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Research Report

A future European FDI screening system: solution or problem?

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Perspectives on topical foreign direct investment issues

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A future European FDI screening system: solution or problem?*

by

Carlos Esplugues **

In line with discussions in other countries,¹ the increase in FDI flows into strategic sectors of Europe's economy has fostered a debate on the need to establish a screening mechanism at the European level, on the grounds of national security and/or public order. M&As undertaken by investors controlled by foreign governments or directed to sectors of the EU economy involving critical infrastructure, technologies and inputs or accessing sensitive information receive special attention. In September 2017, the European Commission submitted a proposal to the European Parliament for a Regulation on FDI control.² In the framework of the EU ordinary legislative procedure and after inter-institutional negotiations, the EU institutions reached a political agreement on a revised version of the proposal on November 20, 2018.³ This revised text will foreseeably be endorsed by the Parliament and Council at a first reading before the end of February 2019 and, then, enacted as a Regulation.

Through the 2009 Treaty of Lisbon, the EU member states transferred competence on FDI issues to the EU, which nevertheless is divided by contradictory interests and opinions on some issues. In particular, the desire of some members for the EU to remain an investment-friendly area contrasts with the desire of other members to protect themselves against foreign control of certain industries. Also, the prospective adoption of a common FDI screening framework aimed at resolving the lack of coordination within the EU in this area whilst guaranteeing legal certainty and predictability for foreign investors clashes with the wish of member states to remain in full control of determining which investments are acceptable and which are not.

The lack of consensus on the establishment of a FDI screening system and its design manifested itself in the original proposal submitted and remains conspicuous in the revised proposal. The Commission has opted for a compromise that seeks to achieve a difficult balance within the existing *status quo* in Europe in this area: the text explicitly recognizes the sole responsibility of member states to manage national security and their ultimate decision-making authority in that regard, both for creating (or not) a national screening mechanism and implementing its decisions.⁴

The proposal is limited in scope, as it consists of a mechanism for the exchange of information on FDI proposals in certain strategic sectors at the European level. However, it has structural problems that raise some doubts about its practicality and usefulness to meet its objectives. Two of these problems are of special relevance:

- The proposal foresees collaboration between the Commission and member states, among member states and with the Parliament, and thus finally relies on the willingness of member states to cooperate. Member states have a general obligation to inform the Commission and other states about, in particular, the sectors and member states targeted by proposed investments, as well as their value and ownership structure of the foreign investors and their funding. Member states must “give due consideration” or pay “utmost account” to the Commission’s opinion or other states’ comments—but they are not compelled to follow them, merely to provide written explanations when they do not.⁵ Additionally, member states may rely on article 346(1) of the Treaty on the functioning of the EU to limit the information they provide.
- These problems are accentuated by the extent of the Regulation’s sectoral coverage and the breadth of the criteria used to evaluate investment proposals. This carries the risk of extending the screening beyond that required by security or public order concerns.⁶

For the proposal to fulfill its goal of creating an effective system of information exchange on FDI, at least four major changes should be made:

- Clear common rules on when FDI in a member state is likely to affect the security or public order of the EU or other member states should be adopted.
- Any obligation imposed on the Commission and member states in the framework of the Regulation should be clearly defined and be mandatory. The system cannot exclusively depend on the will of member states to provide information, take opinions and comments into account and explain non-compliance. The ability to disregard comments and opinions should be restricted to the maximum and made dependent on some limited and objective grounds established by the Regulation itself.
- Rules to ensure the full protection of confidential information acquired in the application of the Regulation should be negotiated.
- The possibility for foreign investors to seek judicial redress against screening decisions should be ensured.

The proposal constitutes an interesting first step in the process of establishing a future European screening mechanism. However, in its current version, it may increase the duration and complexity of national evaluation procedures and create more problems than solutions.

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¹ For instance, on August 1, 2018, the US Senate enacted the Foreign Investment Risk Review Modernization Act; it modifies the legal regime of the Committee on Foreign Investment in the US.

² Fabrizio Di Benedetto, “A European Committee on foreign investment?” *Columbia FDI Perspectives*, no. 214, December 4, 2017.

³ European Parliament, “Provisional agreement resulting from interinstitutional negotiations,” December 6, 2018.

⁴ Article 1(2) and (3).

⁵ Articles. 6(9), 7(7) and 8(2)(c).

⁶ Article 4.

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