

GAO

Report to the Chairman, Subcommittee  
on National Security, Veterans Affairs,  
and International Relations, Committee  
on Government Reform, U.S. House of  
Representatives

September 2002

## DEFENSE TRADE

# Mitigating National Security Concerns under Exon-Florio Could Be Improved



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United States General Accounting Office  
Washington, DC 20548

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September 12, 2002

The Honorable Christopher Shays  
Chairman, Subcommittee on National Security, Veterans  
Affairs, and International Relations  
Committee on Government Reform  
House of Representatives

Dear Mr. Chairman:

The Exon-Florio amendment<sup>1</sup> to the Defense Production Act authorizes the President to suspend or prohibit foreign acquisitions, mergers, or takeovers of U.S. companies<sup>2</sup> if (1) there is credible evidence that a foreign controlling interest might threaten national security and (2) legislation, other than Exon-Florio and the International Emergency Economic Powers Act,<sup>3</sup> does not adequately or appropriately protect national security. The President delegated the authority to review foreign acquisitions of U.S. companies to an interagency group, the Committee on Foreign Investment in the United States. Implementing regulations require that the Committee undertake an initial 30-day review after receiving a voluntary submission from the companies involved in an acquisition. If the Committee decides during this 30-day review that there could be credible evidence to support the belief that the acquisition may threaten national security, the Committee can initiate a 45-day investigation. After completing the investigation, the Committee submits a recommendation to the President. The President has 15 days to decide whether to allow the acquisition to proceed or to suspend or prohibit it. In 1992, the law was amended to require that the President report all cases requiring a presidential determination to the Congress. Previously, the law required a report only when the President took action to block an acquisition.

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<sup>1</sup> 50 U.S.C. app. 2170.

<sup>2</sup> In the remainder of this report, acquisitions, mergers, and takeovers are referred to as acquisitions.

<sup>3</sup> The International Emergency Economic Powers Act gives the President broad powers to deal with any "unusual and extraordinary threat" to the national security, foreign policy, or economy of the United States (50 U.S.C. 1701-1706). To exercise this authority, however, the President must declare a national emergency to deal with any such threat. Under this legislation, the President has the authority to investigate, regulate, and, if necessary, block any foreign interests' acquisition of U.S. companies (50 U.S.C. 1702(a)(1)(B)).

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In response to your request, we examined the process by which the Committee on Foreign Investment in the United States reviews and investigates foreign acquisitions of U.S. companies. Specifically, we (1) determined the circumstances under which the Committee formally investigates acquisitions and (2) identified weaknesses in the Committee's process for implementing Exon-Florio that limit its effectiveness.

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## Results in Brief

The Committee initiates investigations only when it cannot identify potential mitigation measures in the review period to resolve national security issues arising from the acquisitions or when it needs time beyond the 30-day review to negotiate potential mitigation measures and the companies involved are not willing to request withdrawal of their notification. Of 320 acquisitions notified to the Committee from 1997 through 2001, only 4 were investigated; and only 1 resulted in a presidential determination. For acquisitions in which the Committee identified national security concerns but was unable to mitigate them within the 30-day review period, it allowed companies to withdraw and resubmit their notification to provide further information and/or provide additional time to mitigate those concerns. Also, the additional time allowed agencies to take actions under other laws and regulations that could address the Committee's concerns. Where these actions would address concerns, the Committee could approve the acquisition without resorting to an investigation.

The Committee's process for implementing Exon-Florio contains the following weaknesses that may have limited its effectiveness:

- The Committee has not established interim protections before allowing withdrawal when concerns were raised and the acquisition had already been completed. We identified two cases in which the companies completed the acquisition prior to initially filing with the Committee, withdrew their notification because of unresolved national security concerns, and failed to promptly re-file. As a result, potential threats to national security, such as foreign access to export controlled technology, remained.
- Agreements between the Committee and companies contained nonspecific language that may make them difficult to implement. For example, one agreement was modeled on the network security agreements that the Department of Justice has negotiated with some telecommunications companies and that have been attached as conditions to Federal Communications Commission licensing orders.

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However, this agreement contained provisions that Justice Department officials acknowledged were less specific and less stringent than many similar provisions in network security agreements.

- The agreements did not specify responsibility for overseeing implementation and contained few provisions to assist in monitoring compliance. For example, one contained no time frame by which the conditions in the agreement had to be implemented. The other contained time frames but no consequences for failure to meet the time frames.

This report contains recommendations for the Secretary of the Treasury as Chair of the Committee on Foreign Investment in the United States. We are recommending that the Secretary of the Treasury (1) establish interim protections before allowing withdrawal for acquisitions in which companies have completed or plan to complete the acquisition prior to a Committee decision, (2) increase the specificity of actions required by mitigation measures negotiated under the authority of Exon-Florio, and (3) designate in the agreement, the agency responsible for overseeing implementation of the agreement and monitoring compliance with mitigation measures.

In commenting on a draft of this report, the Treasury Department agreed to implement our recommendation to more clearly identify in future agreements the agency responsible for ensuring compliance with mitigation measures, but disagreed with our other two recommendations. Treasury stated that the Committee already has the authority to place conditions on withdrawals and could conclude cases involving withdrawal more expeditiously if it strove to do so, without compromising national security or the U.S. open investment policy. However, in the two cases we identified in which the companies completed the acquisition prior to filing with the Committee and were allowed to withdraw their notifications, the Committee did not use its authority to ensure that the companies re-filed and that the cases were concluded expeditiously. Treasury also questioned whether greater specificity in the agreements would have provided additional national security protections in the two cases we cited. In our opinion, greater specificity would provide greater protection by making it easier for agencies to effectively evaluate compliance with agreements. The Departments of Defense and Justice also provided comments, which are reprinted in the appendixes.

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## Background

In 1975, the President established the interagency Committee on Foreign Investment in the United States to monitor the impact and coordinate U.S. policy on foreign investment in the United States. In 1988, the Congress enacted the Exon-Florio amendment to the Defense Production Act. Exon-Florio authorized the President to investigate the impact of foreign acquisitions of U.S. companies on national security and to suspend or prohibit an acquisition if it might threaten national security and no legislation, other than Exon-Florio and the International Emergency Economic Powers Act, could adequately protect national security. The President delegated the authority to investigate to the Committee.<sup>4</sup>

The Committee operates at two levels: staff representatives who perform initial reviews of companies' notices and principals who are the decision makers on issues of national security. The Secretary of the Treasury serves as the Committee Chair and Treasury's Office of International Investment coordinates the Committee's activities. This office has the dual responsibility of monitoring foreign investment in the United States and advocating free trade and world markets open to foreign investment, i.e., the U.S. open investment policy. In implementing Exon-Florio, the Committee seeks to preserve the confidence of foreign investors that they will be treated fairly while implementing the intent of Exon-Florio. That is, to provide a mechanism to review, and if the President finds appropriate, to restrict foreign investment that threatens to impair the national security.

Exon-Florio and implementing regulations provide the Committee with broad discretion to evaluate and make decisions about issues of potential national security risk. Neither the law nor its implementing regulations define "national security," although the law provides guidance on factors to consider, such as U.S. technological leadership in national security areas. The Committee interprets its authority to conduct an investigation as providing the Committee the authority to negotiate measures to mitigate national security concerns when other regulatory regimes do not apply.

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<sup>4</sup>Membership on the 11-member Committee was established by Executive Order and includes the Departments of Commerce, Defense, Justice, and State; the Council of Economic Advisors; the National Economic Council; the National Security Council; the Office of Management and Budget; the Office of Science and Technology Policy; and the United States Trade Representative. Treasury, as Chair, has discretion to invite other agencies to participate in the Committee's activities.

In an uninterrupted process, the Committee and the President would have up to 90 calendar days to review, investigate, and determine what if any action the President would take concerning an acquisition. The companies can request withdrawal of their voluntary notice at any time up to the President's decision. (See app. I for a detailed discussion of the Committee's process.)

Notifying the Committee of an acquisition is not mandatory. However, the Committee may review any acquisition it identifies that has not been notified. In June 2000, we recommended that the Secretaries of Commerce, Defense, Treasury, and State establish procedures for the Committee and member agencies to improve their ability to identify foreign acquisitions with potential national security implications.<sup>5</sup> The Committee also may reopen a case if it learns that companies submitted false or misleading information in their notice.

From 1997 through 2001, the Committee received 333 notices for 320 proposed or completed acquisitions. Table 1 provides summary data on notices filed with the Committee.

**Table 1: Notifications to the Committee on Foreign Investment in the United States and Actions, 1997-2001**

Year	Notifications	Acquisitions <sup>a</sup>	Investigations	Notices withdrawn after investigation initiated	Presidential determination
1997	62	60	0	0	0
1998	65	62	2	2	0
1999	79	76	0	0	0
2000	72	71	1	0	1
2001	55	51	1	1	0
<b>Total</b>	<b>333</b>	<b>320</b>	<b>4</b>	<b>3</b>	<b>1</b>

<sup>a</sup>Acquisitions that were withdrawn and re-filed are shown in the year of initial notification.

Source: Based on Treasury Department Office of International Investment data.

In most instances, the Committee concluded its activities under Exon-Florio within 30 days of receiving notification because (1) the Committee did not identify any issues of national security, (2) the companies and the government agencies addressed potential national security concerns prior

<sup>5</sup> U.S. General Accounting Office, *Defense Trade: Identifying Foreign Acquisitions Affecting National Security Can Be Improved*, [GAO/NSIAD-00-144](#) (Washington, D.C.: June 29, 2000).

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to filing, or (3) the companies and the government agreed on measures to mitigate national security concerns before the end of the 30-day review. About 96 percent (306 of 320 acquisitions) were concluded within 30 days.

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## The Committee Investigates in Only Limited Circumstances

The Committee has initiated investigations under only limited circumstances, namely, when it could not identify potential mitigation measures in the review period that would resolve national security issues arising from the acquisitions or when it needed more time than the 30-day review period to complete its work and the companies involved were not willing to request withdrawal of their notification. Since 1997, the Committee has initiated only four 45-day investigations. The Committee initiated investigations because of concerns about the potential for unauthorized transfers of technology and because it could not identify measures that would mitigate those concerns or needed extra time beyond the 30-day review to negotiate possible mitigation measures, but the companies were not willing to request withdrawal of their notifications.

As a matter of practice, the Committee tries to avoid the use of investigations and presidential determinations. The Committee reviews foreign acquisitions to protect national security while seeking to maintain the U.S. open investment policy. For many companies, being the subject of an investigation has negative connotations. Avoiding an investigation helps to maintain the confidence of investors that the government does not view the acquisition as problematic. Also, a presidential determination could be politically sensitive. According to one Committee staff member, the Committee looks for the best way to work out national security concerns without an investigation.

Since 1997, the Committee has allowed companies involved in 13 acquisitions (including 3 of the 4 for which an investigation was subsequently initiated) to withdraw their notifications and re-file at a later date rather than initiate an investigation. In some, the time was needed for other agencies to complete reviews of the acquisition under other laws and regulations. For example, the Committee allowed two shipping companies to withdraw the notification of their planned merger to provide time for the companies to request approval from the Maritime Administration. The companies re-filed so that Committee approval would coincide with the end of the Maritime Administration's 90-day review. The Maritime Administration required the companies to transfer operations of

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ships that participated in the Maritime Security Program<sup>6</sup> to a U.S.-owned operator to prevent foreign ownership of ships that the United States would rely on in wartime. According to a Committee official, based on the Maritime Administration's approval, the Committee did not need to initiate an investigation. In others, the Committee used the extra time to clarify such issues as the nature of the foreign ownership, products and technologies that were subject to U.S. export control laws, relationships with countries or companies of concern, and future plans for the U.S. company.

In three acquisitions, the companies chose not to request withdrawal and the Committee initiated investigations. In two of these cases, the companies had withdrawn their notification once to provide more time to negotiate agreements to protect sensitive information and to provide more information. The companies then re-filed with the Committee and began a new 30-day review period. However, by the end of the second 30-day review they had not reached agreement and the companies were unwilling to withdraw again, so the Committee initiated an investigation. In one case, the companies and the Committee agreed on mitigation measures after the investigation ended but prior to a presidential determination. The Committee allowed the companies to withdraw the notification again and re-file it as a new case to avoid the need for a presidential determination. In the second case, the companies were unable to reach agreement with the Defense Department and the investigation ended after the companies agreed to abandon the proposed acquisition.

In the third case, Committee members had raised concerns about the potential for foreign government access to sensitive information and the ability of the foreign company to deny the U.S. government access to information. The Committee and the companies were unable to reach agreement on how to mitigate these national security concerns within the 30-day review period and the companies were unwilling to withdraw the notification, so the Committee initiated an investigation. By the end of the investigation, the Committee and the companies had concluded an agreement in time for the Committee to recommend that the President take no action. Accordingly, the President determined that no further action was necessary and the acquisition was reported to the Congress.

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<sup>6</sup> The Maritime Security Program provides the Defense Department access to commercial vessels operating under U.S.-flag registry and related assets in a time of national emergency. The Department of Transportation's Maritime Administration is responsible for administering the program.

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In another case in which the acquisition had already occurred, the Committee was unwilling to allow a second withdrawal of the notification. The Committee had allowed the company to withdraw and re-file to allow time to address export control concerns. However, the Committee could not resolve concerns about unauthorized transfers of technology. As a result, it initiated an investigation. During the investigation, the company asked to withdraw its notification instead of waiting for a presidential determination. The Committee permitted the company to withdraw on the 45th day of the investigation, with the understanding that the foreign company would divest the U.S. company.

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## The Committee's Process for Implementing Exon-Florio May Limit Its Effectiveness

Weaknesses in the Committee's process for implementing Exon-Florio may in some cases have resulted in ineffective national security protections because the Committee allowed withdrawal of cases in which the acquisition had been completed without establishing interim protections, used nonspecific provisions or language in agreements it had concluded with companies to mitigate national security concerns, and did not identify the agency responsible for overseeing implementation and monitoring compliance with the agreement.

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## Allowing Withdrawals of Completed Acquisitions Can Delay National Security Protections

According to Committee officials, few of the acquisitions for which the Committee receives notification are completed prior to the Committee concluding its responsibilities under Exon-Florio. Therefore, the period before the companies re-file generally creates limited risk to national security because, until the acquisition is completed, the foreign company does not have full access to the U.S. company's resources. Committee officials told us that the companies' desire to conclude the acquisition provides an incentive for the companies to resolve issues and re-file as quickly as possible. However, this incentive does not exist when companies notify the Committee after concluding their acquisition.

We identified two instances where long periods had elapsed between the companies concluding their acquisition and the Committee completing its work. One company that filed its notification almost 2 years after concluding the acquisition asked to withdraw its notification near the end of the 30-day review to provide additional information and to address export control issues the Committee had identified. The company waited over 9 months to re-file. After re-filing, the Committee determined that concerns about unauthorized transfers of technology could not be mitigated and the company agreed to divest the acquired company. However, the foreign company had the ability to access the technologies

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that prompted the Committee's concern for almost 3 years, from the time the acquisition was concluded until the company agreed to divest the acquisition to address the Committee's concerns.

In the second case, the company filed with the Committee more than a year after completing the acquisition. The Committee allowed the company to withdraw the notification to provide more time to answer the Committee's questions and provide assurances concerning export control matters. The company did not re-file for more than a year after withdrawing the original notification. The Committee allowed the company to withdraw its notification a second time because there were still unresolved issues. More than a year has passed since the second withdrawal and the company has yet to re-file.

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### Nonspecific Language May Make Agreements Difficult to Implement

In the two acquisitions that required the Committee to conclude agreements under the authority of Exon-Florio, the agreements contained provisions or language that may make them difficult to implement. In one instance, the Defense Department was concerned about the release of certain technologies to foreign parties and took the lead in negotiating an agreement. In the other instance involving a communications company, the Justice Department was concerned about access to subscriber information, among other matters, and took the lead in negotiating an agreement.

The agreement negotiated by the Defense Department contained language that was open to interpretation. It required a "good faith effort" to divest a subsidiary to mitigate a concern about access to technology and provided an alternative<sup>7</sup> if the company could not find a domestic purchaser to make a "reasonable" offer. The agreement did not include criteria defining what actions would constitute a "good faith effort" nor what would be a "reasonable" offer. Accordingly, when the company divested part, but not all, of the subsidiary and cited the lack of interested buyers as the rationale, the agreement contained no criteria that would allow government officials to determine whether the company's efforts to sell the subsidiary were made in good faith. Likewise, without measurable criteria in the agreement, it was not possible to determine whether the

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<sup>7</sup> If the company was unable to divest the subsidiary, it was required to transfer a certain portion of the subsidiary's business to a new entity that would be controlled by an independent governance board.

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sole bidder for the entire subsidiary made a reasonable offer. Further, although the divestiture or the alternative was considered necessary, there were no criteria for determining whether the partial divestiture served the same purpose. Without clear criteria, government officials could not effectively evaluate compliance with the agreement and could be faced with the need to litigate questions of this nature.

The Justice Department modeled the agreement it negotiated on network security agreements it has used with some telecommunications companies. These agreements are attached as conditions to Federal Communications Commission licensing orders.<sup>8</sup> While the agreement negotiated under the authority of Exon-Florio addressed many of the same issues as the network security agreements, the provisions were often less detailed. In discussions with Justice Department officials, they acknowledged that several provisions were less specific and less stringent than those in some network security agreements. They said that, in their opinion, Exon-Florio offers less bargaining power to the government than the Communications Act, which underlies the Federal Communications Commission licensing process. As a result, conditions negotiated under Exon-Florio may be less stringent than conditions they have negotiated with some telecommunications companies.

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## Provisions on Monitoring Compliance Are Lacking

Exon-Florio implementing regulations do not provide guidance on monitoring company compliance with agreements. Committee officials have stated that the Committee generally defers to various federal agencies for monitoring activities, even in cases in which the authority to negotiate mitigation measures was based on Exon-Florio. One Committee official noted that these agencies have the expertise that the Committee lacks. However, neither of the two agreements negotiated under the authority of Exon-Florio specified which agency would be responsible for monitoring implementation.

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<sup>8</sup> Although the Federal Communications Commission is not a party to network security agreements and defers to executive branch agencies on matters involving national security, the Commission retains discretion to deny, condition, or revoke a license if it determines that the public interest, which includes national security concerns, will be served by doing so. The Justice Department separately negotiates network security agreements with telecommunications companies to mitigate concerns, such as illegal wiretapping. At the Justice Department's request, the Commission has conditioned its approval of some proposed license transfers or assignments on compliance with the signed agreement and has attached such agreements as part of Commission licensing orders.

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Provisions to assist agencies in monitoring agreements were also lacking. One agreement contained no requirement for the company to demonstrate compliance and no time frames by which provisions were to be implemented. The other required the company to appoint a board member, subject to approval by the Secretaries of the Treasury and Defense, to oversee the implementation of the agreement and provide a semiannual status report to the Committee and the Defense Department. It provided time frames for certain actions to occur, but it contained no consequences for failure to comply with the time frames, thus providing no incentive for the company to act within the time frames. And in fact, the company failed to meet the terms of one provision within the agreed upon time frame.

This approach is less stringent than the approach used in consent agreements by the Department of Justice and the Federal Trade Commission in resolving antitrust issues during reviews of mergers and acquisitions. Some consent agreements contain provisions to ensure that the government has access to documents and people to verify compliance with the terms of the agreement. Some also include provisions allowing the government some approval authority over the buyer of a company in the event that a divestiture is required and provide for the government to appoint trustees to monitor the divestiture. If the companies do not divest within the agreed time frame, some consent agreements also provide for a trustee to manage the divestiture.

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## Conclusions

For the most part, the Committee on Foreign Investment in the United States is able to fulfill its responsibility to ensure that foreign acquisitions of U.S. companies do not threaten national security without resorting to investigations. When the process could not be completed within the 30 days, the Committee has allowed companies to withdraw and re-file to avoid initiating an investigation. However, this approach can, in certain circumstances, negate the effectiveness of the Exon-Florio statute. Typically, the Committee reviews a proposed acquisition for national security concerns before the acquisition is concluded. However, when companies have completed an acquisition before filing with the Committee, the potential for harm already exists and any actions to prevent harm can only be after the fact. Allowing companies to withdraw notification to the Committee when an acquisition has already occurred without instituting interim protections risks the very harm to national security that Exon-Florio was enacted to prevent. Likewise, when agreements are concluded to mitigate national security concerns, the lack of specificity in actions called for by the agreements and the uncertain

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responsibility for implementing and monitoring make assuring compliance difficult.

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## Recommendations for Executive Action

In view of the need to assure that national security is protected during the period that withdrawal is allowed for companies that have completed or plan to complete the acquisition prior to the Committee completing its work, we recommend that the Secretary of the Treasury, in his capacity as Chair of the Committee on Foreign Investment in the United States, revise implementing regulations to require specific interim protections prior to allowing withdrawal for companies that have completed or plan to complete the acquisition before the Committee has completed its work. Further, to ensure compliance with agreements concluded under the authority of Exon-Florio, we recommend that the Secretary of the Treasury, in his capacity as Chair of the Committee on Foreign Investment in the United States, (1) increase the specificity of actions required by mitigation measures in future agreements negotiated under the authority of Exon-Florio and (2) designate in the agreement the agency responsible for overseeing implementation and monitoring compliance with mitigation measures.

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## Agency Comments and Our Evaluation

In commenting on a draft of our report, the Treasury Department stated that understanding the context in which the Committee implements Exon-Florio would aid in assessing the report's conclusions and recommendations. Treasury explained in its comments that the Congress intended that Exon-Florio be invoked only in cases where other laws were not adequate or appropriate to protect national security. Further, Treasury noted that the United States has traditionally maintained an open investment policy because it benefits our economy. Both Treasury and Defense disagreed with our recommendations (1) for interim measures to protect national security when companies that have completed an acquisition are allowed to withdraw their notification and (2) that increased specificity of actions be required by mitigation measures in future agreements negotiated under the authority of Exon-Florio. The Treasury Department agreed to act on our recommendation to make the agency responsible for ensuring compliance with mitigation measures more explicit in future agreements.

The Treasury Department stated that we focused on only a few cases and that it is unusual for agreements to be negotiated under the authority of Exon-Florio. We agree. As Treasury noted in its comments, the Congress intended that Exon-Florio be invoked only when other laws are not

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adequate or appropriate to protect national security, and thus acts as a safety net. However, the two cases in which we raise concerns about granting an extended withdrawal period were the universe of cases in which companies that have already completed the acquisition prior to notifying the Committee have requested and been granted withdrawal. Likewise, the two cases in which we believe greater specificity was needed in the agreements represent 100 percent of the cases in which Exxon-Florio was the basis for an agreement. As a result, we believe that the current process is not an effective safety net.

The Departments of Treasury and Defense stated that our recommendation for interim measures is not necessary. Further, the departments said that negotiating interim measures could take considerable time and effort, thus delaying a final review of the acquisition. Treasury also said that the Committee already has the authority to place conditions on withdrawals without amending the implementing regulations and that by striving to do so, it can conclude its cases more expeditiously without compromising national security or the U.S. open investment policy. We did not intend for the regulations to call for negotiating interim measures, but rather for the Committee to use its authority to impose them as a condition of withdrawal under certain circumstances. In one of the cases we identified, the company waited over 9 months to re-file with the Committee, and when the Committee could not mitigate its concerns about unauthorized transfers of technology, the company agreed to divest. In the other case, the company did not re-file for more than a year after withdrawing the original notification, and has yet to re-file more than a year after the second withdrawal. In these cases, the Committee did not use its authority to ensure that the companies re-filed and that the cases were concluded expeditiously. Therefore, for those cases in which the acquisitions occur prior to the Committee completing its work, we continue to believe revising the implementing regulations to require interim protections prior to granting withdrawal would ensure that cases involving completed acquisitions are concluded more expeditiously.

The departments questioned whether greater specificity in the agreements we cited would have provided additional national security protections. In our opinion, greater specificity would provide greater protection by making it easier for agencies to effectively evaluate compliance with agreements. For example, in the instance we noted where an agreement called for a “good faith effort” to sell a subsidiary, the foreign company sold only part of the subsidiary and deemed it a “good faith effort,” even though at least one other company offered to buy the entire subsidiary. Further, the foreign company sold the subsidiary in exchange for stock in

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the acquiring company. The agreement also provided, if divestiture was not possible, for the foreign company to ensure that the subsidiary would be able to support government contracts, such as by continuing a certain level of investment in equipment and personnel. The foreign company maintains that those requirements do not apply to the part of the subsidiary that was not divested. The government officials monitoring the agreement would need to decide whether what the company did constituted a “good faith effort” and whether the partial divestiture was adequate to protect national security as called for by the agreement. In our view, mitigation measures that are open to interpretation increase the difficulty of determining compliance and thus provide the potential for harm to national security.

The Treasury Department agreed to act on our recommendation to make explicit which agency has responsibility for reviewing compliance with mitigation measures. However, Treasury, along with the Defense Department, maintained that the accountability in the two cases we cited was clear because the agreements were signed by policy level officials. During our review, the agencies did not provide evidence to show that anyone was ensuring that the companies were complying with the agreements. Although the Justice Department stated in its comments that officials from the Federal Bureau of Investigation visited the offices of the U.S. company to assess its compliance with the agreement, Bureau officials told us that only one visit took place and that they have no additional plans to verify compliance. In addition, the Defense Department did not provide any documentation showing that it took action to ensure the companies were complying with the agreement beyond some initial meetings. Defense Department officials also had indicated that it was not their responsibility to monitor compliance. Therefore, we believe that it is necessary to be more specific in assigning responsibility to ensure company compliance with commitments to the Committee.

Treasury, Defense, and Justice Department comments are reprinted in appendixes II through IV, respectively.

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## Scope and Methodology

We examined 17 acquisitions notified to the Committee on Foreign Investment in the United States between January 1, 1997, and December 31, 2001. They included the 4 acquisitions that were investigated, 12 of the acquisitions that were withdrawn and re-filed, and 1 acquisition suggested by Committee staff. The objective of the case reviews was to understand and document the Committee’s process for reviewing foreign acquisitions of U.S. companies. We did not attempt to validate the conclusions reached

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by the Committee on any of the cases we reviewed. We analyzed data on acquisitions from relevant Committee member agencies, including the Departments of Commerce, Defense, Justice (including the Federal Bureau of Investigation), State, and Treasury. We also discussed the Committee's process with Committee staff officials.

To determine under what circumstances the Committee formally investigates foreign acquisitions, we interviewed Committee staff level members. We reviewed all four cases that went to investigation since 1997. After reviewing these, we interviewed Committee members, documented their national security concerns, and discussed the measures needed to mitigate those concerns.

To determine whether weaknesses exist in the Committee's implementation of Exon-Florio, we analyzed and discussed with Committee staff members the laws and regulations that grant the Committee authority to identify, negotiate, and mitigate national security concerns. For the telecommunications cases, we interviewed Federal Communications Commission officials and discussed their regulatory processes related to license transfer. We also compared Exon-Florio agreements to consent agreements used by the Department of Justice and the Federal Trade Commission in antitrust actions.

We performed our work from June 2001 through May 2002 in accordance with generally accepted government auditing standards.

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As we agreed with your office, unless you publicly announce the contents of this report earlier, we plan no further distribution of it until 30 days from the date of this letter. We will then send copies to the Chairman and Ranking Minority Member of the Senate Committee on Banking, Housing, and Urban Affairs and the Chairman and Ranking Minority Member of the House Committee on Financial Services and the Ranking Minority Member of the Subcommittee on National Security, Veterans Affairs, and International Relations of the House Committee on Government Reform. We will also send copies to the Secretaries of Commerce, Defense, Justice, State, and the Treasury; the Chairman, Council of Economic Advisors; the Director, National Economic Council; the Assistant to the President for National Security Affairs; the Director, Office of Management and Budget; the Director, Office of Science and Technology Policy; and the United States Trade Representative. We will also make copies available to others upon request. In addition, the report will be available at no charge on the GAO Web site at <http://www.gao.gov>.

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Please contact me on (202) 512-4841 if you or your staff has any questions concerning this report. Major contributors to this report were Thomas J. Denomme, Paula J. Haurilesko, Monica Brym, Gregory K. Harmon, Anne W. Howe, John Van Schaik, and Michael C. Zola.

Sincerely yours,

A handwritten signature in black ink that reads "Katherine V. Schinasi". The signature is written in a cursive style with a large, stylized initial "K".

Katherine V. Schinasi  
Director  
Acquisition and Sourcing Management

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# Appendix I: The Committee on Foreign Investment in the United States and the Process for Implementing Exon-Florio

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In 1975, the President established the interagency Committee on Foreign Investment in the United States to monitor the impact of foreign investment in the United States and to coordinate the implementation of U.S. policy on foreign investment.<sup>1</sup> In fulfilling this responsibility, the Committee was expected to (1) analyze trends and significant developments in foreign investment in the United States, (2) provide guidance on arrangements with foreign governments for advance consultation on their prospective major investments in the United States, (3) review investments that may have major implications for U.S. national interest, and (4) consider proposals for new legislation or regulations relating to foreign investment.

In 1988, the Congress enacted the Exon-Florio amendment<sup>2</sup> to the Defense Production Act. Exon-Florio authorized the President to investigate the impact of foreign acquisitions<sup>3</sup> of U.S. companies on national security and to suspend or prohibit an acquisition if credible evidence exists that a foreign controlling interest may threaten national security and no legislation, other than Exon-Florio and the International Emergency Economic Powers Act, can adequately protect national security.

The President delegated the authority to conduct investigations under Exon-Florio to the Committee on Foreign Investment in the United States. The Committee, chaired by the Secretary of the Treasury, is currently composed of representatives from the Departments of Commerce, Defense, Justice, and State; the Council of Economic Advisors; the National Economic Council; the National Security Council; the Office of Management and Budget; the Office of Science and Technology Policy; and the United States Trade Representative.<sup>4</sup> Figure 1 shows how the Committee's membership evolved from 1975 to the present.

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<sup>1</sup> Executive Order No. 11858, reprinted as amended in 15 U.S.C. 78b (2002).

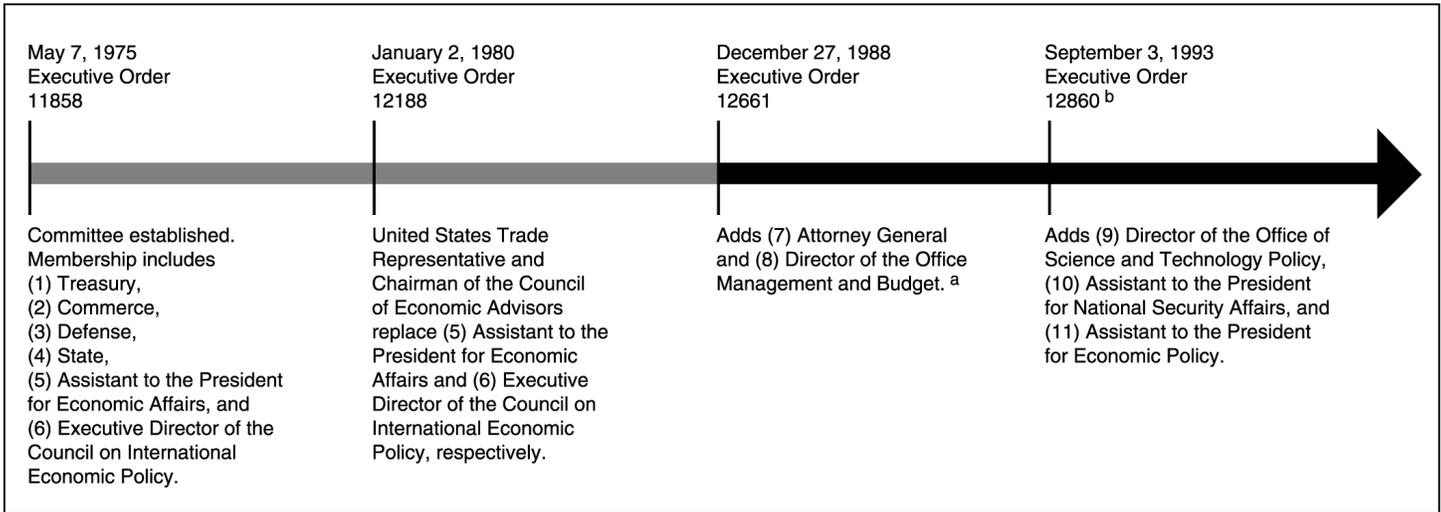
<sup>2</sup> 50 U.S.C. app. 2170.

<sup>3</sup> In this appendix, acquisitions, mergers, and takeovers are referred to as acquisitions.

<sup>4</sup> Treasury, as Committee Chair, can invite other agencies to participate in the Committee's activities. For example, representatives from the Department of Energy and the National Aeronautics and Space Administration participate in reviews and investigations of certain acquisitions.

**Appendix I: The Committee on Foreign Investment in the United States and the Process for Implementing Exon-Florio**

**Figure 1: Evolution of Committee on Foreign Investment in the United States Membership**



<sup>a</sup>Executive Order 12661 also delegated to the Committee the President's authority to investigate foreign acquisitions of U.S. companies.

<sup>b</sup>Executive Order 12860 implemented the suggestion in Public Law 102-484 to add the Director of the Office of Science and Technology Policy and the Assistant to the President for National Security.

Source: GAO.

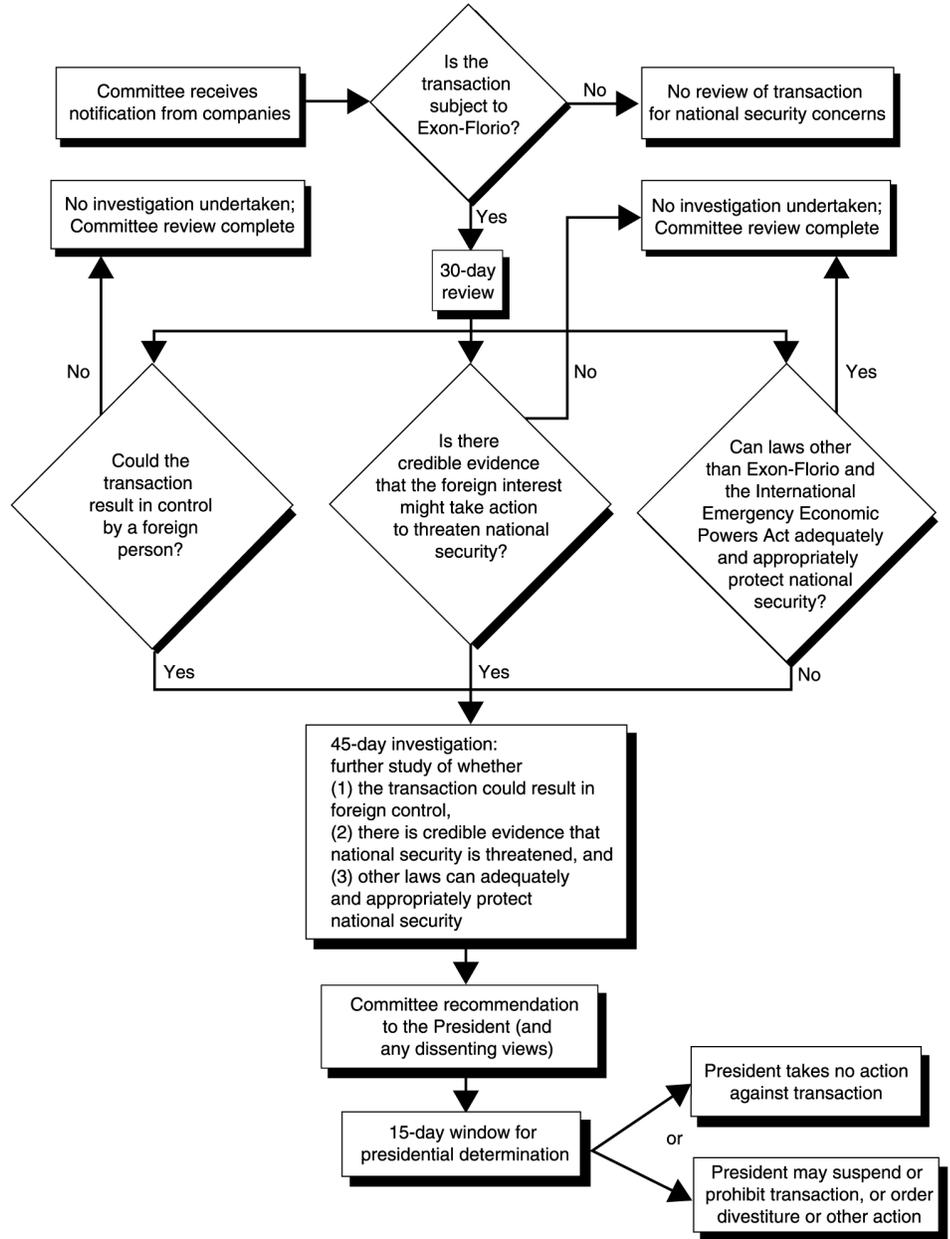
The Treasury Department's Office of International Investment coordinates the Committee's activities and is responsible for monitoring foreign investment in the United States while also advocating U.S. policy on open investment.

In 1991, the Treasury Department issued regulations to implement Exon-Florio.<sup>5</sup> As figure 2 shows, the Committee follows a four-step review process of proposed foreign acquisitions of U.S. companies: voluntary notice, 30-day review, investigation, and presidential determination.

<sup>5</sup> 31 C.F.R. Part 800.

**Appendix I: The Committee on Foreign Investment in the United States and the Process for Implementing Exon-Florio**

**Figure 2: The Committee on Foreign Investment in the United States Process According to 31 C.F.R. Part 800**



Note: Companies may request to withdraw their notification at any time prior to a presidential determination. If the companies re-file, the process begins again.

Source: GAO.

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## Voluntary Notification

The Committee relies on companies to voluntarily report pending or completed acquisitions and Committee members to inform each other about known foreign acquisitions, although neither the companies nor the Committee members are required to do so. Treasury officials generally encourage agencies through their Committee representatives to bring foreign acquisitions to Treasury's attention informally so that the officials may contact the companies involved and encourage them to notify voluntarily. If companies do not voluntarily submit a notification, any member of the Committee may do so. The Committee points out that companies have a strong incentive to notify and obtain approval because the President can order divestiture of unapproved acquisitions. Although the regulations do not require prior notification, in most instances, companies notify the Committee before the acquisition occurs, thus avoiding the risk and expense of forced divestiture.

The implementing regulations require notices to contain detailed, accurate, and complete information about

- the nature of the acquisition,
- the name and address of the U.S. and foreign principals,
- the acquisition's proposed or actual completion date,
- assets being acquired,
- each contract with any U.S. government agency with national defense responsibilities active within the last 3 years, and
- each contract involving classified information active within the past 5 years.

Further, the notice is required to state whether the acquired U.S. company is a Department of Defense supplier and whether it has products or technical data subject to export controls or international regulations.

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## Thirty-day Review Period

To begin the 30-day review, the Committee staff from Treasury notifies the member agencies of the acquisition and provides them with supporting documents. The Committee members then notify their appropriate internal offices to assist in reviewing the acquisition.

During the 30-day review, the Committee considers such factors as whether (1) the acquisition may result in control by a foreign person of a

U.S. company engaged in interstate commerce in the United States; (2) credible evidence exists to support a concern that the acquisition could impair national security; and (3) adequate authority to protect the national security is provided under provisions of laws other than the International Emergency Economic Powers Act (50 U.S.C. 1701-1706). The Committee may invite the parties to meet with the staff to discuss and clarify issues.

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## Investigation

When necessary, Committee members meet to determine whether any concerns raised are significant, thus requiring a 45-day investigation. If the Committee agrees to investigate, the Committee formally notifies the companies about the investigation and its time frame for completion. During the investigation, the Committee may analyze the acquisition in greater depth or attempt to mitigate the national security concerns raised. If national security concerns are not resolved, the Committee informs the companies that a report will go to the President with the Committee's recommendation on the acquisition. If Committee members cannot agree on a recommendation, the report to the President includes the differing views of all Committee members.

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## Presidential Determination

The President has 15 days to decide once he has received the Committee's recommendations. The decision is not subject to judicial review. The President can suspend or prohibit any proposed or completed acquisition. He may require the Attorney General to seek appropriate relief, including divestiture, in U.S. district courts. The President's divestiture authority, however, cannot be exercised if (1) the Committee has informed the companies that their acquisition was not subject to Exon-Florio or had previously decided to forego investigation or (2) the President has decided not to act on that specific acquisition under Exon-Florio. However, if the Committee determines that the companies omitted or provided false or misleading information, the Committee may reopen its review or investigation or revise its recommendation to the President. The President has ordered divestiture in only one case, although other acquisitions have been canceled after Committee action without presidential intervention.

The 1992 Byrd amendment to Exon-Florio requires the President to send a report to the Congress if the President makes a decision regarding a proposed foreign acquisition. This requirement was added in response to concerns about the lack of transparency in the Committee's process. Under the original Exon-Florio law, the President was obligated to report only after prohibiting a proposed acquisition.

---

## **Withdrawal**

Any party to the foreign acquisition may request in writing that the voluntary notice be withdrawn at any time before the President's decision on a proposed acquisition. The request must be addressed to the Committee staff chairman and state the reasons for the request. The Committee decides whether to grant a withdrawal and notifies the requestor in writing of the Committee's decision. After the Committee approves a withdrawal under these circumstances, any prior voluntary notices submitted no longer remain in effect. Also, any subsequent proposals by these parties must be considered as a new, voluntary notice and receive a new case number from the Committee. In some circumstances, companies have received a 5-day expedited review if the re-filed notice did not differ from the original voluntary notice.

# Appendix II: Comments from the Department of the Treasury



UNDER SECRETARY

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C.

June 26, 2002

Ms. Katherine V. Schinasi  
Director  
Acquisition and Sourcing Management  
United States General Accounting Office  
Washington, DC 20548

Dear Ms. Schinasi:

This is in response to your May 28, 2002 letter to the Secretary requesting comments on the GAO draft Report, "Defense Trade: Implementation of Exon-Florio Could Be Improved."

I believe a brief explanation of the Exon-Florio provision in relation to other U.S. laws and regulations that protect national security and the context in which CFIUS implements the provision would assist readers of the Report in assessing the conclusions and recommendations.

#### **Exon-Florio**

When Exon-Florio was enacted, one of the major assumptions behind the legislation was that the President already had at his disposal a number of laws and regulations designed to protect the national security. These range from laws that restrict foreign ownership of U.S. air carriers to laws that regulate the export of sensitive technology or that restrict access to classified information. Congress intended that the Exon-Florio provision be invoked by the President only in those cases where no other law, other than the International Emergency Economic Powers Act or Exon-Florio itself, is adequate and appropriate to protect the national security. Of course, the purpose of Exon-Florio is to provide a statutory framework pursuant to which the President may suspend or prohibit certain transactions where doing so is necessary to protect national security when other laws do not provide the tools necessary to accomplish this.

#### **U.S. Open Investment Policy**

The United States has traditionally maintained an open investment policy. This means that foreign investors are accorded national treatment (i.e., permitted to invest in U.S. companies on the same basis as domestic investors) in nearly all sectors of the U.S. economy, subject to appropriate national security and other exceptions set forth in our bilateral and multilateral trade and investment agreements. Therefore, as a general rule, governmental review and approval of foreign direct investment is not required, except in certain sectors related to national security. The United States adheres to this policy because it is in our interest to do so. The United States receives the largest share of the world's foreign direct investment. This provides numerous benefits to our economy, including introducing new capital, technology, managerial expertise, and jobs. Some of these benefits accrue to sectors of the economy that enhance the U.S. defense industrial base.

The existence of Exon-Florio raises the awareness of foreign investors contemplating acquisitions of U.S. companies to the importance of national security considerations and it helps to ensure that foreign investments are structured in ways to avoid national security problems. Foreign acquisitions are structured to take into account national security concerns because of the existence of Exon-Florio. Moreover, some transactions are not pursued because the parties recognize that the national security concerns raised by the transactions could not be mitigated.

In its 1995 Report on CFIUS, GAO stated that, "The CFIUS review process serves both to protect national security and to minimize any potential adverse effect of the Exon-Florio legislation on foreign investment in the United States."

**GAO's Recommendations**

Based on its review of the implementation of Exon-Florio, GAO is recommending in its report that the Secretary of Treasury, in his capacity as Chair of CFIUS:

1. Revise implementing regulations to require specific interim protections prior to granting withdrawal for companies that have completed or plan to complete an acquisition before CFIUS has completed its work.
2. Assure compliance with agreements concluded under the authority of Exon-Florio by: (a) increasing the specificity of actions required by mitigation measures in future agreements negotiated under the authority of Exon-Florio and (b) designating in the agreement the agency responsible for overseeing implementation and monitoring compliance with mitigation measures.

**CFIUS's View Regarding GAO's Recommendations**

As Chair, Treasury coordinated CFIUS's position on GAO's recommendations. We oppose the recommendations with the exception of 2 (b) for the following reasons:

Recommendation 1: Interim measures in the withdrawal period.

We do not agree with the recommendation that interim measures are necessary in the withdrawal period.

While a party to a transaction can request a withdrawal, it is up to CFIUS whether or not to approve the withdrawal. If necessary to protect the integrity of the process, CFIUS has the authority to condition a withdrawal in writing on specific criteria and timetables that the companies would be required to meet and would inform them that their failure to satisfy these criteria in the allotted time could result in CFIUS's reinitiating the review. Conditioning a grant of withdrawal in this way would not require an amendment to the regulations.

We believe that interim measures could take considerable effort and time to negotiate, and delay a final review of a transaction. We believe it makes more sense for CFIUS and its member agencies to pursue any potential national security concerns in a disciplined manner, consistent with an on-going effort by CFIUS to reform the process implementing Exon-Florio. CFIUS can conclude work more expeditiously than has been the case without compromising the national security or our open investment policy by striving to complete activities during the withdrawal period more rapidly.

We would note that GAO acknowledges that very few of the 1,400 foreign acquisitions notified have been concluded prior to CFIUS's concluding action under Exon-Florio. In fact, GAO identifies only two transactions where potential national security concerns might justify "interim measures."

Recommendation 2 (a): Increasing the specificity of actions required.

GAO raised this concern in connection with two cases. Since the Exon-Florio statute looks to the applicability of existing national security laws and regulations first, it is unusual for agreements to be negotiated under Exon-Florio authority.

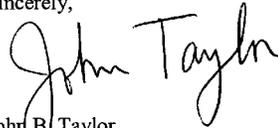
In our view, GAO did not present any evidence that greater specificity of actions required would have provided additional national security protections in these two cases. In fact, the agencies with the greatest interest in negotiating agreements for the two cited cases were both satisfied that the companies involved made commitments that afforded the necessary national security protections.

Recommendation 2 (b): Monitoring compliance with commitments.

In our view the question of accountability is clear in both cases because the agreements were signed at the policy level by both Treasury and the agency with the primary interest in negotiating the commitments and in reviewing compliance with these commitments. However, any future agreements negotiated under the authority of Exon-Florio will make explicit which agency reviews compliance with the commitments.

Thank you for providing the opportunity to review and comment on GAO's report.

Sincerely,



John B. Taylor  
Under Secretary for International Affairs

# Appendix III: Comments from the Department of Defense

Note: A GAO comment supplementing the report text appears at the end of this appendix.



POLICY

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
2000 DEFENSE PENTAGON  
WASHINGTON, DC 20301-2000

JUN 26 2002

Ms. Katherine V. Schinasi  
Director, Acquisition and Sourcing Management  
U.S. General Accounting Office  
Washington, D.C. 20548

Dear Ms. Schinasi:

Thank you for the opportunity to comment on the GAO draft report, "DEFENSE TRADE: Implementation of Exon-Florio Could Be Improved," dated May 28, 2002, (GAO Code 120063/GAO-02-736).

Although your recommendations are addressed to the Secretary of the Treasury, please find our attached comments to the GAO draft report.

Sincerely,

A handwritten signature in black ink, appearing to read "Lisa Bronson".

Lisa Bronson  
Deputy Under Secretary of Defense,  
Technology Security Policy and  
Counterproliferation

Attachment:  
As stated



**GAO Draft Report, "DEFENSE TRADE: Implementation  
Of Exon-Florio Could Be Improved," dated May 28, 2002  
(GAO Code 120063/GAO-02-736)**

**Recommendation 1:**

Revise implementing regulations to require specific interim protections prior to granting withdrawal for companies that have completed or plan to complete an acquisition before CFIUS has completed its work.

**Comments:**

Rather than interim measures, which could take more time and effort to negotiate, and even delay a final resolution, we believe a better solution is greater emphasis on completing a CFIUS review during a withdrawal period for companies that have already or plan to complete an acquisition before CFIUS has completed its work.

We do not advocate setting schedules on such reviews due to the possibility that over-rigorous schedules will prevent agencies from performing a complete review. Rather, the greater need is a commitment by all of the CFIUS members to regard such a situation as one demanding urgent resolution due to the already-present possibility of technology diversion in a foreign acquisition that has not been reviewed. On specific cases in which the parties' level of cooperation during a withdrawal is questionable, CFIUS should condition the withdrawal in writing on specific criteria and timetables that the companies would be required to meet and inform them that their failure to satisfy these criteria in the allotted time could result in CFIUS reinitiating the review.

**Recommendation 2:**

Assure compliance with agreements concluded under the authority of Exon-Florio by: (a) increasing the specificity of actions required by mitigation measures in future agreements negotiated under the authority of Exon-Florio and (b)

designating in the agreement the agency responsible for overseeing implementation and monitoring compliance with mitigation measures.

**Comments to 2(a)**

The GAO raised concern about two cases. In one case the GAO did not provide any evidence that greater specificity of actions required would have provided additional national security protections. We were satisfied that the companies involved in this case made commitments that afforded the necessary national security protections.

Greater specificity will likely engender more U.S. involvement in the business decisions of companies, which should be avoided. The better course of action is that which we have pursued previously, that of tailoring agreements to the national security concerns presented by each foreign acquisition. It is not desirable for CFIUS to become the vehicle for the U.S. Government to impose performance requirements on foreign acquisitions of U.S. companies.

**Comments to 2(b)**

The question of accountability is clear in both cases because the agreements were signed at the policy level by both Treasury and the agency (in one case, Defense) with the primary interest in negotiating the commitments and in "reviewing" rather than "monitoring" compliance with these commitments. (Monitor suggests a far greater involvement in day-to-day oversight of a company than an individual agency with national security responsibilities is able to, or even should, provide. The available means of compliance assurance are better described by the term "review" which implies the periodic look by the responsible agency or agencies at the company's actions in compliance with the agreement, supported by the independent means of review, e.g., site visits, review of reports, etc.)

See comment 1.

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The following is GAO's comment on the Department of Defense's letter dated June 26, 2002.

---

**GAO Comment**

1. Exon-Florio provides the President the authority to take action to suspend or prohibit any foreign acquisition of a U.S. company that may threaten national security. Thus, by its nature, the legislation engenders involvement in the business decisions of companies in the name of protecting national security. Agreements the Committee and government agencies negotiate with companies all require some level of involvement in business decisions. Likewise, antitrust legislation requires government involvement in the business decisions of companies, and in implementing antitrust legislation, the Justice Department and the Federal Trade Commission use consent agreements that are more stringent than the agreements the Committee has used.

# Appendix IV: Comments from the Department of Justice

Note: GAO comments supplementing those in the report text appear at the end of this appendix.



U.S. Department of Justice

Criminal Division

Office of the Deputy Assistant Attorney General

Washington, D.C. 20530

June 25, 2002

Mr. Thomas Denomme  
Assistant Director  
Acquisition and Sourcing Management  
U.S. General Accounting Office  
Washington, D.C. 20548

Re: Department of Justice Comments to GAO Report on the Exon-Florio Amendment to the Defense Production Act (GAO-02-736)

Dear Mr. Denomme:

The following constitute the comments by Department of Justice ("DOJ") to the GAO Report on the Exon-Florio Amendments to the Defense Production Act (GAO-02-736 Defense Trade) (hereinafter referred to as the "Report"):

(1) At the bottom of page 7, the Report states:

In the two acquisitions that required the committee to conclude agreements under the authority of Exon-Florio, the agreements contained provisions or language that may make them difficult to implement. In one instance, the Defense Department was concerned about the release of certain technologies to foreign parties and took the lead in negotiating an agreement. *In the other instance involving a communications company, the Justice Department was concerned about access to subscriber information and took the lead in negotiating an agreement.*

DOJ Comment:

Regarding the second transaction, the Report implies that DOJ took the lead with respect to this transaction solely because it was concerned about access to subscriber information. While DOJ was concerned about this issue, DOJ was concerned about other matters too, which it sought to alleviate through negotiation. The resulting agreement reflects those efforts and concerns.

(2) On page 2, second bullet, second sentence, the report addresses the same transaction and states:

Now on p. 9.

See comment 1.

Now on pp. 2-3.

Page 2 of 4

For example, *one agreement, modeled on the network security agreements that the Department of Justice negotiates with telecommunications companies as part of the Federal Communications Commission licensing process, contained provisions that Justice Department officials acknowledged were less specific and less stringent than many similar provisions in network security agreements.*

Similarly, in the middle of page 8, again referring to the same transaction, the Report states:

The Justice Department modeled the agreement it negotiated on network security agreements used with telecommunications companies as part of the Federal Communications Commission licensing process. *While the agreement negotiated under the authority of Exon-Florio addressed many of the same issues as the network security agreements, the provisions were often less detailed. In discussions with Justice Officials, they acknowledged that the provisions were less specific and less stringent than many in network security agreements.*

DOJ Comment:

These assertions in the Report create several false impressions. They imply that the Department of Justice enters into so-called “network security agreements” in all telecommunications transactions that raise concerns, that such agreements are the same, that they all contain detailed provisions, and that the agreement referred to in the Report was less specific or stringent than those agreements. This is not the case. Different proposed transactions can raise very different concerns. Within the context of the FCC licensing and authorization process, DOJ employs a wide range of measures to address the particular concerns identified based on the particular transaction at hand. These measures range from doing nothing, because DOJ is satisfied that the transaction poses no particular problem, to exchanging letters of understanding with the parties, to negotiating a security agreement, and potentially to objecting to the consummation of the proposed transaction altogether. Further, even in a cases in which the Department of Justice seeks to negotiate an agreement, the terms of the agreement may vary from transaction to transaction. Although it is accurate to say that DOJ modeled the agreement for the transaction referred to in the Report on some of the network security agreements that had been negotiated in past and that, when compared to the FCC process, the Exon-Florio process does not provide a forum that is as efficient or conducive to negotiation, it is misleading to conclude that the terms of the aforementioned agreement were not as specific or as stringent as all the network security agreements.

(3) On Page 8 of the Report, it states:

[N]either of the two agreements negotiated under the authority of Exon-Florio specified *which agency would be responsible for monitoring implementation of*

Now on p. 10.

See comment 2.

Now on p. 11.

Page 3 of 4

*the agreement. . . . Provisions to assist in monitoring agreements were also lacking.*

Similarly, on Page 9 of the Report in the “Conclusions” Section, it states:

*Likewise, when agreements are concluded to mitigate national security concerns, the lack of specificity in actions called for by the agreements and the uncertain responsibility for implementing and monitoring make assuring compliance difficult.*

DOJ Comment:

With respect to the aforementioned agreement, the Department of Justice disagrees with both of these characterizations. Although the agreement did not explicitly state that the Justice Department and the Federal Bureau of Investigation are responsible for monitoring and assuring compliance, it was not deemed necessary to do so because all concerned parties correctly understand that the Justice Department and the Bureau, as party signatories, would be responsible for monitoring and assuring compliance. Failing to state the obvious in an agreement is hardly a deficiency. Indeed, performance of the agreement establishes that this understanding was and is held by all parties. Representatives from the Federal Bureau of Investigation have visited the offices of the U.S. company to assess its compliance with the terms of the agreement.

In addition, it is inaccurate to state that there are no provisions within the agreement that require the U.S. company to assist in the monitoring process. The agreement specifically requires named company officials to report “promptly to [the Department of Justice] and [the Federal Bureau of Investigation] any information that he or she acquires regarding inter alia: (i) illegal or unauthorized access to or disclosure of Classified Information, Sensitive Controlled Information, or Sensitive Information; (ii) electronic surveillance conducted in violation of Federal or state law or regulation; or (iii) illegal access to or disclosure of Subscriber Information.” The agreement also requires the companies to use “all reasonable efforts to ensure that U.S. law enforcement officials have proper access to the relevant officers, employees, independent contractors, and facilities of [the U.S. company] in order to discuss the operation and implementation of [the U.S. company’s] law enforcement policies.” Further, another separate provision, titled “Cooperation in Investigations,” requires the company to extend “complete and courteous cooperation with law enforcement officials involved” in investigations related to the important aspects of the agreement.

Conclusion

The aforementioned comments are not meant to suggest that the Department of Justice believes that the Exon-Florio process cannot be improved upon. To the contrary, the Justice Department believes that the process can be, and should be, improved in order to properly emphasize and adequately protect our national security, with active involvement by those CFIUS

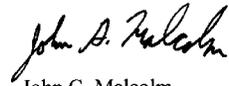
Now on p. 12.

See comment 3.

Page 4 of 4

member agencies that express national security concerns about particular transactions, while still allowing appropriate international transactions and free flow of capital. The Department of Justice is currently working with other CFIUS agencies in considering ways to do so.

Sincerely,



John G. Malcolm  
Deputy Assistant Attorney General  
Criminal Division

---

The following are GAO's comments on the Department of Justice's letter dated June 25, 2002.

---

## GAO Comments

1. We have revised the text to clarify that access to subscriber information is just one of the issues of concern.
2. We believe our draft report accurately reflected information Justice Department officials provided to us. In discussions with department officials about our findings, they concurred with our statement that the agreement was less stringent than other agreements and further stated that the terms were less specific in many provisions. Moreover, a Justice Department analysis provided specific examples of measures that were less stringent than measures the department required in other agreements with telecommunications companies. However, we have revised the text to clarify that the department enters into network security agreements with only some, but not all, telecommunications companies.
3. Text revised to clarify that provisions that assisted the agencies in monitoring agreements were also lacking, as demonstrated in the text following the sentence in question.

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