

Testimony before the Senate Committee on Banking, Housing, and Urban Affairs
Hearing on “Examining Outbound Investment”

Toward a Balanced Outbound Investment Screening Regime

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Thank you, Chairman Brown and Ranking Member Toomey as well as your hard-working staff for inviting me to testify on outbound investment, its implications for national security, and factors to consider if Congress decides to move forward with legislative proposals around screening or controlling such investments. It is an honor to speak with the committee today.

Let me clarify from the outset that the views expressed in my testimony today are my own, and do not necessarily reflect the view of my employer, Indiana University, or of the Atlantic Council, where I am a non-resident fellow.

I speak today as someone with both an academic and a government background. I am an associate professor of international studies at the Hamilton Lugar School at Indiana University. My research expertise includes the politics of investment liberalization, investment attraction, and the intersection of national security and investment policy, most notably inbound investment screening.

As a Council on Foreign Relations International Affairs Fellow, I worked as a policy advisor and CFIUS staffer in the Office of Investment Affairs at the Department of State from August 2019 to August 2020.

And, in my capacity as a fellow at the Atlantic Council I have had the distinct pleasure of co-leading a policy working group on outbound investment controls with Emily Kilcrease of the Center for New American Security. Emily and I recently published a policy brief where we lay out our suggestions for how to design an outbound screening mechanism. Much of my comments today draw directly from that co-authored report.

The point of today’s hearing is to take a step back from tactical issues of policy design to instead:

1. lay out the potential national security risks that outbound investment may engender,
2. identify existing gaps in US authorities to adequately address these risks, and
3. develop overarching principles to guide the development of any additional authorities related to outbound investment controls that the USG, including Congress, may pursue.

The central guiding point of my testimony is this: While there are a set of national security risks that some kinds of outbound investments generate, there remains a great deal of **uncertainty** about the **size** of the problem and the **cost** of potential solutions. Given that the openness of the U.S.

economy has been a major driver in our prominent position in the global innovation economy and therefore our national security, any attempt at addressing the risks of outbound investment must equally consider the potential unintended consequences of action. Smart policy will be narrowly scoped to national security, rooted in fact, tailored to the technologies of greatest concern, mindful of the limits of de facto enforcement power, non-duplicative of existing tools, and attuned to the need to act multilaterally. This is not to say that controls are not desirable or feasible, but that any action should be carefully measured.

I want to use the remainder of my time this morning to offer five observations that Congress should keep in mind while contemplating outbound investment controls:

First, there are **gaps** in the United States' ability to address national security risks associated with some kinds of outbound investment. Export controls can stop the flow of U.S. technology to these activities. **But active forms of U.S. investment** – particularly foreign direct investment (FDI) and venture capital (VC) **can provide intangible benefits** to the Chinese firms and industries in which they invest. The United States can cut off all economic activity between U.S. persons and problematic entities through list-based sanctions programs. However, there are reasonable arguments for why narrowly scoped expanded review authorities are necessary to protect national security.

Second, Congress should **resist temptations to use outbound investment screening for purposes other than national security**. The United States has national and economic security interests that intersect, and sometimes conflict, with the outbound investment activities of U.S. multinationals and investors in several respects. To be consistent with a broader and long-standing commitment to market openness, the authority to intervene in an outbound transaction must be limited to a fact-based national security risk assessment, as is the case with inbound investment through the CFIUS process. **It is my assessment that any outbound screen should focus on national security risks associated with indigenous technology development in countries of concern.**

Third, Congress should recognize the **uncertainty** that pervades this issue. Crucially, current data collection on U.S. investment flows to China is not detailed enough to be able to assess the national security implications of *individual* transactions. This is one reason why I advocate for a notification regime to help scope the size of the problem. An Executive Order related to outbound screening is likely a good first step because it allows for more experimentation before committing to a statutory requirement. This mirrors the experience of CFIUS, which was first established through Executive Order in 1975 and gradually became a statutory requirement through a series of amendments to the Defense Production Act, starting in 1988.

Fourth, Congress should not assume that a mirror image of CFIUS will work for outbound screening. The enforcement issues associated with regulating the movement of investment abroad is more challenging to address than regulating inbound flows. In the CFIUS case, a prohibition is enforced by preventing a foreign entity from buying a domestic asset, which is subject to U.S. regulation. For outbound transactions, the United States can impose penalties on the U.S. entity implicated in the transaction. But enforcement options become much less palatable if a multinational decides to channel the otherwise prohibited investment through a third country. It is also easier to compel a U.S. target of a CFIUS review to provide the committee with the sensitive non-public technical information often required to complete a risk analysis. Compelling similar

information revelation from a foreign target in the context of an outbound review will be much harder. The PRC might simply prohibit the transfer of such information.

Congress should be clear-eyed about the compliance and enforcement challenges likely to arise from outbound investment review that are less problematic in the context of inbound review. It should only move forward with a screening concept if it is reasonably sure that it has adequate monitoring and enforcement capabilities to give the regulation teeth.

Finally, Congress should think in network terms when contemplating what technologies to work hardest to protect. An administrable outbound investment review system will need to be relatively narrow in scope. We should avoid a “boiling the ocean” mentality. A broadly scoped review is likely to generate substantial negative consequences for U.S. companies’ competitiveness and capacity to innovate. Congress can narrow its focus while remaining maximally effective by examining technology chokepoints in supply chain networks where U.S. firms currently have the advantage and where process and know-how are central to the production of these technologies. A recent Center for Security and Emerging Technology report mapped China’s technology chokepoints. It found that the technologies for which China has the least domestic capacity tend to be in areas with very high quality control specifications. These kinds of technologies are likely of high national security value, require substantial know-how to perfect, and have outsized follow-on effects to other technologies relevant to U.S. national security. They are good candidates for review.

At the same time, the United States’ ability to leverage its network position depends on China being integrated to some degree into the technology network. Congress should be mindful to not control technology and outward investment so much as to push China out of the network entirely. Take semiconductors as an example. The sanctions alliance against Russia’s invasion of Ukraine has been highly effective at cutting off Russia’s access to advanced semiconductors. As National Security Advisor Sullivan recently stated, this has substantially degraded the Russian military’s capabilities.¹ However, if Chinese entities could fabricate advanced semiconductors without access to U.S. and other alliance members’ technology, we would lose this powerful tool. Right now, many Chinese companies seem to prefer to use U.S. technology rather than invest the capital and time necessary to develop their own solutions. But, if we cut them off from this technology entirely, or if we develop policies that create enough uncertainty about future access, they will have no choice but to develop critical technologies domestically.

Prudent policy must balance the national security imperative to deny countries of concern indigenous capabilities in technology of high national security import, while also avoiding an overly restrictive regime that would inadvertently further push Chinese entities toward self-sufficiency.

U.S. Investment in China

To determine the size of the problem, we must first gather basic facts about how much U.S. investors are active in China, through what vehicles, in what industries and for what purposes. According to surveys of the Bureau of Economic Analysis’s surveys of U.S. Multinational Corporations activities abroad, U.S. companies have accumulated about \$118 billion in foreign direct

¹ <https://www.whitehouse.gov/briefing-room/speeches-remarks/2022/09/16/remarks-by-national-security-advisor-jake-sullivan-at-the-special-competitive-studies-project-global-emerging-technologies-summit/>

investment positions in China.² This equates to about 1.8 percent of all U.S. FDI abroad. For comparison, 61.4 percent of all U.S. FDI abroad is located in Europe. Measurement of U.S. assets abroad, rather than FDI positions, suggest U.S. multinationals have roughly \$779 billion in assets in China.³ U.S. venture capital, which is usually not included in FDI figures, has invested about \$60 billion into Chinese start ups since 2010. To place this figure in context, venture capital activity in the United States over the same period was roughly \$1.28 trillion.⁴

These numbers suggest that U.S. investment in China remains relatively small compared to U.S. investment activity at home and also compared to U.S. investors' activity overseas. Other argue, however, that evaluating the risks of such investment into China also requires attention to trends and to the specific activities to which U.S. investors are contributing. On the first point, all measures of U.S. investor activity suggest direct forms of U.S. investment into China peaked between 2015-2018 and have declined since then. The second point is harder to address given the data that are currently available. Data on sector specific investments provide some relevant information. U.S. investments in theme parks, real estate, and consumer retail are not likely to have substantial deleterious effects on national security. Investments in some information communication technology businesses and activities – which was the sector that received the largest share of U.S. FDI in recent years – could have security implications. But even sectors are too aggregated of a level of analysis to determine national security concerns. For example, investment in an enterprise software company serving the China market and investment in advanced semiconductor research and development likely have very different national security implications.

In other words, whether U.S. investment in China poses national security concerns is best analyzed at the level of transaction, item, or activity rather than by aggregated investment values. And, currently available data do not provide enough insight to adequately judge the potential national security consequences of these investments because they do not provide detailed enough information about the activities of the investment target.

Defining Policy Objectives of a Potential Outbound Screening Mechanism

The United States has national and economic security interests that intersect, and sometimes conflict, with the outbound investment activities of U.S. multinationals and investors in several respects. These include to prevent U.S. capital from supporting firms implicated in China's systemic abuse of human rights, to enhance the resiliency of critical U.S. supply chains, and to address concerns arising from China's indigenous development of technologies relevant to U.S. national security.

At the same time, an open, market-based economy remains a key source of economic and technological strength of the United States. The fungibility of capital and the global mobility of firms limits the ability of unilateral U.S. actions to prevent capital, knowledge, and technological flows to countries of concern. Policy action in this space needs to balance justifiable national security

² See <https://www.bea.gov/sites/default/files/2022-07/dici0722.pdf>

³ Thilo Hanemann, Mark Witzke, Charlie Vest, Lauren Dudley, and Ryan Featherston. 2022. *Two Way Street – An Outbound Investment Screening Regime for the United States?* Rhodium Group. January. pg. 15. Download here: <https://rhg.com/research/tws-outbound/>

⁴ Data from Pitchbook. Download here <https://www.statista.com/statistics/277501/venture-capital-amount-invested-in-the-united-states-since-1995/>.

restrictions with a broad commitment to an open, market-based economy that seeds and sustains technological innovation. Bureaucratically complex and resource-intensive authorities are likely to have negative effects on competitiveness and could encourage the most innovative and productive businesses to relocate to less restrictive jurisdictions. Authorities that are too broad or ambiguous may have the same effect. Additionally, rules that do not have clear enforcement mechanisms for non-compliance will be of limited value.

The United States should limit any outbound control measures to national security – rather than broader economic competition – policy objectives. Furthermore, it should focus attention at the nexus of the most pressing national security concerns and the areas where interventions are most likely to successfully impede the most problematic policy objectives of countries of concern. This entails strengthening existing authorities before creating new ones and finding opportunities to pursue multilateral coordination or action with allies and partners wherever possible. National concerns related to China’s indigenous technology development are those that can be most directly addressed through an outbound investment mechanism and represent a genuine gap in existing authorities. Human rights concerns and issues of supply chain resiliency are best addressed through other measures.

Human Rights

The United States has several existing tools that can be used to address concerns related to the use of U.S. capital or technology in facilitating human rights abuses. First, it can use the Non-Specially Designated Nationals Chinese Military-Industrial Complex Companies List (SN-CMIC) sanctions program to prevent US capital from contributing to Chinese companies operating in the surveillance technology or defense and related materiel sectors. Second, export controls — via the Entity List or other means — can effectively stop the flow of US technology to these activities, especially if the Export Control Reform Act of 2018 (ECRA) is amended to expand a prohibition on U.S. persons from providing support to a “foreign military, security, or intelligence services.”⁵ The Uyghur Forced Labor Prevention Act is another example of authorities Congress and the executive branch can use to address similar concerns.

Supply Chains

Recent legislative efforts have coalesced around supply chain resiliency issues, which is not surprising in the context of Covid-19 and related supply chain disruptions. However, outbound investment screening is a poor tool for addressing supply chain restructuring. Because so much of the U.S. supply chain is already offshore, policies addressing supply chain security must focus on how to move operations already in countries of concern back to the United States or onward to partners and allies. Blocking a proposed outbound investment on reshoring grounds would not provide the company attempting to offshore with the capability to succeed in the United States on commercially viable terms. In other words, screening would only address a symptom rather than the cause of offshoring.

Moreover, using outbound screening to address supply chain resiliency is likely to generate problematic legal issues as well as complicate economic and security cooperation with our partners and allies. Blocking a proposed outbound investment on issues of supply chain resiliency would require either: a) an outbound review mechanism to provide the President with the authority to

⁵ Currently, the ECRA language prohibits US persons from supporting “foreign military intelligence services.” Rep. Malinowski (NJ) has proposed this targeted change in language.

block a transaction for reasons beyond national security, or b) a further expansion of the concept of national security in ways that would damage the United States' reputation as an excellent place to start and grow innovative companies.

Expanding blocking rationale beyond national security would likely invite increased litigation from U.S. firms subject to an investment prohibition. CFIUS largely avoids such litigation because courts provide the President with substantial deference in the area of national security. Prohibitions on other grounds will likely be easier to challenge in court, and could create lengthy and costly legal battles that would increase regulatory uncertainty, thereby reducing the United States' status as one of the most desirable places to do business.

Further expanding the concept of national security also has important negative consequences. The first has to do with perceived legitimacy of U.S. government action. While the public and industry mostly recognize the right of the U.S. Government to intervene in market activity that generates clear risks to national security, this support rests on common understandings of what is a reasonable claim to national security. Overuse of national security rationales to justify government intervention into private sector transactions decreases the public's trust in the reasonableness of these claims. Eroding trust could lead to reduced voluntary compliance with the law, more creative work-around solutions, and a U.S. public that is increasingly skeptical of U.S. actions in the area of national security and economic policy.

Whatever the United States does with respect to outbound screening, we should be prepared for other countries to develop similar authorities. Outbound mechanisms focused on supply chain structures as an essential security issue and/or an economic resiliency issue that warrants prohibitory intervention could be used among our European allies and others in ways that would create substantial harm to U.S. interests, including by making it harder to develop more redundancy and multiple suppliers in critical supply chains through increased ties with allies' economies.

Establishing more resilient supply chains requires an affirmative industrial policy that addresses the root economic causes of offshoring of critical capabilities long before a company enters an offshoring transaction and that makes reshoring production commercially viable. In this regard, the incentives and other "run faster" provisions of the CHIPS and Science Act of 2022 are an excellent start. Attempts to reshape supply chains must also consider how to do so without creating additional negative supply shocks. These considerations are particularly important in the current context of high inflation that has been largely driven by supply-side shocks.

Impeding Chinese Indigenous Technology Development

Concerns over how U.S. technology and investment can support indigenous technology development in China was central to the policy discussion surrounding the 2018 reforms of CFIUS and export control authorities, through the Foreign Investment Risk Review Modernization Act (FIRRMA) and ECRA. The initial draft of FIRRMA provided CFIUS with review authority over outbound investments. Some lawmakers were especially worried that the PRC was benefitting from critical technology transfer from U.S. firms to Chinese counterparts through joint ventures. After substantial debate, Congress found a compromise in which CFIUS would remain focused on inbound – though it does have jurisdiction over some forms of outbound joint ventures – while national security concerns related to outbound investment would be regulated through expanded export control authorities.

The gap in this approach is that there are ways in which the participation of U.S. multinationals and investors in China's innovation economy can harm U.S. interests through channels other than technology transfer. Decades of research on the role of foreign direct investment in development has shown that inward FDI, particularly when paired with active host country regulatory strategies, can help FDI-receiving countries expand domestic markets and move up the value chain.⁶ Multinational corporations and their affiliates make up 36 percent of global output and are responsible for two-thirds of exports and one-half of imports.⁷ Domestic firms participate in global supply chains largely through incorporation into MNCs supply chain. For instance, MNCs operating in the United States source 25 percent of their inputs domestically. MNCs in Japan source over 50 percent of inputs domestically. The more domestic firms interact with MNCs, the more they learn from those MNC, including how to increase their production capabilities. By interacting with MNCs, domestic firms gain foreign market knowledge to directly compete in international markets. Domestic firms that integrate into MNCs' supply chains are statistically significantly more likely to become exporters, increase their ability to supply the domestic market, and produce higher quality and more complex products. Normally, we view all of these spillover effects of FDI as beneficial to economic development. However, in narrow cases related to specific critical technologies relevant to national security, the linkages literature provides insight into how U.S. MNCs can help develop Chinese critical industries. The issue goes beyond technology transfer. MNCs help foster indigenous industries by incorporating local firms into their supply chains and by importing knowledge about international markets, connections to MNCs' broader supplier and buyer networks, and other managerial practices that increase efficiency and quality control. These, less tangible, contributions to the domestic market are not able to be controlled through export controls.

In the realm of U.S. venture capital (VC), there are also potential concerns that are not addressable through export controls. As the National Venture Capital Association (NVCA) lays out in their 2022 Yearbook, venture is distinct from other types of investing because it typically entails relatively small equity stakes in a company, but the general partner in the investment is much more involved in strategic management decisions of the target than passive investors are.⁸ VCs provide more than an infusion of capital; they mentor and advise founders who often need substantial strategic and logistical help to scale up their business. They often play prominent roles on corporate boards. Moreover, they provide founders and their teams with access to the investors' financial, commercial, professional, and political networks. By investing in a company, VCs are putting their seal of approval on the enterprise, signaling that the company was able to pass a thorough vetting process. And, when VCs invest in a company, they are tying their financial future to the company. It is in a VC's interest to crowd in more investors into future funding rounds so that the companies in which

⁶ The research on horizontal and vertical spillovers from inward FDI is vast. See, in particular: Christine Zhenwei Qiang, Yan Liu, and Victor Steenbergen. 2021. *An Investment Perspective on Global Value Chains*. Washington, D.C: The World Bank Group; Tomas Havranek and Zuzana Irsova. 2011. "Estimating Vertical Spillovers from FDI: Why Results Vary and What the True Effect is." *Journal of International Economics* 85: 234–44. Zuzana Irsova and Tomas Havranek. 2013. "Determinants of Horizontal Spillovers from FDI: Evidence from a Large Meta-Analysis." *World Development* 42: 1–15; Sonal S. Pandya. 2016. "Political Economy of Foreign Direct Investment: Globalized Production in the Twenty-First Century," *Annual Review of Political Science* 19:455-475; Sarah Bauerle Danzman. 2019. *Merging Interests: When Domestic Firms Shape FDI Policy*. Cambridge University Press.

⁷ The figures in this paragraph come from Qiang, Liu, and Steenbergen. 2021. "An Investment Perspective on Global Value Chains," *The World Bank Group*. See especially pp 8, 10-13.

⁸ National Venture Capital Association. 2022. *NVCA 2022 Yearbook*. <https://nvca.org/wp-content/uploads/2022/03/NVCA-2022-Yearbook-Final.pdf> p. 10

they invested increase in value in each funding round, which ultimately leads to an acquisition or initial public offering through which the VC can exit the investment, hopefully at great profit.

Venture Capital plays a critical role in the continued dynamism of the U.S. innovation economy. From 1974-2015, 42 percent of U.S. companies that went public were venture backed.⁹ These 556 companies accounted for 63 percent of the market capitalization of the 1,339 U.S. companies that went public over the period and 85 percent of all the research and development expenditures associated with those companies. The flip side, however, is that these same features that have been so central to the journey from start up to commercial viability in the United States could generate national security risks if U.S. VC contributes to critical technology start-ups in countries of concern. Similarly, to the intangible benefits of FDI described above, export controls do not provide an adequate remedy to these kinds of national security concerns.

Approaching Outbound Controls

As the Congress moves forward with an outbound screening concept tailored to issues of the national security risk of indigenous technology development in countries of concern, it should: 1) be mindful of dynamics that make outbound investment screening harder to enforce than inbound review, 2) measure potential tools against five principles of good design, and 3) follow a strategy that leverages the United States' privileged position in many technology supply chain networks.

Enforcing Outbound Screening

The conversation around outbound screening is colored by the United States experience with inbound review. CFIUS is widely seen as well-designed and effective and Congress should be careful to not overlearn from the CFIUS example. It is much easier from an enforcement perspective to control market access than to limit outflows. In the CFIUS case, a prohibition is enforced by preventing a foreign entity from buying a domestic asset, which is subject to U.S. regulation. For outbound transactions, the United States can impose penalties on the domestic entity implicated in the transaction. But enforcement options become much less palatable if a multinational decides to channel the otherwise prohibited investment through a third country. Enforcing a prohibition in that case would likely require substantial extraterritorial reach that the U.S. government will likely wish to avoid due to issues of proportionality and allies' and partners' sensitivities.

Other aspects of administration and enforcement are much easier for inbound investment than for outbound. For instance, it is easier to compel a U.S. target of a CFIUS review to provide the committee with the sensitive non-public technical information often required to complete their review than it would be to compel the same information from a foreign target in the context of an outbound review. Indeed, other country government may simply prevent the foreign target from providing such information. Additionally, in the case of mitigation agreements, it is reasonable to assume it is much easier for the U.S. Government to monitor behavior of firms in own jurisdiction than firms overseas.

For these reasons, Congress should be clear-eyed about the compliance and enforcement challenges likely to arise from outbound investment review that are less problematic in the context of inbound

⁹ Will Gornall and Ilya A. Strebulaev. 2015. "The Economic Impact of Venture Capital: Evidence from Public Companies." Stanford University Graduate School of Business Research Paper No. 15-55. Available at SSRN: <https://ssrn.com/abstract=2681841> or <http://dx.doi.org/10.2139/ssrn.2681841>

review. Congress should only move forward with a screening concept if it is reasonably sure that it has adequate monitoring and enforcement capabilities to give the regulation teeth.

Design Principles

Along with having enforcement capabilities strong enough to deter, Congress should consider the following principles when designing a screening tool

1. Review should be targeted to **transactions that present the highest national security threat** and any governmental action should be subject to a **national security risk assessment**. As with CFIUS, an outbound mechanism should be narrowly tailored to national security risks rather than a tool to bolster broader economic competitiveness objectives. Congress should instead pursue issues of competitiveness and social standards through affirmative industrial policy such as the CHIPS and Science Act and through trade and investment frameworks such as the Indo Pacific Economic Framework (IPEF).
2. A review mechanism along with any additional outbound controls should be **clearly defined and understandable to private-sector participants**. This includes clear definitions of what types of investors and economic activities are covered. The private sector will be responsible for the first line of compliance, so they must understand to what they are obligated. For the regulation to be seen as a legitimate use of the government's regulatory authority, its purpose and necessity must be explainable to the American public. Without public support, firms will not face substantial reputational costs for evading the spirit or the letter of the regulation. A supportive public is key to regulatory compliance.
3. Any review should be **non-duplicative of existing tools** such as export controls. In the context of inbound transactions, CFIUS is designed as **a tool of last resort**. Any outbound investment screen should be thought of similarly and any use of outbound authorities should occur only when other authorities are insufficient to address the national security risk that arises from the transaction in question.
4. Any review mechanism must be **scoped proportionately to the government's institutional capacity** to effectively administer a new mechanism. We should not take lightly the administrative burden that a well-functioning outbound review process would place on the executive branch. For example, CFIUS requires hundreds of staff and attention across its nine member agencies plus ex officio and support agencies. FIRRMA appropriated \$20 million a year for five years to help build up CFIUS agencies to support the expansion of its authorities.
5. Finally, **any Congressional action on outbound screening should be paired with meaningful multilateral engagement** with allies and partners so that U.S. investors are not disadvantaged and so the goal of impeding national security relevant indigenous technology development in countries of concern is more likely to be met. Similar to export controls and inbound screening, outbound investment controls are more likely to be effective if large portions of the global economy implement similar measures. This is especially important in the context of outbound investment where there is justifiable concern that a U.S. outbound mechanism without coordination with other advanced economies could just lead to MNCs from other OECD countries occupying the investments that U.S. firms otherwise would have participated in. Similarly, multilateral engagement is important in the context of critical technologies, as the United States is not the only relevant member of these supply chains.

Leveraging the U.S. Network Position

As a final conceptual point, I encourage Congress to think in network terms as much as possible when contemplating any outbound investment control mechanisms. Even before the Covid-19 pandemic, scholars of International Relations started to borrow from complexity science to understand on the structure of different kinds of global networks generate power and vulnerabilities. The United States has effectively leveraged its central position in currency and finance networks to extend its power in important ways. Even now, we see how this centrality has imbued the United States with regulatory power over companies that wish to list on U.S.-based exchanges.

As the Congress shifts from conceptual issues to more tactical and technical concerns related to coverage and definitions, I encourage it to use insights from complexity science to design its mechanism. This entails focusing attention on chokepoint technologies as much as possible. Rather than trying to “boil the ocean” and cover all technologies possible, it will likely be more effective for the U.S. to evaluate what specific technologies are especially critical to a host of other technologies. For instance, it may be particularly challenging to cover all manner of Artificial Intelligence technologies. However, limiting investment in specific extreme ultraviolet lithography tools and technology as well as most likely candidates for the next next-generation lithography may be more feasible. To the extent that advanced AI relies on advanced semiconductors, controls on NGL will have spillover implications for AI as well.

As another example, the Center for Security and Emerging Technology recently published a report evaluating “China’s Self-Identified Strategic Technology Import Dependencies.”¹⁰ It found that China’s chokepoints tend to be in technologies with very high-quality control specifications including precision requirements, consistency requirements, and the ability to perform under stress. Focusing attention on these areas — or more broadly, areas that the Chinese self-identify as chokepoints — would likely be particularly because these chokepoints relate to production process issues rather than the underlying technologies. Additionally, research on information problems in authoritarian contexts suggest that achieving high levels of quality control will likely remain a challenge for Chinese companies so long as delivering bad news is politically dangerous. This suggests not only that the PRC currently faces disadvantages in these chokepoint technologies, but also that the United States’ open, democratic system provides us with a clear competitive edge in these areas. This is an important reminder that the United States’ leadership position in advanced technology and economic dynamism is a function of our open, non-arbitrary, rules-based system. To best protect our national security, we should confidently embrace those core principles that have fueled our economic prosperity rather than erect overly complicated bureaucratic structures that emulate competitors’ systems.

Conclusion

I close my testimony where I began. Outbound investment creates a range of policy issues that Congress may want to address. The issue is which issues warrant a policy response and, of those, what policy response, or combination of policy responses, is most likely to produce outcomes that strengthen U.S. national security.

I recommend that Congress consider five issues while contemplating the path forward:

¹⁰ Ben Murphy. 2022. *Chokepoints: China’s Self-Identified Strategic Technology Import Dependencies*. Center for Security and Emerging Technology. Available here: <https://cset.georgetown.edu/publication/chokepoints/>

First, the gaps that currently exist in the government's authorities relate to the ability to control the intangible benefits associated with outbound FDI and VC flows. Export controls already provide authority over technology transfer. Policy solutions will need to address the components of investment that generate risks through managerial expertise, transfer of know-how, connection with supplier and buyer networks, and the legitimation effects of partnering with a U.S. investor.

Second, any outbound investment review mechanisms should be narrowly focused on national security rather than broader policy objectives. Issues of economic competitiveness are best addressed through other tools.

Third, outbound investment screening would be a new authority and represent a substantial break from central tenets of decades of U.S. economic policy. There is a great deal of uncertainty about the size of the problem and the potential negative unintended consequences of outbound review. An approach that is designed to gather more information as well as allow for experimentation is likely to work better than enacting a broad statutory screening requirement all at once.

Fourth, Congress should not assume that a mirror image of CFIUS will work for outbound screening. The enforcement issues associated with regulating the movement of investment abroad is in many ways more challenging to address than regulating inbound flows. Congress should make sure that any mechanism be narrowly scoped to national security, clearly defined and seen as a legitimate use of government authorities, non-duplicative of existing tools, administrable, and paired with meaningful multilateral engagement on the issue with allies and partners.

Finally, smart policy will take cues from networks and complexity science. Clamping down on all outbound investment to countries of concern is not a viable option. By focusing on chokepoint technologies, the United States can scope coverage in a way that is most impactful with the least amount of negative economic consequences.