

## EU goes ahead with a European framework for screening incoming foreign direct investments...moving steps closer to the well-known Committee on Foreign Investment in the US (CFIUS) filings.

### Introduction

On September 13, 2017, the European Commission published the draft of the EU regulation establishing a common European framework for the review of incoming foreign direct investment (FDI), akin to the process in the US administered by Committee on Foreign Investment in the US (CFIUS). The objective of this new proposal is to improve cooperation between the Commission and EU member states that conduct foreign investments screening nationally and to strengthen the role of the EU Commission in these processes.

The draft regulation establishes a standalone definition of a "foreign direct investment." According to it, an investment is any means aiming at maintaining "lasting and direct link" between the foreign investor and the entity or the entrepreneur that will use the capital received from the foreign investor to carry out its business. This covers all investments enabling active participation in management or control of a company or business. The draft regulation will apply to all EU member states' mechanisms that screen non-EU foreign investments.

The proposed regulation is similar to the CFIUS process in that both systems would be able to review foreign investments that confer control over a domestic business (referred to as "covered transaction" in the CFIUS regulations).

### The Upcoming Procedure for Incoming Investment Screening

The draft regulation does not replace all national screening procedures, but regulates how the Commission and other EU member states can intervene in the course of the national proceeding. First, each member state will inform the Commission and other EU member states about investments undergoing review within five days from the beginning of the process. Then, within 25 days, each other member state that considers the investment as a risk for its security or public order will have a possibility to address comments to the member state that conducts the review.

The Commission will issue a non-binding opinion if it considers the investment as affecting public order or security of one or more member states. The Commission and member states will be able to request additional information from the member state that conducts the review. This may have an enormous impact on national screening procedures and lead to their significant extension.

### Investments Affecting EU's Programs or Projects

When the foreign investment affects EU's projects or programs on the grounds of security or public order, the Commission will issue the non-binding opinion as in the regular procedure aforescribed. In the case of this type of investment, the member state – opinion's addressee – will have to explain to the Commission why it has decided not to follow the Commission's opinion.

### Criteria of Screening

The draft regulation provides a non-exhaustive list of factors that the Commission and member states may consider while screening foreign investments. They are, for example, investment's effects on:

- Critical infrastructure (such as energy, transport, communication, data storage, space or financial infrastructure or sensitive facilities)
- Critical technologies (such as artificial intelligence, robotics, semiconductors, dual use technologies, cybersecurity or nuclear technologies)
- The security of critical inputs
- The access or control over sensitive information

### Comparison With US CFIUS Process

The proposed regulation will add an EU level framework to review foreign investments in member states, much in the same way CFIUS has authority to review acquisitions by foreign persons that result in control over a US business. In reviewing foreign investments, the draft regulation considers factors to assess the security implications of proposed transactions similar to the factors enumerated under the statute creating CFIUS (Section 721(f) of the Defense Production Act of 1950, as amended). That is, both consider whether the transaction will result in foreign control over critical technologies, critical infrastructure, critical inputs (particularly in the defense industry) and sensitive information.

Although the objective of the EU proposal and the factors considered in the review process have much in common with the US system, the draft regulation differs from the CFIUS process in that it does not provide a mechanism for parties to voluntarily submit a transaction for review at the EU level (please note, in most instances, parties have the option under member state laws). Under the CFIUS process, it is possible to voluntarily file and subject the transaction to CFIUS review, with a clearance from CFIUS conferring a safe harbor protection on the parties from future action under the Defense Production Act. Thus, the draft lacks a European Union Merger Regulation type of mechanism that would remove transactions with an EU dimension from the member states and place the review authority with the European Commission. In this regard, the draft appears to impose greater scrutiny and oversight on foreign investments, but leaves the option for investors to proactively manage this additional regulatory burden to the member states' laws.

## What Happens Next?

The Commission has opened the public consultation that allows each interested entity or individual to submit feedback and comments on this proposal directly to the Commission until November 8. The Commission will then respond collectively to all submissions, and may revise the proposal or present it unchanged to the European Parliament and EU member states.

## FDI Screening Mechanisms in EU Member States<sup>1</sup>

As mentioned, the proposal will not replace the FDI screenings that exist in the EU. Currently, there are two main approaches toward overseeing direct foreign investments.

- Method 1: EU member states maintain screening processes that may be limited only to the **defense industry** (e.g., Denmark or Romania) or **cover a wider range of sectors** (e.g., France, Italy, Spain or the Netherlands). Fifteen member states of the EU have implemented such measures.
- Method 2: Member states limit presence of foreign investors in certain sectors (e.g., Denmark maintains all gas and electricity infrastructure as public property; Greece, Latvia or Poland have introduced some limitations on foreign ownership of real property). Sixteen EU countries follow this approach.

In practice, many EU member states combine **both** regulatory approaches to supervision of foreign direct investments. See the following examples.

## Germany

There are two screening mechanisms in Germany: one that has general scope of application and the other that uses sector-specific screening mechanism.

The general screening mechanism applies through all sectors when the foreign investor obtains at least 25% of voting rights in the management of the German company. The standard for the screening is security and public order according to the interpretation given to those factors by the Court of Justice of the European Union. For instance, concerns might arise when the investment may affect the security of supply in sectors such as telecommunication or electricity. Under the general scheme, the foreign investor does not have to apply for the license or any type of authorization. On the other hand, the German authorities have the right to initiate the investigation within three months as of obtaining the knowledge about the signing of the binding investment agreement. To ensure greater certainty, foreign investors may also apply for pre-approval of the investment.

The sector-specific mechanism covers defense and other related industries. In this case, all investments that may lead to acquisition of at least 25% of voting rights in the German company are subject to reporting prior to making the investment. German authorities then have three months to initiate the formal investigation. As an outcome of the investigation, the German government might not authorize the investment.

## France

As a general rule, there are no statutory limits on foreign ownership or control of companies in France. However, acquisitions in certain sectors deemed crucial to France's national interests relating to public order, public security or national defense are subject to authorization, screening and approval by the Economy and Finance Minister. Other sectors requiring approval include cryptologic activities; dual-use goods; energy infrastructure; transportation networks; public water supplies; electronic communication networks; public health protection; or installations vital to national security.

## Poland

FDIs in Poland do not generally undergo any general screening process, but some instances require foreign investors to apply for the governmental permission. This includes if the investment entails ownership of real estate in Poland. In addition, there are some restrictions for foreign ownership of companies in certain sectors, e.g., in audiovisual services, aviation or defense.

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<sup>1</sup> For general information about screening mechanisms in EU Member states, see Parliament Research Service Briefing, *Foreign Direct Investment Screening*, May 2017, [http://www.europarl.europa.eu/RegData/etudes/BRIE/2017/603941/EPRS\\_BRI\(2017\)603941\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2017/603941/EPRS_BRI(2017)603941_EN.pdf).

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