To Legislate or to Arbitrate: An Analysis of U.S. Foreign Investment Policy After FINSA and the Benefits of International Arbitration

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Rarely in U.S. history has a single business transaction caused as much of an uproar as the sale of the British company, Peninsular and Oriental Steam Navigation Company ("P&O"), to Dubai Ports World ("DPW"), "a state-owned company located in the United Arab Emirates." The proposed sale would have theoretically placed several U.S. seaports under the direct control of the government of Dubai. When word of this transaction spread from the media airwaves to the halls of Congress, it is perhaps not surprising that the reaction from the American public was almost universal outrage.

Senator Charles Schumer argued, "[The Committee on Foreign Investment in the U.S.] has proven itself unreliable and in matters of national security, the buck stops at the President who should step in now to protect our ports."

Senator Frank Lautenberg warned, "Dubai has allowed terrorists to pass freely through their own country. Why in the world should we let this rogue government control ports in the United States?"

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4 Id.
House Representative Chris Shays opined,

Our ports are a welcome mat for terrorists trying to bring weapons of mass destruction into the United States..I am eager to understand why the Committee on Foreign Investment in the United States approved the sale, handing over several key ports to a company based in the United Arab Emirates, and ensure it is thoroughly inspected and investigated.5

While this controversy provided great fodder for talk radio and internet bloggers, politicians jockeyed to see who could appear the strongest on national security issues. Suddenly, the once unknown Committee on Foreign Investment in the United States ("CFIUS") and the entire process by which foreign investment in the U.S. is vetted and approved became a topic of conversation. Everyone wanted to weigh in on this debate, particularly Congress. To address the apparent shortcomings of CFIUS and the official U.S. policy towards foreign investment, Congress passed the Foreign Investment and National Security Act of 2007 ("FINSA").6

This comment examines the recent changes to U.S. foreign investment policy and the practicality of an international arbitral system to better balance the commercial needs of investors with the security needs of the host nation. Part I of this note describes a history of CFIUS and previous amendments that have reshaped the foreign investment landscape in the U.S. Part II discusses the changes implemented in FINSA and their application to future investment transactions. Part III examines the rise of International Commercial Arbitration and the institutions that currently practice it. Part IV analyzes the viability of an international body to arbitrate and decide investment disputes, particularly those relating to sensitive national security issues.

PART I. A HISTORY OF FOREIGN INVESTMENT REGULATION IN THE U.S.

The United States receives the most foreign investment of any country in the world and is also the world’s largest foreign investor.7 American presidents, over the years, have taken various positions on the issue of foreign direct investment and how the government should control it. Nevertheless, the U.S. is generally viewed as among the world’s most welcoming nations to

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foreign investors. The position of the Carter Administration in 1977 was that the U.S. "will neither encourage nor discourage the inflow or outflow of international investment," because such government interference could lead to retaliatory measures from other nations. A decade and a half later, President George H.W. Bush reaffirmed the United States policy of free and open foreign investment and assured all that his administration is, "aggressively seeking to open markets abroad."  

A. The Creation of CFIUS

In May 1975, President Gerald Ford established CFIUS under executive order. The committee initially consisted of representatives from the State, Treasury, Defense and Commerce Departments, as well as a member appointed by the President's Assistant for Economic Affairs. CFIUS was charged with gathering and reviewing information on proposed transactions in confidence and reporting to the President those investments which, "might have major implications for United States national interests." The Secretary of Treasury was designated chair of the committee and was granted the power to solicit assistance from other departments and agencies, as needed, during the course of an investigation. In 2003, Executive Order 13286 added the Department of Homeland Security to the list of departments comprising CFIUS.

Although CFIUS was given the task of monitoring foreign investment, the committee in its early stages lacked the necessary power to effectively intervene and prohibit a potentially troublesome investment from taking place. This changed with the passage of the Exon-Florio Amendment to the Omnibus Trade and Competitiveness Act of 1988, which provided some much-needed guidelines for CFIUS. Such guidelines included a mandated heightened scrutiny for foreign investments in U.S. defense companies and by nations who

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8 Id.
9 Id. at CRS3.
12 Id.
14 Id.
are on a State Department list for supporting terrorism. Exon-Florio established a formal process for foreign investors by which one of the parties to the transaction voluntarily notifies CFIUS of the terms and conditions, followed by a 30-day review by CFIUS to determine whether any security risks are involved. If, after this initial review, CFIUS determines that there could be security concerns, an additional 45-day investigation ensues ending with a Presidential decision on the matter. It is worth pointing out that under Exon-Florio, notifying CFIUS was entirely voluntary. However, failure to notify CFIUS before a transaction occurs gives the President and CFIUS the ability to still intervene after the fact, and any decision made will be enforced retroactively.

Four years after Exon-Florio, the Byrd Amendment gave CFIUS even more enforcement power and continued to affect the process by which foreign investment is vetted in the U.S. The Byrd Amendment required a formal CFIUS investigation, “in any instance in which an entity controlled by or acting on behalf of a foreign government seeks to engage in any merger, acquisition, or takeover which could result in control of a person engaged in interstate commerce in the United States that could affect the national security of the United States.” This replaced the voluntary notification by the parties only in these specific instances of foreign government control. Additionally, the Byrd Amendment threw Congress into the mix by requiring the President to issue a report to Congress whenever a decision is made regarding a foreign investment.

After Congress passed the Byrd Amendment, President Bill Clinton signed an Executive Order expanding CFIUS membership by adding the Director of the Office of Science and Technology Policy, the Assistant to the President for National Security Affairs, and the Assistant to the President for Economic Policy. The addition of these members to CFIUS reflects the increase in the level of sophistication and specialization required to accurately assess foreign investment transactions.

Despite the evolution of power given to CFIUS, prior to 2005 only one...

18 Id.
19 See Sud, supra note 19, at 1316.
21 See Sud, supra note 19, at 1316.
transaction had been blocked by the committee from going forward. In reality, "this provision for Presidential review has been, like much of CFIUS, more of a formality than an actual bar to cross-border transactions." However, critics argue that CFIUS, in fact, plays a much more important role. As explained by Joseph D. West, Chair of the Government and Commercial Contracts Practice for the law firm Gibson, Dunn & Crutcher, "[a]lthough the CFIUS process has only once resulted in the President prohibiting a transaction, this statistic is quite deceptive. A number of proposed transactions have been abandoned or significantly restructured after initial CFIUS scrutiny signaled that approval was unlikely." Therefore, the fact that foreign corporations and governments are withdrawing their bids before CFIUS can make its recommendation indicates a strong unwillingness on the part of many foreign investors to subject themselves to this intense review process. As a result, the U.S. could very well be missing out on lucrative contract deals with foreign investors.

Although rarely invoked in economic situations, the President has another mechanism to prevent foreign direct investment other than through CFIUS. The International Emergency Economic Powers Act, enacted under President Carter, gives the President the authority to block an economic transaction by declaring a national emergency. The act gives the President the right to prevent, "any unusual and extraordinary threat, which has its source in whole or substantial part outside the United States, to the national security, foreign policy, or economy of the United States, if the President declares a national emergency with respect to such threat." Declaring a national emergency in response to a proposed economic transaction is clearly a dramatic move and to date presidents have been hesitant to go to that extreme in these instances. By contrast, presidential intervention through CFIUS is more discrete and therefore less likely to be scrutinized by Congress or the media.

B. Recent Investor Controversies and Their Impact on the Political Environment

Prior to 2006, when the DPW deal sprung into the public sphere, few Americans outside of Washington knew what CFIUS was or what role it played. However, DPW was not the first time in recent history that a controversy has brewed regarding a foreign takeover. In 2005, China National Offshore

27 See Sud, supra note 19, at 1317.
28 See Sud, supra note 19, at 1317.
31 Id.
Petroleum Company, Ltd. ("CNOOC"), a state-owned oil company, withdrew its $18.5 billion all cash bid for American Unocal in response to strong political pressure from Washington. As CFIUS’ investigation was proceeding, members of Congress wasted no time in proposing legislation that would undermine the transaction in the event CFIUS approved the sale. CNOOC even cites this political pressure as a significant reason for withdrawing its bid, stating that, “[t]he unprecedented political opposition that followed the announcement of our proposed transaction, attempting to replace or amend the CFIUS process that has been successfully in operation for decades, was regrettable and unjustified.”

Supporters of the review process in place at the time of the DPW and CNOOC controversies often cite CFIUS’ insulation from the political process as one of its key strengths “because it intentionally lies out of the reach of Congress.” Unlike legislators who depend on votes from their constituents to stay in power, members of CFIUS are Presidential appointees from various departments and are arguably less susceptible to influence by the politics of the day. Free from such political constraints, CFIUS is more likely to base its decisions on sober analysis rather than political hype. However, as seen in these recent controversies, even CFIUS is not entirely free from legislative influence and the process of foreign investment as a whole continues to be dominated by political interests in Congress. Additionally troubling is the fact that Congressional disapproval over DPW and CNOOC was not entirely based on national security concerns. There is evidence to suggest that the controversies sparked a return to the Cold War standard of “national and economic security.”

A year after the DPW controversy, another Dubai company, Dubai Aerospace Enterprise ("DAE"), raised eyebrows when it acquired two American companies, Standard Aero and Landmark Aviation from The Carlyle Group. After witnessing what happened with DPW, DAE took no chances and immediately hired a lobbyist and PR consultants in anticipation of strong skepticism coming from Congress and the public at large. DAE’s actions

34 See Press Release, CNOOC Ltd., supra note 32.
35 See Sud, supra note 19 at 1320.
36 See Mostaghel, supra note 16, at 608.
38 Kevin Bogardus, Lobbyists helping Dubai company to seal $1.8 billion deal, THE HILL, June 7, 2007.
were significant because they reflected a change in how foreign investors deal with the U.S. regulatory process. Particularly, these changes were indicative of Congress’ increasing role in reviewing these investment matters which have traditionally been under the sole jurisdiction of the President and the agencies comprising CFIUS. Recent acts of Congress have made this trend more likely to continue as the process by which foreign investors are vetted becomes increasingly carried out in the public sphere.

PART II. FOREIGN INVESTMENT AND NATIONAL SECURITY ACT OF 2007

The rising tensions in the aftermath of the DPW and CNOOC controversies sent ripples through Washington. Congressional members of both parties saw this as an opportunity to flex their power on issues involving foreign investment and national security. Almost immediately, Congress proposed legislation aimed at formalizing and streamlining the process by which foreign direct investment comes into the United States. Congress was eager to point out the failures of DPW and CNOOC and blamed those scandals on the lack of active involvement by the legislative branch. In her testimony before the House Subcommittee on Transportation Security and Infrastructure Protection, Rep. Sheila Jackson Lee described the proposed legislation as increasing “the role of congressional oversight by requiring greater reporting by CFIUS on its actions and allowing for a greater amount of detailed information about CFIUS’ operations.”

Congressional oversight of foreign investment is hardly a new concept or idea. The authority to regulate trade with foreign countries is one of Congress’ plenary powers. The Commerce Clause in the U.S. Constitution gives Congress the broad authority to regulate commerce and trade between the states and foreign governments. Courts have long recognized Congress’ power to legislate on these issues. In *Tyson Foods, Inc. v. McReynolds*, the Sixth Circuit Court of Appeals held that, “[t]he control of takeovers of and foreign investments in broadly based national corporations of the United States is clearly a duty of Congress and not the individual states.” Since foreign direct investment is a function of trade, Congress has a legitimate argument that it should have a say on issues such as these. However, the appropriate method

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40 Id.
41 Id.
43 Id.
of Congressional involvement remains the subject of much debate.

Scholars are quick to point out, however, that increased Congressional regulations and oversight on this issue comes with the potential and likely risk of deterring foreign direct investment. The problem, therefore, is not that the current CFIUS system is broken, but rather that the process lacks the necessary confidence from Congress and the American public. Some have asserted that "the existing regime has been successful in maintaining the primacy of traditional U.S. open investment policy without compromising national security. The DPW and Smartmatic deals nonetheless reveal a central problem with the existing paradigm: the lack of public and congressional confidence that CFIUS has conducted an effective review." As Congress debated statutory changes to the foreign investment review process, their actions were making a direct impact on CFIUS. Analysts note that in the aftermath of DPW, CFIUS has taken a markedly more cautious role in their investigations. This, in turn, caused more investors to preemptively file for CFIUS review in the anticipation of heightened analysis. CFIUS filings in 2006 were up 73 percent over 2005 and withdrawals were up 150 percent for the same time period. It is worth noting, however, that along with these increases in CFIUS filings, there is no evidence to suggest that any more risky investments from a national security standpoint are taking place.

Therefore, it stands to reason that the real effect of DPW is that CFIUS must now waste its time and resources on investigating more transactions when there appears to be no increase in the number of potential risks. As a result, "this forces CFIUS and the intelligence agencies to conduct a full analysis of inconsequential transactions, taking their focus off the transactions that really matter to national security." Perhaps more importantly, this new environment has a chilling effect

46 Smartmatic, a voting machine company with ties to the Venezuelan government made headlines in 2006 when it invested in American-owned Sequoia Voting Systems. Smartmatic initially refused to undergo CFIUS review but later withdrew and divested its interest in Sequoia. The deal caused suspicion among Congress due to America's strong concern over voter irregularity in elections. See Haley, supra note 45, at 1158.
48 Id.
50 Id.
51 Id.
52 Id.
53 Id.
on foreign direct investment by creating uncertainty in the eyes of investors.54 A large part of this uncertainty was caused by the inability of government to define what “critical infrastructure” means so that foreign investors may be able to accurately predict what kind of scrutiny they are subjecting themselves to by investing in the U.S.55 Without such guidelines, investment advisors will recommend that their clients proceed cautiously when investing in the U.S., causing many unnecessary filings with CFIUS.56 Skeptics of the new legislation argue that, “[t]he Administration and Congress should work together to determine how best to protect critical infrastructure, regardless of who owns a particular company or asset. Security policies and guidance could be developed on a sector-by-sector basis.”57 Once clear definitions of what constitutes “critical infrastructure” are in place, foreign investors will be better able to assess the costs and benefits of investing in the U.S., even if it means undergoing a complete review by CFIUS.

In addition to causing uncertainty among foreign investors, the lack of a coherent foreign investment procedure can have far-reaching effects on the U.S. economy as a whole. Statistics provided by the U.S. Treasury Department indicate that in 2005, foreign companies employed at least 5 million American workers, accounting for 4.5% of the private sector employment.58 Clearly, foreign direct investment has a very real impact on the U.S. economy.

After months of debate in Congress and the American media, The Foreign Investment and National Security Act of 2007 (“FINSA”), was passed and signed into law by President George W. Bush.59 Effective October 24, 2007, the act makes significant changes to CFIUS and the process by which foreign companies may invest domestically. The new law adds statutory authority to many of the procedures previously followed by CFIUS.60 For instance, FINSA formally recognizes CFIUS’ membership to include representatives from the Treasury, Homeland Security, Defense, and Commerce Departments as well as the Attorney General.61 The Director of National Security is also added in a non-voting role.62 FINSA authorizes the Secretary of Treasury to designate a lead agency during the review process in which the agency will be directly responsible for enforcing and mitigating security

54 Id.
55 Id.
56 Id.
57 Id.
60 Id.
61 Id.
62 Id.
issues.\textsuperscript{63} This flexibility allows CFIUS to adapt to various security situations and to appoint the most appropriate agency to review these issues as they arise. In theory, this lead agency will be most capable of analyzing any potential security risks and conveying the risk to the other members.

In addition to providing more flexibility for the way in which CFIUS designates roles internally, FINSA provides some clear procedural standards for the entire review process. For instance, CFIUS is now required to investigate any proposed investment by a foreign government (or an entity controlled by a foreign government) unless the initial review from the committee or the designated lead agency determines that no national security risks will arise.\textsuperscript{64}

FINSA attempts to correct some of the uncertainties for foreign direct investors following the DPW controversy. The law makes it clear that tougher review standards are in place and that even previously approved transactions are subject to further review by CFIUS.\textsuperscript{65} If any foreign investor is suspected of breaching a national security agreement or has failed to timely notify CFIUS of any changes in status, CFIUS now has the authority to re-evaluate the transaction and take appropriate action.\textsuperscript{66} Furthermore, CFIUS and its agencies have the statutory authority to enforce national security agreements against violators.\textsuperscript{67}

Another significant provision of FINSA is the power it vests in either CFIUS or the President to consider other factors in its review process including a foreign government’s adherence to nuclear nonproliferation and cooperation with U.S. anti-terrorism measures.\textsuperscript{68} These additional factors are not meant to be exclusive and CFIUS or the President maintains the authority to consider additional factors as well.\textsuperscript{69} An obvious side-effect of this statutory requirement is that foreign governments may not want to draw attention to their anti-terrorism efforts and subject themselves to comparison to the U.S. on these sensitive issues.

FINSA attempts to alleviate some of the uncertainty regarding which industries will be subject to the highest level of scrutiny by CFIUS. FINSA defines “critical infrastructure” as those “systems and assets . . . so vital to the United States that the incapacity or destruction of such systems or assets would

\textsuperscript{63} Id.
\textsuperscript{64} 50 app U.S.C.A. §2170, supra note 6, at §(b)(2)(D)(i) “an investigation of a foreign government-controlled transaction . . . or a transaction involving critical infrastructure . . . shall not be required under this paragraph, if the Secretary of the Treasury and the head of the lead agency jointly determine, on the basis of the review of the . . . that the transaction will not impair the national security of the United States.”
\textsuperscript{65} Id.
\textsuperscript{66} Id.
\textsuperscript{67} Id.
\textsuperscript{68} Id.
\textsuperscript{69} Id.
have a debilitating impact on national security." Critical technologies are defined as, "items essential to national defense." While these definitions may provide some minor clarity for foreign investors, it is unlikely that they will significantly lessen the ambiguity that still exists. For instance, investors must still predict which infrastructure and technologies are "essential" to security or national defense. This leaves many foreign investors having to roll the dice to see whether their proposed transaction will raise any red flags. As previously discussed, this in turn leads to unnecessary filings with the CFIUS and raises the costs associated with it.

When determining which industries are critical, FINSA authorizes the President to take into account the levels of domestic production that are necessary for defense purposes, the domestic capability to meet those levels of production, and whether foreign control could negatively impact U.S. capability of reaching those levels. While these guidelines are helpful to the President, they do little to ease the burden on foreign investors. Despite intense market research, foreign investors may not be capable of determining U.S. production capacity and FINSA leaves them guessing whether their transaction will really effect domestic production in the U.S.

Unlike Exon-Florio and previous litigation, FINSA specifically provides for the continued monitoring of risks by CFIUS and its lead agency. Under the statute,

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\text{[t]he lead agency shall negotiate, modify, monitor, and enforce, on behalf of the Committee, any agreement entered into or condition imposed under paragraph (1) with respect to a covered transaction, based on the expertise with and knowledge of the issues related to such transaction on the part of the designated department or agency.}
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This provision bolsters CFIUS' enforcement capabilities by allowing the committee to ensure compliance even after it approves a transaction. Therefore, FINSA puts investors on notice that they can be monitored indefinitely by CFIUS as the committee's lead agency sees fit.

A particularly important feature of FINSA is its ability to mitigate potential security risks without having to block the entire transaction.

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70 50 app U.S.C.A. §2170 (a) (6).
71 50 app U.S.C.A. §2170 (a) (7).
72 See supra notes 52 – 57.
75 Id. §(b)(3)(A).
76 Jonathan C. Stagg, Scrutinizing Foreign Investment: How Much Congressional Involvement is...
Supporters argue that this flexibility helps investors by fostering a more open investment policy. In other words, "[t]his change assures foreign investors that any potential security concerns can be dealt with through agreements or conditions, and it will not necessarily lead to CFIUS blocking the deal." However, certain transactions will never even reach the mitigation stage because many investors will withdraw their bid once it appears that conditions will be placed on the transaction. Furthermore, the take-it-or-leave-it approach to mitigation does nothing to ensure that the restrictions or conditions placed on investors are reasonable. While the ability to mitigate can be helpful to some investors, it leaves others burdened with arbitrary restrictions and little or no avenue for redress.

Perhaps the most significant provision of FINSA is its requirement that CFIUS report its findings directly to Congress. As we witnessed in the DPW and CNOOC controversies, Congressional involvement can undermine CFIUS' investigation by politicizing the entire process. Members of Congress may exploit potential foreign transactions for political gain in an attempt to appear strong on issues of national security. As a result, Congressional involvement and its inevitable politicking can have serious consequences for investors and the public at large. For instance, there is a high potential for "political mischief" since members of Congress must answer to their U.S. constituents who may object to a proposed transaction for reasons other than national security. This pressure from constituents might compel members of Congress to reject a proposed transaction for these illegitimate reasons. For example, a Senator from a heavily agricultural state may object to a foreign competitor relocating in the U.S. because of the negative economic impact it would have on the Senator's constituents. Furthermore, the recent corruption scandals plaguing Congress, particularly those involving gifts from lobbyists, highlights this potential risk.

Another negative consequence of FINSA's Congressional involvement stems from the risks associated with the disclosure of sensitive information. Under FINSA, CFIUS briefings can be provided not only to members of Congress, but also to their Congressional staff who possess the appropriate

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77 Id. at 349.
78 Id.
79 50 app U.S.C.A. §2170 (a)(g)(1) "The Committee shall, upon request from any Member of Congress ... promptly provide briefings on a covered transaction ... or on compliance with a mitigation agreement or condition imposed with respect to such transaction"
80 See Stagg, supra note 76, at 354.
82 See Stagg, supra note 76, at 354.
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security clearance. This obviously opens the door to a huge array of people who could potentially have access to highly sensitive information. The thought of such a large number of people obtaining confidential information on a proposed financial transaction is enough to prevent many foreign investors from agreeing to go through with the process. Accordingly, "[t]his realization will cause many investors to opt out of investing in the United States when comparable investments present themselves in countries without such risky disclosure requirements."  

Perhaps the most troubling aspect of Congressional involvement is the potential for compromising U.S. intelligence and national security efforts. For instance, in its Congressional briefing, CFIUS may be forced to disclose the fact that a transaction was blocked because of top secret information gained from U.S. intelligence services. This disclosure could potentially involve methods and capabilities of U.S. intelligence, causing disastrous consequences for that agency. Furthermore, information that an investor's country is engaging in behavior to which the U.S. objects can cause tension between the countries if that information is ever leaked.  

PART III. THE RISE OF INTERNATIONAL ARBITRATION

As foreign investment increases around the globe, investors and host nations have witnessed a rise in the use of international arbitration to settle investment disputes. Arbitration is a method of dispute resolution by which a neutral third party renders a binding decision on the disputing parties. Using arbitration to settle commercial disputes is anything but a recent phenomenon. In fact, "[c]ommercial arbitration has been practiced in the United States for several hundred years." Traditionally, this arbitration was based on common law principles.

In 1947, Congress officially recognized arbitration as being an enforceable mechanism to settling international disputes by passing the Federal Arbitration Act ("FAA"). The U.S. Supreme Court in Moses H. Cone Memorial Hosp. v. Mercury Const. Corp., recognized the contractual right to

84 See Stagg, supra note 76, at 352.
85 Id. at 357.
86 See Stagg, supra note 76, at 354.
87 Black's Law Dictionary at 112 (8th Ed. 1999).
89 Id.
The court held that under FAA, Congress had intended "to move the parties to an arbitrable dispute out of court and into arbitration as quickly and easily as possible." The Supreme Court began to recognize that in addition to being enforceable, arbitration should be carried out efficiently.

The first big shift towards an international arbitral system came with the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, commonly referred to as the "Washington Convention." The Washington Convention, which was later ratified by the Senate and signed into law by the President, created the International Centre for Settlement of Investment Disputes ("ICSID") headed by the World Bank. The main function of ICSID is to facilitate arbitration proceedings between member states and investors from other member states. ICSID provides the facilities and procedural framework for international arbitration but ICSID itself does not arbitrare disputes. Rather, ICSID provides specific guidelines for selecting arbitrators and conducting proceedings. Such guidelines require that the majority of the arbitrators be nationals of states other than those of which the parties belong.

ICSID is governed by the Administrative Council which contains a representative from each member state. The President of the World Bank serves as the ex officio Chairman of the council but has no vote. The Secretariat makes up the other body of ICSID. The Secretariat is headed by the Secretary-General, the legal representative of ICSID and is elected by the Administrative Council.

In addition to international conventions such as the Washington Convention, countries, including the United States, are signing Bilateral Investment Treaties ("BIT") to promote trade and investment between two sovereigns. These treaties provide substantive and procedural rights for the investor that will be respected by both host states. Included in these BITs is
the right to international arbitration, should an investment dispute arise with the host nation.¹⁰³

BITs have important benefits for all parties involved. For instance, from the perspective of the host country, BITs can lend credibility and strengthen the government’s reputation as an “international actor”¹⁰⁴. From the perspective of the investor, BITs mean that they have a forum to challenge the actions of the host country and are “no longer at the mercy of international politics and governmental bureaucracy”¹⁰⁵. Many BITs give investors a choice of where they can bring their claim, either in the host country’s domestic courts or in international arbitration.¹⁰⁶

When investors do decide to arbitrate, they can do so in a private and confidential environment.¹⁰⁷ Unlike litigation, the arbitration process is highly secretive and amici curie participation from outside interests is restricted.¹⁰⁸ In fact, even the decisions themselves are often confidential.¹⁰⁹ Businesses are likely to take advantage of this secrecy to protect potentially sensitive information involving their investments from becoming public.

When sovereigns sign these BITs with explicit arbitration clauses, they do so with some degree of risk.¹¹⁰ By agreeing to arbitrate disputes, sovereigns have waived their immunity and subjected themselves to the possibility of being found liable.¹¹¹ Host nations may be forced to spend millions of dollars defending their actions in international arbitration.¹¹² Questions arise as to whether international arbitration is worth the risk for sovereign nations.¹¹³ Some analysts argue that investment treaties rarely promote new investment, thereby giving the sovereign almost no benefit at all. According to Susan D. Franck, Assistant Professor of Law at University of Nebraska at Lincoln, “[w]hile investors may be aware of the investment treaties, their existence may

¹⁰³ Id.
¹⁰⁶ Id. at 1541.
¹⁰⁷ Id. at 1544.
¹⁰⁸ Id. at 1544-1545.
¹⁰⁹ Id. at 1545.
¹¹⁰ See Franck, supra note 104, at 346.
¹¹¹ Id.
¹¹² Id.
¹¹³ Id. at 347.
only have a marginal impact on the decision to invest." Studies have indicated that investment treaties are only one of several factors that investors consider in foreign direct investment. The other factors are purely economic, including market size, gross domestic product ("GDP") and current levels of investment in the host country. Developed countries may be even less likely to reap the benefit of investment treaties than developing countries.

With respect to international arbitration clauses in investment treaties, some analysts believe that they negatively impact developing countries by diverting cases away from their national courts. They argue that international arbitration "inhibits the development of the rule of law in national courts by creating a regime that provides a privilege to foreign investors." By contrast, international arbitration may serve as a catalyst for developing nations to reform their national courts and reach international standards of justice. Additionally, international arbitration may give local courts an incentive to compete for the right to settle investment disputes in treaties that provide for choice of venue.

As more and more investors turn to arbitration to settle their disputes, questions arise as to which form of arbitration should be followed. Many U.S. law firms are now offering arbitration services to their clients. In fact, several large firms have even developed separate international arbitration departments. Scholars are debating whether international arbitration should follow the American model of litigation or another form altogether. Some go as far as suggesting that the influence of American law firms has caused international arbitration to become an extension of the American court system; much to the dismay of the rest of the world. While this may be good for the U.S., it has caused some concern among our foreign counterparts. At the very least, it is evidence that international arbitration is no longer foreign to America.

Despite the tremendous growth in the levels of international arbitration, several important reforms have been suggested to make it run more efficiently. Some reformers argue that the variable language often found in
investment treaties should be replaced with strict definitions and terms for arbitration.\textsuperscript{126} They argue this would provide “textual certainty” to protect against the rendering of inconsistent arbitral decisions.\textsuperscript{127} However, too much rigidity will backfire and turn investors off to arbitration. One of the most important aspects of international arbitration is its ability to adapt to different situations and circumstances and render the most appropriate decision in light of this. Erasing this flexibility will destroy a major incentive to arbitrate investment disputes.

Other reformers, referred to as “barrier builders” support tougher preconditions on the right to arbitrate international disputes.\textsuperscript{128} They would require investors to receive permission from the foreign government before they can pursue their claim in arbitration.\textsuperscript{129} This is based on the fear that investors unduly burden host nations by bringing “unmeritorious claims, which arguably have a detrimental impact on sovereignty and the Sovereign’s ability to pass legislation effecting their citizen’s health, safety, and public morals.”\textsuperscript{130} This approach makes international arbitration practically obsolete. In addition to rejecting an investor’s frivolous claims, the foreign government has no incentive to agree to arbitrate even the meritorious claims. There is nothing stopping the government from forcing an investor to bring suit in the domestic courts, an environment likely to be more favorable to the host government. This exact practice is what international arbitration was designed to avoid.

Reformers often cite the lack of an appellate body as a significant drawback to international arbitration. Supporters argue that an appellate body would create a “determinate and coherent jurisprudence” that reviews arbitral decisions.\textsuperscript{131} In addition to restoring faith in the system, they argue it would promote consistency, predictability and prevent the occurrence of conflicting decisions.\textsuperscript{132}

The appropriate body to handle appeals is the subject of much discussion. The United Nations International Court of Justice (“ICJ”) has been suggested, among others.\textsuperscript{133} However, the ICJ’s jurisdiction only applies to UN member states; therefore it could not handle an appeal involving a private investor.\textsuperscript{134} Supporters argue that the ICJ statute should be amended to include

\textsuperscript{126} See Franck, supra note 105, at 1587-1588.
\textsuperscript{127} Id. at 1588-1589.
\textsuperscript{128} Id. at 1589-1590.
\textsuperscript{129} Id.
\textsuperscript{130} Id. at 1591.
\textsuperscript{131} See Franck, supra note 105 at 1607.
\textsuperscript{132} Id.
\textsuperscript{133} Id. at 1607.
\textsuperscript{134} Id.

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jurisdiction over non-governmental investors. Even if that is possible, the ICJ’s limited experience with appeals makes it difficult to predict whether the process would be effective.

Given its affiliation with the World Bank, ICSID is viewed as the leading authority on international arbitration and any reforms to the process would likely begin with ICSID. In 2004, the idea of creating an appellate body as part of ICSID was proposed by the Secretariat, but the plan was later withdrawn after facing criticism. The criticism came largely from investors who “valued the high degree of finality the current ICSID arbitration process provides parties in resolving disputes more than the benefit of substantive consistency.” Despite this criticism, the creation of an appellate division of ICSID some time in the future remains a possibility.

The development of an appellate process would necessarily require a significant restructuring of the entire body as it exists now. ICSID remains a relatively small operation. Although its caseload has grown considerably in recent years, its personnel and resources have remained constant. In 2006, a number of procedural reforms to ICSID were passed for the purpose of making ICSID proceedings, “more streamlined and transparent, while instilling greater confidence in the arbitral process.” As ICSID continues to reevaluate itself and improve transparency, it is likely that more countries will make use of its arbitration process. As confidence in its ability grows, it is possible that countries will eventually agree to ICSID arbitration for their national security and investment related disputes.

**PART IV. APPLYING THE INTERNATIONAL ARBITRATION MODEL TO INVESTMENT DISPUTES INVOLVING NATIONAL SECURITY**

It is one thing for a state to agree to arbitrate a foreign investor’s breach of contract action for the sale of goods, it’s another thing to ask the state to arbitrate investor disputes that may impact its national security interests. For obvious reasons, governments like the United States are particularly sensitive when it comes to ceding sovereignty on these extremely important issues that

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135 Id.
136 Id.
138 See Tuck, *supra* note 137 at 902.
139 Id. at 888.
140 Id. at 886.
may effect that safety of their citizens. Despite the tremendous rise in investment treaties and international arbitration, sovereigns remain committed to resolving any national security related disputes on their own terms. In the U.S., CFIUS is tasked with handling these issues.142 Other nations undoubtedly have their own versions of CFIUS to deal with these matters when they arise in the context of foreign investments. As countries nationalize their risk management procedures for dealing with security-related investment issues, they overlook the important role that international arbitration can play in mitigating these risks.

A. International Arbitration Can Assess National Security Risks Without Politicizing the Process

Despite attempts to insulate members from outside pressure, CFIUS is, and remains, a committee comprised mainly of political appointees.143 In passing FINSA, Congress stated that its objective is, "[t]o ensure national security while promoting foreign investment and the creation and maintenance of jobs"144 While this is clearly a universal goal, the Secretaries of Treasury, Defense, Homeland Security, Commerce, Labor, and the Director of National Intelligence all must answer eventually to the President. As a result, their judgment on investment issues may be subject to political influence. FINSA’s involvement of Congress in this process only adds to the risk of “political mischief”145 A neutral, international arbitration panel would be able to identify those transactions that will effect security interests without being tainted by the political process. International arbitration can provide “a reliable, neutral forum for investors to enforce the rules of law articulated in a specific treaty.”146

Furthermore, the Congressional briefings that are required by FINSA, run the risk of exposing sensitive information to a wide spectrum of individuals, particularly members of Congress and their aides.147 By contrast, arbitration can better guarantee privacy and confidentiality by controlling who hears the information in question.148

142 See discussion supra notes 11 – 15 on the creation of CFIUS.
144 See Foreign Investment and National Security Act of 2007, H.R. 556, 110th Cong. (2007) quoting the stated purpose of FINSA. “An Act To ensure national security while promoting foreign investment and the creation and maintenance of jobs, to reform the process by which such investments are examined for any effect they may have on national security, to establish the Committee on Foreign Investment in the United States, and for other purposes.”
145 See Corr, supra note 81.
146 See Franck, supra note 104, at 344.
147 See Stagg, supra note 76.
B. International Arbitrators Can Be Uniquely Skilled In Evaluating Complex Business Transactions and the Risks They Might Pose

Those who argue international arbitration is not the appropriate forum for handling controversial investment disputes like DPW should bear in mind that international arbitration has been suggested as a means for resolving nuclear non-proliferation. Scholars point out that "arbitration may be more compelling than the ICJ as a method of resolving hard-core disputes over the obligations of the [Non-Proliferation Treaty] Regime."149 If countries are willing to trust international arbitration to handle issues as important as nuclear non-proliferation, they should be willing to accept this forum to resolve their international investment disputes.

As is the case with enforcing nuclear non-proliferation, assessing foreign business transactions requires specialized knowledge and expertise. For instance, before one can accurately predict whether a proposed merger would have a detrimental effect on U.S. national security, one must fully understand the inner and outer workings of that industry as well as the meaning and significance of the investors stake in the company. Allowing nation states to select arbitrators with significant experience in that specific industry would result in a fairer outcome.150 Ideally, international arbitrators will take host state's national interest into account as one of the factors when rendering its decision.151

C. International Arbitration Can Provide Investors and Host States With More Flexibility To Better Serve Their Interest

Arbitration provides flexibility by considering a number of factors when rendering an opinion. By rejecting strict adherence to any one particular rule of law, arbitrators can focus on general legal principles.152 Therefore, arbitration could adapt to the needs of investors while at the same time protecting the security concerns of the host state.

Critics argue, however, that international arbitration is weakened by the fact that its decisions have no precedential value and cannot influence future decisions.153 However, there are real benefits of this for both investors and states. By not contributing to customary international law, arbitration can better

149 Id. at 149.
150 See Nazario, supra note 148, at 148.
151 Id.
153 Id. at 388.
TO LEGISLATE OR TO ARBITRATE

protect the privacy interests of both parties.154 This is significant for investors because, “the privacy of arbitration allows parties to protect business and other confidences, regardless of whether the confidences would qualify for special protection under judicial procedures.”155 Often, investors are not looking to set precedent; they simply want their dispute resolved quickly and efficiently without the possibility of their sensitive financial information being revealed to the public.156 States also want issues resolved without announcing to the world their own intelligence or security procedures. International arbitration is the ideal forum for achieving both of these goals.

The DPW and CNOOC scandals undoubtedly were cause for embarrassment for all parties involved. Arbitration is beneficial because it allows the losing party to “save face” and avoid public humiliation.157 By deciding issues in private, without any precedential value, arbitration is best suited to provide both parties the flexibility they desire.

D. International Arbitration Can Protect National Security Interests By Allowing Sovereigns to Avoid Arbitration In Extreme Cases

Investment treaties between states have often included provisions known as non-precluded measures (“NPM”) which allow states to “take actions otherwise inconsistent with the treaty when, for example, the actions are necessary for the protection of essential security, the maintenance of public order, or to respond to a public health emergency.”158 The United States has been including NPM clauses in its investment treaties since the early 1980’s.159 Therefore, the concept is not at all foreign to our government.

International arbitral tribunals have analyzed these clauses in the past but have never given them the “rigorous treaty interpretation mandated by the Vienna Convention.”160 Some scholars argue for a “nexus requirement” when

155 See Schmitz, supra note 154, at 158.
156 While arbitration proceedings are conducted in private, they are not all confidential. In certain cases, the public has the opportunity to access the record. For a more in-depth analysis of confidentiality issues in arbitration, see Laurie Kratky Doré, Public Courts Versus Private Justice: It’s Time To Let Some Sun Shine In On Alternative Dispute Resolution, 81 Chi.-Kent L. Rev. 463 (2006). Professor Doré’s Article is part of a symposium titled, “Secrecy In Litigation” that appeared in Volume 81 of the 81 CHICAGO KENT LAW REVIEW.
157 See Schmitz, supra note 154, at 158.
159 See Burke-White, supra note 158, at 327.
160 Id. at 316.
analyzing NPMs that insists on their being, “a link between the actions taken by a state that would otherwise violate the treaty and the permissible objectives provided for in the NPM clause.” Assuming this nexus test is met, NPMs could serve as happy medium for some states that are reluctant to give up their sovereignty entirely in this area by allowing them an alternative outlet in extreme cases.

PART V. CONCLUSION

The recent foreign investment scandals such as DPW garnered national attention like never before seen in these types of investment transactions. A once little known governmental agency, CFIUS, suddenly graced the headlines of mainstream newspapers around the country as the controversy unfolded live in front of a watchful and eager audience. In the aftermath of these controversies, Congress responded quickly to the public outrage and decided to act in its legislative authority. In 2007 it passed FINSA in an attempt to prevent future perceived investment risks from slipping under the radar without Congressional approval. Congress wanted to give itself a say on these matters and used FINSA to achieve this. While FINSA means well, it falls far short of its ultimate goal to encourage foreign investment. The additional regulations on foreign investment and involvement of Congress will likely only lead to more confusion for investors. As the U.S. sets up more barriers to its markets, foreign investors are likely to look elsewhere. With the U.S. looking to solve its disputes internally, there is nothing to stop other governments from doing the same and placing more restriction on their markets. This will in turn lead to inconsistent policies and even more confusion and uncertainty for all investors, including Americans.

International arbitration can address these concerns in a neutral, non-biased forum that involves the international community. This will prevent other nations from creating trade and investment barriers all in the name of their own national security. The tremendous rise in the number of businesses and governments turning to arbitration indicates its growing importance and acceptance as a viable means of dispute resolution. Arbitration can better serve the needs of investors and host states by protecting their privacy and avoiding the public humiliation suffered as a result of failed transactions like DPW. In attempting to prevent future investment scandals, the U.S. government and others around the world should not overlook this important resource.

161 Id. at 342.
162 See Haley, supra note 45.
163 See Schmitz, supra note 154.
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