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FOREIGN DIRECT INVESTMENTS SCREENING MEASURES IN THE EU AND DUTY TO GIVE REASONS

ABSTRACT. *Recent reforms in terms of screening measures for foreign direct investments address national security and other risks of public interest. However, they may also conceal other concerns, such as the fear of predatory acquisition of significant local businesses by foreign countries. As a consequence, the above-mentioned measures may be used to create commercial barriers in spite of the many international treaties that guarantee freedom of trade. Further analysis of the ability of national EU governments to make investments in other countries is therefore needed. The present study explores recent cases of the so-called "golden power" in Italy, which have sought to oppose foreign government-driven acquisitions.*

The mechanisms for controlling foreign direct investments (FDI) have increased exponentially in recent years, including via international reforms.

While the flow of investments can be positive for national economies, it may also conceal political and strategic objectives behind a veil of purely economic purpose, objectives such as access to confidential information, advanced technologies, and natural resources.

On closer inspection, the duty to give reasons for these measures does not seem to be explicitly defined by the European legislature. Nevertheless, the obligation to provide the reasons underlying a specific foreign direct investment screening measure, whether it be a veto or the imposition of certain conditions, is implicitly inferable from a series of provisions.

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One must first consider the new EU Regulation 2019/452,[1] whose objective is to create an integrated system that limits predatory acquisitions by non-EU countries for reasons of safety and public order. This falls directly within Article 207 of the Treaty on the Functioning of the European Union (TFEU), which provides that trade protection measures are part of the common commercial policy entrusted to the exclusive competence of the EU.[2]

This system, however, will not be implemented through the establishment at the EU level of control powers over foreign investments, but through the coordination of instruments of control that individual Member States have already prepared or will adopt in the future, via a complex mechanism of cooperation between States and the Commission.

First, the Regulation requires Member States to notify the European Commission of any foreign direct investment in their territory (Article 3). Subsequently, it attributes to the Commission the power to issue a non-binding opinion on the FDI in three cases: (1) where this could adversely affect sectors of relevance for internal security (i.e., infrastructure, energy, patents, the pluralism of information, protection of personal data); (2) in the event that the investment affects a project of European interest which also includes the use of European funds (*i.e., Horizon 2020*, *Galileo*, or the European industrial development program for defence); and (3) when the FDI in one Member State can affect the security or the public order of another Member State.[3]

Article 4, paragraph 2 of the Regulation also contains three potential indicators of the risks that an investment made by a State outside the EU may entail to the security

1 EU Regulation 2019/452 of the European Parliament and of the Council of 19 March 2019, which establishes a framework for the control of foreign direct investment in the Union.

2 Article 207, paragraph 1, of the TFEU: "The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy, and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union's external action."

3 In the latter case, however, the Member State that receives foreign investments will not only have to solicit and then take the "advisory opinion" of the Commission into "due consideration," but will also have to notify the other Member States that might be interested, in order to also collect their opinions.

and public order of the European Union. These are: (*i)* the foreign investor is directly or indirectly controlled by a foreign government; (*ii*) there is a risk that the investor is performing or otherwise connected with the performance of criminal activities; (*iii*) the investor previously participated in activities detrimental to the internal security of the European Union.

The Regulation, therefore, only imposes a certain stringent obligation on states. The new legislation establishes not only duties of communication and the obligation to acquire opinions, it also provides a series of interesting minimum requirements that all States, which already have or intend to adopt a *screening* mechanism, have to comply with for minimising the damage caused by these measures. Among these requirements, we can mention compliance with the principle of non-discrimination based on the State of origin, the obligation to provide instruments of judicial protection for foreign investors who suffer from an illegal ban, and compliance with the foreign investor's transparency and *privacy* rules.[4] Furthermore, Member States are obliged to report to the Commission any proposed reform of their scrutiny instruments and, even if they do not have a control mechanism, they must submit an annual *report* to the Commission on the flow of investments in the country.

In light of the framework outlined by the new Regulation, its clear intention is therefore to guarantee full transparency of the decision-making process on the control of foreign direct investments, in addition to ensuring full and effective jurisdictional protection.

Two questions arise spontaneously: (1) how can it ensure the transparency of foreign direct investment screening mechanisms without providing an obligation of prompt justification for these decisions? (2) How can access to jurisdictional protection be guaranteed without first knowing the reasons that led the State to intervene with a negative provision?

The possibility for investors from non-EU countries to know the reasons that led to the imposition of a veto or a condition appears to be of primary importance in

4 *See* European Commission, *Screening of foreign direct investment - an EU framework*, 2019, available at https://bit.ly/2TsrDFO.

order to protect their interests and to guarantee, in broader terms, the principle of legal certainty. Indeed, the Regulation itself is inspired by the idea of creating a positive framework for foreign investments, considered a source of well-being and economic growth for the EU (recital 1).

The reasons for a State to adopt restrictive measures against foreign direct investments are specified in the Regulation: security and public order. These are broad and undefined concepts and, therefore, require a more precise explanation precisely in the justification of specific decisions.

Article 3, paragraph 2 also states that Member States establish the circumstances that give rise to the control, the reasons for the control, and the detailed procedural rules that are applicable.

Furthermore, in imposing a cooperation mechanism between Member States for the exclusive purpose of protecting security and public order, the Regulation expressly states that all the intra-procedural acts of this mechanism should be explicitly subject to the obligation to justify decisions.[5] This principle must also apply in the cases where it is the Commission that requests information on a specific foreign direct investment or issues an opinion addressed to a Member State. Therefore, it cannot be held that the obligation to justify decisions is foreseen for intra-procedural provisions, nor even for those that have their own external effects.

Finally, the Regulation clarifies that any immediate action must be duly justified. This must be done in a clear manner, due to the exceptional nature of immediate intervention for reasons of security and public order.

It is also interesting to verify if and how the obligation to justify the screening measures of foreign investments at the national level is regulated. I will briefly discuss

5 EU Regulation 2019/452, recital 18: "The cooperation mechanism should be used exclusively for the purpose of protecting security and public order. For this reason, Member States should duly justify any request for information relating to a specific foreign investment directed to another Member State as well as any possible comments addressed to that Member State. The same requirements should also apply when the Commission requests information on a particular foreign direct investment or issues an opinion addressed to a Member State. Compliance with these requirements is also important when an investor from a Member State is in competition with third country investors for the purpose of making an investment or buying assets in another Member State."

the discipline in Italy and France.

In Italy, the guidelines for screening of foreign direct investments are contained in Law Decree no. 21 of 15 March 2012, converted into Law no. 56 of 11 May 2012, as last modified by Law Decrees no. 148 of 16 October 2017, converted into Law no. 172 of 4 December 2017, and no. 22 of 25 March 2019, converted into law no. 41 of 20 May 2019. The exercise of special powers is currently envisaged in the sectors of national defence and security, 5g networks, as well as for activities of strategic importance in the energy, transport, and communications sectors.

Article 3-*bis* of the 2012 law decree contains an important provision on justification. In fact, by 30 June each year, the President of the Council of Ministers must transmit to the Chambers a report on the activities carried out on the basis of special powers, "with particular reference to the specific cases and to the public interests that motivated the exercise of these powers." The legislature, therefore, made explicit the need to state – at least in the annual report – the reasons of public interest underlying the adoption of a screening provision.

This report, however, has not been presented every year, as required by law: to date, there have been only two reports, one relating to the period 3 October 2014/30 June 2016, and the other relating to the period 1 July 2016/31 December 2018.

It is of particular interest to examine these reports in order to understand, in concrete terms, the reasons that justified the exercise of *golden powers* in Italy.

First, one notes a series of significant applications of special powers directly following the recent legislative developments.

On 19 October 2017, via Decree of the President of the Council of Ministers, special powers were exercised on the proposal of the Minister of Defence, through the imposition of conditions, according to Article 1, law decree 21 of 2012, on the sale by the company *Piaggio Aero Industries s.p.a*. to the company *PAC Investment S.A.* (indirectly controlled by the Chinese government), of the *EVO* company branch, relating to the set of activities of research, development, design, and sale of aircraft models and maintenance, aircraft repair and overhaul services.

On 2 November 2017, on the other hand, the Italian Government was firmly resolved to oppose, according to Article 1 of law decree 21 of 2012, the acquisition by

a French group of an Italian company active in ballistics and air control engineering. Although the company involved in the transaction is small, the veto on the *Altran/Next* business marks a new level of intervention for all intents and purposes, as this is the first case ever, in Italy, of an effective ban via *golden power* on acquisition by a foreign operator.

Only in one case, therefore, has the Italian government vetoed the sale of a company: so far, the tendency has been to impose provisions aimed at guaranteeing occupational interests first and foremost, without banning a sale in its entirety.

However, we must acknowledge the beginning of a phase of unprecedented government intervention aimed at protecting national strategic interests.[6] In the recent annual report to Parliament on the exercise of special powers for the period from 1 July 2016 to 31 December 2018, the Italian Government itself recognized the existence of an upward *trend* in protecting national strategic sectors, revealing a threefold increase in the total notifications sent to the Government with respect to the period examined by the previous report (3 October 2014 to 30 June 2016).

But what are the reasons behind the exercise of these special powers referred to in the annual reports to Parliament?

In the reports, reference is always made to the principles of security and public order. As already mentioned, these are generic, broad, and poorly defined principles, which clearly imply a very wide administrative discretion.

Almost certainly, the justification for individual screening measures for foreign direct investments will be more detailed than what appears in the report. However, the individual measures and the related reasons are not published, therefore it is not possible to know their content.

One could hypothesize that, if a private citizen were to present an instance of generalized civic access, this could be rejected, precisely to protect the public interests of security and public order, within the limits set by law.

This is certainly a significant problem, given that the EU regulation, as already

6 The Italian government, for example, contemplated (albeit without concrete consequences) exercising the *golden power* in the case of the acquisition of the *Esaote* company by the Chinese giant *Alibaba*.

stated, imposes transparency obligations.

It would, therefore, be necessary to wait for the publication of jurisdictional measures that refer to the contested veto of or conditions on a foreign investment and the related justification.

In fact, it is widely accepted in Italy, both in doctrine and in jurisprudence, that the screening measures for foreign direct investments fall within the category of the so-called acts of high administration, not considered the same as political acts and, therefore, unquestionable. Acts of high administration are formally and substantially administrative acts, characterized by a strong discretion almost comparable to that of political acts, but not as free in terms of purpose. This is directly reflected in the application of the legal regime of administrative acts and, therefore, the general law on administrative procedure (Law no. 241 of 1990), particularly Article 3, paragraph 1, which establishes a general obligation to state reasons for all administrative measures.

In France, on the other hand, the regulations on screening of foreign direct investments are contained in the *Code monétaire et financier* (French Monetary and Financial Code), as last amended in 2019.

Foreign investments in a business in France are subject to prior authorisation by the Minister of Economy if that business participates, even in an occasional way, in the exercise of public authority or is involved in one of the following areas: (*a*) activities that affect public order, public safety, or national defence interests; (*b*) research, production, or marketing of weapons, munitions, powders, and explosive substances.

Unlike other EU countries, the French legislature has expressly provided an obligation to state reasons in the case of the exercise of special powers. Article R 153-10 of the Code, in fact, states that the Minister of Economy must justify the veto of a foreign investment ("The minister [...] refuses via a justified decision"). In addition, the Code also sets out a specific list of legal grounds on the basis of which the Ministry can refuse to grant authorisation, thus blocking the investment.[7] Consequently, in practice

7 Article R-153-10: "The Minister of the Economy refuses via justified decision to authorise of the planned investment if they find, following an examination of the application: 1) That a serious suspicion exists that the investor is likely to commit one of the infractions addressed by the articles 222-34 to 222-39,223-15-2,225-5,225-

the Ministry uses one of the grounds mentioned in this provision of the Code.

Although the legislature has made the obligation to provide explicit justification only in relation to the power of veto and not in relation to the power of attaching conditions to a foreign investment, it could be said that, since it is still an administrative act – subject to the jurisdiction for substantive reasons of the competent administrative court, it must still be justified in light of the provisions contained in the 2016 *Code des relations entre le public et l'administration* (Code on Relations between the Public and the Administration). In fact, Art. L 211-2 provides a general obligation to state the reasons for the (individual) unfavourable administrative measures.

Finally, it seems appropriate to clarify that in France the foreign direct investments decisions are not disclosed to the public and no annual report is in place.

Law no. 2019-486 of 22 May 2019, known as the *PACTE Law*, changed this situation and does require the Government to disclose key statistical figures about the foreign direct investments screening measures in France, but such information has not yet been published. Therefore, it is not possible to concretely analyse the justifications for screening measures.

6,225-10,324-1,421-1 to 421-2-2,433-1,433-2, 435-3, 435-4, 450-1 of the Penal Code and by the first paragraph of article 321-6 of the same code or provided under the first title of book IV of the same code; 2) Or if the implementation of the conditions mentioned in article R. 153-9 is not sufficient on its own to ensure the preservation of the national interests defined by article L. 151-3 in the event that: a) The continuity of the activities, industrial capacity, and capacity for research and development of knowledge of technology and associated know-how would not be preserved; b) Or if the integrity, security, and continuity of the supply or the integrity, security, and continuity of the business of an establishment, installation, or work of vital importance in the sense of articles L. 1332-1 and L.1332-2 of the Code of Defence or of the transport or electronic communications networks and services or the protection of public health or data protection would not be guaranteed; c) Or if the execution of contractual obligations of the company with headquarters in France as owner or subcontractor would be compromised in the context of public markets or contracts affecting public order, public security, the interests of national defence or research, the production or commerce of arms, munitions, powders, and explosive substances."