries, and the government's stake is merely a voting right or a completely passive investment.[65] Confusion results over whether a potential CFIUS review awaits an international transaction.[66]

Meanwhile, the potential benefits and inevitability of globalization, through the growth of large new multinationals, often go unnoticed.[67] Mergers and acquisitions involving multinationals are done with a long-term focus, and therefore are expected to be a less volatile form of cash flow than typical portfolio investments.[68] Furthermore, these investments are noticeably less prone to sudden changes in investor attitudes, which can have adverse affects on markets.[69]

Other potential actors drawn in by the vague CFIUS requirements include entities such as state-run pension funds or situations where governmental control of a company is limited to so-called "golden shares."[70] Golden shares serve only to allow the government to block certain transactions by a company, which is functionally similar to the CFIUS review in the United States.[71]

The last major actor between foreign investors and the CFIUS review process is the U.S. government.[72] Over the course of 2008, the U.S. government thrust itself into the investment

64. *Kremlin Agrees Price for Gazprom*, BBCNews.com, June 16, 2005, http://news.bbc.co.uk/2/hi/business/4100820.stm.

65. *See* Rubinoff & Savio, *supra* note 27 (explaining how several recent investments by SWFs avoided CFIUS review on this basis).

66. *See id.* (noting that members of the private sector and Congress have asked the Treasury Department for clarification as to what qualifies as "government-controlled").

67. *See Globalisation's Offspring*, *supra* note 60 (explaining that critics of multinationals should wane, as globalization has opened new markets and allowed new multinationals to emerge from the poor world).

68. Marchick & Slaughter, *supra* note 6, at 20.

69. *Id.*

70. Rubinoff & Savio, *supra* note 27.

71. *See id.* (discussing how certain government investments in large companies in other countries are passive investments, except that they occasionally come with a right to strike down certain projects or investments in the name of state security).

72. *See infra* notes 75–87 and accompanying text.

arena in an unprecedented manner.[73] There was considerable debate following the passage of the Sarbanes-Oxley Act ("SOX"),[74] much of which focused on the idea that the federal government was overly involved in what should have been left up to the markets to decide.[75]

The passage of SOX now pales in comparison with the actions of the U.S. government over the course of the last year in response to what started as a housing crisis, became a credit crisis, turned into a financial crisis, and now rests firmly as a global economic crisis.[76] The actions of the federal government included the passage of an unprecedented bill that provided $700 billion in liquid support to faltering financial firms, mortgage lenders, and insurance companies.[77] This measure is often derisively referred to by the media as the "Bailout Bill."[78]

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73. *See* Emergency Economic Stabilization Act of 2008, Pub. L. No. 110–343, 122 Stat. 3765 (2008). The Emergency Economic Stabilization Act provides "authority for the Federal Government to purchase and insure certain types of troubled assets for the purpose of providing stability to and preventing disruption in the economy and financial system . . . ." *Id. See also* Catherine Dodge & Dawn Kopecki, *U.S. Rescue May Reach $23.7 Trillion, Barofsky Says*, July 20, 2009, http://www.bloomberg.com (explaining that the "$700 [b]illion bank-investment program under TARP has evolved into a program of unprecedented in scope, scale, and complexity").

74. *See* Elisabeth Bumiller, *Corporate Conduct: The President; Bush Signs Bill Aimed at Fraud in Corporations*, N.Y. TIMES, July 31, 2002, at A1 (discussing the passage of SOX and the highly partisan nature of the debate surrounding the implementation of the Act).

75. *Id.*

76. *See* Thomas Friedman, *Gonna Need a Bigger Boat*, N.Y. TIMES, Nov. 16, 2008, at WK12 (discussing the progression of the current financial crisis from a collapse of the subprime mortgage system all the way to the current consumer spending problems).

77. *See supra* note 73 and accompanying text.

78. *See* Jim Popkin, *Critics Say Bailout Bill is Stuffed with Billions in Pork*, MSNBC, Oct. 3, 2008, http://deepbackground.msnbc.msn.com/archive/2008/10/03/1489413.aspx (referring to the $700 billion stimulus as a "bailout bill"); Jay Newton-Small, *The Bailout Bill That Nobody Likes*, TIME, Sept. 29, 2008, http://www.time.com/time/business/article/0,8599,1845325,00.html (same); *see also* Mark Landler & Steven Myers, *Buyout Plan for Wall Street is a Hard Sell on Capitol Hill*, N.Y. TIMES, Sept. 23, 2008, http://www.nytimes.com/2008/09/24/business/ economy/24fannie.html (referring to the stimulus as a "bailout measure"). *But see* Jim Abrams, *Congress Extends Jobless Benefits; Stocks Fall 400*, HUFFINGTON POST, Nov. 20, 2008, http://www.huffingtonpost.com/2008/11/20/fed-sees-economic-woes-pe_n_145111.html (referring to the stimulus package repeatedly as a "rescue plan").

The federal government has also taken an unprecedented role in the American auto industry by initially propping up Chrysler and General Motors with cash infusions.[79] When that did not work, the federal government pushed both companies through the Chapter 11 bankruptcy process in such an unprecedented fashion[80] that many felt it ran roughshod over the laws governing bankruptcy proceedings.[81]

What will government receive in return for injecting capital into the financial industry and other market sectors? The simple answer is the government will receive preferred stock in these firms in the hope that, should these firms return to profitability, the government can cash in these stocks for a modest profit.[82] For many, this creates a noticeable moment of cognitive dissonance because this action by the U.S. government can be characterized in several ways:[83] 1) the government has begun a rapid fall towards socializing the economy;[84] 2) the government is not properly punishing the failure of management in these industries and is giving them a way out;[85] and most interestingly for foreign observers and investors, 3) if one focuses on the fact that the $700 billion is going into private companies, even if they are American companies, does the $700 billion "bailout" make the U.S. government one of the largest SWFs in the world?[86]

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79. *See Chrysler, GM Race Clock to Finish Viability Plans*, ASSOCIATED PRESS, Feb. 2, 2009, http://www.mlive.com/auto/index.ssf/2009/02/chrysler_gm_race_clock_to_fini.html (discussing the viability plans both Chrysler and GM had to finish as part of the list of requirements needed to obtain government loans).

80. *See* Jonathan Carson, *The Role of Chapter 11 in Today's Economic Climate*, ANDREWS DEL. CORP. LITIG. REP., Oct. 5, 2009, at 24 (asserting that the corporate restructuring of Chrysler and General Motors through bankruptcy represents a level of government involvement that is unprecedented).

81. *See* Neil King, Jr. & Jeffrey McCracken, *Chrysler Pushed into Fiat's Arms*, WALL ST. J., May 1, 2009, at A1 (discussing how the rights of Chrysler's secured creditors were being pushed aside in the bankruptcy proceeding).

82. *Breakdown of the Final Bailout Bill*, WASH. POST, Sept. 28, 2008, http://www.washingtonpost.com/wp-dyn/content/article/2008/09/28/AR2008092800900.html.

83. *See infra* notes 85–91 and accompanying text.

84. Landler & Meyers, *supra* note 78.

85. *Id.*

86. *Wall Street Bailout: The World's Largest Sovereign Wealth Fund?*, CITIZEN

The large stake the U.S. government is taking in private companies seems close to Truman's definition of a SWF as a "separate pool of international assets owned and managed by governments to achieve a variety of economic and financial objectives."[87] In the case of the United States, the funds used did not come from a trade surplus or a large commodity gain.[88] Rather, the funds are coming from U.S. taxpayers,[89] and the implications of that difference should draw the close attention of the numerous SWFs, multinational corporations, and other foreign sources of investment capital. The fact that taxpayer money is being used means the investments will likely be scrutinized much more closely; in addition, there will be considerably more at stake for those who might mismanage the money.[90]

A concern of foreign investors with the system in the United States is that their money is treated differently than American money simply because of its source.[91] However, American taxpayers are far more concerned with how their money is spent by their government than how foreign money is privately invested.[92] Foreign investors should thus note that U.S. taxpayers are about to subject the government to strict scrutiny concerning the bailout. Foreign investors seeking SWF money should realize that dealing with a CFIUS review and FINSA is a walk in the park compared to dealing with a horde of irate taxpayers and a reticent Congress.[93]

ECONOMISTS, Oct. 24, 2008, http://www.citizeneconomists.com/blogs/2008/10/24/wall-street-bailout-the-world's-largest-sovereign-wealth-fund/.

87. Truman Statement, *supra* note 37, at 2.

88. Zachary Kouwe, *As Banks Repay Bailout Money, U.S. Sees a Profit*, N.Y. TIMES, Aug. 30, 2009, at A1 (discussing where the funds come from).

89. *See id.* (explaining that the U.S. government used taxpayer money for the bailouts).

90. *See* Landler & Myers, *supra* note 78 (noting the fear that the bailout will harm taxpayers).

91. *See* O'BRIEN, *supra* note 8.

92. *See* Landler & Myers, *supra* note 78.

93. *Id.*

III. POTENTIAL PLANS FOR REFORM IN THE U.S. FINANCIAL INDUSTRY AS A RESULT OF THE FINANCIAL CRISIS

Whenever there is a tragedy in the United States, from hurricanes to bowl rankings, politicians seize the headlines to discuss potential legislative responses to the crisis.[94] The current financial crisis in which the United States finds itself is no different.[95]

Certainly, though, a major result of the current financial crisis will be increased regulatory oversight and shifting control of the financial markets from the markets themselves to the U.S. government.[96] The new regulations will be enacted because of two driving forces.[97] The first and most obvious force is the U.S. government's desire to prevent this kind of crisis from happening again.[98] The second and more subtle force is the need to properly safeguard the vast sums of tax dollars funding the recent economic bailout plans.[99] Both forces will be at the forefront of congressional debate as Congress mulls the options for financial market regulation reform.[100]

Exactly what form the regulation reforms will take remains to be seen, but some of the more influential proposals are outlined below, including the broad principles for financial reform championed by President Barack Obama,[101] the

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94. *See, e.g.*, Matt Stiles, Janet Elliott, & Clay Robison, *2009 Legislature: Proposals Aplenty in Ike's Wake*, HOUSTON CHRON., Jan. 18, 2009, at 1 (discussing potential legislation after Hurricane Ike struck Texas); *see also Lawmakers Protest Gators' Title*, SPORTS ILLUSTRATED, Jan. 22, 2009, http://sportsillustrated.cnn.com/2009/football/ncaa/01/22/lawmakers.protest.bcs.ap/index.html (discussing the lawmakers who have decided to grab headlines to protest the BCS system in college football despite the decidedly larger problems going on in the United States).

95. *See, e.g.*, Michael Kranish et al., *Senate Firmly Backs Bailout*, BOSTON GLOBE, Oct. 2, 2008, http://www.boston.com/business/articles/2008/10/02/senate_firmly_ backs _bailout/.

96. Dixon & Wutkowski, *supra* note 4.

97. *See infra* notes 99–100 and accompanying text.

98. Dixon & Wutkowski, *supra* note 4.

99. *Id.*

100. *See id.*

101. *See* JAMES HAMILTON, FINANCIAL REGULATION REFORM: WHAT TO EXPECT IN THE 111TH CONGRESS (2008) (outlining President Obama's six core principles for financial reform which include: 1) devising a 21st century regulatory structure to replace

regulatory structure reforms suggested by former Federal Reserve Board Chair Paul Volcker[102], and the reform suggestions proposed by a roundtable of the 100 largest financial services companies in the United States.[103]

A. *President Obama's Principles for Financial Regulation Reform*

In a recent white paper, James Hamilton lists the financial regulatory reforms that will likely result from President Obama's six principles for economic recovery, in conjunction with the desires of congressmen in key positions on financial committees.[104] Hamilton's list of reforms includes:

> reform of the securitization process, federal regulation of credit rating agencies, creation of a market stability or risk management regulator, federal regulation of hedge funds and other alternative investment vehicles, mandated shareholder advisory votes on executive compensation, reform of fair value accounting, consolidation of federal financial regulatory agencies, regulation by objective, increased cross-border regulatory cooperation, creation of a Financial Products Safety Commission, increased transparency in the

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one that is a creature of the 1930s; 2) giving the Federal Reserve authority over the financial institutions to which it makes loans as a lender of last resort; 3) enhancing capital requirements for financial firms and applying new standards of managing liquidity risks; 4) regulating financial institutions based on what they do as opposed to their legal status; 5) pushing the SEC to aggressively track down reports of market manipulation and insider trading; and 6) establishing a wide reaching mechanism that is better at identifying and addressing systemic threats to the financial system as a whole).

102. *See* PAUL VOLCKER ET AL., THE STRUCTURE OF FINANCIAL SUPERVISION: APPROACHES & CHALLENGES IN A GLOBAL MARKETPLACE (2008) (discussing how the new reforms should focus on the structure of the regulatory agencies with a particular interest in structuring the new agencies, both to supervise the activities of the regulated entities and to protect the consumer interests).

103. *See* RICHARD KOVACEVICH ET AL., THE FINANCIAL SERVICES ROUNDTABLE, THE BLUEPRINT FOR U.S. FINANCIAL COMPETITIVENESS: PRINCIPLES-BASED REGULATION, AN AGENDA FOR REFORM & MODERNIZED CHARTERS (2007) (discussing in depth the types of reform measures those in the banking industry see as both necessary to maintain a competitive advantage on the world stage as well as to protect the interests of the consumers).

104. HAMILTON, *supra* note 101, at 1–2.

> financial markets, federal regulation of credit default swaps, and investor protection regulation placed on equal footing with safety and soundness.[105]

Hamilton's list is both broad and deep. He sees President Obama as attempting to transform the financial regulatory structure from one designed to deal with the banks of the 1930s into one that can handle the myriad complexities of today's financial world.[106] The list of potential changes is vague in parts, however, as Hamilton does not detail how these objectives might be achieved; nevertheless, several of these reforms could have wide ranging consequences on money coming into the United States from SWFs.[107]

Specifically, SWFs will watch closely the regulatory reform of hedge funds and other alternative investment vehicles ("AIVs"), because many of them have loudly complained that the regulatory scrutiny they receive under FINSA for being foreign is unfair[108] compared to the freedom afforded to many hedge funds and private equity funds operating in almost complete regulatory secrecy.[109] Greater congressional regulation of AIVs may calm the dissatisfaction of many SWFs. For instance, greater regulation would put SWFs on the same regulatory footing as hedge funds because hedge funds would be required to be as transparent to investors and federal regulators as SWFs are required to be transparent under a CFIUS review.[110] But as

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105. *Id.*

106. *Id.* at 2–3.

107. *See id.* (listing various potential reforms). Although Hamilton's paper touches on the details of some of the potential reforms, he does not address how the new Congress might implement a plan for better cross-border regulation.

108. *See Rise of State Capitalism*, *supra* note 35, at 23–24 (discussing the hypocrisy of the United States in its current treatment of SWFs in comparison with how the American banks acted in the Asian banking crisis of the 1990s. American private banks took large stakes in these floundering Asian banks when they were at their weakest, analogous to how SWFs want to invest in the United States now).

109. *See* HAMILTON, *supra* note 101, at 12.

110. *See id.* (explaining that Senator Grassley's proposed legislation would require registration of hedge fund managers as well as increased transparency of the funds, especially as applied to their increasingly large connection to pension funds); *see also* Stoll & Goldfein, *supra* note 26 (discussing several issues an attorney must consider when dealing with a potential CFIUS review in an international transaction, whereas an

Senator Grassley points out, only Congress can accomplish this because of the recent D.C. Court of Appeals decision that strikes down the requirement that hedge fund advisers register with the SEC.[111]

B. Regulatory Structure Changes Proposed by Former Federal Reserve Board Chair Paul Volcker[112]

In a review of the financial regulatory structures of seventeen countries, Volcker and his team analyzed the effectiveness of four primary approaches to supervision.[113] Although a detailed discussion of these four regulatory approaches exceeds the scope of this Comment, Volcker's report states that "[a]s much as any jurisdiction reviewed, the United States is a prime example of the role that historical precedent, politics, and culture have played in the regulatory structure. The current structure is quite complex and has come under increased scrutiny."[114] Volcker's statement falls directly in line with President Obama's desire to bring the financial regulatory structure into the 21st century, by creating a structure not bound by historical precedent—one capable of dealing with the large complex financial firms that now dominate the economic landscape of the United States and the world.[115]

The language of President Obama, his top financial markets adviser, and many of the congressmen in charge of steering financial policy legislation seems to indicate a major shift in how

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attorney working on the transaction with a hedge fund, which is not subject to a CFIUS review, would not have to consider). *But see* Goldstein v. S.E.C., 451 F.3d 873 (D.C. Cir. 2006) (striking down as too arbitrary an SEC rule requiring the registration of hedge fund advisers, which has essentially halted all registration with the SEC by hedge fund advisers).

111. HAMILTON, *supra* note 101, at 12.

112. Michael A. Fletcher, *Obama Names Volcker to Head New Economic Advisory Board*, WASH. POST, Nov. 26, 2008, http://voice.washingtonpost.com/44/2008/11/26/obama_names_volcker_to_head_ne.html. It is also important to note that Mr. Volcker's proposals take on added weight because of his position as President Obama's principal adviser on financial and securities markets. *Id.*

113. VOLCKER ET AL., *supra* note 102, at 12–14.

114. *Id.* at 14–15.

115. *See* HAMILTON, *supra* note 101, at 2–3.

financial markets will be regulated.[116] It emphasizes getting the government up to speed in dealing with the highly complex financial entities that were at the forefront of the crisis.[117] Although the newly elected President and Congress both appear eager to tackle the problem of regulatory change in the coming months,[118] there is another important group whose opinions count as well: the financial entities being regulated.[119]

C. Regulatory Changes Proposed by the Financial Services Roundtable ("Roundtable Report")

The Financial Services Roundtable is composed of representatives from the 100 largest financial services companies in the United States.[120] The Roundtable Report, therefore, does not directly recognize the voice of the smaller investment vehicles like hedge funds or private equity firms; rather, it covers the desires of large financial institutions.[121] The Roundtable Report seeks to make changes to increase the competitiveness of the U.S. financial industry in the world.[122] The Report goes so far as to say these changes are necessary because the United States is losing its position atop the world's financial markets.[123]

The breadth of the suggestions in the Roundtable Report is beyond the scope of this Comment; however, several of them are

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116. *Id.* at 1–2.

117. *See id*. (further discussing the positions held by Senate Banking Committee Chair, Christopher Dodd, and House Financial Services Chair, Barney Frank, as well as several other Congressmen who support many of these proposed regulatory changes).

118. *Id.*

119. *See infra* Part III.C.

120. *See* KOVACEVICH ET AL., *supra* note 103, at 5. This particular report was chaired by Richard Kovacevich, Chairman of Wells Fargo, and James Dimon, Chairman & CEO of JPMorgan Chase. *Id.* at 4.

121. *See generally* Andrew Ross Sorkin, *Those Other Guys on the Street*, N.Y. TIMES, Sept. 27, 2008, at WK4, *available at* http://www.nytimes.com/2008/09/28/weekinreview/28sorkin.html (discussing the ability of hedge funds to become more powerful than the fallen investment banks in the future, should hedge funds avoid increased regulation by Congress).

122. KOVACEVICH ET AL., *supra* note 103, at 7.

123. *See id.* (citing Michael Bloomberg & Charles Schumer, *To Save New York, Learn From London*, WALL ST. J., Nov. 1, 2006, at A18).

worth noting due to their similarities and differences to President Obama's plans.[124] The Roundtable Report discusses ten specific reforms.[125] These include:

- enact principles-based regulation as opposed to rules-based regulation;
- apply prudential supervision to all financial services firms;
- reform securities litigation and other class-action litigation;
- improve consumers' access to both credit and opportunities for long-term financial security;
- make anti-money-laundering supervision more effective;
- expand the risk-based focus of capital regulation;
- ensure the effective implementation of Sarbanes-Oxley Act (Section 404) regulatory reforms;
- accelerate the modernization of U.S. accounting standards;
- modernize existing charters; and
- enact new national charter options. [126]

Of these ten suggestions, all of them are in some form of agreement with President Obama's plans, save for the securities litigation reform mentioned in the third suggestion.[127] In fact, aside from the securities litigation reform, President Obama's guidelines are very much in accord with the suggestions of the Roundtable Report.[128]

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124. *See supra* notes 120–21 and accompanying text.

125. KOVACEVICH ET AL., *supra* note 103, at 11–15.

126. *Id.*

127. *See* HAMILTON, *supra* note 101, at 2–3 (noting that nowhere in President Obama's plan does he mention need for reform in the arena of class-action securities litigation).

128. *See generally* KOVACEVICH ET AL., *supra* note 103; HAMILTON, *supra* note 101 (discussing the similarities between the Roundtable Report, which calls for principles-based regulation instead of rules-based regulation in order to bring the United States up to levels of regulation similar to the rest of the world, and President Obama, who calls for a change in regulatory regimes to bring the United States into the 21st century;

The Roundtable Report was published in 2007 as a response[129] to Treasury Secretary Paulson's assessment, which stated:

> When it comes to regulation, balance is the key. And striking the right balance requires us to consider the economic implications of our actions. Excessive regulation slows innovation, imposes needless costs on investors, and stifles competitiveness and job creation. At the same time, we should not engage in a regulatory race to the bottom, seeking to eliminate necessary safeguards for investors in a quest to reduce costs. The right regulatory balance should marry high standards of integrity and accountability with a strong foundation for innovation, growth, and competitiveness.[130]

Therefore, the Roundtable Report was not specifically keyed to the current economic crisis; rather, it was keyed to the general belief that the United States has fallen behind in its regulation of financial markets.[131] Notably, in the wake of a financial crisis, and a political desire to address it,[132] the interests of financiers and politicians are aligning.[133] With political pressure pushing for a major change in the regulatory

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including other points of agreement, such as an expansion of risk-based focus in capital market regulation, a focus on cracking down on market manipulation crimes, and the creation of regulatory agencies that have broader powers and are better equipped to handle the more complex financial firms in today's marketplace).

129. KOVACEVICH ET AL., *supra* note 103, at 9–10.

130. Henry M. Paulson, Jr., U.S. Treasury Sec'y, Remarks on the Competitiveness of U.S. Capital Markets at the Economic Club of New York (Nov. 20, 2006).

131. *See* KOVACEVICH ET AL., *supra* note 103, at 8 (quoting a report from Mayor Michael Bloomberg and Senator Charles Schumer stating ". . . [O]ur regulatory framework is a thicket of complicated rules, rather than a streamlined set of commonly understood principles, as is the case in the United Kingdom and elsewhere . . . ").

132. Kevin Drawbaugh et al., *Obama Takeover Augurs Financial Regulator Shakeup*, REUTERS, Jan. 4, 2009, http://www.reuters.com/article/businessNews/ idUSTRE50324V20090104.

133. *Compare* KOVACEVICH ET AL., *supra* note 103, at 131–44 *with* HAMILTON, *supra* note 101, at 1–3. This fact is borne out by the similarities in the proposals made in the Roundtable Report and President Obama's regulatory reform principles as stated in the Hamilton white paper.

structure of the U.S. financial industry,[134] and the industry itself having sought such a change for several years,[135] the question becomes not if these reforms are likely to occur, but when and with how much force. This question will soon become relevant for SWFs and other foreign investors, as major changes in the regulation of domestic financial firms will directly impact the cost of obtaining foreign investments into the United States, as opposed to obtaining domestic investments from an American firm under increased regulation and cost.[136] In the section that follows, this Comment will discuss whether SWFs are still interested in investing in the United States within the current economic and political environment, as well as whether any of the potential regulatory changes might lead SWFs down a path of investment or avoidance.[137]

IV. THE NEW REGULATORY REGIME IN THE UNITED STATES AND WHY SWFS SHOULD SEEK TO BENEFIT FROM IT

The combination of the recent large and well publicized investments in U.S. companies resulting in tremendous losses to several SWFs,[138] and the FINSA barrier that could be deemed dangerously protectionist,[139] and the worst economic crisis since the Great Depression,[140] begs the question: Are the potential regulatory reforms sought by President Obama and the large

134. *See* Drawbaugh et al., *supra* note 132.

135. *See, e.g.*, KOVACEVICH, *supra* note 103.

136. *See id*. at 40 (discussing how increased economic liberalization in the global economy is a direct threat to the United States' position in world capital markets).

137. *See infra* Part IV.

138. *See Once Bitten, Twice Shy*, ECONOMIST, Oct. 18, 2008, at 87, *available at* http://www.economist.com/businessfinance/displaystory.cfm?storyid=12436197 (discussing the tens of billions of dollars lost by the SWFs that invested in several troubled U.S. banks at the beginning of 2008 due to share prices of those banks being cut in at least half since the time of the investment); *see also* Heyward, *supra* note 5, at 20 (discussing several of the large headline-grabbing investments made by SWFs in 2007 and 2008 in large U.S. financial firms).

139. *See The Battle of Smoot–Hawley*, ECONOMIST, Dec. 20, 2008, at 125 (discussing the Smoot–Hawley tariff bill that exacerbated the Great Depression and has come to represent the dangers of legislation restricting free trade).

140. Heather Stewart, *We Are in the Worst Financial Crisis Since the Great Depression, Says IMF*, GUARDIAN (UK), Apr. 10, 2008, at 28, *available at* http://www.guardian.co.uk/business/2008/apr/10/useconomy.subprimecrisis.

financial institutions enough to convince SWFs to continue investing in the United States? Evidence that there are several factors coming together that could provide SWFs with a strong impetus to continue investing in the United States, despite the impact of the CFIUS review and the global economic crisis.[141] In the sections that follow, this Comment will discuss factors that could positively influence SWFs to increase investment in the United States. These include: 1) the availability of assets at historically low prices across the spectrum of industries,[142] 2) the increased desire of firms to obtain capital in order to survive, no matter where the capital comes from,[143] and 3) the regulatory changes within the United States that could put SWFs, hedge funds, and private equity on more level footing from the standpoint of regulatory costs and burdens.[144]

A. *Historically Low Asset Costs as Encouragement for SWF Investment*

The primary way to make money in a securities investment is to follow the old mantra "buy low, sell high." Currently, there are publicly listed companies in the United States that are trading at historic lows across many industries.[145] The SWFs

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141. *See* Heyward, *supra* note 5, at 21–22 (discussing the unease with which SWFs are treating the U.S. markets after the losses they suffered at the beginning of the year, but noting that investment should be encouraged by legislators and by those seeking money due to dire need for capital and the minimal risks SWFs actually pose); *see also* Dennis Moore, *Fed Welcomes Sovereign Wealth Fund Capital Raised by U.S. Banks*, FORBES, Apr. 24, 2008, http://www.forbes.com/afxnewslimited/feeds/afx/2008/04/24/afx4930025.html (further discussing the positive response the Federal Reserve gave the SWF investments in U.S. banks, as well as the criticism the investments received from several legislators concerned about selling too many U.S. assets at fire-sale prices to foreign government-controlled entities).

142. *See infra* Part IV.A.

143. *See infra* Part IV.B.

144. *See infra* Part IV.C.

145. *See, e.g.*, Christopher Hinton, *Airlines Hit New Revenue Lows*, MARKET WATCH, Jan. 12, 2009, http://www.marketwatch.com/news/story/major-carriers-trading-historical-lows/story.aspx (discussing the current historic lows of airline stocks in relation to their revenues based upon investor belief that there are bankruptcies on the horizon); Ben Rooney, *Builder Confidence Holds at Historic Lows*, CNN MONEY, Dec. 15, 2008, http://money.cnn.com/2008/12/15/real_estate/builder_confidence/ (detailing the impact the confidence crisis is having upon the homebuilding industry, real estate prices,

that invested in the financial industry at the beginning of 2008 did so because they thought they saw value in their investments.[146] These investments were somewhat premature;[147] however, such decisions were made based upon the belief that if the value of the stocks was not at the bottom, it was very close.[148]

In the investment world it is generally understood that picking the bottom of a market is more a function of luck than skill;[149] however, the simple truth is that the lower stock prices go, the closer to the floor, and thus, the better the investment.[150] As stock price volatility increases,[151] and the worldwide market continues to show who is "swimming naked,"[152] some stocks will

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and homebuilders' stock values); *see also* Sara Lepro & Tim Paradis, *Stocks Turn Lower on Anxiety Over Earnings*, ASSOCIATED PRESS ONLINE, Jan. 13, 2009 (discussing the negative impact poor 2008 fourth quarter earnings will continue to have on stock prices in numerous industries).

146. *See Qatar Fund Sees Opportunities in U.S. Banks*, REUTERS, Dec. 10, 2007, http://www.reuters.com/article/ousiv/idUSL1061718420071210 (discussing how Qatar's SWF felt there were "'tremendous opportunities'" for sovereign wealth funds like itself to invest in U.S. financial-services firms battered by a mortgage market crisis" at the end of 2007).

147. *See* Heyward, *supra* note 5, at 22.

148. *See id.* (detailing how the staggering losses taken by these SWFs should prove they made a bad investment decision and were not motivated by ulterior political motives).

149. *See* Michael Grynbaum, *Forecasters Race to Call the Bottom of the Market*, N.Y. TIMES, Oct. 27, 2008, http://www.nytimes.com/2008/10/27/business/27markets.html (discussing both the obsessive way the media seeks to quickly label the bottom of the market and how this behavior has the potential to lead to bad investment behavior).

150. This assumes that the investment is in a stock near its true bottom from which it will eventually rise.

151. *See* Peter McKay, Geoffrey Rogow & Rob Curran, *Bank Turmoil Sinks Stocks*, WALL ST. J., Jan. 14, 2009, http://online.wsj.com/article/SB123193261478480971.html (detailing several of the recent economic reports and indicators that have sent share prices falling across all sectors).

152. *See* Warren Buffett, *Chairman's Letter to Berkshire Hathaway*, (Feb. 8, 2002), http://www.berkshirehathaway.com/2001ar/2001letter.html (stating that the only way to determine whose business practices are sound is to wait for an economic downturn, similar to how "you only find out who is swimming naked when the tide goes out"); *see also* Heather Timmons & Bettina Wassener, *Satyam Chief Admits Huge Fraud*, N.Y. TIMES, Jan. 7, 2009, http://nytimes.com/2009/01/08/business/worldbusiness/08satyam.html (discussing how the recent discovery of a fraud in one of India's largest companies is comparable in scale to the Enron scandal in the United States).

eventually become truly valuable. If it is assumed that SWFs are truly seeking a valuable investment,[153] their money should return.

B. Companies Still in Need of Capital Infusions as Enticement for SWF Investment

There is little doubt the demand for SWF investment in the United States exists as strong as ever.[154] This is because of the simple truth that in an economic downturn, companies that are unable to secure enough capital to keep their operations running will go under.[155]

The reality of the current credit market and the lack of available credit have left many large businesses without access to federal bailout money and in dire need of capital with nowhere to turn.[156] As a result of most of the federal bailout money going to large financial firms,[157] companies in other industries are left gasping for credit.[158] Thus, there eventually will be a significant number of investment-grade companies

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153. *See* Heyward, *supra* note 5, at 22 (discussing SWFs' recent investments in Citigroup and other U.S. financial institutions, and how these SWFs took smaller stakes in the companies specifically to avoid the scrutiny and handwringing a large controlling stake would have garnered; notably, this tends to show these SWFs are less interested in control of U.S. companies and more interested in a positive return on their investment).

154. *See* Heyward, *supra* note 5, at 22 (stating "as the turmoil in our financial markets continues with no end in sight, it seems likely that U.S. investors and policy makers alike will welcome new investment in our financial sector from wherever it may come").

155. *See* Louis Uchitelle, *Pain Spreads as Credit Vise Grows Tighter*, N.Y. TIMES, Sept. 18, 2008, at A1, *available at* http://www.nytimes.com/2008/09/19/business/economy/19econ.html (discussing how the difficulties in obtaining credit have spread from Wall Street to Main Street and how the lack of liquidity has made even daily transactions more difficult for small businesses and individuals); Edmund Andrews & Eric Dash, *Banks in Need of Even More Bailout Money*, N.Y. TIMES, Jan. 13, 2009, at A1, *available at* http://www.nytimes.com/2009/01/14/business/economy/14.html (concluding that even after the capital injections from the U.S. government, large U.S. banks are not yet out of the proverbial woods yet and will likely need considerably more money to remain solvent).

156. *See* Andrews & Dash, *supra* note 155.

157. *See id.* (noting the tightening of the credit market).

158. Uchitelle, *supra* note 155.

acquiescing to the demands of anyone offering them credit,[159] including SWFs willing to step into the arena.

C. A New Regulatory Environment that Could Increase the Value of Money from SWFs

The question remains: will the new regulatory environment that previously added costs to the SWF investment process now provide a favorable environment for new SWF investment?

This Comment has attempted to address two angles of this question. The first is the direct regulation of SWF investments through FINSA.[160] The second is the proposed regulation of the SWFs' competitors within the United States, such as hedge funds, private equity groups, and large commercial banking companies.[161]

The passage of FINSA has resulted in less of a concern with domestic security, and more of a concern with causing a political disruption stemming from a CFIUS review.[162] Furthermore, due to the lack of clarity as to what specifically falls under the purview of FINSA,[163] future practitioners running investment transactions may choose to voluntarily file for the review in the interest of time and good faith.[164] SWFs will be likely candidates for the more extensive second-level review; however, this review will probably be mitigated by a well-thought-out plan implemented in advance to save a deal from being bogged down in an unexpectedly complicated CFIUS review.[165]

Even though the passage of FINSA will have a disparate impact on SWFs compared to a domestic firm that generally

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159. *See* Jack Healy & Vikas Bajaj, *Cost of Borrowing Zooms Up for Corporations*, N.Y. TIMES, Jan. 18, 2009, at B1, *available at* http://www.nytimes.com/2009/01/19/business/economy/19debt.html (discussing the unprecedented cost of credit many companies now face when trying to obtain financing in the debt markets, noting that these companies are often willing to pay that cost to survive).

160. *See supra* Part I.

161. *See supra* Part III.

162. Claire Spencer, *The Impact of FINSA on Foreign Acquisitions in the U.S.*, FINANCIER WORLDWIDE, Feb. 2008, http://www.morganlewis.com/pubs/FinancierWW_ImpactOfFinsa-Mahinka_Feb08.pdf.

163. *See supra* notes 53–59 and accompanying text.

164. Spencer, *supra* note 162.

165. *Id.*

does not deal with the cost of a CFIUS review,[166] this cost will likely be mitigated, if not overshadowed entirely, by the costs resulting from changes to the financial regulatory system in the United States.[167]

Although SWFs will still be subject to a higher level of scrutiny when they invest in "critical infrastructure,"[168] this should not prevent a continued aggregate increase in SWF investment[169] consistent with global trends.[170]

The imbalance in value between an SWF investment slightly hindered by a CFIUS review and a domestic investment greatly hindered by the cost of coping with an entirely new and unprecedented regulatory structure will eventually reach an economic equilibrium, as business leaders and politicians will respond to this lack of global competitiveness.[171]

In the interim, though, SWFs will likely see the value of their investment dollars increase because they can avoid some of

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166. *Id.*

167. *See generally* HAMILTON, *supra* note 101 (discussing proposals to change the structure of the financial regulatory system in the United States, all of which involve increased government oversight and involvement in the dealings of domestic financial firms, including proposals to statutorily empower greater shareholder control over executive compensation and proposals to require increased disclosure from hedge funds and private equity firms); KOVACEVICH ET AL., *supra* note 103, at 88–94 (discussing the need for new risk-based capital requirements for the entire spectrum of banks in order to avoid banks over-leveraging).

168. *See* Spencer, *supra* note 162 (listing the types of investments currently understood to trigger a review for critical infrastructure, including electric power generation, oil and gas transmission lines, certain IP technologies, bioterrorism drugs, bridges and ports).

169. *Id.* (stating "[t]he overwhelming majority of transactions should still be approved by CFIUS").

170. *See* Marchick & Slaughter, *supra* note 6, at 23 (discussing the rapid increase in foreign direct investment from new source countries into the United States in the past several years).

171. *See* KOVACEVICH ET AL., *supra* note 103, at 7 (listing the United States' faltering position as a world financial leader as the primary reason for a change in the financial regulatory structure); HAMILTON, *supra* note 101, at 4 (discussing the need to overhaul the U.S. financial regulatory structure in order to bring it up to speed with the 21st century and to recreate it in a similar manner as those used in Europe and Australia); *see generally* PAUL A. SAMUELSON, FOUNDATIONS OF ECONOMIC ANALYSIS (Harvard Univ. Press 1983) (1947) (explaining the properties of economic equilibrium).

the costs domestic firms will face from the new financial regulatory scheme.[172]

V. SUGGESTIONS FOR SWFS TO MAXIMIZE THEIR INVESTMENT POTENTIAL DURING THE COMING REGULATORY SHIFT WHILE STILL ABIDING BY THE REQUIREMENTS OF FINSA

The final section of this Comment will attempt to lay out a series of suggestions for SWFs to look beyond what seems like a valuable investment and attempt to find several "once in a lifetime" investments that will arise from the confluence of regulatory changes and the depression of asset prices due to the economic crisis. These suggestions include: 1) seeking a clearer definition of the requirements under FINSA, 2) avoiding investment in assets that come with too much political or regulatory baggage, and 3) choosing assets that hedge funds and private equity firms would invest in were it not for the lack of assets and newly created regulatory handcuffs.

A. Push for Increased Clarity of FINSA's Requirements

Since its inception, one of the major complaints against FINSA by those subject to its jurisdiction is that the definitions within the law are conspicuously vague.[173] Since FINSA went into effect at the beginning of 2008, dozens of reviews have taken place and these are being used to get a sense of the gray areas in FINSA.[174]

The Treasury officials responsible for clarifying the FINSA regulations have stated, at the urging of politicians and business interests, that they will focus on several key issues that need clarification.[175] These issues primarily include what it means for

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172. *See* KOVACEVICH ET AL., *supra* note 103, at 88–94 (discussing the capital and disclosure requirement proposals for domestic firms that SWFs would not be subject to, thus giving SWFs an advantage over the domestic firms); *see generally* HAMILTON, *supra* note 101, at 5 (discussing the need for compulsory regulation and increased disclosure across financial institutions because SWFs are already subject to disclosure requirements through FINSA.) This would put domestic firms on equal footing with SWFs as far as disclosure requirements.

173. Rubinoff & Savio, *supra* note 27.

174. *Id.*

175. *Id.*

a foreign entity to "control" an American asset, what constitutes "foreign government-controlled transactions," and what constitutes "critical infrastructure."[176]

First, the issue of "control" concerns whether the investment by the foreign entity would result in a controlling stake in an American asset through stock ownership or voting rights; currently CFIUS has declined to include a bright-line test for this issue.[177] This is a key issue because if left as it stands, the CFIUS review is up to the discretion of the reviewers with those being reviewed having a weaker understanding of whether their particular transaction should be subject to review.[178] SWFs would do well to lobby for clear demarcations of control, in order to gain a clear understanding of what transactions might be subject to a CFIUS review.[179] This will allow for necessary planning in advance, to avoid a potentially crippling delay during the review.[180]

Second, Treasury officials have focused on how to define "foreign government-controlled transactions."[181] For the most part, SWFs will be less concerned with this definition because they are essentially the paradigm of what constitutes foreign government-controlled.[182] Although SWFs will more than likely trigger a CFIUS review as a covered transaction under this requirement,[183] they should lobby for certain suggestions. These suggestions were made in a letter written to the Treasury by Representatives Franks, Maloney, and Gutierrez, who recommended CFIUS take into account positive factors of SWFs

176. *Id.*

177. *Id.*

178. *Id.*

179. *Id.*

180. *See* Spencer, *supra* note 162 (discussing the need for a well planned approach to the CFIUS review in order to mitigate as much as possible the costs of the review).

181. Rubinoff & Savio, *supra* note 27.

182. *See* Crocker, *supra* note 34, at 462–65 (stating that the United States Treasury defines SWFs as "a government investment vehicle funded by foreign exchange assets and which manages those assets separately from official reserves").

183. Rubinoff & Savio, *supra* note 27.

when deciding whether SWFs should be subject to review as foreign government-controlled.[184]

Lastly, the final section of FINSA that needs clarification denies foreign investment in "critical infrastructure." Although this is the one section most SWFs would like to see explicitly defined, it is also the least likely to be clarified.[185] This section is of particular interest to SWFs because even if they are able to survive a CFIUS review as a foreign government-controlled entity, their choice of investment could potentially fall into the gray area of "critical infrastructure" and be unexpectedly denied by CFIUS.[186]

Currently, the only specific guidance FINSA provide as to what constitutes "critical infrastructure" is that it includes "major energy assets."[187] Many comments submitted to the Treasury express concern over the ability to expand this category to include assets affecting economic security, public health, and public safety.[188] SWFs should follow the lead of these comments and at a minimum request that FINSA define assets that are definitely not critical infrastructure, and lobby FINSA to more clearly define what definitely constitutes critical infrastructure.[189] Although there is a general understanding of what investments will trigger the "critical infrastructure" review under FINSA,[190] until there is clearer guidance on the matter many SWFs will likely file for voluntary CFIUS reviews in order to clear this hurdle early rather than have their transactions

184. *See id.* (listing certain positive factors as reasons to potentially not review certain funds as foreign government-controlled, including commercial investment mandate, and policies and procedures funds use to follow worldwide best practices).

185. *See* Spencer, *supra* note 162 (discussing the need to come up with a clear definition of "critical infrastructure," although this will be both extremely difficult and not in the best interest of the United States because cutting-edge technology is constantly changing).

186. Rubinoff & Savio, *supra* note 27.

187. *Id.*

188. *Id.*

189. *See id.*

190. Spencer, *supra* note 162 (listing the assets generally thought to be covered by the term "critical infrastructure").

blocked much further into the process and at much greater cost.[191]

B. Avoid Potential Political Landmines

The greatest concern for SWFs investing in the United States is getting involved in a transaction that draws a large negative political reaction, similar to that which occurred during the Dubai Ports World deal.[192] Even if the potential investment were to meet the FINSA requirements, as the Dubai Ports World deal actually did,[193] an uprising of political opposition could be the death knell of an otherwise legitimate investment opportunity.[194] In order to avoid these potential value-destroying political landmines, SWFs can and should take several steps both when choosing a potential investment and during the initial stages of the investment and CFIUS review.[195] These steps include: 1) avoid investment in assets currently considered "critical infrastructure" or assets that fall into the gray area of potentially "critical infrastructure," 2) employ lobbyists to ensure that the investment will be able to make it through the halls of Congress without creating an uproar, and 3) harness the fear of the current economic climate by making investments in assets that have economic value and which will create goodwill with the American people, who will view the investment as a helping hand instead of a controlling fist.[196]

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191. *See* Stoll & Goldfein, *supra* note 26 (stating there is considerable value in voluntarily filing for a CFIUS review early due to both the safe harbor provisions contained within FINSA and the fact that the costs of preparing for a review pale in comparison to the costs of having the deal blocked or unwound well into the deal process).

192. *See* Stagg, *supra* note 8, at 354 (stating that some of the big risks stemming from the political involvement authorized by CFIUS are the ability of special interest groups to influence the process and the ability for some politicians to see a CFIUS review as an opportunity to appear tough on national security issues in an effort to outdo the other side's similar efforts).

193. *Id.* at 344 (stating President Bush approved the Dubai Ports World deal in January 2006, following a CFIUS review that found that the transaction posed no credible threat to national security).

194. *See id.* at 353 (stating that the politicization of foreign investment could have "unintended, negative effects" and "deals will be scuttled for political purposes").

195. *See* Hunt, *supra* note 14, at 309–10.

196. *See* Paul Rose, *Sovereigns as Shareholders*, 87 N.C. L. REV. 83, 99–100 (2008)

Although the first suggestion may initially be a little difficult due to the lack of clarity as to what constitutes "critical infrastructure,"[197] avoiding the paradigmatic investments in this category should not be as difficult. Avoiding paradigmatic investments includes eschewing investments in assets heavily involved with nuclear power, electrical power generation and transmission, cutting-edge technological firms, bioterrorism drugs and vaccines, natural gas and oil reserves, pipelines, refineries, bridges, and ports.[198] Even though this list is in no way exhaustive,[199] it still leaves a potential investor asking: what is left to invest in?

The answer rests in sectors of the economy that were the harbingers of the current economic malaise.[200] Investments in real estate, financial firms, and industries tied to these sectors are both selling at historically low prices[201] and are unlikely to trigger the need for a CFIUS review.[202] The value in these areas will be strong not only in economic terms, but also in terms of avoiding a potential political uproar over foreign investment in critical infrastructure.

Next, SWFs must properly plan well in advance their navigation of the CFIUS review process in order to avoid the

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(suggesting that SWFs should avoid investments in certain sectors such as energy or government contracting); Spencer, *supra* note 162 (advising potential foreign investors to retain lobbyists at the initial stages of CFIUS review); Heyward, *supra* note 5, at 20 (noting that foreign investments in troubled U.S. banks would be expected to receive "unalloyed gratitude").

197. *See* Spencer, *supra* note 162 (discussing the need for CFIUS to come up with a concrete definition for critical infrastructure); Stoll & Goldfein, *supra* note 26 (discussing the need to be careful when choosing possible investments in the United States due to a lack of clarity on what constitutes critical infrastructure).

198. *See* Spencer, *supra* note 162 (stating that these industries currently qualify as "critical infrastructure").

199. *See id.*

200. *See* Friedman, *supra* note 76 (stating how the global financial crisis began with the subprime mortgage crisis, consumed the financial industry in the United States, and then spread across all other economic sectors throughout the world).

201. Rooney, *supra* note 145.

202. David Richards, *United States: Sovereign Wealth Funds and U.S. Real Estate Investment*, MONDAQ, Sept. 15, 2009, http://www.mondaq.com/article.asp?articleid=83734; Maya Jackson Randall, *U.S. May Clarify Scrutiny of Foreign Investments*, WALL ST. J., Apr. 22, 2008, at A4.

fate that befell the Dubai Ports deal.[203] Properly employing lobbyists as well as opening an ongoing dialogue with politicians from both sides of the aisle will go a long way towards ensuring there are no potentially deal-breaking surprises before, during, or after the CFIUS review.[204] This is also a particularly important time to forge relationships with new employees in President Obama's administration, specifically because many of the current rules President Obama is implementing will make lobbying more difficult in the near future.[205]

Although the final suggestion is by far the most difficult to carry out, it is the one that can separate the good investments from the once in a lifetime variety.[206] This process entails determining which investments are likely to be out of reach for the vast majority of private equity firms and hedge funds due to lack of available credit and other restrictions or barriers resulting from new regulations.[207]

Doing this will likely prove exceptionally difficult, as there appears to be a shortage of sound investment opportunities anywhere, even for the struggling hedge fund industry.[208] Luckily, two recent investments have provided examples of what

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203. Spencer, *supra* note 162.

204. *Id.*

205. Dan Eggen & R. Jeffrey Smith, *Lobbying Rules Surpass Those of Previous Presidents, Experts Say*, WASH. POST, Jan. 22, 2009, at A4.

206. *See generally* Andrew Barry, *Warren Buffett Makes an Offer Goldman Sachs Can't Refuse*, WALL ST. J., Sept. 28, 2008, at 3, *available at* http://online.wsj.com/article/SB122256922970483051.html (stating that Buffett's investment in Goldman Sachs shows how a firm with enough capital to impact a large well run company that needs a capital infusion can extract tremendously favorable terms from that company).

207. Press Release, Rothstein Kass, Hedge Fund Managers Anticipate Increased Regulation Under New Presidential Administration, Nov. 13, 2008, *available at* http://www.marketwatch.com/news/story/Hedge-Fund-Managers-Anticipate-Increased/story.aspx?guid={12003B48-8D2B-410E-9CC6-096287469E4D} (discussing a survey finding that hedge funds feel the new regulations coming from the Obama administration will make their funds more costly to operate); *see also* David Lawder & Tim Ahmann, *Geithner: Strengthen Derivatives, Hedge Fund Rules*, REUTERS, Jan. 23, 2009, *available at* http://www.reuters.com/article/ousiv/idUSTRE50M4W420090123 (speaking about looming regulations to improve market transparency).

208. Saijel Kishan, *Hedge Fund Assets May Fall $450 Billion This Yea r*, BLOOMBERG, Jan. 23, 2009, http://www.bloomberg.com/apps/news?pid=20601085&sid=a9K0oMRQvf5o&refer=Europe.

to do-and what not to do. As an example of what not to do, some of the poorest recent investments have been made by what could be called the world's largest SWF—the U.S. government.[209] The Trouble Asset Relief Program ("TARP") money invested thus far has been criticized and ridiculed for lacking proper diligence.[210]

As an example of what to do, the other headline-making investment hailed as another in a long line of brilliant moves was the investment in Goldman Sachs by the "Oracle of Omaha," Warren Buffett.[211] Buffett's investment in Goldman came with many terms favorable to him because of the weight of his name and the size of his wallet.[212]

Accordingly, SWFs seeking to make a "once in a lifetime" investment in the battered United States economy would be wise to follow the Buffett model of choosing sound companies in a little trouble and using some of the tremendous leverage that comes with great wealth to extract the most favorable terms possible. This model is far superior to following the U.S. government's model of spending in the name of economic rescue with seemingly reckless abandonment and little oversight.[213]

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209. *See supra* Part II (discussing the similarities between the U.S. government's actions in the recent financial stimulus bills and the actions of SWFs).

210. Lee Brodie, *See What People Are Saying About: Scathing TARP Criticism*, CNBC: FAST MONEY, Jan. 9, 2009, http://www.cnbc.com/id/28579036.

211. *See* Zachery Kouwe, *Buffett's Goldman Stake Pays Richly*, DealBook, http://dealbook.nytimes.com/2009/07/24/buffetts (July 24, 2009, 7:12 EST) (noting Buffett's success as an investor, the success of the Goldman–Buffett deal and Goldman's subsequent rise in stock price).

212. *See id.* (discussing the allure of a deal with Buffet).

213. *See* David Leonhardt, *Could Warren Buffett Negotiate a Better Deal for Taxpayers?*, N.Y. TIMES, Sept. 25, 2008, at C1, C14; Daniel Wagner, *Geithner "Ultimately Responsible" For Failed AIG Oversight, Bailout Watchdog Says*, STAR TRIBUNE, Oct. 14, 2009, http://www.startribune.com/politics/64209712.html.