EXAMINING THE FLOW OF U.S. MONEY INTO CHINA'S MILITARY MIGHT

HEARING

BEFORE THE

COMMITTEE ON FOREIGN AFFAIRS
HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTEENTH CONGRESS

SECOND SESSION

JANUARY 17, 2024

Serial No. 118–76

Printed for the use of the Committee on Foreign Affairs

Available: http://www.foreignaffairs.house.gov/, http://docs.house.gov, or http://www.govinfo.gov

U.S. GOVERNMENT PUBLISHING OFFICE
55–922PDF WASHINGTON : 2024

COMMITTEE ON FOREIGN AFFAIRS

MICHAEL T. MCCAUL, Texas, *Chairman*

CHRISTOPHER H. SMITH, New Jersey
JOE WILSON, South Carolina
SCOTT PERRY, Pennsylvania
DARRELL ISSA, California
ANN WAGNER, Missouri
BRIAN MAST, Florida
KEN BUCK, Colorado
TIM BURCHETT, Tennessee
MARK E. GREEN, Tennessee
ANDY BARR, Kentucky
RONNY JACKSON, Texas
YOUNG KIM, California
MARIA ELVIRA SALAZAR, Florida
BILL HUIZENGA, Michigan
AUMUA AMATA COLEMAN RADEWAGEN, American Samoa
FRENCH HILL, Arkansas
WARREN DAVIDSON, Ohio
JIM BAIRD, Indiana
MICHAEL WALTZ, Florida
THOMAS KEAN, JR., New Jersey
MICHAEL LAWLER, New York
CORY MILLS, Florida
RICH MCCORMICK, Georgia
NATHANIEL MORAN, Texas
JOHN JAMES, Michigan
KEITH SELF, Texas

GREGORY MEEKS, New York, *Ranking Member*
BRAD SHERMAN, California
GERALD E. CONNOLLY, Virginia
WILLIAM KEATING, Massachusetts
AMI BERA, California
JOAQUIN CASTRO, Texas
DINA TITUS, Nevada
TED LIEU, California
SUSAN WILD, Pennsylvania
DEAN PHILLIPS, Minnesota
COLIN ALLRED, Texas
ANDY KIM, New Jersey
SARA JACOBS, California
KATHY MANNING, North Carolina
SHEILA CHERFILUS-MCCORMICK, Florida
GREG STANTON, Arizona
MADELEINE DEAN, Pennsylvania
JARED MOSKOWITZ, Florida
JONATHAN JACKSON, Illinois
SYDNEY KAMLAGER-DOVE, California
JIM COSTA, California
JASON CROW, Colorado
BRAD SCHNEIDER, Illinois
GABRIEL AMO, Rhode Island

BRENDAN SHIELDS, *Staff Director*
SOPHIA LAFARGUE, *Staff Director*

CONTENTS

EXAMINING THE FLOW OF U.S. MONEY INTO CHINA'S MILITARY MIGHT

Wednesday, January 17, 2024

HOUSE OF REPRESENTATIVES,
COMMITTEE ON FOREIGN AFFAIRS,
Washington, DC.

The committee met, pursuant to notice, at 10:15 a.m., in room 210, House Visitor Center, Hon. Michael McCaul (chairman of the committee) presiding.

Chairman MCCAUL. The Committee on Foreign Affairs will come to order. The purpose of this hearing is to examine the flow of U.S. capital into China's military and technological development.

I now recognize myself for an opening statement. I want to thank the witnesses for being here as well. Unfortunately, one of our top-tier witnesses who was going to testify, Mr. Matheny, came down with COVID this morning, so I hope he gets better. But we are delighted to have the two of you.

The Chinese Communist Party's goals and actions are a clear and present danger to the security interests of the United States and our allies. We are in a generational competition with a determined adversary set on upending the global balance of power. Technology is at the center of this competition, and the CCP is using it as a weapon for its military and surveillance state. These technologies can be used to advocate and safeguard democracy, or they can be used for subversion and oppression.

We must understand that whoever controls the best technology will likely prevail in this great power competition. And while we can restrict China's access to U.S. critical technology through export controls, we cannot stop big investors from using their money, know-how, and network to help build highly advanced technology companies in China.

Regrettably, U.S. money is fueling the CCP war machine and surveillance state. Look no further than the CCP's dystopian oppression of the Uyghurs and the successful hypersonic missile test which circled the globe and landed with precision. This was built on the backbone of U.S. technology.

The ranking member and I were disturbed that we have no effective tools to stop these key investments. They harm U.S. national security and endanger our partners and allies like Taiwan. And we also want to congratulate Taiwan on their recent elections and to the DPP.

So, the ranking member and I acted. In November, this committee, on a unanimous bipartisan basis, passed the Preventing Adversaries from Developing Critical Capabilities Act. This bill has been one of the most important steps this committee has taken to protect U.S. national security and counter the CCP. This bill may also be one of the most bipartisan efforts that we have worked on.

This effort spans the past two Administrations. It was then-Secretary Mike Pompeo who urged in 2020 to stop the flow of U.S. money into national security sectors in China. The Trump national security team supports this legislation, but so too does the Biden Administration. More recently, the Biden Administration took the idea and developed an executive order targeting outbound rule.

While Ranking Member Meeks and I and a growing number of members, as well as outside groups like Heritage, Hudson, and American Compass, plan to get this bill signed into law. We thought we had it done in the National Defense Authorization. It got pulled. We need to get this new version that was introduced by the ranking member and myself signed into law. We cannot wait.

This hearing today plays an important role in that process. The witnesses today were selected by both of us. This hearing should help clear up a lot of misconceptions about the threat, current situation, and examine tangible solutions.

It should come as no surprise that China's military and surveillance state are exploiting loopholes in U.S. policy to access billions of U.S. investment dollars and expertise. We know that U.S. investment has not democratized China, and companies which are controlled by the CCP have no power over the applications of their technology. The CCP can direct it to be used for military or surveillance purposes. And we know China's military-civil fusion strategy undermines an entity-by-entity sanctions approach and instead requires country-wide prohibitions for key technologies.

Ranking Member Meeks and I requested that the Treasury Department decide whether to sanction Hikvision, a CCP surveillance company contributing to the Uyghur genocide, but Treasury decided not to sanction the company. The weakness of the sanction model, is that Treasury Department will not sanction.

Our witnesses today can provide further evidence on these points and articulate why an outbound, forward-looking, sector-based regime is necessary. And we'll see, whether Republican or Democrat, those that examine China objectively, analytically, and realistically have reached the same conclusion. And while existing tools, such as sanctions, have an important role, they simply cannot be a substitute for an outbound investment regime that is authorized by Congress.

And that is our goal: restricting key outbound investments. And a whole-of-government approach ensures America's national security comes first.

And with that, the chair now recognizes the ranking member.

Mr. MEEKS. Thank you. Thank you, Chairman McCaul, for organizing this important and timely hearing. I also want to thank our distinguished witnesses for appearing before the committee.

Our discussion today is critical for America's national security and our strategic competition with China. But let me also just say to the Chairman: I want to thank you for working—we have worked very closely together to get this bill passed in a bipartisan way. And I also want to thank our staffs who worked very closely to jointly organize this hearing, which we worked on collectively and together, which I hope advances the joint work that we have done together to pass our bipartisan bill, H.R. 6349, the Preventing Adversaries from Developing Critical Capabilities Act, out of committee.

Today, what we are doing, we are demonstrating to the United States, to the country, that when it comes to issues of critical importance to American interests, Republicans and Democrats can come together to solve big problems.

We know that Beijing is developing advanced technologies, critical for military, intelligence, surveillance, and cyber-enabled capabilities, with dangerous implications for our security. We also know that Beijing is busy synergizing its civilian and commercial sectors with its military and defense industrial sectors. And we also know that Beijing is intent on exploiting, stealing, and diverting the world's cutting-edge technologies to fuel its military buildup. So, we should not be making Beijing's job easier by having Americans fund the very PRC companies that are developing these technologies.

Despite a bipartisan, bicameral desire to address this significant national security challenge, for several years now, Congress has not coalesced around a solution. But we are doing so now. And that is why I want to give credit, in a bipartisan way, to Mr. McCaul in what we are doing collectively together. And that is why I want to give credit to the Biden Administration for tackling this challenge.

On August 9th of 2023, President Biden issued a game-changing executive order on outbound investment that calls for prohibitions and notification requirements on specific types of American investments in China, or in certain Chinese companies that develop or produce semiconductors, quantum computers, and artificial intelligence applications. As we speak, the Biden Administration is busy establishing a process and crafting regulations to implement the executive order.

But that does not mean that we, in the U.S. Congress, that we are off the hook. We need to create a statutory framework for the executive order, provide the Administration with the resources and tools that are necessary to effectively implement an outbound screening program, and provide certainty to our allies in the private sector that Congress stands firmly behind these carefully tailored restrictions. That is our responsibility. We should not shrink from that.

An outbound regime that combines transparency with prohibitions on investments in the most sensitive technology sectors is the very best way to safeguard the United States' national security while also maintaining open global capital flows and the United States' preeminent position in global financial markets. The only legislation that balances these equities, the only one that I think has that true balance, is H.R. 6349. It is the most effective and robust legislative solution.

So, I look forward to the discussion today and hearing from our witnesses about how best to address this challenge. Thanks again for working so closely, Chairman McCaul, and our staffs. And I yield back.

Chairman McCaul. I thank the ranking member. I always think we're stronger as a nation and a Congress when we are united on these issues and speak with one voice to our adversaries, like communist China.

So, we have a distinguished panel here today. First, Mr. Honorable Matt Pottinger is Chairman of the China Program at the Foundation for Defense of Democracies and a distinguished visiting fellow at the Hoover Institution. From 2019 to 2021, he served as the U.S. Deputy National Security Advisor. Thank you, sir, for being here today.

Mr. Peter Harrell is a nonresident fellow of the Carnegie Endowment for International Peace. From January 2021 through 2022, he served at the White House as Senior Director for International Economics. We are grateful for you being here today.

The Chair now recognizes Mr. Pottinger for his opening statement.

STATEMENT OF HON. MATTHEW POTTINGER, CHAIRMAN OF FDD CHINA PROGRAM, FOUNDATION FOR DEFENSE OF DEMOCRACIES

Mr. POTTINGER. Chairman McCaul, Ranking Member Meeks, and distinguished members of the committee, I am grateful for the opportunity to speak to you today.

We're at a juncture now where the scales of global power are beginning to tip toward America's adversaries, in part because of the leverage that we are providing them. American know-how and capital are seeds and fertilizer that have helped foster the growth of China's military might. U.S. companies and investment funds have, sometimes inadvertently, sometimes carelessly, helped to underwrite and expedite the modernization of the People's Liberation Army and China's high-tech surveillance and intelligence apparatus.

Americans do not typically invest with the intention of harming U.S. national security, but that is often the result when they put their capital into Chinese companies that are working with dual-use technologies, those technologies that have the potential for military as well as commercial applications.

It is hard and increasingly meaningless to try to distinguish between a Chinese enterprise with commercial aims and one with military objectives, and it is hard because Beijing actually designed it that way. Corporate independence in today's China is an illusion. The truth is that the single-party dictatorship that rules China has powerful authorities and influence over all entities, whether private-or state-owned, civilian or military, domestic or even foreign. Beijing has built a business and regulatory ecosystem to facilitate and mandate the transfer for dual-use technologies to military and intelligence programs.

China's military-civil fusion strategy, for example, exists for that very purpose. So does China's National Intelligence Law of 2017, which compels "all" organizations and citizens to secretly support, assist, and cooperate with China's espionage activities. Chinese Communist Party organizational cells, rather than entrepreneurial founders, call the shots now from inside many of China's most famous technology companies.

Some American investors try to conduct due diligence to reassure themselves about where their money and technology are ultimately ending up inside China, but that, too, is an increasingly fraught exercise. Beijing is running a "rectification campaign" to shut down or assert heavy influence over research, consulting, and due diligence firms operating in China. So no wonder that U.S. investors who are seeking a return on their capital are often blind to the strategic costs that they are incurring for America's national security and prosperity. I have listed some concrete examples of how that plays out in my written testimony, which I have submitted for the record.

Allow me to close with just a handful of recommendations. Congress has an opportunity to build on the initial steps taken by the Trump and Biden Administrations to prevent U.S. capital from fueling China's military and intelligence capabilities.

First, Washington should take a sectoral approach, rather than merely an entity-based approach. The Treasury Department has demonstrated since at least 2021 that it is disinterested in using even its existing narrow authorities to limit investment in Chinese military-linked companies.

And in fairness to the Treasury Department, tackling the problem on a company-by-company basis would be a resource-intensive and gargantuan task. Chinese firms commonly dodge U.S. controls with shell companies and complex subsidiary arrays, and it would be better, simpler, and less resource intensive to apply new rules to entire sectors.

Second, the rules should cover all strategic and military technologies. The Biden Administration's draft rules are a good start. They are designed to impact semiconductors, artificial intelligence, and quantum computing. Proposed bipartisan legislation also seeks to strengthen outbound investment screening in the field of hypersonics. Congress and the Administration should consider adding other technologies listed as "critical and emerging technologies," as the White House puts it, and as outlined by the National Science and Technology Council. These include biotech, directed energy, space technologies, advanced manufacturing, autonomous systems and robotics, and even some green energy technologies.

Third, apply rules to all kinds of investments. The Biden Administration rules, as currently written, would impact venture capital, private equity, greenfield, joint ventures, and certain debt financing transactions. And this is very welcome. Congress should also seek to cover investments in publicly listed companies.

Fourth, include existing transactions, not just future ones, within the scope of legislation. And, finally, seek to block investments and not merely review them. Mandating transparency for U.S. investments in to China is a welcome step to better understand the scope of the problem, but Congress should also consider broadening transparency to full prohibitions on investments in targeted sectors.

Thanks very much for inviting me to deliver this testimony.

[The statement of Mr. Pottinger follows:]

CONGRESSIONAL TESTIMONY: FOUNDATION FOR DEFENSE OF DEMOCRACIES

House Foreign Affairs Committee

Examining the Flow of U.S. Money into China's Military Might

MATT POTTINGER

China Program Chairman
Foundation for Defense of Democracies

Former Deputy U.S. National Security Advisor

Washington, DC
January 17, 2024

FDD
FOUNDATION FOR DEFENSE OF DEMOCRACIES

www.fdd.org

Introduction

Chairman McCaul, Ranking Member Meeks, and distinguished members of the committee, I am grateful for the opportunity to speak before you today. We're here to peel back the layers on a matter that strikes at the core of our national security — how some of our financial engagements with China are actually strengthening its military and its intelligence services.

The unchecked flow of U.S. investments and technology to China has far-reaching implications for our national security and that of our allies. We're at a juncture where the scales of global power are tipping toward America's adversaries, not by chance, but in part because of the leverage we provide them.

'Military-Civil Fusion'

American know-how and capital are seeds and fertilizer from which China's formidable military might has sprouted. U.S. companies, financial institutions, and investment funds have — sometimes inadvertently, sometimes carelessly — helped underwrite and expedite the modernization of the People's Liberation Army (PLA) and China's high-tech surveillance state. Our ingenuity and money are supplying so-called dual-use technologies: ones with civilian as well as military or other national security uses. These range from advanced semiconductors and cutting-edge artificial intelligence (AI) applications to unmanned aerial vehicles and next-generation communications systems, all of which have been integrated into Chinese military and intelligence programs. American money and the transfer of knowledge that often accompanies it allow Beijing to circumvent many of the costs and risks associated with research and development. In other words, they act to subsidize Chinese leader Xi Jinping's national ambitions at a time when China's economy is weakening.

China has built a business and regulatory ecosystem to facilitate, and even mandate, the acquisition and transfer of dual-use technologies to military and intelligence programs. China's "military-civil fusion" strategy, for example, exists to convert civilian innovations for military purposes.[1] This means that outwardly commercial entities that receive American capital can be, and in fact routinely are, linked to the PLA and that many U.S. investors seeking a return on their capital are blind to the strategic costs to our country.

China's strategy is exemplified by the saga of semiconductor manufacturing, where Chinese firms, backed by U.S. funds and expertise, have made significant inroads. Chips are dual-use linchpins, as essential to stealth fighters as they are to smartphones. Artificial intelligence (AI) offers a similarly sobering view of dual-use technology's potential. American investments have helped propel Chinese AI firms that are now at the forefront of commercial innovation. Yet many of those same innovations are just as useful at equipping the PLA with capabilities ranging from autonomous weapons systems to advanced surveillance.

American educational and academic research institutions have also become conduits of expertise and innovation to Chinese firms supporting China's military-industrial complex. Collaborative

[1] Emily de la Bruyere and Nathan Picarsic, "Defusing Military-Civil Fusion," *Foundation for Defense of Democracies*, May 26, 2021. (https://www.fdd.org/analysis/2021/05/26/defusing-military-civil-fusion)

research, born out of a quest for academic advancement, is being co-opted to advance Beijing's military objectives. Chinese companies with military ties — like Megvii, SenseTime, and even Huawei — have in recent years forged partnerships with U.S. universities, effectively transforming these bastions of learning into outposts of the Chinese government's technological ambitions.[2] Left unregulated, such partnerships will contribute to the PLA's modernization in ways we won't fully understand until those capabilities are used against Americans at home and on distant battlefields.

The Myth of the Chinese 'Private' Company

The idea that we can easily distinguish between Chinese private enterprises with strictly commercial aims and state-backed entities that harbor military ambitions is increasingly illusory.[3] Corporate independence in today's China is a façade that tries to hide the Chinese party-state's pervasive influence over all entities, whether "private" or state-owned, civilian or military, domestic or even foreign. The Chinese regime's grip on industry is multi-faceted, intertwining regulatory and legal mandates with Chinese Communist Party (CCP) doctrine and the objectives of its "core leader" at the top. CCP party cells and party secretaries now keep watch and influence decisions within nominally private companies across China, including many foreign joint-ventures.

The CCP's omnipresence is enshrined in Chinese law. The National Intelligence Law of 2017, for instance, compels "all" organizations and citizens to secretly support, assist, and cooperate with state intelligence efforts.[4] This law, among others, like China's recently revised Counter-Espionage Law, has transmuted Chinese companies into espionage vectors for China's military.[5] The CCP's strategy of military-civil fusion has further obliterated any pretense of separation, as it systematically mandates that all technological advancements, irrespective of their origin, must be at the disposal of China's military and intelligence services.

Look no further than the case of ByteDance, the parent company of the Chinese social media platform TikTok, which has come under scrutiny for its role in amplifying pro-Beijing and antisemitic propaganda.[6] ByteDance's investors include Goldman Sachs, SoftBank Group,

---

[2] Craig Singleton, "The Middle Kingdom Meets Higher Education," *Foundation for Defense of Democracies*, December 9, 2021. (https://www.fdd.org/analysis/2021/12/09/the-middle-kingdom-meets-higher-education)

[3] Craig Singleton, "Beijing's Power Play," *Foundation for Defense of Democracies*, October 23, 2023. (https://www.fdd.org/analysis/2023/10/23/beijings-power-play)

[4] National Intelligence Law of the People's Republic of China, (Adopted at the 28th session of the Standing Committee of the 12th National People's Congress on June 27, 2017), (China), accessed on January 12, 2024. (https://www.chinalawtranslate.com/en/national-intelligence-law-of-the-p-r-c-2017)

[5] "China: Counterespionage Law Revised," *Global Legal Monitor*, Library of Congress, accessed on January 11, 2024. (https://www.loc.gov/item/global-legal-monitor/2023-09-21/china-counterespionage-law-revised)

[6] "Discourse Power: CCP's Strategy to Shape the Global Information Space," Select Committee on the Chinese Communist Party, U.S. House of Representatives, accessed on January 15, 2024. (https://selectcommitteeontheccp.house.gov/about/events/hearing-discourse-power-ccps-strategy-shape-global-information-space)

Sequoia Capital, Morgan Stanley, and Susquehanna International Group.[7] In 2018, ByteDance, with backing from China's Ministry of Science and Technology and Beijing's municipal government, established the Beijing Academy of Artificial Intelligence.[8] This program was part of a broader effort to use civilian AI research for military purposes and involved collaboration with three military-linked Chinese universities on research initiatives involving critical technologies.[9]

Publicly available Chinese government documents also directly link ByteDance to the Chinese government's surveillance state, including at least five Chinese surveillance companies. These companies, including iFlyTek and SenseTime, have been implicated by the U.S. government in the CCP's severe repression of the ethnic Uyghur people and were added to a U.S. government blacklist in 2019.[10] Dawning Information Industry Company, also known as Sugon, another company collaborating with ByteDance, has contributed to the simulation of nuclear weapons and testing of hypersonic glide vehicles, activities highlighted in reporting from *The Washington Post*.[11] And yet, American investments into ByteDance continue unimpeded, even to this day, and its subsidiary TikTok entrenches itself ever more deeply as a dominant source of news and information for tens of millions of Americans.

ByteDance is just one example of U.S. capital in companies tied to China's military modernization. Some others include the following:

- **4Paradigm:** Goldman Sachs and Sequoia Capital China invested in this Chinese AI firm, which reportedly sold software to China's military for "battalion command decision-making and human-machine learning."[12]

- **Microsoft Research Asia:** This Beijing-based center is a key example of how U.S. investment backs research collaboration that ends up assisting China's military modernization. It has been one of the most important institutions in the development of

[7] "Principal Investors in ByteDance," *Crunchbase*, accessed on January 12, 2024. (https://www.crunchbase.com/search/principal.investors/field/organizations/num_investors/bytedance)
[8] Rachel Lee, Prudence Luttrell, Matthew Johnson, and John Garnaut, "TikTok, ByteDance, and Their Ties to the Chinese Communist Party," Submission to the Senate Select Committee on Foreign Interference through Social Media (Australia), March 24, 2023.
[9] The three Chinese universities are: Huazhong University of Science and Technology, People's Public Security University of China, and Tsinghua University.
[10] David Shepardson and Josh Horwitz, "U.S. Blacklists Chinese Tech Firms Over Treatment of Uighurs," *Reuters*, October 9, 2019. (https://www.reuters.com/article/idUSKBN1WM25M)
[11] Greg Timberg and Ellen Nakashima, "U.S. Expands Tech Battle with China, Barring More Technology Sales," *The Washington Post*, June 21, 2019. (https://www.washingtonpost.com/technology/2019/06/21/us-expands-tech-battle-with-china-barring-more-technology-sales)
[12] Ellen Nakashima and Jeanne Whalen, "Biden administration concerned about U.S. investments in Chinese tech companies with military or surveillance ties," *The Washington Post*, December 16, 2021. (https://www.washingtonpost.com/national-security/us-investments-china-biden/2021/12/15/835876a0-5772-11ec-a808-3197a22b19fa_story.html)

China's artificial intelligence sector.[13] In 2018, academics from the lab co-authored three papers on AI with China's National University of Defense Technology.[14]

- **Biren Technology:** Biren, one of China's most advanced semiconductor designers, hopes to compete with Nvidia in China. It is on the Commerce Department's Entity List for its technology's potential ties to "weapons of mass destruction, advanced weapons systems, and high-tech surveillance."[15] Walden International and GREE VR Capital have invested in Biren.[16]

- **DJI:** This heavyweight of drone manufacturing represents some 70 percent of the global consumer drone market.[17] Some of its lead investors have been American.[18] DJI's key role in arming both sides in the ongoing war in Ukraine shows how critical a nominally civilian company could be for China's military.[19]

Today's Limited Toolkit

Existing tools, while seemingly robust on paper, are ill-suited or inadequate for this challenge. The only active regulatory regime that limits the flow of U.S. capital into China today is a Treasury Department blacklist called the Chinese Military-Industrial Complex Companies List. But this tool has barely been used since it was created more than three years ago.

Established by a presidential executive order in November 2020, it originally allowed the Defense Department to bar U.S. persons from investing in public securities of certain companies tied to the Chinese defense industry. The Trump administration listed 44 companies, along with 1,108 subsidiaries.[20]

---

[13] Karen Weise, Cade Metz, and David McCabe, "Microsoft Debates What to Do with A.I. Lab in China," *The New York Times*, January 10, 2024. (https://www.nytimes.com/2024/01/10/technology/microsoft-china-ai-lab.html); Jeffrey Ding, "ChinAI #37: Happy 20th Anniversary to Microsoft Research Asia," *Substack*, accessed on November 19, 2018. (https://chinai.substack.com/p/chinai-37-happy-20th-anniversary)
[14] Madhumita Murgia and Yuan Yang, "China's Tech Ambitions May Upset the Global Trade Order," *Financial Times* (UK), April 10, 2019. (https://www.ft.com/content/9378e7ee-5ae6-11e9-9dde-7aedca0a081a)
[15] Entity List Additions, U.S. Department of Commerce, 88 Federal Register 71991, October 17, 2023, page 71991-71994. (https://www.federalregister.gov/documents/2023/10/19/2023-23048/entity-list-additions)
[16] "Investor Financials for Biren Technology," *Crunchbase*, accessed on January 12, 2024. (https://www.crunchbase.com/organization/biren-technology/investor_financials/investors)
[17] Nessa Anwar, "World's largest drone maker is unfazed — even if it's blacklisted by the U.S.," *CNBC*, February 7, 2023. (https://www.cnbc.com/2023/02/08/worlds-largest-drone-maker-dji-is-unfazed-by-challenges-like-us-blacklist.html)
[18] "Company Financials for DJI," *Crunchbase*, accessed on January 11, 2024. (https://www.crunchbase.com/organization/dji/company_financials)
[19] Greg Myre, "A Chinese drone for hobbyists plays a crucial role in the Russia-Ukraine war," *NPR*, March 28, 2023. (https://www.npr.org/2023/03/21/1164977056/a-chinese-drone-for-hobbyists-plays-a-crucial-role-in-the-russia-ukraine-war)
[20] "Communist Chinese Military Companies Listed Under E.O. 13959 Have More Than 1,100 Subsidiaries," *U.S. Department of State*, January 14, 2021. (https://2017-2021.state.gov/communist-chinese-military-companies-listed-under-e-o-13959-have-more-than-1100-subsidiaries/index.html)

In 2021, the Biden administration expanded the authority to also target surveillance technology companies linked to human rights abuses. The order, however, took a narrower approach toward subsidiaries, removing more than 1,000 impacted firms.

An even more important change was to move the authority for designating blacklisted companies away from the Department of Defense and to give it to the Treasury Department. Since then, the list has grown to a mere 68 companies. The last time Treasury added any new firms was in December 2021.[21] I will go out on a limb and posit that China has more than 68 companies involved in its military modernization and its surveillance apparatus!

Frankly, giving the Treasury Department additional authorities to target *specific* Chinese firms is unlikely to succeed when Treasury has already demonstrated insufficient will and ability to use existing tools. In fairness, even if leaders at Treasury had the will to enforce these authorities, the fact remains that it is hard to target China's military modernization company by company — as opposed to sector by sector. It is highly taxing in terms of manpower and other resources. This is particularly true given China's recent clampdowns on independent research and due-diligence firms. Simply put, acquiring accurate information about Chinese corporations, business relationships, and supply chains has never been more difficult — and is growing more difficult by the day. This opacity is a deliberate feature of Xi Jinping's China.

Fortunately, last August, the Biden administration unveiled its draft outbound investment rules that aim to take a *sector-by-sector* approach to the problem. In its current draft form, it would bar certain categories of U.S. investment — private equity, venture capital, greenfield projects, joint ventures, and some debt financing — from flowing into China's semiconductors, quantum computing, and AI sectors and require investors to notify the Treasury Department about certain investments into those sectors.

Recommendations

Congress has an opportunity to build on the approach taken by the Biden administration last year. As Congress considers how it should move forward in taking on this important issue of U.S. capital and know-how funding the growth of China's economy, I respectfully recommend the following:

1. Washington should take a sectoral, not entity-based approach. As mentioned above, the Treasury Department has demonstrated since 2021 its disinterest in using its authorities to limit investment in Chinese firms. Chinese companies also commonly dodge U.S. controls with shell firms and subsidiaries. It would instead be better to apply new rules to entire sectors.

2. Rules should cover all strategic and military technologies. The Biden administration's draft rules are set to impact semiconductors, artificial intelligence, and quantum computing. Proposed bipartisan legislation also seeks to strengthen outbound investment screening in the field of hypersonics. Congress and the administration should also consider other technologies listed as

[21] "NS-CMIC List - NS-CCMC List - Consolidated Sanctions List," *U.S. Department of the Treasury's Office of Foreign Assets Control*, accessed on January 12, 2024. (https://ofac.treasury.gov/consolidated-sanctions-list/ns-cmic-list)

"critical and emerging technologies" outlined by the National Science and Technology Council, such as biotechnology, directed energy, space technologies, advanced manufacturing, autonomous systems and robotics, and green energy technologies.[22]

3. Apply rules to all kinds of investments. The administration's rules, as currently written, will impact venture capital, private equity, greenfield, joint ventures, and certain debt financing transactions. Congress' bill should also cover investments in publicly listed companies.

4. Impact existing transactions, not just future ones. Biden's draft rules only apply to future investments. This leaves out investments that Washington should see every reason to unwind, including all of those listed above — into ByteDance, 4Paradigm, Biren, and Microsoft Research Asia.

5. Block investments — don't only review them. Mandating transparency into U.S. investment into China is a strong start to better understand the scope of the issue. Congress should also consider broadening transparency to full prohibitions of investments into targeted sectors.

Thank you for inviting me to deliver this testimony.

[22] The White House, "Critical and Emerging Technologies List Update," February 2022. (https://www.whitehouse.gov/wp-content/uploads/2022/02/02-2022-Critical-and-Emerging-Technologies-List-Update.pdf)

Chairman MCCAUL. Thank you, Mr. Pottinger. The chair now recognizes Mr. Harrell for his opening statement.

STATEMENT OF HON. PETER HARRELL, NONRESIDENT FELLOW, CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE

Mr. HARRELL. Chairman McCaul, Ranking Member Meeks, honorable members of the Committee, it is an honor for me to testify in front of the Committee today on one of the most important aspects of America's strategic competition with Beijing: managing the flow of American capital to China. I have submitted a statement for the record and will confine my in-person testimony to just several points.

In August of last year, with President Biden's issuance of Executive Order 14105, the Administration took an important step toward regulating U.S. investment in China's AI, semiconductors, and quantum computing sectors. EO 14105 is intended to begin addressing the risk that certain U.S. investments can help China develop an edge over the U.S. and our partners in key technologies.

Over the last decade, for example, we saw comparatively early stage U.S. investment in a number of Chinese technology firms that later engaged in problematic activities. An example of this is Chinese surveillance technology firm SenseTime, which attracted U.S. investment as early as 2017, but only in 2019 did the U.S. Government understand that SenseTime was engaging in China's surveillance in Xinjiang, triggering export controls on the company.

Unlike an outbound investment regime that focuses on sanctions against specific Chinese companies—which would require the U.S. Government to know up-front every Chinese firm that is problematic, a virtually impossible task given the scale of China's economy and the civil-military fusion doctrine in China—a sectoral outbound investment regulation can limit risky investment in early stage Chinese companies, as well as direct U.S. investments in those sectors that pose long-term risk to U.S. national security.

While Executive Order 14105 is an important authority to address the risks posed by U.S. investments in strategic technologies in China, it is still vital for Congress to act. Legislation along the lines of H.R. 6349, the Preventing Foreign Adversaries from Developing Critical Capabilities Act, which Chairman McCaul, Ranking Member Meeks, you and other Members of Congress have introduced and have pushed through this committee, would put U.S. investment restrictions on a permanent statutory foundation, signal Congress's agreement that the U.S. needs a targeted regime to regulate U.S. investment in a handful of high-tech sectors, and strengthen and expand on the Administration's initial action.

As Congress acts, I urge you to do so in a way that reinforces rather than undermines the regulatory processes that are already underway, as H.R. 6349 would do, reinforcing and expanding on already-existing regulatory processes.

While I understand the legitimate desire by some members of this committee and many Members of Congress for a more expansive approach than is in H.R. 6349, I am also cognizant that regulating U.S. investment in specific Chinese sectors is a new endeavor, and it is appropriate for the focus today to be on the most important and most critical technology sectors. There is going to be a learning curve, a need for agencies and companies to build expertise, and a risk of unintended consequences.

Legislation had a very different set of goals. For example, it would cover a hugely different number of sectors, would risk actually undermining progress by forcing a restart of rulemaking, overtaxing agencies, and creating confusion for the corporate sector and American allies. Congress should start with a tailored and scoped approach, focused on appropriate sectors where we know there are problems. And, of course, Congress can later add to the program if circumstances dictate.

The final point I want to make is in response to arguments that restricting U.S. investment in China somehow undermines our own free market principles and will weaken U.S. influence over China's corporate sector. The U.S. tried, going back to the 1990's, to use economic engagement with China to make China more like the U.S. and to pool Chinese companies and Chinese society toward our direction.

What we have found is that, under President Xi Jinping, that strategy simply does not work. The Chinese State, not American investors, ultimately tells Chinese companies in strategic sectors what to do. With respect to China, a geopolitical and economic competitor, we need to accept that we will have to more actively manage the economic relationship to make sure that it serves American national security interests and not simply the economic interests of American companies.

That does not mean cutting off all, or even most economic ties, but it does mean that, where we see a pattern and practice of U.S. investment helping China grow critical technologies, the U.S. Government has a legitimate regulatory interest.

Thank you, members of the Committee, for your focus on this issue, and I look forward to your questions.

[The statement of Mr. Harrell follows:]

Hearing Entitled "Examining the Flow of U.S. Money into China's Military Might"
House Foreign Affairs Committee
January 17, 2024
Testimony of Peter E. Harrell

Chairman McCaul, Ranking Member Meeks, Honorable Members of the Committee—

Thank you for the opportunity to testify today and it is a pleasure for me to be here with my distinguished co-panelists.

In recent years members of this Committee have drawn significant, welcome attention to the subject of today's hearing, the regulation of U.S. investment in China. With China's rise as America's foremost geopolitical competitor and with hundreds of billions of dollars of U.S. investment having flowed into China over the past several decades, American policymakers need an effective legal regime to regulate U.S. investment in China to ensure that such investment is consistent with, rather than contrary to, America's national security interests.

I welcome and strongly support President Biden's decision in August 2023 to sign E.O. 14105, which directs the Treasury Department to begin establishing a regime to require the notification of, and in some cases to limit, certain investments in China, pursuant to the International Emergency Economic Powers Act (IEEPA). But it remains important for Congress to legislate in this area to ensure an enduring statutory foundation for the regulation of U.S. investments in China and to ensure appropriate congressional input into and oversight of an outbound investment screening program. I welcome H.R. 6349, the "Preventing Adversaries from Developing Critical Capabilities Act," which Chairman McCaul and Ranking Member Meeks, alongside other Members of Congress, introduced last November as an important framework for Congress to consider.

My opening remarks today will focus on the *why* and the *how* of regulating U.S. investment in China, and I look forward to your questions.

Why regulate American investment in China:

Public data indicates that the value of annual flows of U.S. investment to China have fallen since the late 2010s. The Rhodium Group, for example, estimates that annual flows of U.S. direct investment in China (FDI), both greenfield investment and acquisitions, fell to approximately $8 billion in 2022, down nearly 50% from peaks a decade earlier. Venture capital investment has fallen by an even more significant percentage.[1] But the stock of existing investment, including FDI, venture capital, and portfolio investment remains large: U.S. multinational companies likely have existing assets in China valued in the hundreds of billions of dollars, and Chinese companies listed in the U.S. had a market capitalization of just over $1 trillion at the beginning

[1] Reva Goujon, Charlie Vest, and Thilo Hanemann, "Big Strides in a Small Yard: The New US Outbound Investment Screening Regime," *Rhodium Group*, Aug. 11, 2023, https://rhg.com/research/big-strides-in-a-small-yard-the-new-us-outbound-investment-screening-regime/.

of last year, according to the U.S.-China Economic and Security Review Commission.[2] Moreover, the importance of an investment to U.S. national security interests is not determined solely by its value: a comparatively small investment that enabled a Chinese semiconductor firm to develop a new leading edge design could have substantial implications for U.S. national security, whereas a large investment in Chinese consumer retail shops would have a minimal impact on our national security.

In recent years Congress and the U.S. Executive Branch have begun to take important steps to address certain risks associated with U.S. investment in China. For example, U.S investors, like retirees and everyday investors, face the risk of losses associated with China's opaque investment environment. This spurred Congress in late 2020 to pass the Holding Foreign Companies Accountable Act (HFCAA), which requires Chinese companies listed in the U.S. to comply with basic U.S. audit transparency requirements.

Let me give another example. U.S. national security faces a risk when Americans invest in specific Chinese companies that are tied to the Chinese military, or in Chinese companies that engage in activities contrary to U.S. national security interests. That's why in November 2020, when my fellow panelist Matt Pottinger was serving as Deputy National Security Advisor, President Trump signed E.O. 13959, which prohibited U.S. persons from investing in the publicly traded securities of companies that the U.S. government has identified as being linked to the Chinese military. President Biden strengthened this program, the "China Military Companies Sanctions List," or "CMIC List" in June of 2021 by expanding it to also prohibit U.S. persons from investing in specific Chinese companies the U.S. government has identified as being linked to the Chinese surveillance state. Furthermore, U.S. persons are prohibited from investing in—or doing any other business with—companies that the U.S. puts on its so-called "SDN sanctions" lists, such as companies that the U.S has determined should be sanctioned for engaging in serious human rights abuses in China.

Last year, President Biden signed E.O. 14105 to regulate certain investments in key high-tech sectors in China because those investments can pose another type of risk: that U.S. investors will help China open an edge in key technologies that have both civilian and military applications. U.S. export controls, particularly after Congress strengthened them in 2018 with the Export Control Reform Act (ECRA), provide a strong tool to prevent U.S. companies from sending specific technologies to China. But export controls focus on the flow of technology, and thus are poorly designed to prevent a U.S. person from investing in a Chinese company. Prior to E.O. 14105, this created the perverse situation where the U.S. government prohibited U.S. companies from, for example, sending high-end semiconductor tools and the designs for high-end chips China. However, the U.S. did not prohibit U.S. companies, whether venture capitalists or operating companies, from investing in Chinese companies that were trying to build their own semiconductor tools and which are working to design their own leading-edge chips. This is the gap that E.O. 14105 is working to close, and Congress should enact legislation to bolster it.

---

[2] U.S.-China Economic And Security Review Commission, "Chinese Companies Listed on Major U.S. Stock Exchanges," Jan. 9, 2023, https://www.uscc.gov/sites/default/files/2023-01/Chinese_Companies_Listed_on_US_Stock_Exchanges_01_2023.pdf.

Moreover, E.O. 14105, like H.R. 6349, will help bring greater transparency to U.S. investment in China's high-tech sector, which is important for effective policymaking. The reality is that the U.S. government currently has limited insight into the nature of U.S. investments in China: for obvious and important reasons the U.S. cannot use intelligence collection tools to monitor U.S. companies to identify what they are considering investing in China. Instead, government officials must rely primarily on public and commercial databases and on private research to understand investment flows. Given the complexity and scale of both the U.S. and the Chinese economies and both countries' high-tech sectors, this leaves large gaps in the government's knowledge. Tools that require U.S investors to report certain types of higher-risk investments will increase the data available to policymakers and ultimately make for stronger policy outcomes.

How to regulate American investment in China:

When it comes to the *how* of regulating U.S. investment in China, there is an important debate here in Congress about whether to regulate U.S. investment in specific Chinese sectors or whether to focus on prohibiting investment in specific Chinese companies, for example, by putting more Chinese companies on U.S. sanctions lists.

I want to make a strong recommendation for the sectoral approach, which is the approach taken by both E.O. 14105 and by H.R. 6349. As I discussed several minutes ago the U.S. already has the authority, pursuant to the CMIC List, to restrict U.S. investment in the publicly traded securities of companies linked to China's military. But relying solely on this approach fails to capture important investments in early and mid-stage companies as well as direct investments by U.S. companies in strategic technology sectors in China.

Allow me to offer two examples to illustrate the gap. The first example is SenseTime, a Chinese surveillance technology firm whose surveillance technology China has deployed in its Xinjiang province. SenseTime was founded in 2014 and U.S. investors started investing in the firm by at least 2017, according to publicly available data. But in 2017, when those investments were being made, SenseTime remained a mid-size company worth a few billion dollars that almost no American government officials had heard of and which was still in the comparatively early stages of developing its technology. As a result, it would have been practically impossible for SenseTime to be on a relevant U.S. government list at that time, and, indeed, SenseTime was not on any U.S. government restriction lists in 2017. Later, as the company continued to grow, U.S. policymakers began to understand the risks the company posed, adding SenseTime to the Entity List export controls restriction in 2019 and to the CMIC List in 2021. But sectoral regulations on U.S. AI investment in China, like those contained in E.O. 14105 and H.R. 6349, would have required U.S. investors to disclose their investments to the U.S. government—which would have brought SenseTime to the U.S. government's attention much earlier and likely resulted in such investments being prohibited several years before they actually were.

Let me give another example, a hypothetical. Suppose that a U.S. company chooses to set up a high-tech AI research lab in China. There are many reasons why a U.S. company might choose to do so, for example, to have access to China's significant domestic engineering talent and to keep an eye on technology developments within China. Yet the U.S.-owned high-tech research lab would undoubtedly provide value to China over time—it would bring together top Chinese talent, provide funding for research, offer professional exposure, and foster innovation. After improving their skills, Chinese employees of the lab could well go on to work for competitors or found their own companies, just as engineers at U.S.-based corporate research labs do. The U.S. government has a clear interest in understanding what this type of high-end research lab is doing, and ensuring that it is not engaging in activities that could, over time, strengthen China's relative capabilities. Yet because this hypothetical lab is owned and run by a U.S. company in China, it would never by covered by an outbound investment regime that simply prohibited investment in designated Chinese companies.

I do not want to suggest that U.S. companies should be prohibited from doing any high-tech research in China. There is strong engineering talent in China and I want U.S. companies, where consistent with national security, to be able to benefit from that. Indeed, that is one reason I welcome recent work the State Department and DHS to expand visas for top AI and other technical scientists and researchers to come to the U.S. to innovate here. But in our era of geopolitical competition, the government has a legitimate interest in understanding investments in key technologies and sectors in China and, where appropriate, regulating those investments.

Keeping regulations narrow:

In considering legislation to further restrict U.S. investment in key sectors and technologies in China, I urge Congress to pass a narrow and tailored approach.

Regulating U.S. investment in China is very different than just banning investment in a small economy like Iran or North Korea, which we have done with our sanctions. The scale of the economic relationship is vastly bigger, making the economic stakes for U.S. companies and the United States much larger. The U.S. has an interest in ensuring that it does not prohibit investments that pose no national security risk to the U.S., but which have the potential to benefit U.S. companies and ordinary Chinese consumers. The goal should not be to cut off all investment ties, but rather to address discrete national security risks. The implementation challenges of regulating U.S. investment in China are also harder, creating a need for to build appropriate government staff and expertise to analyze and regulate investment. A narrowly tailored approach that focuses on critical technology sectors is a valuable start. Over time, I would recommend also at least requiring disclosures of investments that could increase China's leverage over critical U.S. supply chains, and potentially regulating them—but those are the sorts of expansions that can be added after the program is initially established and up and running.

Other actions:

Beyond enacting legislation that would codify and expand on the type of investment regime the Biden Administration is developing pursuant to E.O. 14105, there at least two other steps that I recommend Congress and the Executive Branch consider to effectively regulate the U.S.-China investment relationship.

First, basic data about U.S. investment in China remains far too opaque. The Biden Administration's outbound investment regime, and legislation such as H.R. 6349, if passed, should begin to bring transparency to U.S. investments in the covered sectors. But a substantial share of U.S. investment in China will not be covered by such a regime. Congress could direct the Treasury Department and Commerce Department to expand the type and frequency of data the agencies currently compile and publish about the U.S. investment position in China to better inform both policymakers and the public about investment stocks and trends, as Derek Scissors at the American Enterprise Institute has recommended.

Second, I have spoken about the value of the existing China Military Industrial Complex Sanctions Program to limit investment in specific companies that support the Chinese military. However, the Biden Administration could strengthen this program by more actively reviewing companies for inclusion on the list. Moreover, while this program currently prohibits U.S. investment in the publicly traded securities of covered Chinese companies, it does not prohibit private investments, such as bank loans, in the same companies. The Biden Administration could expand the scope of the prohibitions to cover all new investments in the covered companies.

Concluding remarks:

In closing, let me step back and offer a broader comment on the U.S.-China economic relationship. The U.S. and China are the world's two largest economies. While U.S. trade dependencies on China are declining, economic ties between the two countries will likely remain substantial in the years ahead, with hundreds of billions of dollars of economic activity at stake in the relationship. The U.S and China are also major geopolitical competitors, and the economic and technological domains are central to that competition.

Against this backdrop, there are no simple answers for what the U.S.-China economic relationship should look like. We need to manage the economic relationship to derisk strategic dependencies and to maintain our economic and technological edge. We need to manage the economic relationship to promote our national security interests. But we also need to manage the economic relationship to promote strategic stability, and to support U.S. economic interests while remaining true to our values. There are times when geopolitical tensions will be higher, and the U.S. will need to respond by tightening controls on economic and technological ties. Hopefully, there will also be times when tensions will be lower, and we can enable more economic activity.

Managing the economic and technological relationship will be as much an art as a science. But across the ups and downs, American policymakers need a flexible regulatory toolkit to manage the economic and technological relationship to ensure that it promotes America's national security interest. Tools to manage investment flows to ensure that American investment in China is consistent, with rather than contrary to, U.S. national security interests are a key component of that overall toolkit. I welcome the Committee's interest in developing effective policy tools to regulate American investment in China and look forward to taking your questions.

Chairman MCCAUL. Thank you, Mr. Harrell. Let me just say first, you know, I have been studying this issue for quite some time.

Mr. Pottinger, you were the architect of the Trump Administration's China policy. I was in full agreement. In fact, your team was the one that came to me, and Secretary Pompeo, and National Security Advisor O'Brien regarding the CHIPS Act that we were able to pass to get off the supply chain that threatens our national security issue. But when I looked at the way Treasury works with sanctions on the entity approach, as you mentioned, versus the sector-based approach, it seemed to make more and more sense to me.

I had a discussion with Undersecretary Estevez of the Bureau of Industry and Security. And he said instead of just providing a sanction on a company, and then China will turn around and call it something else the next day or take it off the books, the sanction has no effect. And they are very smart about this.

So we started talking about this sector-based approach, and the key sectors are the semiconductors, AI, quantum, hypersonics, high-performance computing. And to your point, Mr. Harrell, we know these are the sectors that go right into the PLA's military war machine or civil-military fusion. So if we have a prohibition based on the sector, to me, that seems to be more effective than this entity-based approach that can change overnight.

I want to get your thoughts on that.

Mr. POTTINGER. Mr. Chairman, I agree with Peter's opening remark on that very point. I think your point was that it is much simpler. It is less confusing for American businesses. It is less resource intensive.

That is not to say that I do not think that the Treasury Department should have authorities to target specific entities, but a sector-by-sector approach is just much more clear-cut. It allows for the compliance teams at various American financial institutions and investment funds to simply adjust and not to get caught in this very complex web of subsidiaries and shell companies.

The Treasury Department has had the authority to target Chinese military-affiliated companies going all the way back to late 2020. President Trump signed a couple of executive orders that gave them that authority. President Biden reaffirmed with some changes, his own executive order to that effect.

But since then, I think only 68 companies have been added to the list of prohibited Chinese firms for American investment, and I can tell you that the galaxy of Chinese entities that are involved in China's military modernization is many, many orders of magnitude greater than the number 68.

Chairman MCCAUL. That is very good. So when you look at export controls, this committee has jurisdiction over that as well, but it seems to me that alone is not going to solve this problem, and that is dual-use technologies.

I remember prosecuting the Johnny Chung case of the money that was coming from China, military intelligence, China air space, funneled through his Hong Kong bank accounts to influence the Presidential election. Why? Because they wanted the satellite technology, aerospace. They also wanted to become part of the WTO, and guess what? They got all of it. And that was 1997. Where are they today?

So, I think using both the export control laws that we have that Mr. Meeks and I worked on, but also the sector-based approach on capital flows going into China, that combination seems to be a powerful one, in my opinion.

Mr. POTTINGER. I agree. And I commend the bipartisan spirit reflected today in Congressman Meeks' remarks, as well.

Chairman MCCAUL. I do not know if you have noticed, it is a little rare these days. Mr. Harrell, just one thing, you know, defining technologies, like advanced semiconductors, AI, or quantum, we did this with AI. In terms of the business community understanding what we are talking about when we talk about a sector, can you elaborate on that?

Mr. HARRELL. Absolutely, Mr. Chairman. Obviously, in implementing legislation like this or the Biden Administration's executive order, you are going to need a rulemaking process that is going to lay out in some detail exactly what parts of the semiconductor ecosystem we are talking about here, the most advanced, and what parts of the AI ecosystem we are talking about here, not just kind of customer service chatbots but the high-end models that we are actually concerned about. But the thing is that we have that experience in export controls where we have had to define a lot of different kinds of semiconductor technology. The business community understands that regime, and they will understand that regime when, with appropriate tailoring, you move it over to an investment, a complementary investment restriction regime.

Chairman MCCAUL. Thank you. The chair recognizes Mr. Meeks.

Mr. MEEKS. Thank you, Mr. Chairman. I thank both of you for your statements. I think that they were excellent and show the bipartisan nature of both Administrations on this particular issue, which I think is extremely important.

You know, in recent years, consecutive Administrations and congresses have strengthened the United States' foreign investment review and export control authorities to bolster national security protection. But, Mr. Pottinger, I will start with you, you know, because I hear some things come back and forth to me about our existing CFIUS process, sanctions and export controls. Can you tell us what are some of the critical problems that an outbound regime should tackle that cannot be addressed through CFIUS sanctions or export control regimes?

Mr. POTTINGER. Thank you, Congressman. You know, it is interesting that the money that is represented by, you know, big name private equity and venture capital firms in the United States represents more than just the dollar signs. It represents know-how. It represents networks to talent and board members and technologies that reside in the portfolios of these venture capital firms that then work at the service of other companies in their investment portfolios, including companies in China.

So if we look at something like export controls are kind of a lagging indicator. It takes a long time for us to even recognize new technologies that are being developed in China, for example, using U.S. capital and some U.S. know-how. By the time those technologies mature and are ready to be harvested by smart people scouting technology for the Chinese intelligence agencies or for the Chinese military, the cat is already out of the bag, the horse is out of the barn, whatever farm animal, you know, analogy you like; it is too late.

And so I think the reason that we were focused, particularly in 2020 during the Trump Administration and Peter and colleagues who are currently and recently in the Biden Administration have been focused on trying to close that loophole to actually capture technologies before those seeds are planted and before they can sprout into something that is going to be weaponized against us.

Mr. MEEKS. So let me just followup that up with Mr. Harrell. So those gaps, can you tell us specifically how the Biden Administration's outbound executive order addresses them?

Mr. HARRELL. Absolutely, Congressman. And thank you for the question. Let me give a hypothetical example that I think will help illustrate the gap here that we are all trying to close.

So since October 2022, the Biden Administration, with strong support from Congress, has imposed pretty tough export controls on China in semiconductors where U.S. companies cannot send tools and designs for high-end semiconductors to China. How is China responding to this? Well, they are trying to build an indigenous capability for those same tools and designs.

Export controls alone do not provide a tool to prevent an American venture capitalist from saying, you know what, that is an interesting opportunity. I might not be able to ship a tool over to China, but I could invest $20 million in this upstart Chinese firm that is trying to build that same tool or that same design here in China. And then, as Matt says, helping that Chinese firm recruit talent, helping that Chinese firm build contacts in the industry to help them grow, because none of that expertise is technology. The export control just focuses on the technology, and what we are worried about is that the capital can still go over there to help them innovate around our export controls, which is why I think an approach like that in your bill, sir, would be helpful in closing that gap.

Mr. MEEKS. Thank you. And I will try to get this in real quick because the Biden executive order identifies three sectors that are critical for the military, intelligence, and surveillance or cyber-enabled capabilities of the PRC that could cause or pose a national security threat to the United States: semiconductors, microelectronics, and quantum information.

So either Mr. Pottinger or Mr. Harrell, in the short time that I have or do not have, what are the benefits of utilizing a sector-based approach for countries of concern instead of having a case-by-case review or a company-by-company based approach to address outbound investment?

Mr. HARRELL. Just very briefly, Congressman. I actually think there is a helpful lesson again from export controls. So when Matt was in the White House, the Trump Administration took very important actions against a couple of Chinese technology firms, like Huawei Technologies, limiting exports from Huawei. What we have seen since is that China, of course, sets up lots of front companies and other companies to get that technology that Huawei then couldn't get, which is why in October 2022, with its export controls, the Biden Administration expanded beyond this company-by-company approach to go after semiconductors going to China as a whole, and I think that lesson in how China evaded the export controls shows why, in the investment regime, as well, we should have a sectoral and not just a company-by-company approach.

Chairman MCCAUL. The gentleman yields. The chair recognizes Mr. Smith.

Mr. SMITH. Thank you very much, Mr. Chairman. Thank you for your bill, 6349, you and Ranking Member Meeks, an excellent piece of legislation, and I do hope it becomes law sooner rather than later and then is faithfully implemented. So often we get great bills passed, and I do not care who is in the White House, implementation falls far short.

But let me just say, you know, often we quote the fact that, you know, there was a famous quote that came out of the Soviet Union: we'll hang the West and they'll sell us the rope. That has never applied to the Soviet Union. It applies to China, especially under Xi Jinping. I was one of those who led the effort against MFN delinking of human rights. I believe when Clinton delinked MFN from human rights on May 26, 1994, that was a catastrophic game-changer for the dictatorship, and ever since they have believed, and maybe rightfully, with some exceptions, that they can do whatever they want and no sanctions will be forthcoming that are meaningful.

I held hearings on not allowing China in the WTO, believing that they would change the WTO and not the other way around. And it is my sense that that has been somewhat vindicated, that view. And we have had hearings over the years, many of them. I have chaired 97 hearings on human rights abuse in China; we just counted them up. I am shocked that we still have not learned, and that is why this bill is so important, we still have not learned that they will do everything they can to take anything we sell, particularly in the area of electronics and really high tech, and use it dual use, use it for the military. They have been doing that for decades. We do not learn. We think somehow, if you trade more, they will matriculate from dictatorship to a democracy. Not going to happen under Xi Jinping and the CCP.

Outbound investment is a very, very good concept that needs to be further backed up through law, and I would also add outbound enabling. You know, I got a bill passed almost a year ago, and it was totally bipartisan, two votes against it on the floor of the House, to try to end, certainly expose and end the egregious practice of forced organ harvesting. Tens of thousands of young people, average age 28, are killed to get two or three of their organs each and every year. The problem is not only a gross human rights abuse, but it is absolutely being enabled by the PLA. And there is even a hospital, a 301 military hospital in Beijing where, you know, if Xi Jinping wants a new liver, he will probably get it from a Falun Gong practitioner who is 28 years old. I mean, how perverse is that?

So I would like, you know, from our panel, and I thank you both for your expertise, are you aware of the PLA's role in this terrible practice? And, again, what are they doing is, they do it with all kinds of pharmaceuticals, they try to get a monopoly on just about everything. But in this case, it is a huge moneymaker for the PLA. It is also a way of regenerative medicine for their elite and for their military. Your thoughts.

Mr. POTTINGER. Congressman, thanks for your leadership over the years on China human rights. I wish we had all listened when you had the foresight 30 years ago on most favored nation status. That really was, you know, the snowball that led to an avalanche.

China's human rights abuses are so grotesque and the scope is so big now with what is happening in the northwest of the country, in Xinjiang, whole ethnic groups which are being—well, in the words of both then Secretary of State Pompeo and current Secretary of State Tony Blinken, it is a genocide. I have heard over the years about and partly thanks to what you have uncovered with witnesses that you have spoken to over the years, the forced organ transplant business, I would not be shocked to learn the full scale of that industry, but I do not have particular insight right now into the scale of it.

Mr. HARRELL. Yes, I just want to echo Matt in thanking you, Congressman, for your leadership on the human rights issue over many, many years, a really important set of issues with respect to China. Unfortunately, like Matt, I do not have specific insight into what the PLA is doing on organ harvesting.

Mr. SMITH. I appreciate that. Well, our bill, it has been languishing in the Senate for months, would, in addition to sanctioning those who are, with knowledge, procuring these organs, it would do a serious work within the U.S. Department of State to investigate and to expose. That is the beginning of trying to bring an end to this horrible abuse. But, again, the PLA is benefiting usually from it. I yield back.

Chairman MCCAUL. The gentleman yields. The chair recognizes Mr. Sherman.

Mr. SHERMAN. Mr. Chairman, thank you for holding these hearings. I would like to put in the record a list of nine hearings of the Financial Services Committee that are relevant to this hearing.

Chairman MCCAUL. Without objection, so ordered.

Mr. SHERMAN. And, in particular, we have dealt in the Financial Services Committee on making sure that American investors do not get phony financial statements and that Chinese companies are not able to raise money from American investors with phony financial statements, and Senator Kennedy and I have passed the Holding Foreign Companies Accountable Act and the Accelerating Holding Foreign Companies Accountable Act to at least deal with that issue. We also had a hearing earlier last year on combating the economic threat from China.

There are two aspects to this. There is the macroeconomics: does China have enough capital to build its economy; and the micro: can a particular company get its hands on an idea, a technology, an introduction? What is not polite to mention is the enormous trade deficit. We are running a trade deficit of a third of a trillion dollars with China, so every 10 years they have $3 trillion of capital decade after decade that they can deploy where pretty much wherever they want. Why this trade deficit? Well, both our countries are mercantilist to some degree. We want to export more, import less, we want more investment in the United States, less investment elsewhere. But China has two ways to achieve this. First, they could have tariffs. Second, they can orally tell their companies just do not buy the American stuff. I cannot imagine a Member of Congress calling a company in our district and telling them do not buy the Chinese stuff, do not buy the German cars.

But China has higher tariffs on our goods than we have on theirs. So we have only one device and, even as to that device, they are using it better. We, therefore, have a situation where China has $1.2 trillion of our bonds. We need that capital because we have to finance our trade deficit. Now that as to debt equity. As to stocks and other equity investments, the flows are roughly equal.

Now, one of our witnesses mentioned that venture capital situation. A company needs $20 million. I do not think we are going to be able to stop that because, if it is a good investment, the Chinese have $20 million. They have, as I say, a third of a trillion every year just from their trade surplus.

But we can deal with the technology. We saw an example a decade and a half ago where American satellites were being put into space on Chinese rockets. What happened? Our satellite companies and their insurers found it in their interests to make sure the rockets did not blow up. So they provided good technical advice to China, and now China has better rockets.

When we have a situation where Americans have it in their interest to transfer technology to China, it will be transferred. And it may not be a patent; we can outlaw that. But unless we outlaw the kind of investment where you have a controlling interest, when you are a consulting company, when you are a venture capitalist, and prevent the flow of technology there, we will continue to provide advice and contacts and know-how to Chinese companies.

I commend the chairman and the ranking member for their bill. There is more to be done. I am working on legislation to make sure that we do not see—that every American company disclose to its shareholders its China risk and what it is doing to prevent its China risk for two reasons. First, so that the investors will know. Second, so the company will start working, as they have not sufficiently, on derisking themselves from China. Second, we have got to prevent index funds from investing in China because this is not paint by the numbers. It is too complex to figure out how and which companies in China to invest in. Third, on the human rights side, we have to prohibit American investment in sanctioned companies, particularly those sanctioned for the activities that Chris Smith recounted for us. It may not deprive those companies of capital, but it will at least prevent us from being involved. And fourth and most importantly, we need to prevent a capital gains allowance for investing in Chinese companies. This costs our Treasury many tens of billions of dollars. And I will ask our witnesses: does it make any sense for us to be providing an investor with a low tax rate on profits they make by investing in Chinese companies? Do either of you think that is a good idea?

Mr. POTTINGER. I do not like that idea. That is to say that we are giving tax incentives to invest in our chief adversary.

Mr. SHERMAN. And I will point out China has incentives for investment that are only applied to investing in China. So it is both unfair and stupid for us to be providing a capital gains allowance, and I look forward to working with members on this committee to make sure that the capital gains allowance, which is designed to get people to invest in building an economy, is not an incentive to build a Chinese economy. And I yield back.

Chairman MCCAUL. Excellent point. The chair recognizes Mr. Wilson.

Mr. WILSON. Thank you, Chairman Mike McCaul, and I also want to thank Ranking Member Greg Meeks for the bipartisan dedication to exposing the single-party dictatorship of the Chinese Communist Party. And it is also very revealing that, amazingly enough, I agree with everything that Congressman Brad Sherman just said. And I do not want to ruin his reputation back home, but, hey, I even agreed frequently with Kathy Manning, too. So I am going to, I will brand several of you. Hey, we are working together in a bipartisan manner on this.

It is sad to me that the people of China are impressed by the Chinese Communist Party. I appreciate firsthand the people of China. My father, First Lieutenant Hugh Wilson, served in the Flying Tigers, the 14th Air Force, in Kunming, Shantou, and Xinjiang. Our family has great affection for the people of China. We are inspired by the people of Taiwan in this week's elections. Courageously, the Taiwanese have voted for democracy and freedom. Taiwan is a beacon of success for a free market democracy.

With that in mind, Mr. Pottinger, since the murderous October 7th terrorist attacks by Iran puppets of Hamas into Israel, the Chinese Communist Party has stepped up their outreach to the gulf allies of America and partners, hoping to capitalize on destabilization caused by the Iranian regime's terrorist networks and is working together with war criminal Putin to gain a foothold in the region. There is a significant increase in media by the Chinese Communist Party and by war criminal Putin across the region in Arabic.

The question: how do you see the CCP working to increase its influence interview he Middle East and what can be done to counter the increased role in the region and how is the threat to U.S. interests, as we, sadly, are in a conflict we did not choose, of dictators with rule of gun invading democracies with rule of law?

Mr. POTTINGER. Congressman, thank you for those comments. And I would love to see photos of your father in Kunming with the P–40 Flying Tiger. Fantastic legacy. Brilliant.

Look, I think you are exactly right that these conflicts that are beginning to spread us thin are, in fact, related. I believe the incoming Chinese foreign minister was here recently and made a remark to a U.S. audience when he was in the U.S. specifically that they are not related. Of course he would say that. They are very much related. China is the number-one backer economically for Russia, certainly diplomatically for Russia. According to a State Department report that came out last year from the Global Engagement Center, China is spending more money on pro-Russian propaganda worldwide than Russia is spending on pro-Russian propaganda worldwide.

China is a key backer for Iran. It is no coincidence, I liked the way that you put it, that they are trying to capitalize on this situation. I have noticed that Chinese shipping is not affected in the Red Sea the same way that everyone else's shipping is. That is not by accident. That is being engineered by virtue of the fact that China is one of the main buyers of Iranian oil. These things are related.

And I will paraphrase Xi Jinping, who has said something frequently, going back at least to 2021. He has given internal speeches where he has said the lead word to describe the global situation today is chaos. Chaos. And he has gone on in those speeches to make clear that he views that as a favorable condition for China achieving its ambitions worldwide.

So here we are. Chaos is something that is part of the design of China's global ambitions and of its foreign policy, and we, at our peril, fail to connect those dots. Those dots are very much connected, sir.

Mr. WILSON. Indeed they are. And I really appreciate, one of the great achievements of President Donald Trump were the Abraham Accords to provide stability and success for our Middle Eastern allies. And then, sadly, I really believe one of the reasons that Iran, through their puppets of Hamas, attacked murderously and conducted the mass murder in Israel was to disrupt the ability of Saudi Arabia to join in, which would have been so beneficial to Saudi Arabia and to the Middle East region.

And so with that, I thank both of you for being here, but I really want to thank again the chairman and ranking member. All of this needs to be exposed. I yield back.

Chairman MCCAUL. The gentleman yields, and I appreciate the, you know, you mention Abraham Accords. The security agreement with the Saudis, it is going to be so important between Israel and the United States and Saudi Arabia. It could truly bring peace to that region. So thanks for bringing that up.

The chair recognizes Mr. Bera.

Mr. BERA. Thank you, Mr. Chairman. And for the millions of viewers on C-SPAN that are watching this, the media does not cover the bipartisan nature of how Democrats and Republicans work on policy. I commend the chairman and the ranking member and the members of this committee to work on a challenge that addresses our vulnerabilities as a nation but also strengthens America's security.

If we were to go back a decade, two decades, three decades ago, you know, there was a hope that, you know, as China built a middle class, an entrepreneurial class, that they would become responsible partners in a global economy. Obviously, that isn't where we are today. We clearly understand what Xi Jinping's policy objectives are, what Beijing's policy objectives are, and we have to address the reality that we face today.

I think, Mr. Pottinger, I would use the term the panda has left the zoo. The panda has left the zoo, so I think we have got to address that.

Mr. Harrell, you used a statement, I think, is important for us to understand. I think the term you used was a civil-military fusion doctrine. And if you could just take a minute to expand on that doctrine.

Mr. HARRELL. Absolutely. So this has been one of the defining societal doctrines in China, particularly under Xi Jinping, where, under Xi Jinping thought, if you will, and, certainly, he calls it Xi Jinping thought, there is an idea of mobilizing all of China's society behind China's ultimately military aims. And so what we have seen over the last, well, going back many years but particularly over the last decade is increased efforts, not only through sort of official spending and subsidies but through a variety of regulatory mechanisms, as well as informal mechanisms, to galvanize China's technology sector, universities, major SOEs behind building China's military might, such that, sort of to come back to today's hearing, I think really only a sectoral approach that says we are going to limit investment in these key sectors is going to work to prevent Americans from supporting the development of those key technologies in China because, if you just go after one or two firms, China's response is we're just galvanizing all the other firms in this sector to do what that firm can no longer do.

Mr. BERA. So super important for American and Western industry and investors to really understand the root of that doctrine and the foundation. These may be patriotic companies that are profit-driven, that are just looking for good investment opportunities; but if they do not truly have an understanding of how those investments potentially could be used to undermine our own national security.

Mr. Pottinger, let me ask you a question that touches on that. International coalitions are going to be important. And, again, I commend the chairman for his work on the CHIPS Act, an incredibly important piece of legislation. You know, Micron has a presence in my community, and we saw some economic retaliation from China on Micron. I do think we were successful in keeping, you know, international companies from seeing a market opportunity and saying, OK, well, we will go and undermine that. But I think it will be really important for us to have these international Western coalitions of like-valued countries that understand this. It won't be easy, but I think it is important.

Mr. POTTINGER. Congressman, I agree with you. And I found that, over the years, when the U.S. leads, our allies tend to eventually follow, sometimes very quickly. In the case of sanctions on Russia, I mean, it would have been even better if we had credibly threatened them in advance of an invasion by Putin, war criminal Putin, as Congressman Wilson, put it, which is a great title for Vladimir Putin. It would have been better to have had that advance, but, once that invasion began, the G7 and other allies began to coalesce very quickly. So I think it is incumbent upon the United States to lead and others will follow.

You made a comment a moment ago just about how private equity firms and others, you know, often need to be told or, actually, in some cases, want to be given those guardrails. I have had conversations with investment funds that have said, look, we have a compliance shop. If Congress will tell us where those guardrails are, we will abide. And in some cases, they want those guardrails to come in more tightly because that means that they are not missing out on opportunities that, you know, less scrupulous competitors could take advantage of. And then, over time, it is not just American competitors but others in Europe and Japan and elsewhere that will follow with similar types of rules and regulations.

Mr. BERA. Great. Again, I commend the chairman and the ranking member for their work and leadership on this topic.

Chairman MCCAUL. Thank you, Mr. Bera. The chair recognizes Mr. Mast.

Mr. MAST. Thank you, Mr. Chairman. I appreciate the expertise you both bring today, the work that you all have done. I am over here, Mr. Pottinger. I know you were looking for where we are at. I have read work from both of you over the years. I want to start with you, Mr. Pottinger. How many times can you recall in speeches Xi Jinping talking about preparing for war?

Mr. POTTINGER. Well, Congressman, last March, so less than a year ago, China held its annual two meetings, what they call the lianghui, two meetings. It means the National People's Congress and another gathering called the Chinese People's Political Consultative Conference.

Mr. MAST. Simultaneously.

Mr. POTTINGER. Simultaneously. Xi Jinping gave four addresses to delegates to those two meetings. All four of them had the common theme of the need for China to prepare for war. And in the lead-up, there were changes that were being made to laws, for example, on making it easier to put the military in charge of Chinese society in the event of war; new rules to retain reserve military personnel for longer periods of time, particularly if they have key skills; new mobilization, military mobilization offices that have popped up in most of the provinces around China; building air raid shelters right across from Taiwan, as well as starting to create authorities for building military hospitals that can do combat care. I do not take comfort in any of those signals, any one of them, much less the constellation that is painted by all of them combined.

So I think that war is on Xi Jinping's mind. He has told us as much.

Mr. MAST. Anybody preparing for war, obviously they are looking at a number of different facets of where they could weaken their enemy. And whether that is through their military might, whether that is economically, whether that is in any place domestically, there could be a host of places that they try. What worries you most out of any of those areas that you see them working to weaken the United States of America as they prepare for war?

Mr. POTTINGER. Well, I think that all of the things that add up to deterrence are built on one factor in particular, and that is hard military might, the credible availability of decisive military force. I worry that if we do not keep pace with the crises that Beijing, in some cases, is adding fuel to, we will not have sufficient capacity, munitions, whether it is torpedoes or anti-ship missiles or the ability to build more of those things relatively quickly. It is not like the days of World War II with Rosie the Riveter where you can build bombs on what the day before was an auto factory quickly. These are very sophisticated munitions that take sometimes years for those supply chains to add up.

So my biggest concern is we do not meet this moment that Xi Jinping is talking about as a moment where he can take advantage of what he calls an opportunity of a hundred years.

Mr. MAST. We quite often in this body talk about the Belt and Road Initiative and largely focus on these developing countries where they can put a road in, extract something that they need for their supply chain. To that effect, I do not think we look enough internally about where does the U.S. investor, the U.S. investment into China, how is that making us subservient to that Belt and Road Initiative as Americans and where does that advance their preparation or where could it pull their preparation back were that U.S. investment to decrease?

Mr. POTTINGER. Well, the Belt and Road Initiative is really a vehicle for corruption. It is a means to expand China's influence around the world through co-opting elites and governing elites in foreign countries. There is a reason why most of the Belt and Road agreements that China signs with foreign governments are not available to the light of day. They are secret. Some of them have been leaked over the years, and they have these common patterns to them. They involve countries pledging sovereign assets, I mean, things that belong to the people of those countries, whether it is a port or it is telecommunications and rail infrastructure. And so China is weakening the ability really of those countries' people to maintain something like a democratic—in some cases they are democracies and that democracy is at risk or they aspire to be democracies and are undermined by the enormous debt and corruption that these agreements saddle on them. So that hurts our interests. When corruption and co-optation of elites is the mode for advancing power in the world, that is terrible for our values and our influence.

Mr. MAST. Thank you, Mr. Chairman.

Chairman MCCAUL. The chair recognizes Ms. Manning.

Ms. MANNING. Thank you, Chairman McCaul and Ranking Member Meeks, for holding this hearing. And I do appreciate the bipartisan nature of the hearing on this critically important issue. And thank you to our witnesses for being here today.

I want to get into some of the details that are involved in this issue. So, Mr. Harrell, in your view, which Chinese State activities or industrial policies, including the forced or coerced transfer of technology, IP theft, data localization, or others, which pose the greatest risks to our national security and how can greater scrutiny of our outbound investments help combat these practices?

Mr. HARRELL. I think there are many things, obviously, the Chinese do that pose a threat to U.S. national security, but I want to focus on two in response to your question. I think, fundamentally, we need to keep an edge in a number of critical high-technology areas that are going to be hugely important to both military and economic and societal goals over the next decade. And here I am thinking semiconductors, AI, quantum, certain parts of the green technology revolution, that are coming where we need to both be innovating more here at home and then we need to make sure that our technology and our expertise is not helping them catch up and indeed overcome. And that is why I really think that on those kind of key technologies, making sure we have both an export control regime so we do not give those technologies, semiconductors, green technologies, AI, a couple of other sort of high-end military dual-use technologies, both we are not giving them the technologies and also our capital and kind of business know-how expertises and helping them catch up and ultimately overcoming us.

Separately a little bit from the focus of today's hearing but I do think is important is making sure we are not dependent on China for key supply chain inputs, things like critical minerals, things where, if we got to that situation where there is a conflict, they would have leverage over us. A little separate from today's hearing, but I know the committee has done important work on those supply chain vulnerabilities and would urge the committee to continue that work, as well as the focus on technology and investment we are talking about today.

Ms. MANNING. Great. Thank you. And I want to focus in a little bit on the AI issue. While the Biden executive order on outbound investment pertains to AI, not all applications and investments in AI technology are equally risky to our national security. You mentioned in your testimony the need for greater scrutiny into high-level AI research lab owned and run by a U.S. company in China. How should our outbound investment regime treat different types of research or applications within a sector like AI?

Mr. HARRELL. So when I was in the Administration working on the Biden Administration's executive order, which came out after I left, this definitional issue was one of the most complicated ones because the goal, at least from the Administration's perspective, is not to sort of prevent a Chinese hotel from having a chatbot, you know, for basic customer service. I think what we have seen is a need to focus on a couple of different types of AI. One is obvious, which is specific applications of AI that have clear military or other harmful impacts, like facial recognition and other kinds of AI-enabled surveillance technologies. We clearly need to focus on that.

I also think we need to focus on the underlying development of advanced high-end models like we have seen here in the U.S. with ChatGPT–3, ChatGPT–4, because the reality is, if China develops those models, they can then develop the applications of them. So I focus on both a set of applications and then also higher-end large-language models and other large-application models generally.

Ms. MANNING. So one of the areas that I focus on where I think we continue to miss the boat in this country is the need to reform and update our immigration laws. They have not kept up with the economic needs of our country. So I think, in your testimony, you welcome State Department and DHS efforts to expand visas for top AI and other technical scientists and researchers to come to the U.S. to help us innovate here. Can you talk about how we can leverage visa and immigration policies in ways that best serve our interests?

Mr. HARRELL. I very much appreciate that question and your focus and leadership on this issue. As part of the Biden Administration's AI executive order a couple of months ago, a little-noticed provision in there directed the State Department, DHS, to set up a program to speed visas for top AI researchers, including in China, so that we can actually get them to come here and innovate and help do research here. Now, of course, there are security risks. You need to think through, you know, the vetting process. But, ultimately, I think we want to have a country where we continue to bring the best AI talent from around the world and have them come here and develop those innovations here. The Administration is doing what it can under existing authorities, but, obviously, immigration requires statutory change, including in this area. And so I do urge the committee to look at that important issue.

Ms. MANNING. Amen I meant to say. My time is expired. Mr. Pottinger, I have some questions for you that I will submit in writing, but thank you and I yield back.

Chairman MCCAUL. The gentlelady yields. The chair recognizes Mr. Barr.

Mr. BARR. Well, let me first thank and commend Chairman McCaul and Ranking Member Meeks for their work and certainly very well intended to protect our national security by restricting U.S. investors for unwittingly financing certain sectors in China that threaten our national security, and I share their goal. But I do want to unpack this discussion about an entity-based approach versus a sector-based approach, and, first of all, the chairman and I have had many discussions on this in working through this with other colleagues on both this committee and the Financial Services Committee. I do not think the two are necessarily incompatible, and we are working on potentially marrying both approaches. But I also would disagree with the suggestion, respectfully, that a sector-based approach is, quote, stronger than an entity-based sanctions approach when, in some cases, in some cases, the exact opposite is true.

So let's unpack that for a minute here, Mr. Pottinger. Does a sector-based outbound investment restriction block Beijing-directed subsidies at a state-owned enterprise?

Mr. POTTINGER. Not necessarily. Right? If these are Chinese-invested companies——

Mr. BARR. Right. So if we are restricting Americans from investing in a Chinese military company but it is subsidized by Beijing, that regime does not affect the funding of that entity.

Mr. POTTINGER. Right.

Mr. BARR. And then revenue generated by the sales of goods and services, if the Chinese military or surveillance or technology company is selling goods and services globally, restricting U.S. investment does not impact that, correct?

Mr. POTTINGER. That is true.

Mr. BARR. Also, investment from non-U.S. investors, does a restriction on U.S. investment, outbound investment, does that impede investment from non-U.S. investors into that Chinese entity?

Mr. POTTINGER. No, not unless we build a coalition to support that goal.

Mr. BARR. And, Mr. Harrell, would the Biden executive order, does that, in any way, that is the CMIC companies, the Chinese military industrial complex companies, are investors in other countries in any way affected by that executive order?

Mr. HARRELL. They are not directly affected by it, though they cannot use a U.S. bank to facilitate that investment. So it probably makes it a little harder for——

Mr. BARR. So here is the point I am trying to make: would full-blocking SDN sanctions, if Treasury actually did it, would full-blocking SDN sanctions have a multilateral extraterritorial effect that these restrictions that only apply to U.S. investors have? Would a full-blocking SDN sanction have a multilateral extrajurisdictional effect?

Mr. POTTINGER. Yes.

Mr. BARR. So this is why I think we ought to not just dismiss this entity-based approach. And, certainly, the chairman is right and you all are right that China changes names and whatnot, but OFAC is particularly equipped in conjunction with the intelligence community to continue to adjust those sanctions.

I want to also mention the fact that the Financial Services Committee bill that we have marked up, the Chinese Military Surveillance Companies Sanctions Act, would require Treasury. And I think this letter that Treasury sent back to the chairman and ranking member on Hikvision is troubling, but that is exactly why the Financial Services Committee bill would require Treasury to not just send a perfunctory letter back to the chairman but require Treasury to do much more than that and inform the chairman of this committee, the Financial Services Committee, the Senate counterparts, on an annual basis why the Treasury Department is not imposing full-blocking sanctions on Hikvision and continually update the sanctions list, the Entity List at Commerce, the CMIC list, the DoD military list on an annual basis to keep up with the changes with China.

Last point and it is a question about the bill before us today. What I am worried about, and it is a good bill, but on page 20 and 21, it specifically talks about exceptions, covered activity. Covered activity does not include an investment in publicly traded security or an index fund or a mutual fund or a venture capital fund. In other words, we might be restricting the funding, U.S. funding, but Americans, under this bill, because there is not full SDN-blocking sanctions, would still be able to trade in those securities, whereas if we sanctioned, full-blocking sanctions, on these entities, there could be no trading of these securities at all. There could be no contracts, and it would not just apply to U.S. but also non-U.S. citizens.

My time is expired, but if you could comment on the strength of sanctions versus a non-sanctions approach.

Mr. POTTINGER. Congressman, I agree that sanctions, when applied, really come at a company from more angles than just an export control or even just an investment restriction for sure. I think the challenge are ones that we have talked about, simply how do you incentivize the Department of Treasury to really apply those? You mentioned just a moment ago, I think, the idea of an annual requirement and so forth. I mean, I think that would be welcome.

Mr. BARR. Thank you. I yield.

Chairman MCCAUL. The gentleman yields, and we will have further discussion. I know we are meeting with the majority leader. It seems to me you could take the provisions of this bill—I am not opposed to sanctions. It is just that we have to have a compromise, and I think that is the bottom line.

So the chair now recognizes Ms. Dean.

Ms. DEAN. Thank you, Mr. Chairman. I thank you and Ranking Member Meeks for this legislation, for working together so well and guiding this committee in a bipartisan way. I want to go back to something that Mr. Bera was talking about, and I wanted to ask you, Mr. Pottinger, you, too, spoke of and wrote in your testimony about the military-civil fusion. For those who are in far into that, you know, in a democratic society we do not fully appreciate that strategy, the depth and breadth of it, would you want to add anything to what Mr. Harrell spoke of also?

Mr. POTTINGER. Congresswoman, thank you. I think that, under Xi Jinping in particular, he has really reoriented the State around his personal goals, which have now become the goals of ruling party that he leads. And those tools are sometimes laid out explicitly, for example in things like this military-civil fusion strategy and some of the laws. One that I mentioned was this national intelligence law that mandates that anybody must serve the Chinese intelligence apparatus and do so in secret when asked.

There are also a lot of intangible ways that the party forces business, irrespective of whether it is nominally private or State owned, to align itself with the interests of the party. And one of the ways that Xi Jinping has done that has been to establish committees, Communist Party committees and cells at multiple levels within existing companies. So a very good example would be if you look at something like Alibaba where Jack Ma, who, by the way, is a party member according to Chinese public accounts, but was really an entrepreneur at heart who founded this incredible company, and it was an incredible success within China and beyond. He was eased out of, you know, away from the steering wheel of that company shortly after he made remarks criticizing China's regulatory environment under Xi Jinping. That was back in 2020.

And so there is a Communist Party secretary of ByteDance, which is the controlling shareholder of TikTok. He also, the Communist Party secretary of ByteDance is also the editor-in-chief of all the applications under ByteDance, presumably including TikTok. So those are a couple of examples of things that are hard to see but are going on.

Ms. DEAN. Thank you for those explanations. Mr. Harrell, I was thinking you are both coming from such important background in two Administrations on this issue. Can you speak to this bill and in what important ways does H.R. 6349 go farther than the executive order issued by the president in August either by sector or by investor?

Mr. HARRELL. Thank you very much for the question, Congresswoman. And as I said in my opening remarks, I do think it is very important for Congress to act here. I think what the Administration has done, while an important start, is not sufficient to meet the challenge.

And I think the bill does a couple of important things. First, it does expand the technology, the covered technology sectors to focus on some high-performance hypersonics in a couple of areas that are important to China's defense industrial base that I think are valuable additions. It also adds a permanent statutory footing to the Biden Administration approach, which I think is important both for signaling purposes, that there is bipartisan support on this issue. We, as a country, are united on this. I also just think, over time, you know, Administrations come and go. And I think having a permanent feature in American law, just as we do under CFIUS, which also got started in the 1980's by executive branch action but which Congress later came in and codified and expanded on, really important to have that statutory basis here.

Ms. DEAN. And we, as Members of Congress, agree with you on that. It is better to have a statutory basis in something that is quite clear. Mr. Harrell, do we have any calculation, does anybody have any calculation of outbound investments that have really ultimately done harm either to our national security or global security?

Mr. HARRELL. So I am not aware of public sort of top-line figures of here are the investments that have caused national security harm. When I was in the Administration and, obviously, I am still under confidentiality provisions, the Administration did do a very lengthy detailed analysis cataloging many different investments that we determined the Administration did think later caused harm, one of which I talked about in my opening statement on SenseTime. That is one that is now public and sort of easy to talk about. But I think what we have seen is a wide range of investments over many years have later caused harm, but I am not aware of any public kind of top-line number of the dollar value of those.

Ms. DEAN. Again, I thank you both, and I thank the chairman. I yield back.

Chairman MCCAUL. The gentlelady yields. The chair recognizes Ms. Kim.

Mrs. KIM OF CALIFORNIA. Thank you, Chairman McCaul and Ranking Member Meeks for holding today's hearing on outbound investment regulations. So I am hearing that there are generally two approaches to addressing outbound investment concerns. One is, you know, the broad investment restriction in technology sectors where there are national security concerns; and the second one is the Entity List-based sanctions approach focused on specific foreign companies that are linked to CCP military or intelligence agencies. As you know, this is a debate we are having right now and trying to decide which of these approaches is best.

So in your view, is there a way to reconcile these two different policy approaches; and, if so, can you describe how Congress can go about doing that?

Mr. HARRELL. Maybe if I could just offer a minute of remarks and then see if Matt has anything to add. I do think a sanctions approach with respect to China has value.

Clearly where there are Chinese companies that are engaged in human rights abuses, in truly nefarious kinds of activities, we should sanction them. I also think the Biden Administration should be more aggressive, as Matt said in his opening remarks, on using the existing executive order first signed under President Trump that limits U.S. investment in the publicly traded securities of big Chinese companies that are linked to the Chinese military. I think the Administration should be more aggressive in prohibiting American investment in these publicly traded securities.

I think there are a couple of notes of caution on SDN sanctions though when it comes to big Chinese companies.

And, again, I think there are times when it is appropriate.

But if I look at, for example, the Defense Department list of Chinese companies linked to the Chinese military, all of China's major mobile telecommunications providers are on that list, understandably. They are all, I am sure, providing telecommunications to the Chinese military.

On the other hand if we sanctioned all of China's mobile telecommunications providers, you would effectively prohibit all American companies from doing business in China because none of their employees in China could use the telephone.

So I do think there is a place for SDN sanctions, but I think we also have to be careful in our application to not, you know, kind of inadvertently do something like preventing American companies in China from using the telephone.

Mrs. KIM OF CALIFORNIA. Sure. Mr. Pottinger, do you want to add to that and hopefully quickly?

Mr. POTTINGER. Sure, Congresswoman. I agree with what Peter just laid out. SDN, to Congressman Barr's point, is a more powerful tool. But sometimes it can be overkill or inappropriate if it is applied in ways that the example that Peter just laid out sort of illustrated.

This sector approach, I think the importance of that is the simplicity. It is less resource intensive for the Treasury Department. It is easier for companies to understand what is off limits and not to cross those barriers.

So I wouldn't know how to describe the way to meld those together. But it would have to have enough flexibility built in so that it did not mandate, for example, that you would have to use both simultaneously necessarily.

Mrs. KIM OF CALIFORNIA. I appreciate both of your perspectives on that. Hopefully, we can come together and hopefully reconcile but find a way that we can really make this work because both options do present its pros and some concerns as well.

But resourcing will be important as Congress moves to establish an outbound investment regime. But I am interested in hearing from you about where these new resources would be best suited. Yes.

Mr. HARRELL. I do think to manage effectively an outbound investment regime, it is important for the executive branch to have adequate resourcing. These are complicated issues.

I think fundamentally probably in three places you need resources. One is at the Treasury Department, just it manages investment. It needs some resources.

One is probably in the Commerce Department where they need some additional technical expertise, which they are already staffing up because of export controls, but they need that there.

The third, of course, is in the intelligence community to kind of better understand what's going on within China and the dynamics there.

Mrs. KIM OF CALIFORNIA. Do you think that establishing an outbound investment regime requires the creation of a new office, or agency for that matter?

Mr. POTTINGER. I think that—I have asked myself that at times when I was in office and thought it might be easier if it was put into some other entity. But I think it really ultimately boils down to leadership, that Congress has the ability to hold accountable leaders of the departments and agencies that currently have those authorities.

I think that is the fastest way to exert the authorities and intention that you were legislating.

Mrs. KIM OF CALIFORNIA. OK. I think my time is up. Thank you. I yield back.

Chairman MCCAUL. The gentlelady yields. I just want to make a point that the two witnesses have made. You know, the executive order just applies to China. This bill, it's not only China, but it's Iran, Russia, and North Korea as well as China.

As we see the current unholy alliance forming between these four countries against the West, the United States, our interest, and our NATO allies, I think that's a very important point.

The Chair recognizes Mr. Schneider.

Mr. SCHNEIDER. Thank you, Mr. Chairman. And I want to associate myself with your remarks. As you said, it is more than just China. And it is immediate, mid-term and long-term. And that is one of the things I want to touch on.

I also would like to associate myself with the comments earlier of my colleague, Mrs. Manning, on immigration. But in particular, as everyone has said, thank the witnesses here today but also the chair and the ranking member for bringing this legislation forward.

I join with colleagues on both sides in commending the Biden Administration executive order on outbound investment, and I want to thank the committee for having this hearing today on this legislation. I am proud to join in co-sponsoring it.

A thoughtful outbound investment regime is necessary to building on the work of CFIUS and making sure that U.S. investment is used to uplift communities around the world rather than strengthening our strategic adversaries and empowering totalitarians.

We have already had an impressive conversation about the technical aspects of this legislation and specific concerns regarding the People's Republic of China semiconductors, microelectronics, quantum information technologies, artificial intelligence, and other technologies of the future. And it is our job here in Congress to make sure that we keep the United States, U.S. interests, U.S. population, U.S. citizens safe and prosperous.

I want to start, and I will go back to something we were talking about earlier with Mr. Barr, the idea of sector versus company specific.

The sanctions approach led by Treasury, Mr. Pottinger, I will ask you, would it catch a startup, for example, AI company, that is in its earlier stages just beginning to develop its technology may not even be on the radar other than with venture capital, would it catch and prevent them from developing civilian military technology?

Mr. POTTINGER. Congressman, it could easily miss that. It is very difficult to map China's AI ecosystem. Oftentimes, it takes sometimes years before the importance of a particular entity really makes itself apparent.

Mr. SCHNEIDER. Mr. Harrell?

Mr. HARRELL. I completely agree with what Matt said. Now it very likely would not capture that simply because Treasury does not know all of the millions of companies in China that are out there.

Mr. SCHNEIDER. Conversely would the sectoral approach likely catch such a startup?

Mr. HARRELL. Not only would it likely catch such a startup, but it might actually require the investor, if the investment wasn't prohibited, if it was sort of outside of prohibited, to come in and tell the U.S. Government about that that startup so the U.S. Government could begin better understanding it.

Mr. SCHNEIDER. Mr. Pottinger, do you agree?

Mr. POTTINGER. I agree with Peter's remark.

Mr. SCHNEIDER. Thank you. Let me shift gears. H.R. 6349 adds hypersonic technology to the list of covered technologies. We have seen hypersonic missiles as a priority for Tehran, Moscow, Pyongyang. In fact in the Ukraine War, in Putin's War against Ukraine, we have seen for the first time the Kh–47M2 Kinzhal or Dagger in action.

My question for whichever one of you wants to answer this, now looking at the immediate term where they are currently being used but long-term threat to the United States, how will this prospective outbound investment regime affect the short-term application of hypersonic technology like what Russia is using against Ukraine, Iran, or North Korea and what do you think the long-term impact would be?

Mr. POTTINGER. Hypersonics is one of those that I think the United States was hemorrhaging our technology early on before there was a consensus like what we've heard in this room today about the nature of the threat that China poses to our interests.

And I know stories of conferences that China held where American scientists showed up to talk about their latest findings with respect to hypersonics. And in some cases, China ended up putting that theory to practice before the United States did.

If we had had outbound export controls earlier on that, that would have helped. Outbound investment restrictions might have helped with that as well.

Mr. SCHNEIDER. Thank you. And just to wrap up, with my colleague, Mr. Wilson, he and I have been pushing to curb the export of high end machine tools, especially CNC machines, to Russia.

Treasury did sanction 130 entities related to this effort, and we are grateful to see that. But with respect to China and this policy, can you talk about how it might affect machine tools, if at all? Either one?

Mr. POTTINGER. I do not have a specific answer on that, but I will say I recently met someone after I had given a talk out in Arizona who told me about how much damage our transfer of our machine tooling capabilities, particularly to China, have been to some of the problems that we're trying to solve for now, for example building up our own defensive capabilities, munitions, things that are wholly civilian, commercial capabilities as well. Machine tooling was really one of the things that allowed us to win World War II.

Mr. SCHNEIDER. Thank you. And it is critically important today. And I know we will continue to focus on that in this committee. But again, I thank the chair and the ranking member for this legislation, and I yield back.

Mr. SCHNEIDER. The gentleman yields. The chairman recognizes Mr. Davidson.

Mr. DAVIDSON. I thank the chairman for holding this hearing, and I thank the body for paying attention to an important issue.

Back in 2018, we passed the bill called the Foreign Investment Risk Reduction Modernization Act. Part of the reason we are here today is presumably that bill is not adequately. Why not?

Mr. HARRELL. Thank you very much, Congressman, for that question. I think that the steps that Congress took back in 2018 with FIRRMA were really important in expanding the limits on Chinese investment in the U.S. There was a pattern that we were seeing at the time, Congress certainly saw at the time, where Chinese companies were investing in a whole range of technology——

Mr. DAVIDSON. Specific to outbound investment. I mean, we, of course, dealt with Chinese investment in CFIUS. But there is still the export control portion.

And frankly, we had lots of companies that were concerned even as we had done the research and development tax credit. We have done things to incentivize investing and doing your research and development in America. But they were concerned that if I am going to do research and development in America, do I own the intellectual property or does America own it?

And if at the end of the day, they cannot export the technology, they just simply invest elsewhere. So is that a flawed approach or is there some other thing that we are looking to capture here that isn't captured by FIRRMA?

Mr. HARRELL. Well, Congressman, I would just say that because FIRRMA to my knowledge is only for inbound investment into the United States, that this in some ways is almost a mirror image of FIRRMA. So it is trying to achieve some of the things that FIRRMA was trying to solve for but whereas FIRRMA is trying to prevent——

Mr. DAVIDSON. But we stopped too short on FIRRMA. We did not get an adequate way to address the outbound controls. Obviously, Mr. Barr and Mr. McCaul have different approaches.

I will tell you as a private sector business guy, I go back to the days of conflict minerals. You know, so there was this idea, you know, that certain minerals in countries, primarily in Africa, that are involved in conflicts, we do not want those things to show up in American products. And so the solution was that you have every company that uses metal report on it.

I had at the time a small business in Western Ohio, and I am signing off on a statement that the metal I am using contains no conflict minerals. Now that is essentially Mr. McCaul's approach. You go all the way down to the small business level, and you hold every business in America accountable for something.

Frankly they are, like, why am I signing this? I have no idea. I certainly do not have a way to trace all the origin of the tin that is in the steel here to where in Africa the tin was cut. Why do not you ask U.S. Steel on that?

And frankly that is Mr. Barr's approach. Mr. Barr's approach says, let's use OFAC. And, you know, we use OFAC just short of conflict, right? We go with a sanctions regime as a tool short of going to war. Is that a more serious toolkit than just regular laws that apply to small businesses?

Mr. HARRELL. Sir, I very much understand and sympathize with the challenges of supply chain sourcing that your business faced in Ohio.

I guess I see things a little differently where you have an American company, whether it is a big company or whether it is a small company investing in China. Presumably that company knows that it is investing in China and is making a decision to invest and knows what sector in China it is investing in.

So I think that if you are a company that wants to make a—an American who wants to make an investment in AI sector in China, you probably do know what you are doing and could make a decision on the sector about whether or not to invest there.

Mr. DAVIDSON. I guess speaking of conflicts, maybe we could just go, like, who else do you guys represent? Do you represent big tech? You know, because it seems to me as a small business guy, just like we did this business, you know, beneficial ownership disclosure.

Originally, every business in America was going to have to report all of this and essentially negotiated it down to where the smallest of the small businesses, businesses under 20, now have some reporting requirement because apparently that is how all the bad stuff happens, not the big companies. It couldn't be those guys.

So all the lobbying stopped because the small companies do not have enough lobbying power to do it. So either of you guys represent big tech companies?

Mr. POTTINGER. I am a small business owner. I am not representing any company's interest here today. I have no financial interest in the outcome of any of the bills that you are talking about. I am representing myself. I am representing the think tank that I work for as well, Foundation for Defense of Democracies, sir.

Mr. DAVIDSON. All right.

Mr. HARRELL. I just want to say the same. I am here representing myself. I have no financial interest in the outcome of this or in the sanctions approach.

Mr. DAVIDSON. This is the challenge. The biggest of the big companies get lobbied and represented. And you pass this off, and Congress will hold up the shiny object and say we did something. It does not solve the problem.

The sanctions regime works pretty well. I am highly biased. And frankly it is the committee of jurisdiction. I am on both. I think that's the right way to solve the problem. And I yield back.

Chairman MCCAUL. The gentleman yields. I just want to say first that the witnesses filled out a truth in testimony form regarding any motivation to impugn your character before this committee is not well served in my judgment. Perhaps for Mr. Davison, since he missed your testimony, Mr. Pottinger, why do not you describe the difference between a sector-based approach and an entity-based approach.

Mr. POTTINGER. Congressman, if you are looking at an entity-based approach, that requires the U.S. Government, probably the Department of Treasury, to look at each specific company that it wants to prohibit Americans from investing in.

So they actually have that authority from the executive orders that emerged from the late Trump Administration and the early

Biden Administration, but only 68 companies to my knowledge were ever actually designated for prohibition on U.S. investment into Chinese military-affiliated companies.

So a sector approach, the idea is that you do not have a barn full of analysts, God bless them, over at Treasury. They are often having to divide different problem sets as well.

I mean, I have been over there when I was in office. You know, if North Korea is testing a nuke or a missile, that team has to really shift to start targeting North Korean entities. And by the way, you know, Iran is creating problems. Russia has now launched the biggest war in Europe since World War II. That Treasury team is getting spread very, very thin. I know how hard they work.

If you have a sectoral approach that just says, look, Americans, U.S. persons, are not allowed to invest in these particular sectors that are relevant to China's military and surveillance state as well as Russia's, North Korea's, and Iran's, it makes it simpler, and it is less resource intensive for the U.S. Government.

Chairman MCCAUL. So it in fact provides more clarity to the private sector and businesses, correct?

Mr. POTTINGER. I would argue it provides more clarity, yes.

Chairman MCCAUL. And an entity can be changed overnight in China, correct?

Mr. POTTINGER. Sure.

Chairman MCCAUL. And so a sector-based approach would get around that?

Mr. POTTINGER. One of the things I mentioned earlier is that China has systematically shut down the research enterprise in China so that it is harder for foreign companies to acquire real-time information about ownership structures, supply chain flows, and the like. Those companies are being systematically rolled up and dismantled or co-opted to serve and align themselves with the Chinese Communist parties.

Mr. DAVIDSON. Will the gentleman yield for a question?

Chairman MCCAUL. I am not finished yet. We attempted to sanction under Treasury, Hikvision, which is a State surveillance company on the Uyghur Muslims, and guess what the Treasury Department said? In a letter to me and the ranking member, it cannot be done.

So I guess it depends on who is at the Treasury Department. But, yes, I will yield.

Mr. DAVIDSON. Is it the gentleman's contention then that OFAC and the current sanctions regime is inadequate to the task of preventing sanctions of Asia?

Chairman MCCAUL. I think the question is what is most effective? And I think the sector-based approach is going to be a more effective way to capture capital flow and investment into these five sectors that we know are responsible for the buildup of the PLA and their war machine.

An entity-based approach can be manipulated by the CCP as the former deputy national security advisor to President Trump has just told this committee and testified to.

I am not saying that sanctions aren't an effective tool. In fact, Mr. Barr and I have had many discussions trying to come to some sort of rational, you know, conclusion of this, but it has to be in good faith.

And I think you can take the best of both perhaps and that's precisely what we are working on.

Mr. DAVIDSON. Hopefully, we will wind up with good amendments. I yield back.

Chairman MCCAUL. All I really care about, sir, is we have got to stop selling China the technology. We have got to stop investing in their war machine, particularly at this dangerous time that we find ourselves in as we look at Taiwan and the Taiwan Straits. And you look at TSMC and semiconductors and the whole thing. So I appreciate your spirited debate. The chair now recognizes Mr. Mills.

Mr. MILLS. Thank you, Mr. Chairman. I think we can all realize the significant importance of strengthening not only our supply chain and industrial capabilities but also limiting our adversarial reliance upon China.

You know, for far too long we have listened to many people on the other side of the aisle talk about the competition with China as opposed to what they really are is an adversarial nation.

We have seen where China continues with their Belt and Road initiatives that has expanded out their Eurasian borders, attempted to take Africa, Oceania, in an effort to essentially cutoff Western Hemisphere supply chain and further impact America economically while simultaneously utilizing propaganda and misinformation warfare campaigns in developing nations to try and create doubt in American currency value to try and prevent that from being utilized as the U.S. global currency.

Now this is all in an effort, as we know, and the chairman had pointed out with the Russia, China, Iran, and North Korea geopolitical alignment, this is an effort to try and attack the West in many different facets. But we have to understand that we cannot help to continue to propagate that for them.

I think that's where I actually agree that the outbound investment into China and critical sectors actually does provide our competition and our adversaries with the invaluable information, skills, and innovation that poses potential harm to America's national security interests.

Dating back to the 1990's and potentially even earlier, there are obvious instances in which U.S. investments on the ground floor of Chinese tech startups have been instrumental in developing China's current surveillance, defense, and other technological capabilities that threaten the U.S. interests at home and around the world and also advancing their alliances.

So my question is if a U.S. investor supports the development or acquisition of a critical technology by a Chinese company, can intellectual property protections or U.S. export controls effectively stop that Chinese company from transferring it to China's military surveillance state?

Mr. POTTINGER. So the question, could we know in advance if we are investing in a Chinese company whether we could prohibit it from transferring its——

Mr. MILLS. I know you said right now almost every company is State controlled. And I do acknowledge that Chairman Xi's role in

The CCP is to take over everything. But I am just curious, what would be an effective tool that we could utilize that would help to prevent this and kind of get a bit of a heads up on it?

Mr. POTTINGER. Yes, you know, China uses these what they call force technology transfer. In other words, it is sort of the price of admission for a lot of companies to have access to the Chinese market.

I think, I mean, on the top of my head you could require that they would have to report to their shareholders, which I think would be good practice anyway if they were planning on transferring, you know, hard won, hard researched, and developed technologies as a price of admission for getting into that market. But it is——

Mr. MILLS. And, Mr. Harrell, some argue that China has sufficient resources, domestically and abroad, to invest in the high tech companies. In addition to money, what value do U.S. investors bring supporting China technologies and ambitions?

Mr. HARRELL. I think that is a great question, Congressman. Because when a U.S. venture capital company, whether it is like a VC company or whether it is a venture arm of a big AI or semiconductor company goes into China, it is not just putting that cash in that Chinese company. It is providing expertise to that Chinese company on how to go to market. It is probably doing some door opening and introductions to potential customers. It is providing expertise on how to run that company effectively. There is really a lot that goes alongside that investment that is value in addition to the cold hard cash itself.

Mr. MILLS. I think we can all agree that one of the things that America needs to do is invest in building up our industrial base, ensuring that we have more capacity here at home, stopping our reliance upon China, looking at things like eliminating the double taxation of Taiwan, which will allow the nearly 92 percent of global semiconductor manufacturing to actually be brought to the United States and other areas. But critical sectors of technology, research and innovations represent the next generation of information. And I think that opens up Pandora's Box as we continue to support that.

I am not trying to be hyperbolic, but the potential applications of AI, machine learning, quantum mechanics, hypersonics, and others are difficult to underState.

The U.S. should absolutely seek to mitigate the threats from our adversaries who are actively seeking to beat the U.S. in these research races. And I think that is why it is so critical for us to start focusing in on the quantum data computing as well as for the quantum entanglement capabilities for AI autonomous drone sets.

So for that, I yield back. Thank you so much.

Chairman MCCAUL. The gentleman yields. The chair recognizes Mr. Self.

Mr. SELF. Thank you, Mr. Chairman, and thank you for—I think our ground has been well plowed so I want to go a little bit further afield.

First of all, I appreciated Mr. Barr's comments about the total integration of the Chinese private sector in military. Money is fungible. I think we need to expand our view here. Dual use capability in precursor chemicals, the supply chain rare earths, I have not heard the rare earth minerals mentioned here at all. And we could go on.

So this is not just technology. And I think we ought to move beyond technology. I realize we may be addressing technology here. But the broader picture to me is well beyond technology.

So I want to go to the WTO and the PNTR. The WTO, the first question for you gentlemen, is are they still meeting the policies that China had to agree to in order to get most favored nation? That's one question.

And then when we go to the U.S. PNTR, I understand the concern with repealing that. The tariffs would be larger. But I would like for you to comment on is this the standard CVO static scoring, if you will, as opposed to the dynamic scoring because U.S. manufacturing would pick up the slack?

So I would like for you to address both the WTO, are they still meeting it and is there anything we can do about it if they are not meeting those policies?

And second when we talk about our PNTR, would you address my question on static versus dynamic scoring? Thank you.

Mr. POTTINGER. Congressman, thanks for those remarks and questions. With the WTO, I mean, I'm not a trade expert, but I remember because I had been working as a journalist at the time in China writing for the Wall Street Journal when China came into the WTO.

China made all sorts of promises about market access and the like in exchange for us bringing them into the WTO and giving them market access. I am confident that if you were to ask folks over at the U.S. Trade rep's office, they would tick off a long list of promises that were not kept by Beijing. And it is very hard to enforce because in cases that we brought in the WTO Beijing has been able to run out the clock and sort of game the system in those ways.

The WTO has worked, I think, a lot better for trade between countries that enjoy the rule of law.

Mr. SELF. Of course.

Mr. POTTINGER. So it is not to knock what we created with that system, but by bringing in a single party dictatorship that was intent on not holding and keeping up its obligations.

When I was working at the White House, I kept a list that my staff compiled for me of all of the agreements China had signed with the United States that they had abrogated. It was a long list. It was several pages. And trade was only the beginning of it.

Mr. HARRELL. OK. Let me just associate myself with Matt's remarks on whether China has lived up to its WTO obligations, sir. Of course not. I mean, it has been very, very clear for many years now that they have not lived up to their obligations under the WTO. As Matt says, that is only one of many sort of agreements they have made that they have not lived up to.

On your question about tariffs, I do think tariffs can be a valuable tool to help reduce our dependencies on China. As you note, we are dependent on China for certain things like critical minerals that are not sort of high technology kind of things but instead go into lots of products, including high technology products.

And I do think it would be valuable for the Administration to really take a hard look at the important tariffs that the previous Administration started, but to look at kind of what isn't working and where are we still dependent, and maybe critical minerals is a good example. We actually do not tariff our imports of critical minerals from China.

And I understand why we do not want to hike prices on critical minerals. On the other hand, if we are letting them come in tariff free, it is really hard to build a vibrant U.S. ecosystem for critical minerals. So I think we do need to look at tariffs through that supply chain lens on how can we wean ourselves off of Chinese supply chains.

Mr. SELF. Well, rare earths, critical minerals, as you call them, we do not mine because of our own environmental laws, not because of tariffs on China. With that, I yield back. Thank you.

Chairman MCCAUL. The gentleman yields. The chair recognizes Mr. Stanton.

Mr. STANTON. Thank you very much, Mr. Chairman. I want to thank you and Ranking Member Meeks for holding this important hearing today and for your leadership on H.R. 6349. It is much appreciated and much needed.

The United States and U.S. companies are strong in large part because of our commitment to open capital markets, and a belief that free flowing capital and knowledge will lead to innovation. But spending that capital on critical technology innovation in China can lead to serious problems, specifically as it relates to national security.

For example, prior to President Biden's August 9 executive order, U.S. entities were able to invest in China's Semiconductor Manufacturing International Corporation, also known as SMIC.

The first question is for Mr. Harrell. Could you tell us why SMIC's technology might worry the United States of America?

Mr. HARRELL. So SMIC is one of China's major semiconductor development firms. And one thing we have seen over the last year and a half, particularly as the U.S. has put pressure on China to deny them access to tooling, is we have seen SMIC and other Chinese companies double down on trying to develop things indigenously in China to overcome the restrictions we have put on their semiconductor sector.

And I think the fact we are seeing China double down makes it all the more important to make sure the wall that we have in those key high end semiconductors is even higher, which is why I think it's so important to focus on investment in that sector as well as export controls.

Mr. STANTON. The same question—or another question for you, Mr. Harrell. When American companies or venture capital firms invest in a business, including in China, they also provide know-how, technical transfers, and legitimacy to those businesses. Can you tell me why sharing this with China's critical technology sector will hurt U.S. interests?

Mr. HARRELL. We clearly want to keep our edge here in the U.S. in these critical technologies, AI, semiconductors, quantum, things like that.

And as you say, Congressman when an American venture capitalist goes over to China to invest over there, it's not just the money that he or she takes with them. It is opening doors to customers. It is putting board members who help manage the company on the board. It is providing them kind of expertise on how to grow and how to expand.

And those are all really important aspects to that company and whether that company is going to be able to actually succeed in developing that technology over in China, which we do not want them to do.

Mr. STANTON. This is a question for both Mr. Pottinger and Mr. Harrell. What if we do not do it? What are the ramifications of not using an outbound investment regime to address concerns about the PRC's critical technology sector? Please touch upon both human rights concerns and the impact on U.S. global leadership.

Mr. POTTINGER. Peter mentioned earlier the example of Sense Time, which had come on my radar when I was in office. On the human rights front, these are cutting edge technologies that are applied specifically for the purpose of monitoring the thoughts, the actions, the communications.

I mean, this is George Orwell's thought police in action, building systems for identifying people based on their ethnic or racial background from a distance so that they can then be put under surveillance or segregated or even sent to a re-education camp.

So on the military side we're seeing—you know, you take a company like DJI, for example, right? This is the Chinese heavy weight drone manufacturer that has got something like 70 percent of the consumer drone market. Well, they are supplying drones that are being used for military use on both sides of the conflict in Europe. And that was a company that was—it got its lead early investment from Americans.

Mr. STANTON. That is great. Mr. Harrell, anything to add to that?

Mr. HARRELL. No, I think Matt put it very well.

Mr. STANTON. I will be very brief. My last question, we are investing historic amounts in U.S. critical technology through the CHIPS and Science Act. It is so important for the United States to be a leader in a semiconductor production and not to undercut our investment by also giving a leg up to China in this crucial sector.

The U.S. Chamber of Commerce supports the Biden Administration's efforts to develop a thoughtful regime that safeguards American national security and economic leadership without unnecessarily restricting beneficial U.S. business activity.

Mr. Harrell, can you describe how the Biden Administration's tiered approach in the August 9 executive order tries to balance national security and be beneficial to business activity?

Mr. HARRELL. I think the Biden Administration, and I think legislation this committee is looking at, really provides an important highly tailored approach, right? We are not talking about all sectors. We are not talking about all or even most investment. We are talking about a set of investment in sectors that we know are critical to our technological and national security edge.

The Biden Administration, I think the legislation would accomplish the same goal, also plans to provide clear guidance on what are the investments that are prohibited to make it reasonably straightforward for companies to know what they and cannot do so they aren't just going to have to hire, you know, armies of lawyers to advise them on it.

So I think we do want, and I think we are expecting, very clear guidance on definitions and what kinds of investments are off limits

Mr. STANTON. Thank you so much. I yield back.

Chairman MCCAUL. The gentleman yields. The chair recognizes Mr. Hill.

Mr. HILL. I thank the chairman. Thank you, gentlemen, for sharing your views with us today. And I think it is important to note that all members on both sides of aisle and in all the committees and certainly our China task force want to get to the sweet spot on this topic for an effective regime that has a reasonable cost-benefit metrics in order to screen and block where appropriate outbound investments to China. I just think that's where we are.

We are going a bit around and around on how this would sit in the menu of what we have today from all the lists that we have, export controls, tariffs in some instances. And so I want to thank you for trying to add clarity to it.

Mr. Harrell, you, in your testimony, you praise President Biden's investment prohibitions on publicly traded securities issued by Chinese military industrial complex companies, the CMIC designation. However, since being put on that list, Hikvision's revenues are up by 30 percent. SINOCAM's revenues are up 60 percent. China Mobile's stock price is up 67 percent, Huawei and SMIC went on to develop an advanced 5G chip.

So that does not seem like this system is working. How do you expect, you know, an additional layer on that to be more successful?

Mr. HARRELL. So I think—Congressman, thank you for the question. I think it is important to think through different kinds of goals we have with respect to limiting investment in China. So I think the goal of the Biden Administration's executive order from last year is really to go after investment in these kind of early stage companies that are developing technologies.

I think that the CMIC list, which President Trump stood up in late 2020 and which President Biden has continued, is really to take an approach of where we know there is a Chinese company that is linked to the military, we are going to say Americans cannot invest in that.

Now maybe those companies can raise money domestically or that sort of thing, but we think it's important that Americans aren't raising money in those big Chinese companies that are linked to the military.

It is not to say that limiting investment is the only tool we should take. I think where you have a Chinese company that is linked to the military, it is engaged in some activity, like SMIC and semiconductors, you also have to have an export controls approach, right? Make sure they cannot get the capital. They also cannot get the technology.

And if we find that that isn't working, maybe at that point we need to look at additional measures. But I think that the—I will leave it at that.

Mr. HILL. Let me followup on that and say so that is U.S. only. But if we want to maximize the impact to remove the fungibility aspect of this and everybody trying to make a living, wouldn't having whatever decision we take here being put on the OFAC list and governed by the Treasury gives us some G7 clout on enforcing like a sanctions regime.

So if you wanted to have maximum pressure campaign here, to use a phrase, you might have—they would be on the list. They would have export controls over the certain technologies. They would have a prohibition on investment, and they would be sanctioned so that our G7 colleagues would actually put them on the list and not actually go or—pick a country. Wouldn't that be the strongest possible menu?

Mr. HARRELL. So I certainly agree we want a multilateral approach to investment restriction.

Mr. HILL. So if we just do something here, do we get a multilateral approach?

Mr. HARRELL. I think it is important for America to lead on this. And I think having an approach that limits investment and then making sure the rest of the G7 comes along, building that diplomatic coalition is important.

Mr. HILL. Thank you. Let me slip in one question for my good friend, Mr. Pottinger, and thank you for your fantastic work in the National Security Council.

The sector approach, I got it. I think every bill we are talking about has identified the sectors now, but some of them having really broad listings. You are proposing, or I heard maybe Mr. Harrell say, might leave that to regulatory definitions. But AI for example, I cannot think of anything more broad. It is integrated in every single thing every single person does. Won't that require an army of lawyers to figure out? What is your thought there, Matt?

Mr. POTTINGER. Yes. Congressman, it is good to see you. Look, no question, I mean, AI is tricky. What Peter was laying out earlier was sort of a nexus for looking at where there is a reasonable use case for military and intelligence uses, so the application on the one hand. And the other is the power of the actual model that is making possible all those applications and looking at that.

I think that it is not clear-cut, I would agree. AI, it is a big deal. But I would say this though. AI is already being weaponized against us——

Mr. HILL. Oh, yes.

Mr. POTTINGER [continuing]. By a company that Americans invested in, ByteDance. It is a TikTok platform.

Mr. HILL. I will yield back, Mr. Chairman. That is an example of where naming that company is better than saying we want to cutoff investment to AI. I will yield back to the chair.

Chairman MCCAUL. Well, I appreciate the gentleman's diplomacy. I think there is a sweet spot here as you said. Hopefully, we will get some of this resolved tomorrow. The chair now recognizes Mr. McCormick.

Mr. McCORMICK. Thank you, Mr. Chair. U.S. investors in 58 investment deals related to China's semiconductor industry over the last 3 years represented 17 percent roughly of all investments into the Chinese artificial intelligence industry.

I am a big pre-market guy. And I know we have some bills on the table to talk about investing with the conversations going on today. But, Mr. Pottinger, specifically, given your experience in the Trump Administration, how would you compare the Biden Administration versus the Trump Administration's limitations and direction as far as what can we do to keep us from investing?

I know we talked about this kind of ad nauseam today. But specifically, how would you compare the Administrations and the way they are facing down this specific problem? And obviously we in Congress have some ability to affect this, and we want to. But if you could compare side-by-side the most recent Administrations, what is the difference?

Mr. POTTINGER. Yes. I think it might actually be a good test case for how you eventually find that sweet spot because there were some things that the Biden Administration did that I wish that we had done in the Trump Administration. And then there were a couple places where the Trump Administration was stronger on this specific area.

For example, when President Trump signed those two executive orders prohibiting U.S. investment into Chinese companies, he included subsidiaries of those companies. So even those there was 40 some odd companies that the Department of Defense put on the list, that immediately accordioned out to about 1,100 companies.

The Biden Administration, I was disappointed that they got rid of the subsidiary requirement. But on the other hand, they expanded the authority to cover not only Chinese military affiliated companies, but also Chinese companies that are involved in egregious human rights violations, the surveillance state stuff that we have been talking about. That was a good move.

So I think if you put these things together, you end up with a stronger whole.

Mr. McCORMICK. OK. Great. And so that does not necessary increase—our proposed bills do not necessarily increase executive permission. It is basically an overall blanket to help us direct money away from these Chinese——

Mr. POTTINGER. I think one of the things it does, I mean, if you have got a law to support, in essence, the Trump and Biden executive orders, you give them—you give it much more credibility. You give spine to executive branch officials who might be afraid that they are going to get sued by the companies that end up in the cross hairs.

But if you have got a law behind that, a court in the United States is going to give that a lot more weight than a mere pen stroke from a President.

Mr. McCORMICK. Excellent. Mr. Matheny, do you believe that had the United States banned outbound investments to Chinese about 15 years ago or so would have made a different in the ultimate outcome of the advancement of AI and other technologies that are possibly harmful in the competition and strategic outcome with what we have done?

Mr. HARRELL. It is obviously hard to know the counterfactual history. But I think there are many cases over the last 15 years where we have seen a U.S. investor come in to a Chinese high tech company. We talked earlier about Sense Time. Matt talked about ByteDance, the owner of TikTok where that early U.S. investment was absolutely essential to that Chinese company being able to thrive and grow both domestically and in China and then ultimately around the world.

And so I do think just looking at the history of these kinds of cases that had we had a tailored investment restriction regime 10, 15 years ago, we probably would see a less well-developed Chinese high tech industry in some of these key technologies. And that would be very much in our interest.

Mr. MCCORMICK. I think in some ways it is kind of a rhetorical question. It takes investment to make R&D, and it takes investment to make a company grow. That is exactly what happened. We were a big part of that, almost 20 percent.

Mr. Pottinger, do you think any of our partner nations and allies have adopted restrictions to their citizens investing in Chinese defense sectors?

Mr. POTTINGER. Not that I am aware of. I think that there is sort window guidance in some countries where, you know, we have seen investment drop off from Japan, for example, into certain Chinese sectors. But, again, I think this is one of these areas where we lead and eventually others follow.

The United States, President Trump was the first official anywhere to put human rights sanctions on Chinese officials who were involved in the Uyghur genocide. It wasn't Europeans. It wasn't anyone anywhere else. But eventually Parliaments in Europe began to follow suit. Canada and others followed the lead of the United States.

Mr. MCCORMICK. And I know I am out of time. But just a yes or no question. Does the PRC limit their citizens and private industry from investing in our industries?

Mr. POTTINGER. They heavily regulate depending on where they want to see strategic gains. So there is a constant give and take in terms of the instructions that industry receives in China for coming into the U.S.

Mr. MCCORMICK. So with that comment, just that it is an unfair system. I yield. Thank you, Mr. Chair.

Chairman MCCAUL. That is an excellent point. Thank you for bringing that up. The chair now recognizes Mr. Moran.

Mr. MORAN. Thank you, Mr. Chairman, and thank you to the witnesses today. A very important topic we are talking about today.

I first want to, though, thank the chair and Representative Barr for working to reconcile these two approaches that have been talked about so much, the entity-based approach, the sector-based approach are really reflected in the different bills that are going through this committee and the Financial Services Committee.

I agree with the chairman that there is going to be a way, and we must find a way, to reconcile these because both have some issues that we need to deal with. Both do not actually get us completely to the end that we are all after, and that is frankly to quit assisting and helping China build its technology to the point where it is harmful to the United States national security interest and our economic interest. That is certainly not the end that any of us want.

So I applaud both the chair and Representative Barr for their work on this matter. And I just wanted to say I am encouraged by the discussion today because it tells me we are going to get somewhere eventually.

Now other countries have developed and implemented formal outbound investment restrictions, South Korea, Taiwan, and even China themselves have done that. I would like to direct my first question to Mr. Harrell.

What has been the economic outcome for countries like South Korea and Taiwan by imposing outbound investment restrictions?

Mr. HARRELL. Thank you very much for the question. I know that when the Biden Administration was looking at this issue, they looked at both South Korea and Taiwan which have, frankly, fairly narrow, but I think nonetheless important, limits on semiconductor investment by their companies in China. Obviously, both Korea and Taiwan have very advanced semiconductor companies. And a number of years ago, those countries restricted or imposed a regime to make sure that their companies weren't putting the most advanced technologies in China.

Now that was a really pretty narrow only going after really the very, very bleeding edge of the technology. I think we need something broader than that. What the Biden Administration would do is broader than that.

But the reality, looking at those cases, is the costs were quite limited. I mean, South Korea and Taiwan have the world's most successful, or are among the world's most successful, semiconductor companies. We obviously have some here too.

And so I think what that experience shows is that you very much can impose a tailored and scoped restriction on investment in China and have very much a global leading company here at home.

Mr. MORAN. Thank you, Mr. Pottinger. Do you have anything to add to that?

Mr. POTTINGER. I think that covered it pretty well.

Mr. MORAN. Good. I also want to ask you guys about the fact that China openly seems to want to overthrow the U.S. dollar as a global currency. They have partnered with countries to create BRICS. We have seen the BRICS conference. There is an argument that something such as BRICs would offset U.S. financial leadership and that a concept like outbound investment will expedite that shift.

On the contrary though, if the U.S. develops an outbound regime we would, in my opinion, be able to garner support from allies like Japan and the UK to develop their own.

Mr. Pottinger, I will start with you this time. How impactful would that be for the U.S. national security for us to do that?

Mr. POTTINGER. Well, I do think that there is an argument that can be made. And I have heard it made by Treasury officials that if we overuse our SDN sanctions authority, it creates an incentive for other governments, particularly adversarial governments, to try to find work-arounds to the U.S. dollar. So that might be a consideration as well in this debate.

But if I understood correctly, your broader point is what is China doing to try to undermine?

Mr. MORAN. That is correct.

Mr. POTTINGER. Yes, they are, on the one hand, asking their trade partners increasingly to settle trade in Chinese currency. They have launched a Central Bank digital currency, which I certainly wouldn't want my savings denominated in Chinese digital currency, which could just evaporate from your account at any moment. But that is another tool they are using.

Perhaps the most important one is they are trying to build new plumbing for settling transactions worldwide, sort of like our Swift banking system. They are trying to come up with successor systems to that that bypass U.S. dollar and Treasury——

Mr. MORAN. Before my time is up, I want to ask you about one more thing that Mr. Barr had mentioned because one of the holes that we are trying to fix here is that if we go at this alone, we still have the problem that many of our allies around the world can still invest in China, and they will not feel hardly the impact of what we need them to feel to be able to change their behavior.

So what are we doing to work with other nations to ensure that whatever we do here, they are joining us in that effort against China?

Mr. POTTINGER. I think in part it is pointing to the example of what happened with Ukraine where companies still wanted to get in there and open shops or buy oil or what have you from Russia. And people convinced themselves that commerce would mitigate against something as crazy as invading your neighbor and getting hundreds of thousands of people killed. But that is exactly what Vladimir Putin did.

I think it is simply leading our allies to see the long-term benefits of tackling this problem. I think many of them will.

Mr. MORAN. Thank you to both of you guys. Mr. Chairman, I yield back.

Chairman MCCAUL. The gentleman yields. We have two more members if the two witnesses have the time. Mr. Huizenga.

Mr. HUIZENGA. Thank you, Mr. Chairman. And let me first start by saying I know this is an issue that is near and dear to you. It is certainly an issue that is near and dear to me and Mr. Barr and others. We have got a number of folks on the Foreign Affairs Committee who also serve on the Financial Services Committee, which has been sort of the epicenter of a lot of the sanctions regimes that have gone on.

And, you know, my own experience goes back to my third term where I was named chair of the Monetary Policy and Trade Subcommittee and was brought in for a SCIF review regarding a CFIUS review of A123 Battery, a company that was sold to a Chinese company. Michigan has been sort of the epicenter of a lot of the debate surrounding batteries and Gotion, for example. But really a lot of it is centered around automotive.

And so we have been dealing with this collectively for many, many years because this is a real issue. It is a problem. And COVID, I think, just underscored this in ways that nobody really expected, everything from paper masks to ventilators, and, you know, having the Defense Production Act, the DPA being invoked to bring about medical equipment, not to mention pharmaceuticals, not to mention, you know, the myriad of food items and all the things that we have become, in my opinion, overly dependent on China.

So Congress has maybe been collectively maybe—well, maybe I will put it this way. Because I think the conversation has been happening within Congress, but maybe society as a whole has kind of come late to the game a bit with the dangers and the overdependence on China.

And so we have—my whole point in this is we have many common goals, which is to limit the economic and military influence that China has certainly over the United States and, I would argue, in the Indo-Pacific region.

So what we are having the discussion about is the methods. All right? And what I personally am looking for is making sure that we have an effective and real way of curbing and bending that influence that China has had.

We have done a lot of work on that with the Financial Services Committee over the years, the work that has been here on the Foreign Affairs Committee is important, the China Select Committee. I have been working with Mr. Barr for a long time on these issues. And in my mind, Treasury is still sort of that main thrust of where the most effective sanctions can be.

But as we know with a lot of other things here in Washington, DC, whether it is the border, whether—you pick the issue, if you are not willing to enforce the rules and the laws that are already on the books in the systems that are in place, just adding a new system isn't necessarily the solution on that. And I just want to be very careful that we are doing that.

So I do have some concerns about the authority being turned over to an agency that may not have the experience in that. I have little confidence in the Commerce Committee for example or, you know, some other committee, State Department, I mean, that sort of to me does not make a whole lot of sense. The State Department, that is not their bailiwick.

So I have a quick question for both of you. If you can let me know, are you aware of any U.S. companies that have invested in Chinese companies that have gone into partnership with the PLA? Go ahead.

Mr. POTTINGER. Sure. One that I was looking at as I was crafting the testimony was a company called 4Paradigm. 4Paradigm is, you know, an AI firm in China that has reportedly sold software to China's military for what they called, quote, battalion command decisionmaking and human machine learning. That company was seeded by Goldman Sachs, Sequoia Capital, and probably some others as well.

Another would be Biren Technology, B-I-R-E-N. That is an advanced semiconductor designer that wants to compete with Nvidia in China. In fact it is already on the Commerce Department's entity list for potential ties to, quote, weapons of mass destruction, advanced weapon systems, and high tech surveillance. And that one was invested by a couple of American venture capital firms.

Mr. HUIZENGA. OK. I know my time has expired. I do not know, Mr. Harrell, if the chairman will indulge. Otherwise, we can do this in writing. So I appreciate that. Mr. Chairman, I yield back. Thank you.

Chairman McCaul. Thank you. The Chair now recognizes Mr. Lawler.

Mr. Lawler. Thank you, Mr. Chairman. Last year Chairman McCaul and I sent a letter to BIS Secretary Estevez with questions about how commerce is implementing U.S. export control laws in response to China exporting goods to designated State sponsors of terrorism, Cuba, North Korea, Iran, and Syria.

The indirect resourcing of State sponsors of terrorism from U.S. entities is a serious concern and should be met with strict reform. It took the Biden Administration 6 months to respond to our inquiry, and they seemed to share our commitment for preventing U.S. tech from being illicitly acquired by our adversaries. But actions certainly speak louder than words. So we will see what they do on that front.

Just as concerning though as using U.S. tech for nefarious purposes is U.S. investment in nefarious technology. Not only should we not be providing resources to terror, but we should not be providing their funding. It is past time to establish outbound investment restrictions to ensure U.S. dollars are not funding the development of tech that will be used counter to our national security interests.

Is it possible to utilize or expand existing export controls to restrict U.S. capital investment into China?

Mr. Harrell. So my understanding, and I know there has been a bit of debate on this, but my understanding is that even with the important reforms to U.S. export controls that Congress enacted in 2018, the Export Control Reform Act, it remains really technology focused and is just not well suited through ECRA and through the export controls to go after dollars where there is not a technology flow alongside that.

Mr. Lawler. So are you of the mindset that we need to develop a different vehicle or regime by which to do this?

Mr. Harrell. I am. I think it is very important to develop what I would view as different but also complementary. I mean, it should be done in parallel, a complementary regime to go after the dollars so that Congressman, as you say, not only are we not giving the Chinese technology, we are not investing in their ability to develop the technology.

Mr. Lawler. Are you aware currently of any instances in which U.S. Government tools, such as export controls, were unable or insufficient to mitigate the risk presented by U.S. investments into China and any specific examples?

Mr. Pottinger. Well, earlier, Peter was talking about the example of Huawei where President Trump took action to prevent Huawei from being able to acquire high end semiconductors that had been made with American technology.

That approach bought time. It slowed down Huawei, but ultimately they were able to fashion a work-around using new companies that they had established, bringing in equipment that hadn't really been geared for sale to Huawei but ended up in service of Huawei's goals.

So I think with investment, it is sort of a similar principle at work except it is the capital flows as opposed to the technology. By limiting the capital flow, you are able to go after early stage things that you wouldn't see in time to apply necessarily an export control restriction.

Mr. LAWLER. This past May, leaders of the G7 countries issued a joint statement recognizing that outbound investment could be important in complementing existing export controls and inbound investment controls as well.

When President Biden issued Executive Order 14105, which focused on outbound investment in August, to your knowledge did he consult further with our G7 partners?

Mr. HARRELL. My understanding is the Administration has been in a very active discussion with G7 partners, that American diplomacy was instrumental in getting that statement that you alluded to in May.

I think ultimately the way the U.S. is going to get our partners to come along is the way we always have, which is a combination of us acting and us engaging in diplomacy.

I think it is going to take the European Union and some of these others a bit of time. But I am optimistic that with us acting and strong diplomacy by the executive branch, but also by Congress, we will pull them along with us.

Mr. LAWLER. Are you aware of any similar executive actions being taken by any of our allies and partners?

Mr. HARRELL. So the European Union has begun a regulatory process to look at this. Obviously, we are going to have to keep up the pressure on them to get it over the finish line, but they have begun a regulatory process on this.

Mr. LAWLER. Great. Thank you. I yield back.

Chairman MCCAUL. The gentleman yields. I want to thank the witnesses for their valuable testimony. Additional questions may be submitted by members of the committee that we will ask you to respond to in writing.

Pursuant to committee rules, all members may have 5 days to submit statements and questions for the record. Without objection, the committee stands adjourned.

[Whereupon, at 12:42 p.m., the committee was adjourned.]

APPENDIX

COMMITTEE ON FOREIGN AFFAIRS
FULL COMMITTEE HEARING NOTICE
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, DC 20515-6128

Michael T. McCaul (R-TX), Chairman

January 10, 2024

TO: MEMBERS OF THE COMMITTEE ON FOREIGN AFFAIRS

You are respectfully requested to attend an OPEN hearing of the Committee on Foreign Affairs to be held at 10:00 a.m. in room 210 of the House Visitor Center. The hearing is available by live webcast on the Committee website at https://foreignaffairs.house.gov/.

DATE:	Wednesday, January 17, 2024
TIME:	10:00 a.m.
LOCATION:	HVC-210
SUBJECT:	Examining the Flow of U.S. Money into China's Military Might
WITNESSES:	The Honorable Matthew Pottinger Chairman of FDD China Program Foundation for Defense of Democracies
	Mr. Jason Matheny President and Chief Executive Officer The RAND Corporation
	Mr. Peter Harrell Non-Resident Fellow Carnegie Endowment for International Peace

*NOTE: Witnesses may be added.

By Direction of the Chair

The Committee on Foreign Affairs seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202-226-8467 at least four business days in advance of the event, whenever practicable. Questions with regard to special accommodations in general (including availability of Committee materials in alternative formats and assistive listening devices) may be directed to the Committee.

COMMITTEE ON FOREIGN AFFAIRS
MINUTES OF FULL COMMITTEE HEARING

Day *Wednesday* Date *17 January 2024* Room *HVC-210*

Starting Time *1015* Ending Time *1242*

Recesses ____ (____to ____) (____to ____) (____to ____) (____to ____) (____to ____) (____to ____)

Presiding Member(s)

Chairman McCaul

Check all of the following that apply:

Open Session ☑
Executive (closed) Session ☐
Televised ☑

Electronically Recorded (taped) ☑
Stenographic Record ☑

TITLE OF HEARING:

Examining the Flow of U.S. Money into China's Military Might

COMMITTEE MEMBERS PRESENT:

Attached

NON-COMMITTEE MEMBERS PRESENT:

NA

HEARING WITNESSES: Same as meeting notice attached? Yes ☑ **No** ☐
(If "no", please list below and include title, agency, department, or organization.)

STATEMENTS FOR THE RECORD: *(List any statements submitted for the record.)*

Attached

TIME SCHEDULED TO RECONVENE ________
or
TIME ADJOURNED *3:52pm*

Meg Wagner
Full Committee Hearing Coordinator

Committee on Foreign Affairs

118th Congress

ATTENDANCE

Date: January 17, 2024

Representative	Present	Absent	Representative	Present	Absent
Mr. McCaul	X		Mr. Meeks	X	
Mr. Smith	X		Mr. Sherman	X	
Mr. Wilson	X		Mr. Connolly		X
Mr. Perry		X	Mr. Keating		X
Mr. Issa		X	Mr. Bera	X	
Mrs. Wagner		X	Mr. Castro		X
Mr. Mast	X		Ms. Titus		X
Mr. Buck		X	Mr. Lieu		X
Mr. Burchett		X	Ms. Wild		X
Mr. Green		X	Mr. Phillips		X
Mr. Barr	X		Mr. Allred		X
Mr. Jackson	X		Mr. Kim		X
Mrs. Kim	X		Ms. Jacobs		X
Mrs. Salazar		X	Ms. Manning	X	
Mr. Huizenga	X		Mrs. Cherfilus-McCormick	X	
Mrs. Radewagen		X	Mr. Stanton	X	
Mr. Hill	X		Ms. Dean	X	
Mr. Davidson	X		Mr. Moskowitz		X
Mr. Baird		X	Mr. Jackson		X
Mr. Waltz		X	Mrs. Kamlager-Dove	X	
Mr. Kean	X		Mr. Costa		X
Mr. Lawler	X		Mr. Crow		X
Mr. Mills	X		Mr. Amo	X	
Mr. McCormick	X		Mr. Schneider	X	
Mr. Moran	X				
Mr. James	X				
Mr. Self	X				

STATEMENT FOR THE RECORD FROM REPRESENTATIVE CONNOLLY

"Examining the Flow of U.S. Money into China's Military Might"
House Foreign Affairs Committee
10:00 am, Wednesday, January 17, 2024
HVC-210
Rep. Gerald E. Connolly (D-VA)

More than forty years ago, the United States and the People's Republic of China established official diplomatic relations. Since that time, China has transformed into an economic powerhouse with a growing middle class, an emerging military juggernaut, and an increasingly urbanized population all supported by significant investments in education and infrastructure. Competition with the PRC represents the greatest challenge to American foreign policy and a rules-based international order. Under the leadership of Chinese President Xi Jinping, China has exerted its economic, political, cyber, and military or quasi-military force to shift the power dynamic in the Indo-Pacific in their favor. Over the last decade, China has accelerated its foreign investment, expanded its foreign influence operations, and leveraged unfair economic and trading practices into greater economic development.

The flagship of Beijing's tactics, especially within the economic sphere, is the Belt and Road Initiative (BRI). A massive infrastructure project that China promises will attract more than $1 trillion of investment over the long-term, BRI projects often solicit unsustainable debt burdens for recipient countries, employ Chinese state-owned enterprises or labor, and lack transparent financing and contracting practices. Countries like Sri Lanka or Djibouti have entered into agreements with China, only to regret their participation in the BRI. In Sri Lanka, a Chinese state-owned company took control of the deep-sea port it had built in Hambantota after the Sri Lankan government was unable to service its loans. In Djibouti, China Merchants Bank signed a lease for property and subsequently developed a military base. Understanding China's playbook will be critical to shape U.S. strategy to counter its malign influence.

These pernicious practices underscore why I, as President of the NATO Parliamentary Assembly (NATO PA), urged NATO to put China on its agenda. In November 2020, I wrote a report for the NATO PA Political Committee entitled, "The Rise of China: Implications for Global and Euro-Atlantic Security" to encourage NATO to adapt to a new balance of power that reflects China as a world power. In this report, I urged my colleagues to include reference to China's actions in NATO's strategic documents, including the Strategic Concept which was unveiled in April 2022 and highlighted the stated ambitions and coercive policies that challenge the Trans-Atlantic Alliance's interests, security, and values. I welcome the newly adopted NATO Strategic Concept which does just that.

China has limited foreign competition in its domestic market and props up private enterprises with Chinese state funding and intelligence. For example, in order to bolster China's semiconductor industry, the Chinese government launched a $150 billion public-private fund to subsidize investment, acquisitions, and the purchase of new technology from 2015 to 2025. The Chinese government has also restricted U.S. cloud service providers from providing services in China. In the 117th Congress, under the leadership of President Biden, we passed the CHIPS and Science Act, legislation that will bring investments in semiconductor development and supply chains to $150 billion. Democrats also passed the Uyghur Forced Labor Prevention Act, the Inflation Reduction Act which increased competitiveness in EV's and renewable energy, and our committee held a 4-day markup for the EAGLE Act, legislation that every Republican voted against. As biased PRC policies flood global markets with cheap supply, undercut foreign competition, and create an environment where it is impossible for U.S. companies to compete, the United States responded emphatically to make our own significant investments.

The Biden administration has tackled the issue of outbound investment to China directly by issuing Executive Order 14105, an order executive branch the ability to balance U.S. economic and national security interests, specifically for sensitive technologies that would not otherwise be captured by export controls. In the 117th Congress, the CHIPS and Science Act of 2022 mandated and implemented new sectoral outbound investment restrictions, ensuring that companies receiving U.S. taxpayer money would not produce semiconductor technology in China below the 28-nanometer node for 10 years.

The United States had an opportunity to set the rules for economic engagement in the Asia-Pacific with the Trans-Pacific Partnership (TPP), which accounted for 40 percent of global GDP and 20 percent of global trade. A high-quality TPP deal would have given the United States the tools it needed to combat China's gray zone tactics by strengthening ties to emerging partners and creating a rules-based order that set the parameters for labor, environmental, human rights, and intellectual property standards. Conversely, the U.S. withdrawal from TPP created a vacuum that gave an unbelievable gift to the Chinese. They continue to pop champagne in Beijing.

In the Trump Administration, the story of U.S.-China relations was one of gobsmacking incoherence. President Trump complained about China's unfair trade practices, yet it was he who abandoned the Trans-Pacific Partnership, allowing China to write the region's trade rules. President Biden has luckily charted a new path, increasing budget requests for aid to the Indo-Pacific and working with partners and allies in the region to develop the Indo-Pacific Economic Framework. The Biden Administration's reversal of our unilateral withdrawal from the Indo-Pacific will buttress U.S. economic engagement in the region and finally place the United States in a position to compete with China.

China is playing the long game. For the United States to compete strategically, we need to make investments beyond the immediate horizon. Under the 117th Congress controlled by Democrats, we did just that with the CHIPS and Science Act and the development of an Indo-Pacific Economic Framework. Now, we must follow up on that work and ensure the United States, as a pacific power, sustains long-term engagement in the Indo-Pacific.

WITNESS TESTIMONY SUBMITED FOR THE RECORD FROM MR. MATHENY

RAND

Testimony

JASON MATHENY

Implications of Outbound Investment Controls

CT-A3186-1
Testimony presented before the U.S. House Committee on Foreign Affairs on January 17, 2024

For more information on this publication, visit **www.rand.org/t/CTA3186-1**.

Testimonies

RAND testimonies record testimony presented or submitted by RAND associates to federal, state, or local legislative committees; government-appointed commissions and panels; and private review and oversight bodies.

Published by the RAND Corporation, Santa Monica, Calif.

Implications of Outbound Investment Controls

Testimony of Jason Matheny[1]
RAND[2]

Before the Committee on Foreign Affairs
United States House of Representatives

January 17, 2024

Chairman McCaul, Ranking Member Meeks, and members of the committee: Good morning, and thank you for the opportunity to testify today. I am the president and CEO of RAND, a nonprofit and nonpartisan research organization. Before RAND, I served on the National Security Council and in the White House Office of Science and Technology Policy, as a commissioner on the National Security Commission on Artificial Intelligence, as assistant director of national intelligence, and as director of the Intelligence Advanced Research Projects Activity, which develops advanced technologies for the U.S. intelligence community. For the past 75 years, RAND researchers have conducted research in support of U.S. national security, and we currently manage four federally funded research and development centers for the federal government: one for the Department of Homeland Security and three for the Department of Defense.

RAND researchers have analyzed the strengths and weaknesses of outbound investment controls as a feature of U.S. industrial strategy.[3] That analysis is not available to the general

[1] The opinions and conclusions expressed in this testimony are the author's alone and should not be interpreted as representing those of RAND or any of the sponsors of its research.

[2] RAND is a research organization that develops solutions to public policy challenges to help make communities throughout the world safer and more secure, healthier and more prosperous. RAND is nonprofit, nonpartisan, and committed to the public interest. RAND's mission is enabled through its core values of quality and objectivity and its commitment to integrity and ethical behavior. RAND subjects its research publications to a robust and exacting quality-assurance process; avoids financial and other conflicts of interest through staff training, project screening, and a policy of mandatory disclosure; and pursues transparency through the open publication of research findings and recommendations, disclosure of the source of funding of published research, and policies to ensure intellectual independence. This testimony is not a research publication, but witnesses affiliated with RAND routinely draw on relevant research conducted in the organization.

[3] Bryan Frederick, Bonny Lin, Howard J. Shatz, Michael S. Chase, Christian Curriden, Mary Kate Adgie, James Dobbins, Kristen Gunness, and Soo Kim, *Extending China: U.S. Policy Options for Asymmetric Advantage*, RAND Corporation, 2021, Not available to the general public.

public, but I am happy to arrange a briefing from the research team to this committee. My testimony today is based in part on that analysis and based in part on my work on this topic for several years prior to my joining RAND.

Currently, investments by U.S. entities in foreign technology firms based in or owned by strategic competitors are essentially unlimited unless the foreign firm is sanctioned. Restricting such investments would have several costs and benefits. Among the costs of doing so are the following:

- U.S. investors often find such investments profitable. Left to their own devices, investors will attempt to make the most profitable investments. Barring them from categories of investments is likely to reduce their profits.
- In response to investment restrictions, alternative sources of capital are likely to be substituted for U.S. sources, reducing the financial impact on targeted countries.

On the other hand, restricting such investments would have several benefits:

- While funding is frequently substitutable, the intangibles that accompany funding are frequently not. A primary benefit of controls on outbound investment is a restriction on what often accompanies funding from U.S. investors: business know-how, strategic advice, business connections, and credibility that can yield additional fundraising. For some of our strategic competitors, most notably the People's Republic of China (PRC), the provision of critical management expertise is often the most valuable contribution that U.S. venture capital funds make to emerging companies. Our strategic competitors want access to this U.S. strength.
- U.S. investments could shift to U.S. firms, growing domestic strength in important industrial sectors. U.S. investments could also shift to firms in countries that are, or could be, strategic partners. These investments could improve our diplomatic relations with those countries, support their economic growth, and decrease their vulnerability to economic coercion by our competitors.

As an economist, I should offer an apology. Economists generally support free markets. But an exception is warranted when a company's activities produce *negative externalities*: effects whose costs to society are not paid by the company. Pollution is the classic example of a negative externality. To address a negative externality, some form of governmental action is usually needed, such as prevention of the activity, or a tax on the activity equal to its cost to society.

A premise of outbound investment controls is that U.S. investors are generating costs to the United States that they are not paying. As one example, consider U.S. investments in PRC high-performance computing. There are substantial security concerns about how advances in high-performance computing contribute to the PRC government's offensive cyber operations against the United States and to the design of weapon systems, such as hypersonic missiles, that threaten the United States and its allies. Both represent negative externalities of U.S. investments in PRC computing capabilities. U.S. investors do not pay back Americans for the damages caused by PRC cyber operations, and they do not pay for the consequences of PRC military modernization.

Instead, other parts of U.S. society are likely to pay these costs. Given these negative externalities, U.S. government action seems justified.

One such option is a broad investment restriction of the type described above. Another option is list-based sanctions focused on specific foreign companies that are linked to military or intelligence agencies. List-based sanctions have the disadvantage of playing "whack-a-mole" with entities whose legal names frequently change and whose relationships are intentionally obscured. Indeed, the PRC can create new companies faster than U.S. agencies can identify them. Detecting the ties between foreign companies and their governments, especially their intelligence agencies, is already an extremely challenging task. Expanding list-based sanctions would further increase the analytic burden on U.S. agencies that are already stretched thin as they attempt to track companies in countries unfriendly to the United States. Even sector-wide investment controls will need to be accompanied by additional resources for the responsible U.S. agencies, but such resources would need to be significantly greater if controls were entity-based.

The U.S. government could also consider excluding punitive actions that slow down the development of new technologies by our competitors and focus its actions exclusively on increasing investment in U.S. companies. Going faster is certainly an essential part of industrial strategy, but it can be accompanied by measures that slow down the competition. If I were in a car race, pressing down on the accelerator, I would not simultaneously syphon gas from my gas tank and give it to my competitors. Fair play does not require fueling the competition.

I thank the committee for the opportunity to testify, and I look forward to your questions.

RESPONSES TO QUESTIONS SUBMITTED FOR THE RECORD

Questions for the Record: January 17, 2024
House Foreign Affairs Committee Hearing
"Examining the Flow of U.S. Money into China's Military Might"
Representative Mark Green (TN-07)

Question 1:

Mr. Pottinger, is the Foundation for Defense of Democracies (FDD) currently taking, or has it ever taken, money from TikTok or its technological competitors? For example, Meta or X.

Answer: No, the Foundation for Defense of Democracies is not currently taking, and has never taken any money from TikTok or its technological competitors, for example Meta or X.

Question 2:

Mr. Pottinger, if the Foundation for Defense of Democracies (FDD) has taken or is currently taking money from TikTok, Meta, X, or similar technology companies – what was the amount, why was the payment issued to the foundation, and why did the foundation accept payment?

Answer: Please see response to Question 1 above.

Questions for the Record Submitted to
Mr. Peter Harrell by
Representative Dina Titus House
Committee on Foreign Affairs
January 17, 2024

Question 1:

I will soon be introducing my *Public Assistance for Chinese Engagement Act* which will establish an ODNI-led interagency working group to create and maintain a public database for U.S. entities to consult. This will allow them to do their due diligence before pursuing partnerships with Chinese businesses or universities to determine if they have ties to any agency within the CCP responsible for its security apparatus. They can thereby assure they are not inadvertently assisting the PLA, United Front Work Department, Ministry of State Security, or other entities known to carry out state-sponsored technology transfers and supervision of civil-military fusion plans. Do you think such a database would help U.S. investors, universities, and businesses avoid this issue when seeking to invest in or partner with Chinese entities?

No Response

Question 2:

The security challenges we are discussing are shared by our closest allies and partners. Once the U.S. develops an outbound regime, it is important that our closest friends develop similar restrictions so that we can collectively ensure that we are not contributing to the development of advanced military capabilities that present a shared threat. To your knowledge, are other nations in the Indo-Pacific that are directly threatened by the PRC's military considering adopting similar restrictions to ensure that they are not bankrolling potential risks to their own national security? What should the U.S. government be doing to inspire more international collaboration and coordination on this front?

No Response